

European Climate Change Programme
**Linking with Emissions Trading Schemes of Third
Countries**
Implications of Supplimentarity Limits

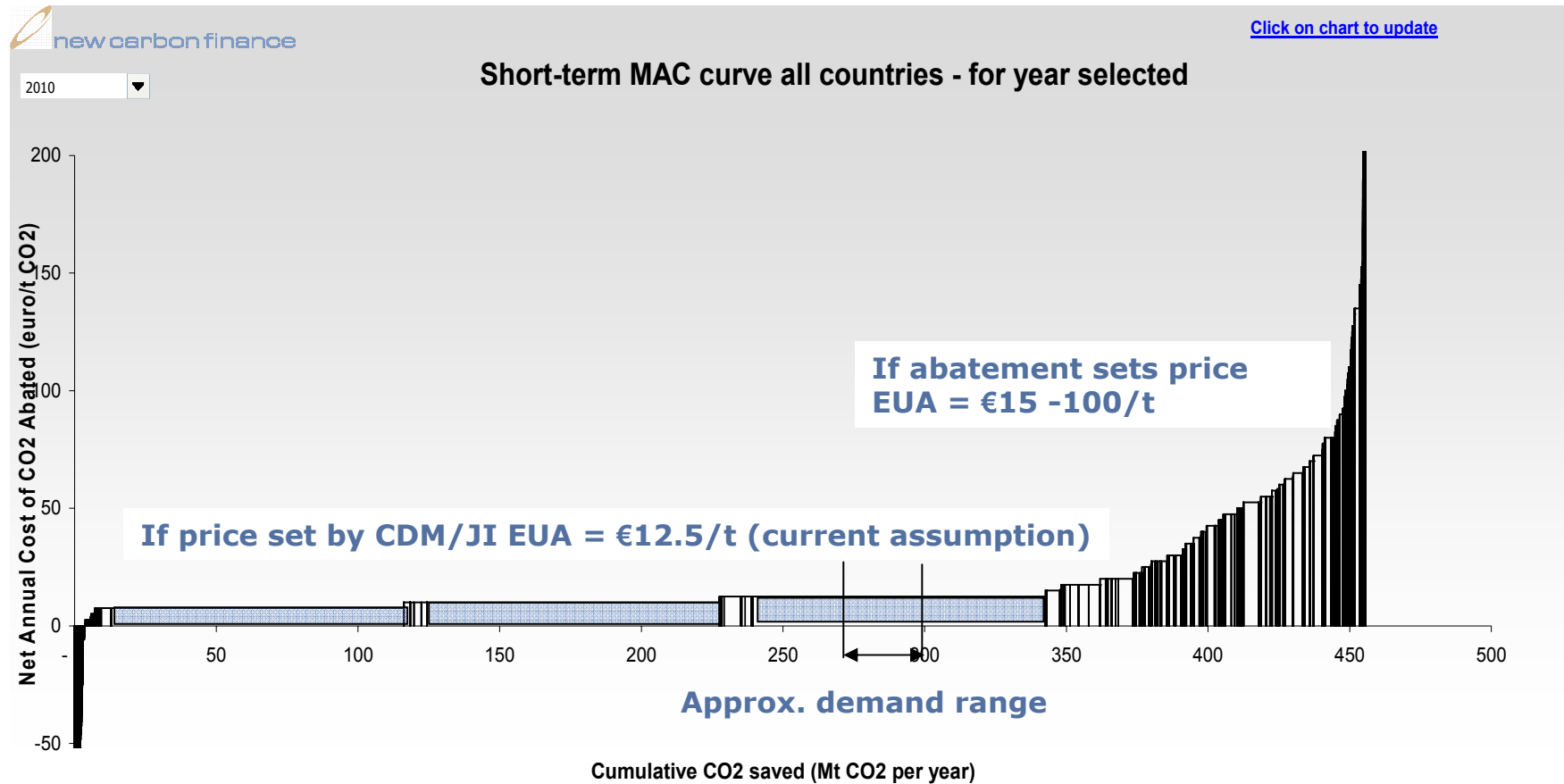
15th June 2007



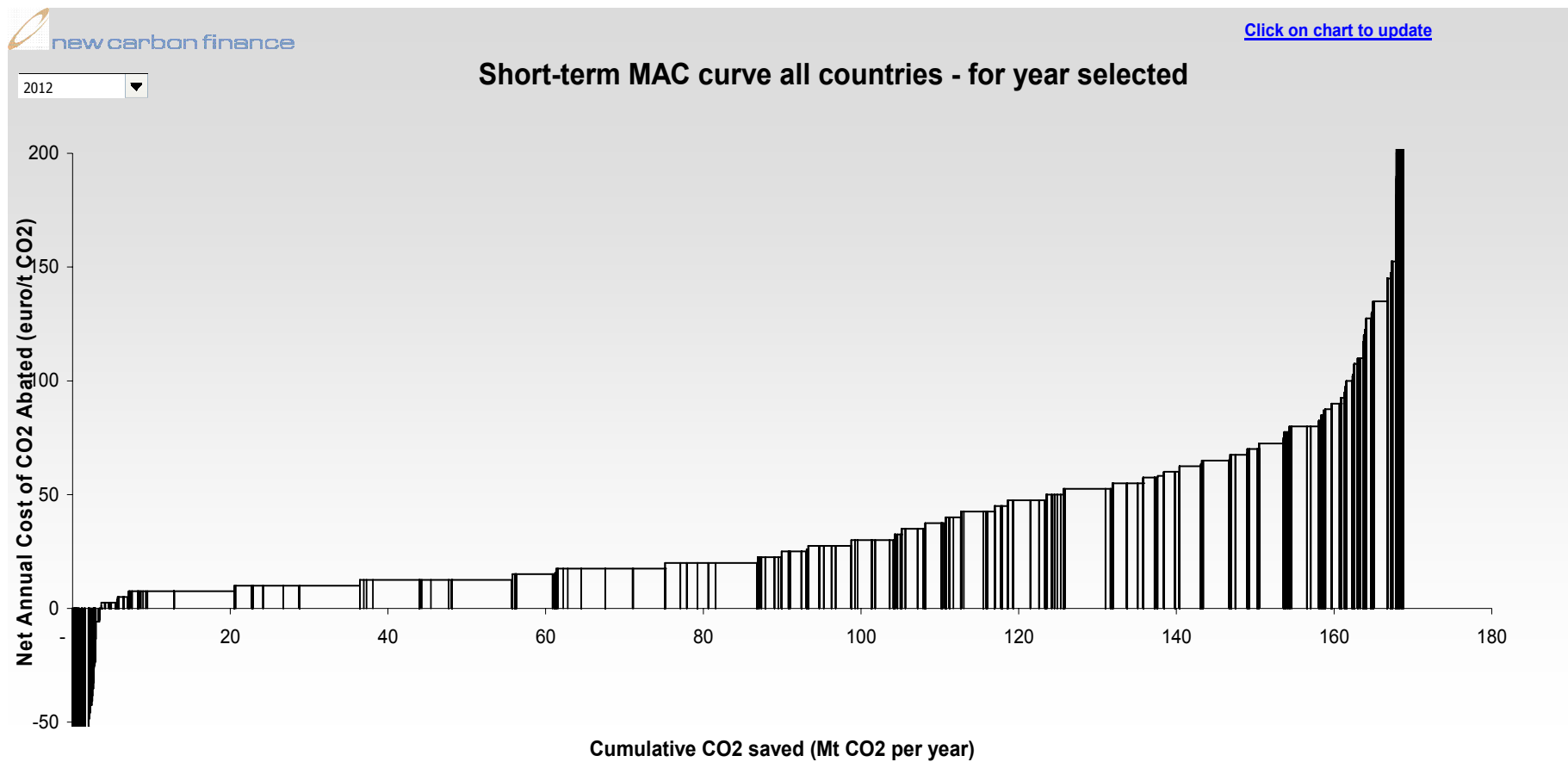
Contents

1. Phase II fundamentals
2. Phase III Implications
