Carbon Market Australia-New Zealand

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Reports of A$23 as Australia braces for carbon tax details

Unsourced reports surfaced in Australian media on 7 July that the government will set a starting price on carbon at A$23 per tonne of CO2 equivalent, starting 1 July 2012.
Prime Minister Julia Gillard refused to comment on that figure, but a compromise has been negotiated between Labor, the Greens and independents, and the full details of the carbon regime will be made public this Sunday, 10 July.
Members of the multi party committee on climate change, which has negotiated the deal, have been tight-lipped about the details of the scheme, although a few issues have been clarified in recent weeks:

• Petrol will not be covered by the carbon tax, meaning the amount of covered firms will drop to 500 from the initially planned 1,000;
• Only installations emitting more than 25,000 tonnes of CO2 equivalent per year will be included;
• Producers of synthetic greenhouse gas emissions will be excluded.

The domestic debate has been strongly dominated by claims of how much/little the scheme will cost for industries and households, and how and how much these will be compensated. It is clear that many sectors will receive compensation, including gas and coal producers, who will receive free permits to cover a certain amount of their needs.
Another report has been that the Greens have successfully negotiated a A$2bn renewable energy fund as part of the deal.
From a market perspective, most of the details that will shape the future market are set to be revealed on Sunday.
However, unconfirmed reports have **Continued on page 2**

NZ emitters surrender 8.3 million permits for 2010

Companies covered by the New Zealand emissions trading scheme surrendered 8.3 million permits to cover their 2010 emissions, a 1 July update from the New Zealand Emissions Unit Register showed.
The report showed participants in the scheme emitted 16.3 million tonnes of CO2 equivalent in the last six months of last year, after the ETS was expanded to cover energy, industry and transport on 1 July, 2010.
Under the scheme, NZ emitters only have to surrender one permit for every second tonne of CO2e they emit, meaning the covered companies were obliged to hand in over 8.1 million permits to the government.
In addition, 200,000 permits were surrendered by owners of deforested land. The report did not specify whether the surrendered units were New Zealand units (NZUs) or UN-

Continued on page 3

Contents

Market comment

The last four weeks has been a steep ride south for New Zealand carbon units. Under pressure from diving EU carbon, spot NZUs lost 8.1 per cent - a drop of NZ$1.60 - over the period to close 7 July at NZ$18.15, the Point Carbon News price assessment showed. CERs in the NZ market fared even worse - falling 16.7 per cent or NZ$3.73 to NZ$18.64.

The driving factor has been a one-way route down in Europe, where the front-year EU allowances lost over 20 per cent of its value in a three-week period on the back of a series of bearish news. Energy prices in the 27-member bloc have gone down, 300 million EUAs for the third trading scheme are set to become available to market players already later this year, and huge problems in the economies of Greece and Portugal have spread fears of tough economic times ahead for Europe, which could hit industrial production, causing emissions to fall and increase oversupply in the market.

In turn, CERs in Europe fell 11.6 per cent over the period, to close on 6 July at €10.79, down €1.41 over the four weeks.

"There's been lots of downward pressure from CERs and a continued lack in demand," one broker told Point Carbon News, although the last week in June saw a boost in liquidity, when 600,000 NZUs changed hands. Overall, some 1.35 million NZUs have traded since 9 June, while as many as 2 million CERs are thought to have been bought by NZ emitters.

NZU sellers have resisted the downward trend hoping the permits would be rebound, even though at one stage in late June they traded below NZ$18.

The crash in CER prices, helped by a stronger kiwi dollar against the euro, meant that at times it was cheaper for NZ firms to buy CERs than NZUs, although this imbalance has since been corrected by the market.

At the time of press, NZ traders expected the down trend to continue as the EU economic problems look set to linger.

Continued from page 1

circulated lately that instead of aiming to transit from a fixed price to an emissions trading scheme after sometime between three and five years depending on an amount of external factors, the final provisions will fix the switch to 1 July 2015.

"The main point for me will be to see which provisions they have included to get the scheme across the line," said Anthony Hobley, global head of climate change and carbon at lawfirm Norton Rose.

He referred to previous reluctance within the Greens to embrace the scheme amid concerns that Australia would lock in under-ambition in terms of future emission cuts. The government as well as the opposition wants to cut emissions to 5 per cent below 2000 levels by 2020, while the Greens have been advocating cuts up to 40 per cent, in line with recommendations by climate scientists.

"It will be interesting to see to which extent they have a framework that can get tightened up later," Hobley said.

He told Point Carbon News that the government should do its best to frame the scheme as a market mechanism, and not as a tax, which the opposition has hammered Labor over in recent months with big success. One way to achieve this would be to sell allowances during the fixed price period rather than simply implement a tax structure.

