

UK sets high standard for Europe's CER quality

The UK government this week said it will use only Gold Standard carbon credits to offset emissions from official travel.

Emissions resulting from flights undertaken by ministers and civil servants on official business will be offset by "high-quality" UN-backed carbon credits selected by the Gold Standard, a Switzerland-based foundation.

The deal itself is only a small step in terms of overall volumes, although it sets the tone for what is likely to be one of the most hotly-debated issues remaining to be decided for the third phase of the EU emissions trading scheme (ETS).

With the EU agreement struck last December, the limits on how many offset credits installations can use for compliance in the scheme between 2013 and 2020 is more or less on the table.

What is still less certain however, is any firm decision on whether the EU will impose quality restrictions beyond those used by the UN's registration process on what credits will be allowed into the ETS.

Initial drafts in the EU parliament last year referred to only allowing in credits of a "Gold Standard-type". These drafts did not survive the final axe but the deal did state credits should have clear sustainability benefits and cause no significant environmental impact.

The final ext also said: "A procedure should be

established which allows for the exclusion of certain project types".

The UK government's wish to appear to be setting its own house in order raises expectations that it will look to push for a stringent quality test for ETS-bound credits in the accelerated EU lawmaking process later this year.

Such a prospect could cause alarm among some project developers or buyers who have invested in projects which could eventually be shut out of the EU. Despite the likelihood of the credits finding other buyers worldwide, the price of credits generated from such projects would tumble.

There is unlikely to be a specific reference to the Swiss foundation in an eventual deal, because of the vast difference in scale needed to accommodate the estimated 1.7 billion credits of EU ETS demand from the period 2008-2020.

Gold Standard aims to finance greenhouse gas reduction projects with proven sustainable development benefits by selling the credits to both the compliance and voluntary markets.

Late last year, the Gold Standard said projects overseen by the foundation had the potential to generate 15 million carbon credits from the Kyoto protocol's clean development mechanism by the end of 2012.

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EUA closing prices - historical

EUA prices for December 2009 delivery, as assessed by Point Carbon. Prices are published daily at www.pointcarbon.com



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EUA closing prices, OTC

Contract	Bid	Offer	Close	Change
EUA spot	13.35	13.45	13.40	+0.50
EUA 2009	13.75	13.80	13.78	+0.46
EUA 2010	14.42	14.52	14.47	+0.46
EUA 2011	15.05	15.15	15.10	+0.43
EUA 2012	15.91	16.01	15.96	+0.34

Secondary CER assessment

Contract	Low	High
Dec-09	10.80	10.90
Dec-09-12	11.12	11.22

Quoted prices are euros per EUA/CER, at close of market 16 April, as assessed through Point Carbon's bid-offer-close methodology for the over-the-counter (OTC) market. Changes refer to the last issue of CME.

For methodology, see www.pointcarbon.com.

Market comment

Nearby European CO₂ allowances climbed some 3.5 per cent over the past week, with the front-year contract scaling a three-month peak.

By 17.30 CET on Thursday, the 2009 EUA was valued at €13.78 in the cleared brokered market, up €0.46 from the same time in the previous week.

Earlier this week, the contract struck €14.50 – its loftiest price since 9 January.

But the market succumbed to profit-taking, particularly amid indications that it may be getting cheaper for utilities to burn cleaner natural gas than coal.

Next year's UK summer fuel switch values – the theoretical carbon price where it becomes profitable for power generators to switch from burning coal to gas – fell €0.79 during the week.

That means demand for EUAs should have been deterred by natural gas prices edging down and coal prices holding steady.

Meanwhile, prices in Brent crude and German power were little changed for the week.

The longer-dated 2012 EUA rose just over 2.1 per cent for the week, putting its spread above the 2009 contract at €2.18.

That compared with the EUA 2009-2012 price spread of €2.30 by the market's close on 9 April.

Despite a four-day Easter holiday weekend which resulted in just three trading days, volume in EUAs reached 76.5 million allowances on all platforms.

In UN-backed CERs, the 2009 delivery climbed 1.4 per cent for the week.

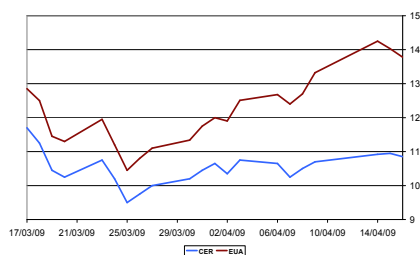
And the price difference between the EUA-CER 2009 contracts widened to €2.93 versus €2.62 during the same period.