3. Pricing trends
4. Summary

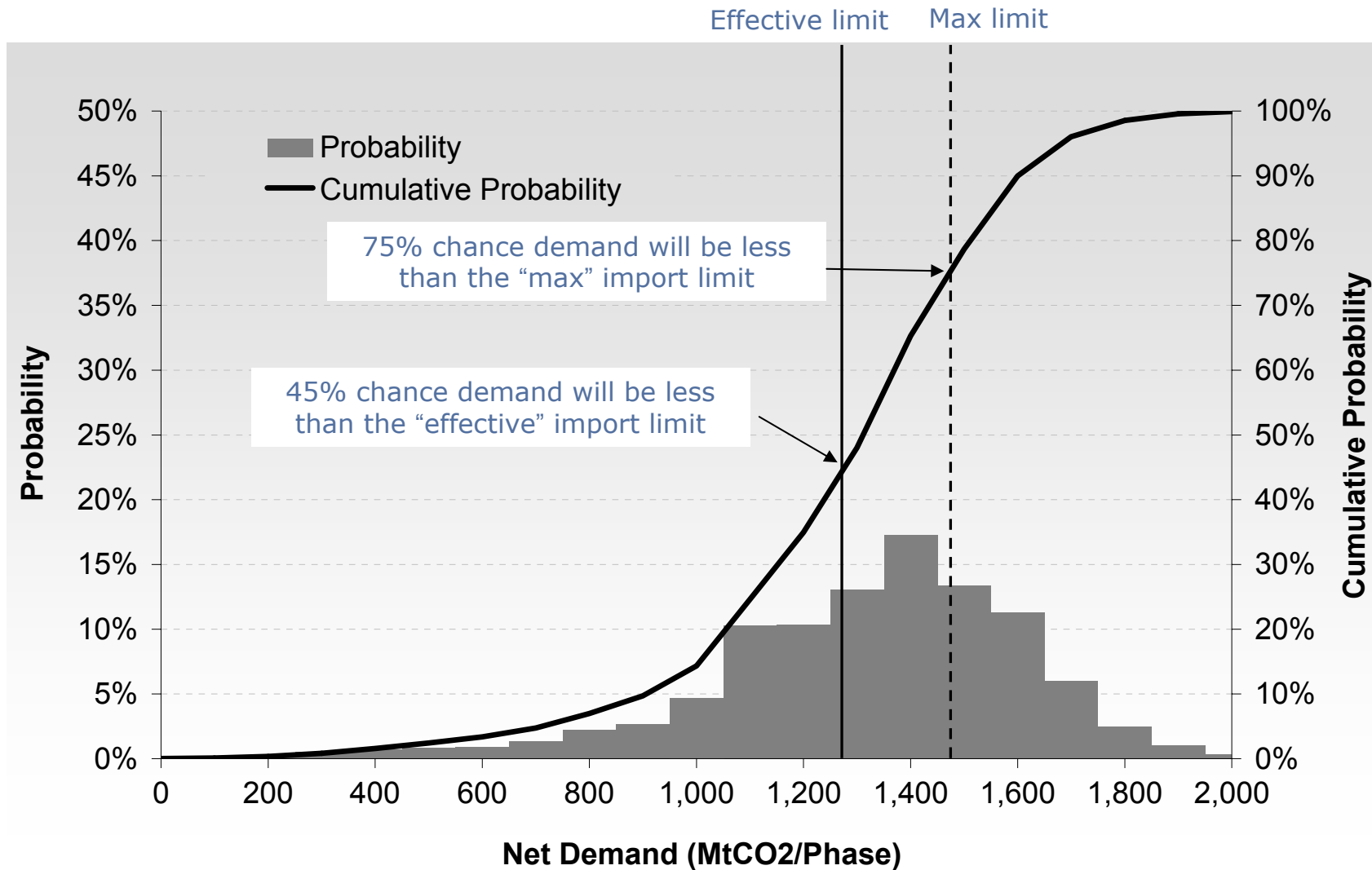
Phase II – EUA price highly influenced by volume of CDM/JI in the EU ETS.