How and when the scheme would transition to an ETS would also be key in this respect, Hobley said:

"Moving to a floating price sooner would make it harder for a potential Liberal government to unravel the scheme, and it would create greater certainty."

The New Zealand ETS is a traded market despite offering a fixed price option at NZ$25 for emitters. This is possible because the country's forestry sector is able to supply permits below that price. A similar provision is not existent in Australia's plans, although a certain amount of credits from the Carbon Farming Initiative (CFI) is expected to be allowed for compliance purposes during the fixed price period.

Hobley did not expect, however, that the government will have changed its mind when it comes to international offsets, and said certified emissions reductions (CERs) is only likely to be eligible after the transition to an ETS.

The legislation is expected to be introduced to parliament next month, and could be approved in October or November. Until then, expect a loud media debate focusing on the compensation measures.

NZ emitters surrender 8.3m permits for 2010 (cont.)

issued credits such as certified emissions reductions (CERs). In total, scheme participants emitted 33.4 million tonnes for the entire calendar year, according to the report.

The government also received nearly NZ$1 million in cash payments from companies that chose to pay the fixed price of NZ$25 per tonne directly to the government instead of buying permits in the market.

The fuel sector was by far the biggest-emitting sector in the scheme, releasing 7.7 million tonnes of CO2e into the atmosphere in the last half of 2010, followed by natural gas miners (4.2 million tonnes).

Purchasers of natural gas were responsible for just over 1 million tonnes of CO2e in emissions in that period.

Unlike in the EU carbon trading scheme, NZ emitters do not have a cap on their emissions, but are allowed to emit as much as they want as long as they surrender the required amount of permits or pay the fixed price to the government.

The report showed that by 24 June, the government had allocated nearly 12.8 million NZUs to forest-owners storing carbon in their trees and to trade-exposed industries receiving permits in compensation for the increased costs imposed by the ETS.

It said that from 1 January 2008, when the ETS started for foresters, until 31 December 2010, 10.3 million tonnes of CO2e had been removed, mainly through planting new trees.

However, that number is not final as foresters can choose whether to submit their removal activities annually or at the end of the first trading period, 31 December 2012.

According to the registry, over 600,000 CERs were transferred to New Zealand in 2010, as NZ emitters can use an unlimited amount of them for compliance purposes.

NZ firms are thought to have bought well over 1 million CERs in January and February this year, when the international CER price – normally trading NZ$3-4 above NZUs – fell to trade at par.

The same trend has been seen in recent weeks, as NZ firms bought up to 2 million CERs in June, according to market observers.

Scheme participants must surrender permits for their 2011 emissions on 31 May 2012.

The government is currently considering whether to remove the fixed price option and the 50 per cent surrender obligation from 1 January 2013.

NZ carbon scheme faces first challenge

From moribund to modestly active, New Zealand's carbon trading scheme has picked up since the entry of big polluters a year ago but faces a major challenge in how to ramp up pressure on firms to take more steps to cut emissions.

The emissions trading scheme, or ETS, remains the first national scheme outside Europe's $120 billion a year programme.

Industry is questioning whether New Zealand should toughen its scheme given the glacial pace of UN negotiations on a new climate pact and slow progress in other competitors in bringing in a national price on carbon.

Neighbouring Australia is struggling to win support for its carbon pricing plan.

A toughening could boost trading of pollution permits in the ETS, deepening the market, which is currently limited by availability of tradable New Zealand Units, a price cap of NZ$25 for NZUs, lack of national emissions reduction target and a series of sweeteners for industry during the first phase to end-2012.

Climate Change Minister Nick Smith declared the past year a success, saying trading had been in line with expectations.

"There is broad acceptance across the business community as to the merits of an ETS, but there still remains some quite difficult decisions about the pace of which we advance this scheme forward," Smith said.

The three-year old ETS was expanded on July 1, 2010, when the transport, industry and energy sectors, which account for about half of the country's emissions, were included.

Since then, average weekly trade of NZUs in the over-the-counter market has averaged about 300,000, according to data from Thomson Reuters Point Carbon. Forestry was the first sector in the ETS, which started in 2008.

