

# Will the ETS Survive its own Success

Europe is leading the way in using market forces to reduce environmental pollution. However, according to Axel Posthumus, CEO of New Values, the current high price of CO<sub>2</sub> certificates means that Governments are under pressure from industry to take steps to minimise the impact of the EU ETS on power costs and competitiveness.

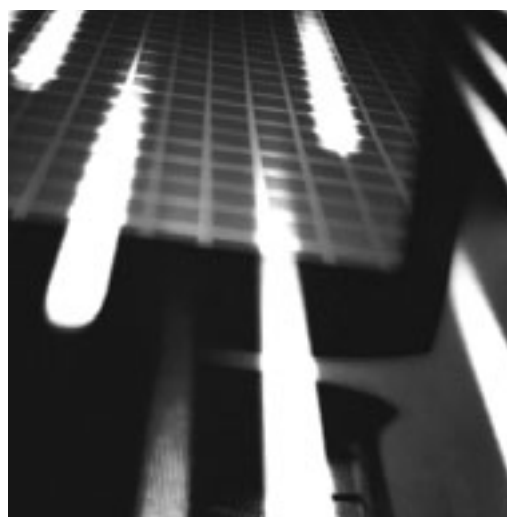
It's a great idea to control the freedom of industry to pollute the environment – by allocating a limited number of free, transferable CO<sub>2</sub> certificates and creating a market with the intention of allocating a cost associated with emitting CO<sub>2</sub> and therefore incentivising industry to use cleaner technology.

The new EU ETS started 1 January 2005 and in total 2,273 million tons of CO<sub>2</sub> certificates (EUAs) have been issued to companies throughout Europe. 94 million tons of EUAs have so far been traded up to September 2005 (4%). This is a good result, considering the fact that only 11 out of 25 registries are active, which results in a large number of EUAs not being available combined with the fact that most industries are not yet actively trading. Nobody can deny that the CO<sub>2</sub> emissions market has arrived.

It is clear that only a small part of industry has been active so far, but banks in general have jumped at the opportunity to get their share of this new market. Prices are much higher than expected. Around 6 Euros in January, but in May, prices had increased to over 30 Euros per tonne of CO<sub>2</sub>. Since then, prices have fallen again down to 22 Euros but are still a lot higher than expected. European Commission research has showed that it

should not cost the EU more than 20 Euros per ton to comply with "Kyoto".

The link to other related products is also becoming more apparent. Because of the rise in oil prices, the price of gas increased as well. Therefore, it is cheaper to burn coal instead of gas. But by burning coal, pollution increases and more CO<sub>2</sub> emission certificates will be required. Not only is it necessary to buy more EUAs but the price is rising because of the increase in demand. Should this continue, and the general expectation is for oil prices to remain high, then more companies, particularly in the power sector will all fall short of EUAs. This will force up the price of EUAs even further. Already, power producers are warning of further rises in power prices. ▶



An increase in prices was what politicians intended when they introduced the system. But the extent of price effect, can lead to second thoughts in politics, especially when the consumer (read: the voter) is hit financially. And there is also the impact on economic growth which leads to more production, more pollution and an increase in the demand for EUAs.

Plenty of reasons therefore for Governments to want to tinker with the ETS. However, the potential adverse effect on the market is evidenced by what happened with the Green Certificates in the Netherlands. This was also a successful market, but there were a few adverse side effects and because of Government intervention, the price of a Green Certificate dropped from 30 Euros to 30 Eurocents per MWh and the market collapsed. Let us hope Europe is not going in the same direction. The

environment and therefore all of us, would be the main loser.

*Axel Posthumus is CEO of New Values, a network organisation to which various parties contribute their expertise. It is owned by the Rabobank and TenneT.*

*The trading platform "Climex", launched by New Values, offers free of risk spot trading in CO<sub>2</sub> allowances and Kyoto certificates and bilateral forward trading and has been operational from the end of June 2005.*

*Climex is unique because it is easy to use, and at low cost, for both small and large traders through a secure internet connection. Climex provides anonymous matching between buyers and sellers and functions as a central counter party covering settlement risks.* ■