Earlier this week, one trader attributed the widening EUA-CER spread to a lack of confidence in the CER market.

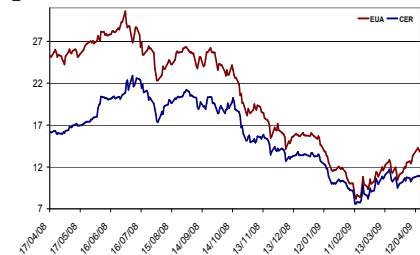
"I think some people want to build more confidence in the (CER) market" before prices catch up to EUAs, he said.

EUA and secondary CER prices [€/t]

Last month



Last 12 months



For methodology, see www.pointcarbon.com

UK sets high standard for Europe's CER quality (continued)

But only a tiny fraction of those have been issued so far amid delays in getting projects through the CDM pipeline.

"We all need to reduce and avoid carbon emissions as far as possible. But carbon offsetting has a legitimate role in helping to address the climate change impact of unavoidable emissions," said Joan Ruddock, a minister with the Department for Energy and Climate Change (Decc).

A spokesman for the department said the government had not yet selected projects from where they will source Gold Standard credits.

"Many of the credits we aim to buy haven't been generated yet," the spokesman said.

The Decc spokesman said it was not possible to say how many Gold Standard offsets would be required to cover future flights by government ministers and civil servants.

In a previous phase of the government programme to buy UN-backed offset credits – known in the official jargon as certified emissions reductions (CERs) – 305,000 were bought by the UK government to cover flights taken between April 2006 and April 2009.

Most but not all of those credits in that phase were sourced from the Gold Standard, although sectors such as wind energy, small-scale hydro and biomass were selected as the source for the offset credits.

The UK's scheme, known as the Government Carbon Offsetting Fund is unconnected with government moves to issue quality assurance for credits in the voluntary market.

The government wants only CERs to qualify for a quality stamp it terms as a 'kitemark.'

China insists CER floor price to stay at €8

China reaffirmed its price floor for UN-backed carbon credits will stay €8 despite contrary claims.

Government officials responsible for regulating carbon trading in China said they would continue to insist that primary CER (certified emissions reduction) projects fetch a minimum of €8.

"We have no plans to lower the price that buyers must pay," said an official with China's Office of National Climate Change Coordination.

The official was speaking amid reports that China

lowered the price floor below €8 earlier this month for some projects in response to falling prices for secondary credits.

Secondary credits have been moving in a range of €7.50-11 for the last several months.

Secondary credits are guaranteed by the seller, and buyers of UN offsets say they would rather pay for these credits than use primary emissions reduction credits, which are sourced directly from projects in developing countries.

Participants in the market for CERs were divided as to whether the Chinese government had lowered the price floor by approving projects where prices had been agreed at below €8 in binding contracts.

"Waste heat recovery, industrial energy efficiency projects are being sold at €7, biomass at €8.50-9.00 and wind at €10.50," said one broker.

He explained that China had relaxed prices for primary CERs in some instances, mainly because prices for secondary CERs have failed to recover.

But other market participants said they hadn't seen any first-hand evidence of primary CDM credits being sold below €8.

Barcap says EU ETS long in phase two

UK bank Barclays Capital said that the EU ETS would have a surplus of EUAs in phase two.

Lower than expected emissions in 2008 and a sharp contraction in the EU economy means that the scheme will have a surplus of 23 million allowances over its five-year phase.

The bank said the EU economy would contract 3.2 per cent this year, down almost 0.9 percentage points on its previous estimate, while any shortfall in allowances in 2008 would be outweighed by a surplus of allowances in the remaining years of the scheme.

"...meaning that, given our expectations of economic growth, the EU ETS does not need to have offsets for ensuring market balance in phase two alone," the report said.

The revised estimation has led the bank to revise its price forecast for 2011 and 2012 to €16.00.

It said EU allowance prices will average €10.00 for the first half of this year and €8.00 for the second half.

The bank said that companies had to buy more

allowances than originally thought in 2008, but that this was due to underallocation of EUAs as opposed to underestimating emissions.

It said it expected the shortfall in allowances in 2008 to be made up in the last four years of the scheme through auctioning allowances and issuing EUAs from member states' new entrants reserves as well as companies from borrowing from 2009 allocations.