"We really have pioneered something in terms of emissions trading insofar as how the market was regulated. I don't think we've pioneered anything in terms of markets," said Richard Hayes of EITG, a carbon project developer and

advisory.
EITG joined other firms in submitting recommendations to the government as part of a mandatory review of the ETS.
Polluters such as coal-fired power generators, refiners and cement plants have to buy NZUs to meet government-set emissions obligations, while foresters are given NZUs for the carbon locked away in their trees.
Exporters are given a large number of NZUs for free to equalise carbon costs with competitors.
Hayes has called for rolling issuance and surrendering of NZUs, instead of set annual dates for these, to ensure smooth supply and reduced costs for market players.
Smith declined to comment on changes the government will look at, but it is expected to include the possible extension of sweeteners, such as surrendering only one NZU for every two tonnes of emissions, beyond the current expiry date of 2013.
Agriculture, a major export earner and which accounts for almost half of emissions, enters the ETS in 2015. Dairy exporter Fonterra is New Zealand's largest company, and is still liable through its milk processing operations.
New Zealand was exposed to greater emissions costs than other agricultural producers, so it was imperative transition measures remain until competitors move to similar schemes, said Fonterra's General Manager Sustainability John Hutchings.
Greenpeace said the sweeteners offer a lifeline to heavily polluting industries and are not sending a strong enough message to change long-term investment decisions.
"This will render the ETS ineffective and risks locking New Zealand into a high-carbon, inefficient economy," campaigner Nathan Argent told Reuters.
State-owned Genesis Energy, which operates New Zealand's largest power station, said it also wants the transitional measures to continue, and it also wants to see greater depth and liquidity in the market.
"What companies like ours need is certainty of policy and liquid markets in which to function," Genesis Public Affairs Manager Richard Gordon said.
"We can cope with the ETS, we can live with it, but we need certainty."
Both Genesis and Fonterra said they have been active in the market since July last year, however both companies said there were issues with market liquidity, with too few credits coming to market.
Hayes said another major problem was lack of information.
"There's an absolute lack of concrete, discoverable and open information and that has a pretty significant downstream effect the operation of businesses."
Lack of supply has seen spot prices for NZUs slip over the past few months to sit below NZ$20, which Fonterra's Hutchings noted was likely due to sellers, which are mostly foresters, sitting on credits awaiting better prices.
The Ministry of Agriculture and Forestry says about 14 million NZUs have been issued to date (mid-June) to forest owners that fall under Kyoto Protocol rules and that about 57 million will be issued during the 2008-12 period.
The government also estimates nearly 12 million NZUs will be given to exporters by end 2012.
Carbon consultant Stuart Frazer said the market was currently narrowly focused on compliance, and it would not develop into a fully liquid market until it had reached a point where secondary traders were active in the market.
The price cap is also limiting the chance for polluters to buy UN carbon offsets called certified emissions reductions.
The ETS allows these to be imported and used for compliance and a recent drop in the value of the euro, CERs and strengthening New Zealand dollar saw polluters snap up large volumes of CERs.
Smith reiterated the review would be influenced by the progress of international negotiations.
Frazer said there were risks with pegging the scheme to international progress and that the government could lose focus on the way scheme could best function.
Smith also believed the ETS was lowering emissions and encouraging greener investments.
Greenpeace disagrees, saying many decisions were still based around fossil fuels, such as state-owned miner Solid Energy's plans to mine lignite to convert into liquid fuels.

California, Quebec postpone emissions trading schemes

California and Quebec have both postponed the introduction of their carbon trading schemes under the Western Climate Initiative by one year, to 1 January 2013. Both quoted the need to get the rules and regulations of their systems right, and allow 2012 to be a test year.
"The first year will be transitional and allow emitters and

market participants to familiarise themselves with how the system works," officials from Quebec's environment department said on 6 July.
"This phase will also enable partners to make any required fine-tuning in order to make a smooth transition to their obligations under the GHG cap-and-trade system that will come into force on January 1, 2013," the officials said.
A second Canadian province set to trade carbon under the regional climate regime, British Columbia, is also expected to postpone its market, as liquidity would suffer without California presence.
Prospects of a growing carbon trading market in North America was recently dealt a blow when the governor of New Jersey, one of the ten northeastern US states participating in the Regional greenhouse Gas Initiative (RGGI) announced he would pull his state out of that market from next year. Tea party-led lawsuits against RGGI are underway in several other states, including New York.
But market participants in California welcomed the one-year delay, saying it was crucial to get the rules right.
Jean-Yves Benoit, an economist with Quebec's climate change office told Point Carbon News he was positive the WCI markets would go ahead as planned, and that by the end of this year the governor of California and the premiers of British Columbia, Quebec and possibly Ontario will sign a memorandum of understanding (MOU) recognising each system as equivalent.
"Once we sign those agreements, then the allowances will be fully fungible between jurisdictions," Benoit said.
"That will create the North American carbon market under the Western Climate Initiative."