Phase II – Without CDM/JI Phase II prices would much higher, c. €100/t

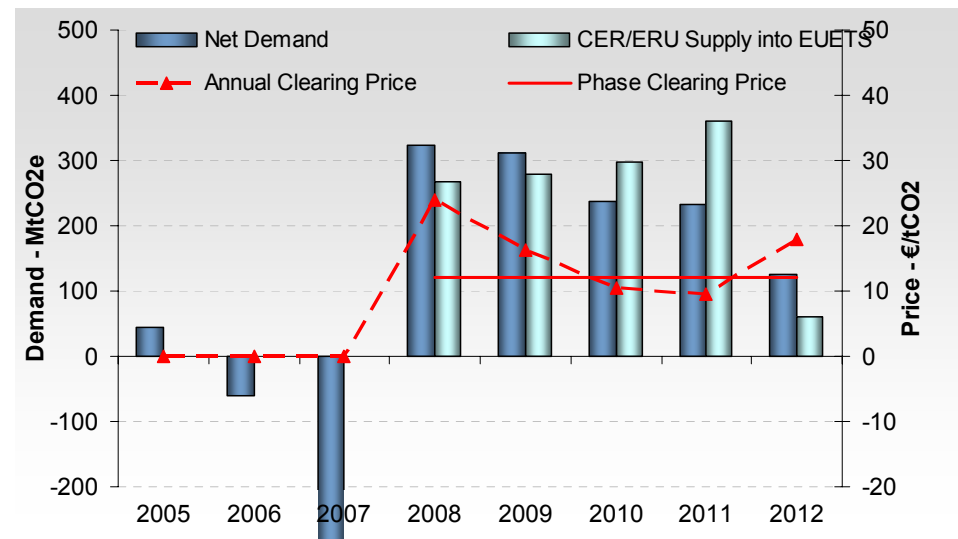
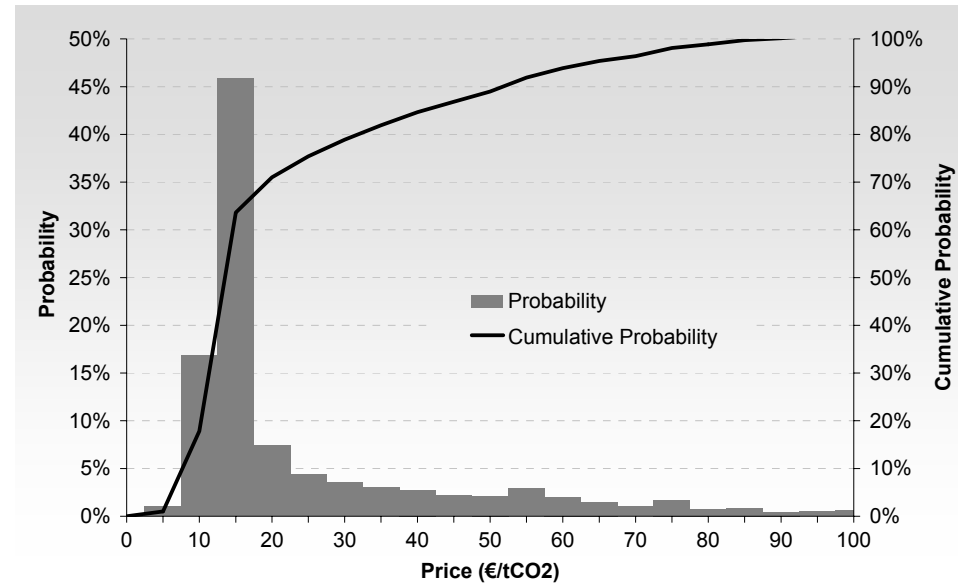


Phase II – Latest NCF analysis shows EU ETS net demand very close to CDM/JI supplementarity limit



Phase II - this acts to reduce EUA price forecasts

- Central price = **€12.5/t** (range **€10 – 20/t**).
- 50% prob price = **€14/t**
- Over next two years will see **high prices** as buy side pressure runs ahead of selling activity
- Prices then reduce as CDM/JI imports increase
- Possibility of CDM/JI import limit + banking into Phase III supports prices to end of Phase.



Phase III – If complementarity limit applied in Phase III price likely to be in range €20/t (short term) - €60/t (long term) or higher.