Russian emissions creep up 0.3% in 2007

Russian GHG emissions climbed to 2.193 billion tonnes of carbon dioxide equivalent in 2007.

The figures, submitted yesterday to the UN, showed a rise in greenhouse gases (GHG) of almost 7 million tonnes of carbon dioxide equivalent over 2006 levels, up 0.3 per cent.

Increased emissions of methane and nitrous oxide accounted for a 7.2-million tonne increase, with higher production of oil and natural gas a major factor.

This was partly offset by a 2.8-million tonne decrease in carbon dioxide emissions, helped by lower emissions from the energy sector.

Emissions from hydrofluorocarbon (HFC) gases rose by 1.8 million tonnes of carbon dioxide equivalent, while perfluorocarbon (PFC) emissions were up 750,000 tonnes of carbon dioxide equivalent and sulphur hexafluoride (SF6) emissions were relatively stable.

But while the figures show an increase in emissions, they still leave Russia with a huge surplus of emission rights under the Kyoto protocol. Under the 1997 global climate pact, Russia has a target to freeze GHG emissions at 1990 levels from 2008 through 2012.

But the country emitted around 34 per cent less in 2007 than in 1990, according to the data. The big fall in emissions compared to the Kyoto baseline is due mainly to the closure of many Soviet-era industries during the 1990s.

If emissions stay stable from 2008 through 2012, Russia would have a surplus of over 5 billion assigned amount units.

Austria buys 2 million Latvian AAUs

Austria will buy Kyoto emission units from Latvia before the end of April.

Representatives of the two countries will meet in Vienna to sign a purchase agreement on assigned

amount units (AAUs), an official from the company administering the Austrian purchasing programme told Point Carbon.

A Latvian government official said 2 million AAUs will change hands.

It will be the first Austrian AAU deal, which paves the way for more purchases, Wolfgang Diernhofer with Kommunalkredit Public Consulting said.

Diernhofer said Austria plans to buy up to 6.75 million AAUs by 2012 to help the country meet its obligations under the Kyoto protocol.

Austria's target under the Kyoto protocol is to cut greenhouse gas emissions to 13 per cent below 1990 levels over the 2008-2012 period, according to UN data.

Diernhofer said Austria is interested only in "high quality" AAUs, similar to the Latvian units.

The quality of AAUs depends on how beneficial revenue from their sale will be to the climate. Latvia has pledged to spend Austrian AAU-revenue on renewable energy and energy efficiency projects.

The Austrian government has also been buying UN-backed carbon offset credits for compliance with its Kyoto target.

The planned purchases, including the AAUs, will cover up to 45 million tonnes, Diernhofer said. In 2007 Austrian greenhouse gas emissions totalled 88 million tonnes, up 11.3 per cent from 1990 levels.

The Austrian deal takes the total of publicly known AAU-purchases so far to 93 million, of which 75 million changed hands this year.

CDM sector shapes for consolidation

Lower CER prices and tough credit conditions make consolidation among CDM developers more likely.

But some market participants and observers told Point Carbon they have yet to see many clean development mechanism (CDM) portfolios come up for grabs, let alone deals at bargain prices.

"I would expect there to be consolidation at the moment but there just aren't the transactions that are being done," said Simon Shaw, of EEA Fund Management, advisor to UK-listed CDM developer Trading Emissions plc.

"We are in a false world to some extent. People were thinking about it a couple of months ago, but perhaps

because there has been a rally in the carbon price, we haven't seen much come to light," he added.

Share prices of listed developers and aggregators crashed since the price of secondary CERs fell from a peak of €22.90 in July last year to as low as €7.60 in early February.

The price of Trading Emissions shares fell 50 per cent while shares in Camco and Ecoscurities collapsed by more than 80 per cent. But their value has since shown signs of recovery as CER prices climbed towards today's levels of €10.75.

Despite the recent price upturn, Dutch bank Fortis Netherlands was reported to be interested in acquiring stakes in project developers or taking on their portfolios because such assets were available cheaply.

But other sources said few such opportunities were available.

There are more companies in the market looking to buy portfolios of certified emission reduction (CER) credits than firms keen to sell the assets, according to Markus Huewener, CEO of German-based project developer, investor and carbon credit aggregator First Climate.

"We haven't really seen very many of what you might call 'distressed' portfolios coming onto the market. Our shareholders have been keen for us to look at opportunities but the prices have not been attractive."