Panama to host pre-Durban UN climate talks in October

Panama will host a final intersessional round of UN climate talks in October before an annual summit in South Africa, the UNFCCC said on its website.
The meeting, to be held in Panama City between 1-7 October, will give negotiators one last chance to advance efforts to agree a new climate regime or extend the Kyoto protocol before November's conference of the parties (COP) in Durban.
The last intersessional talks, held in Bonn, Germany in June, saw little progress with delegates claiming small advancements in cleaning up technical text but nothing in the way of getting the world's top emitters to commit to binding emissions targets beyond 2012.
In early July Germany hosted separate ministerial talks, while the South African COP hosts will arrange for heads of state to gather on the sideline of the UN general assembly in New York in September.
However, expectations remain low that a significant breakthrough in the talks will be reached this year.

UN doles out 70m CERs in Q2, 2011 poised for record

The UN handed out 1.7 million certified emissions reductions (CERs) in the last week of June, capping off a record first half of the year which saw more than 150 million credits issued, UN data showed.
The UN has handed out on average 25.1 million credits a month so far this year. A total 70.7 million CERs were awarded in the second quarter of 2011, nearly three times the 23.9 million units handed out in the same period last year, but 11 per cent below the 79.8 million issued in the first three months of 2011.
Calls for a further 20 million CERs have also been submitted to the UN for potential issuance in July, the UNFCCC website showed.
If the current pace of issuances is maintained, the UN could hand out well over 300 million CERs this year, according to calculations by Point Carbon News.
The average issuance so far in 2011 was 206,400 units in size, down slightly from last year's average award of 214,200.
The UN has recorded 736 separate issuances so far this year, putting it on track to more than double the 618 credit issuances in all of 2010.
Research group UNEP Risoe forecasts 1,090 million CERs will be awarded by the end of 2012, while analysts at Thomson Reuters Point Carbon predict 1,244 million will be issued by May 2013, the compliance deadline for the second phase of the EU ETS.
CERs are an additional source of supply for companies needing to comply with the New Zealand emissions trading scheme, and are likely to be eligible in the Australian scheme when it transits from a tax to an ETS.

NZ carbon market shifts from stand-off to sell-down

By Mike Mitchell, Carbon Business Manager, IFS Growth

The last two months have seen notable shifts in the New Zealand carbon market causing some parties in the forestry sector, the largest source of units, to question the ability of the market to deliver stable and realistic prices to holders of units.

Whilst the recent dramatic fall in price has been of concern to forest owners, the resulting reaction from the holders of forestry units has reinforced the stereotype of the typical forestry investor - patient, with a focus on the long term.

The end of May saw domestic demand for units dry up with New Zealand emitters fulfilling their requirements and what little overseas demand there was, being largely negated by the closing price gap between NZUs and CERs. The resulting slip in prices from the heady heights of NZ$21 per NZU in March to mid-NZ$19 saw a stand-off between holders of forestry units and domestic purchasers with foresters preferring to hold units rather than drop offers to match buyers' expectations.

A $20 per NZU price is a significant psychological barrier for some forest owners, with many refusing to deal at any terms under this price. Rightly or wrongly, this stance has seen large volumes held back from sale. Additionally, stuttering supply from government has precluded many current holders of units from taking advantage of the March and April market highs, further adding to the estimated millions of NZUs that are yet to make it to market.

But even the most stoic of foresters has been tested by plunging carbon prices over the last month. Day after day falls on the back of European problems saw some sellers abandon hopes of NZ$20 and sell down between NZ$19 and NZ$18 in the hope of retrieving decent returns from the market whilst they still could. These jitters saw significant volumes being sold, with lower prices encouraging bids from domestic emitters for reasonable volumes for the first time in weeks.

Where to from here? Many foresters have had to readjust their price expectations away from the magical $20 per NZU mark. This readjustment will see increased volumes coming to market, particularly from pre-1990 forest owners who are still being drip-fed compensatory NZUs by government. The compensatory nature of pre-1990 forestry allocations dictates that these holders tend to be more concerned with cashing in quickly, rather than price.

On the political front, the independent review of the New Zealand emissions trading scheme (ETS) was delivered to the Minster of Climate Change at the end of June. Market participants have placed pressure on government to deal with the issues of the 2 for 1 surrender obligation for emitters, the NZ$25 market cap, and the implementation of a ban on the importation of industrial gas CERs.

Many sellers will be hoping that at least one of these market constraints will be dealt with by the review, leading in the short term to some form of market rebound, and in the long term, carbon prices that are more palatable to enduring New Zealand foresters.

A sense of perspective is a wonderful thing. It's worth noting that current carbon prices are well within the NZ$17-$21 range that has existed within the New Zealand carbon market since its inception. The reluctance of some forest owners to sell should be tempered by the fact that carbon is a vastly different commodity to timber; compliance carbon units only have value whilst governments say they do. Perhaps the financial pragmatism of selling units and generating income whilst the opportunity presents should override the fear of sellers' remorse.

Do you want to write a guest commentary for Carbon Market Australia-New Zealand?

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