SRMC of coal to CCGT = €30/t (existing coal, existing CCGT)

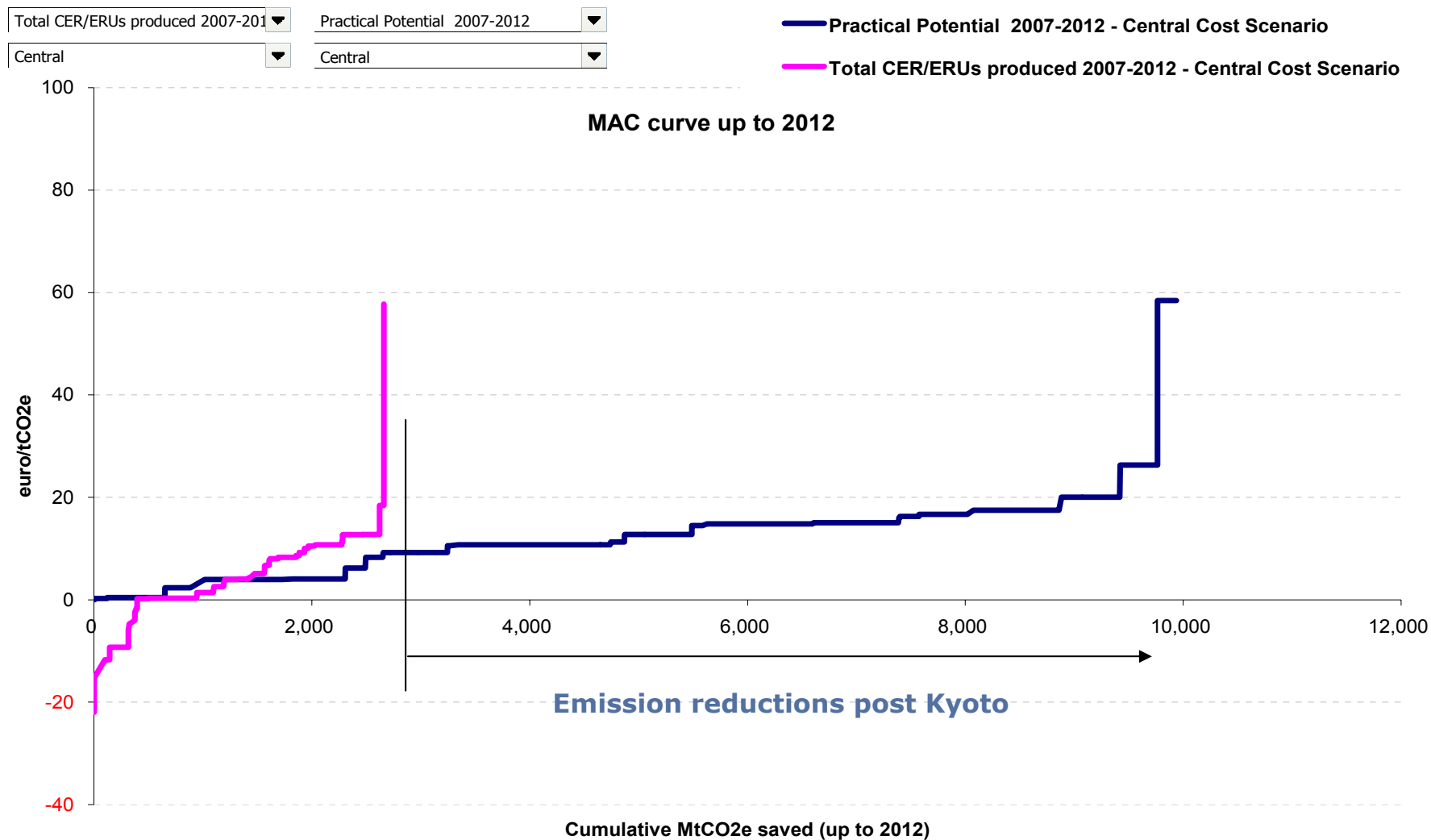
LRMC of coal to CCGT = €20/t (new coal, new CCGT)

LRMC of coal to CCGT = €60/t (existing coal, new CCGT)