Huewener still reckoned that restricted access to cash caused by a lack of available credit lines could force some pure aggregators to sell their portfolios.

Consolidation should be expected among project developers and investors, as happens in any maturing market, according to Richard Gledhill, global leader of carbon market services at consultancy PricewaterhouseCoopers.

"Now, because of the credit crunch, there is additional pressure on those with weaker balance sheets so it is reasonable to expect there will be further consolidation," he said.

In its annual results last month, Trading Emissions plc said it had taken full control of developer and fund manager Carbon Capital Markets (CCM), in which it previously had a smaller share. CCM will continue to operate under its own name but has scaled back

investments and reduced staff levels.

EU production falls 1.9% in February

EU industrial production continued to slow down in February 2009 as the recession took its toll.

Production in the 27 member state bloc fell 1.9 per cent compared with January 2009 and 17.5 per cent compared with February 2008, according to figures from the EU's statistic agency Eurostat.

Energy production fell by 1.3 per cent compared to January 2009 and was down 3.5 per cent compared to the same month in 2008, indicating a large fall off in carbon dioxide emissions.

Industrial production fell in all member states compared to February 2008, but most notably Germany and Italy saw production fall by 3.2 and 3.5 per cent respectively.

The figures tally with analyst expectation that 2009 will bring a notable decrease in carbon dioxide output from companies covered by the emissions trading scheme.

In 2008, the bloc's carbon market is estimated to have a deficit of allowances, with some companies expected to either borrow from their 2009 allocation or use UN carbon credits to comply with the scheme. But 2009 is expected by most analysts to reveal a surplus of allowances.

EU nears deal for energy funding

The EU is nearing agreement on using unspent economic stimulus funds for energy projects.

MEPs and the council presidency reached a compromise today that could pave the way for €3.98 billion (\$5.26 billion) to be allocated to gas and power infrastructure, offshore wind and carbon capture and storage (CCS).

An expansion of renewable energy and development of CCS technology is likely to help the EU reach its binding target to cut greenhouse gas emissions by 20 per cent below 1990 levels by 2020.

The informal compromise still needs to be backed by parliament and the council of ministers, the European parliament said in a statement.

A full vote among the full 785-strong parliament is planned for 4-7 May. The European commission had proposed to earmark €3.5 billion to the three energy programmes with economic recovery funds not spent by 2010.

MEPs in the parliament's industry committee and the council presidency, held by the Czech Republic, agreed that the commission will monitor the implementation of the programme and publish a report each year together with its proposal for the budget of the following year.

"If this report in March 2010 identifies 'serious risks in implementing the priority projects', the commission should propose additional energy projects," according to the agreement.

Last month, EU leaders agreed to spend €1.05 billion on developing CCS technology.

Germany, the Netherlands, Poland, Spain and the UK will each receive €180 million, while Italy will receive €100 million and France €50 million. The money is part of a €5-billion stimulus package that will be taken from the EU budget in 2009 and 2010 and spent on energy and broadband technology projects.

UK proposes 11 new nuclear sites

The UK government proposed 11 sites which could be used to build new nuclear power plants.

All the sites are either in the same place as existing nuclear facilities or close to current sites, according to a statement from the UK Department of Energy and Climate Change.

A one-month public consultation on the sites opened today, after which the government will select favoured locations as part of a newly-implemented planning process intended to make quicker decisions on energy policy.

Around 15 per cent of the UK's power is generated from the 10 operating nuclear plants, but this is down from a peak in the mid-1990s when over a quarter of the UK's electricity came from the carbon-free form of generation.

Some plants have since closed and most of the UK's ageing nuclear capacity needs to be replaced. Six plants are due to close by 2015 and all but one of the current units are planned to shut by 2023.

"This is another important step towards a new generation of nuclear power stations. Nuclear power is part of the low carbon future for Britain," said Ed Miliband, Secretary of State for Department of Energy and Climate Change, in the statement.

The sites have been proposed by large energy companies EDF, RWE and EON, as well as the

government's Nuclear Decommissioning Authority, which holds ownership of three sites which it hopes to sell in an auction process. The UK is legally bound to reduce its greenhouse gas emissions by at least 26 per cent under 1990 levels by 2020.

Germany nets €46m from EUAs in March

Germany raised €46 million (\$60.85m) by selling 4.022 million EU allowances in March.

