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## Carbon 'Like Titanic' Sinking on EU Permit Glut

By Ewa Krukowska - Mar 30, 2012 1:01 PM GMT+0200

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The plunge in European Union carbon permits is putting prices on course for their longest-ever decline and shows no sign of ending as member states wrangle over curbing a glut in the market.

EU allowances for December fell 4.9 percent this year, extending a streak of quarterly losses stretching back to March 2011. Prices may drop a further 50 percent and lawmakers will probably fail to cut supply in the world's largest emissions market through a so-called set-aside process, according to UBS AG. For First Climate AG, an asset manager that advises the [European Investment Bank's](#) carbon funds, emissions are unlikely to recover in the next quarter.

 Enlarge image



Smoke rises from a chimney behind stacks of coal at a coal fired power station in Belchatow, Poland. Photographer: John Guillemin/Bloomberg

"Unless EU governments come up with a surprise decision to strongly support the set-aside or ambitious mid-term emission-reduction targets, I don't see prices moving up much over the coming months," Tuomas Rautanen, head of regulatory affairs and consulting at First Climate in Zurich, said by e-mail.

A surplus of permits and the inability of European nations to agree how to tackle the glut in the \$120 billion market sent prices to an all-time low this year. Verified emissions data due on April 2 may show 2011 discharges from more than 12,000 factories and power plants in the region's trading system fell short of the number of issued and sold permits for a third year, according to Bloomberg New Energy Finance.

### Low-Recovery Odds

Permits for December, the benchmark contract, slid as low as 6.38 euros (\$8.47) a metric ton on Jan. 4 on [London's](#) ICE

Futures Europe exchange. The current-year contract was up 1.6 percent at 6.96 euros at 11:29 a.m. today. The average in the past year was 11.87 euros.


Prices will probably fall to about 3 euros before lawmakers are able to tighten the bloc's emissions targets, a process that may take "years," Per Lekander, UBS's Paris-based global head of utilities research, said in a phone interview yesterday.


"It's not that I'm skeptical on the set-aside, it's just not going to happen," he said. "It's going to get blocked."


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Permits have slid 61 percent in the past 12 months as industrial production slowed, reducing demand. Companies covered by the trading program discharged 1.93 billion tons of carbon in 2010, compared with their allocated 1.99 billion tons.

A potential set-aside of permits may offer only a temporary relief to the system, which needs a "deep overhaul" after expectations that a global climate deal will lead to a system of interlinked national markets failed to materialize, according to Jan Pravda, director of Prague-based Pravda Capital Trading.

## U-Turn or Crash

"It's a big challenge to re-design the ETS and make it a system that would reward both [energy efficiency](#) and pure emission reductions, but you can't avoid it," he said today by phone. "It's like being on the Titanic and seeing the iceberg in front of you; either you make a U-turn or crash."

The EU's cap-and-trade program, which imposes emission quotas on businesses and requires those exceeding their limits to buy permits from companies that discharge less, allows unused allowances to be rolled over into later years. That may produce a 1.1 billion-ton oversupply of permits in the 2008-2012 trading phase, equal to about 53 percent of an average annual EU pollution limit in that period, according to BNEF.

The current price of greenhouse-gas pollution is less than a fourth of what policy makers expected it to be when the system was reviewed in 2008 to meet the bloc's climate-protection targets and encourage investment in low-carbon technologies, Peter Liese, a German member of the European Parliament representing the European [People's Party](#), told reporters Feb. 29.

## 'Necessary Amount'

According to one of [104 amendments](#) to a planned energy- efficiency law endorsed by the parliament's industry committee on Feb. 28, the European Commission may propose to withhold a "necessary amount of allowances."

To become binding, the changes would need backing from member states, which may decide to leave out the alterations in their version of the law, according to a draft proposed by [Denmark](#), which holds the EU rotating presidency.

Even if the set-aside option is removed from the planned law, the commission has the right to come up at any time with a proposal to withhold permits.

Any proposal to delay auctions of allowances from 2013 would need the support from national governments in a separate regulatory process. The commission will probably get enough backing from nations to set aside 700 million of permits in the eight years through 2020, according to Barclays Plc.

## Set-Aside

Prices may rise to 9 euros a ton in the second half should there be a "positive outcome on the set-aside," [Trevor Sikorski](#), the London-based director of energy-markets research, said in a March 26 report. The bank previously forecast prices would climb to 8 euros a ton.

While a move to temporarily withhold permits may help prices, it's unlikely to affect investment in clean energy unless the EU sends a signal that allowances will be subsequently canceled, Sikorski said.

Any permanent removal of allowances would mean a tighter emissions cap for the bloc, a step that would require a revision of the emissions-trading legislation and also involve the European Parliament and may take more than a year.

The EU is on course to meet its goal to reduce [greenhouse gases](#) by 20 percent in 2020 compared with 1990 levels and [member states](#) remain divided over the need for stricter climate policies. Poland blocked a statement by energy ministers March 9 on post-2020 emission-reduction goals, which it said may result in discussions about revising the existing target.

### Undermine Confidence








Poland also opposed the idea of a set-aside, which Environment Minister Marcin Korolec said would destroy the essential market features and undermine investor confidence in the stability of European legislation, according to a letter he sent to his counterparts.

Any developments on the possible structure of the set-aside and support for or opposition to the measure triggers carbon- price swings, UniCredit SpA analyst Heiko Siemann in Munich, said in a report on March 23.

"Until we have credible coordinates on these matters, prices will remain unpredictable," they said. "After breaking the mark of 7 euros per ton, we can't exclude that the all-time low of 6.38 euros from Jan. 4, 2012, will be reached."

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