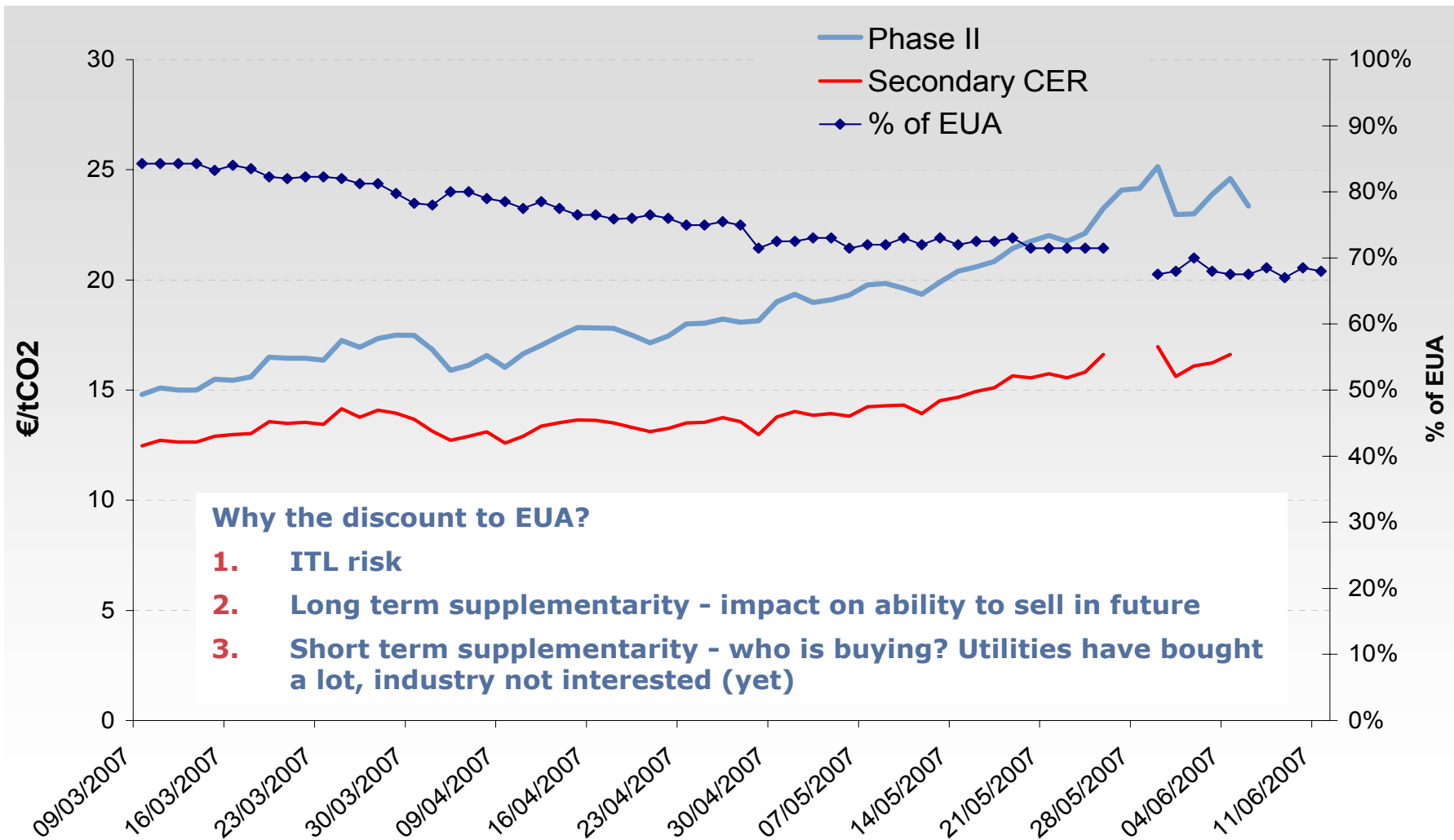
(assumes 35p/therm gas, \$60/t coal)

If replace 50% of coal capacity with CCGT (eg by 2015) could reduce emissions by 300Mt/yr (c. 15% of EU ETS emissions)

Phase III – Still large potential volume from CDM/JI after 2012 at < €20/t. Much more if include sectoral / programmatic CDM.



CER/ERU prices already reflect supplementarity risk.



Summary

- ✍ Use of low cost credits can help reduce prices within the EU ETS
- ✍ Supplimentarity is necessary to maintain sufficiently high EU prices to give strong investment signal to firms within the EU
- ✍ But...
 - Use of supplimentarity limits can lead to increased price volatility – difficult to manage limit level
 - Gives large gains to importers of CERs
 - Need to maintain credibility of imported credits

Guy Turner
Director, New Carbon Finance
+44(0)207 467 2660
www.newcarbonfinance.com
www.newenergyfinance.com

Phase II – If limit is reached market likely to go through a downturn before increasing again. Due to (i) sufficient global CDM/JI supply (ii) short term nature of market pricing