The country sold 3.781 EU allowances (EUAs) as December 2009 futures contracts for an average price of €11.49 and 241,000 spot allowances for €10.93 each, according to data published on a government web site.

This was the first time Germany sold EUAs on the spot market within its monthly sales, which have been going on since last January.

By the end of March, state-owned bank KfW, on behalf of the government, sold more than 28 per cent of the 40 million EUAs earmarked for sale throughout 2009.

Revenue from the EUA sales goes to climate change-related projects, as well as covering the operating costs of the German carbon registry.

Germany, the biggest emitter in the 27-nation EU bloc, has set aside 8.8 per cent of its EU allowances to sell in the second phase of the EU emissions trading scheme, which runs from 2008-2012.

UK utility looks to downsize CDM investment

A Scottish power company is pushing for green investment to be spent domestically.

Scottish and Southern Energy (SSE) is calling for an amendment to the Scotland's Climate Change bill that will ensure that at least 80 per cent of any emission reductions set are achieved through domestic cuts alone.

This would stop the country buying large volumes of international emission rights, known as Assigned Amount Units (AAUs).

But the amendment would also stop Scotland buying large volumes of certified emission reduction (CER) credits generated from carbon-cutting projects in developing countries to meet its targets.

Guest commentary***Mind the post 2012-gap, tackle the risk***

By Alina Averchenkova and Tuomas Rautanen, First Climate Group

The adoption of the legislation for the third phase of the EU emissions trading scheme (ETS) a few months ago added some optimism to the carbon market, which was already struggling with the financial credit crisis.

However, the more recent proposals from the European Commission to phase out the clean development mechanism (CDM) in advanced developing countries and to limit the use of the certified emission reduction credits (CERs) from certain CDM project types coupled with the remaining uncertainty on the post-2012 framework under the UN make it increasingly risky for project developers to invest in origination of new CDM projects.

It is no secret that those advanced developing countries to which the commission is referring are the ones that currently host the majority of CDM projects and cover the largest share of CER supply to the EU ETS market.

Uncertainty over what happens to the CDM projects implemented in those countries post-2012 should the CERs they produce become ineligible in the EU ETS or at the international level hampers new investment as the remaining period for generating credits under the current rules shrinks.

These policy-related risks and the effect of the recession on financing new projects are being felt already on the growth of the CDM pipeline. The inflow of projects into validation is slowing down.

According to the recent data, CDM origination in 2009 fell by some 30 per cent compared to 2008, with the monthly average of projects going for validation coming down to 70 compared to the average of 130 a month in 2008.

Credit is tight due to policy uncertainty but also due to financing conditions.

Banks are reluctant to accept Kyoto-period emissions reduction purchase agreements (Erpas), the binding contracts between project developers and the buyers of the credits, as collaterals for new project financing.

Proposing a 2012 Erpa is often received with even more doubt.

At first sight a fall-off of the pipeline would not

necessarily have a huge impact on the EU ETS - even out until 2020.

Most of the projects in the current pipeline have a European counterparty.

With current crediting rules, these projects can supply a large share of the EU demand by 2020.

However, if the crediting rules change or if there be a "black list" of host countries prevented from developing EU-bound credits, the supply might be at risk.

Times of scarcity would push up the price of the EU-eligible CERs while devaluing the ineligible ones. Thus the cost-containment function of this flexibility mechanism does not get fully realised.

A smooth transition to the post-2012 regime and the willingness to set up proper emission trading schemes in other geographies is dependent on a functioning carbon credit market.

Not only is this in the interest of the EU, which is pushing hard for a global climate solution, but also in the interest of the installations covered by the EU ETS as carbon markets become ever more global.

In an effort to bridge this policy and credit gap for post-2012 investments, the Post-2012 Carbon Credit Fund was set up by the European Investment Bank and four other European public banks, and enables the monetisation of post-2012 carbon revenue streams.

In the current environment, the credit quality of the carbon stream purchaser is decisive. An Erpa with a solid buyer can be monetised to finance projects.

Sponsored by AAA-rated investors, the Post-2012 Carbon Credit Fund, for which First Climate is an investment adviser, enables monetisation of post-2012 carbon streams.

The fund serves thus as a unique vehicle to contribute to the inflow of CERs into the EU ETS in difficult times and helps to maintain positive prospects for the carbon market post-2012.

Do you want to write a guest commentary for Carbon Market Europe? Don't hesitate to contact us at news@pointcarbon.com

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