Options and requirements of auctioning allowances in the EU ETS

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Auctions – new market dynamics

”Implementation of auctioning”

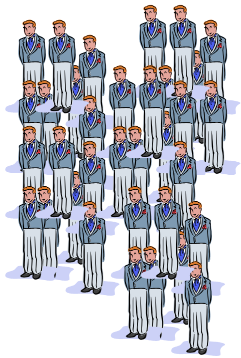
Prime objective: Ensure a functional and efficient market

Prerequisites:

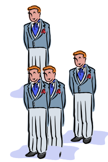
- reliable price signal for least cost ”abatement” options
- liquidity – create smooth interaction with secondary market
- transparency - symmetric information – level playing field
- available market places
- low transaction cost
- avoid market power

Auctions – new market dynamics

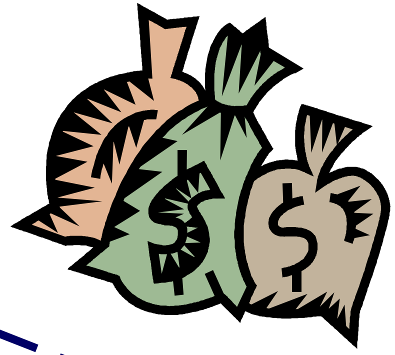
95% Grandfathering → 100% Auctioning



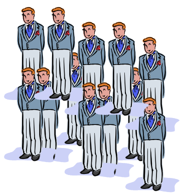
Net sellers

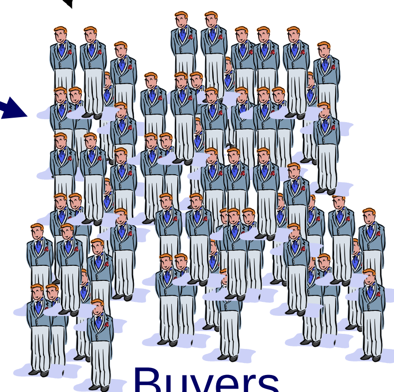


Sellers



Net buyers





Buyers

Observations

- many sellers/few buyers turned into few sellers/many buyers
- low to high volume – must buy to comply
- ”inactives” forced to come to market
- governments enter as direct market participants

Auctions – new market dynamics

1. Short term challenge – Phase 2 – 2008-12 (low auction %)

- Small volume to be auctioned
- Experience: Pricing largely governed by behaviour/perceptions
- Uncertainty re arrival of CERs & NER to market – short term supply squeeze?
- Auctions may impact market balance
- Timing and volume of auctions may prove important in price formation

Auction mechanics

Volume can easily be absorbed through existing exchanges e.g. with trustees for maximum return

Auctions – new market dynamics

2. Long term challenge – post 2012 (high auction %)

Important considerations:

- Auction frequency & timing - Liquidity build up! (temporary market squeezes ?)
- Behaviour of buyers – match emissions or accept carbon exposure?
- Behaviour of sellers - governments (”for profits” or ”programmed” auctions)
- Efficiency of multiple market places/multiple auctions – transaction cost
- Access to auctions – barriers to entry – asymmetry large/small buyers?
- Market power (Sellers, large Buyers?)

Conclusions

Clear objectives behind EU/MSs auction strategy (address issues of market power, price regulation etc)

Understand market behaviour and timing considerations

Use carbon exchanges/energy trading platforms for auctioning (routines, software, clearing routines etc at hand)

Limit number of ”auction houses” and frequency of auctions

Uniform price auction – simple and most common approach

Low barriers to participation – transaction cost

Contact

Thank you for your attention!

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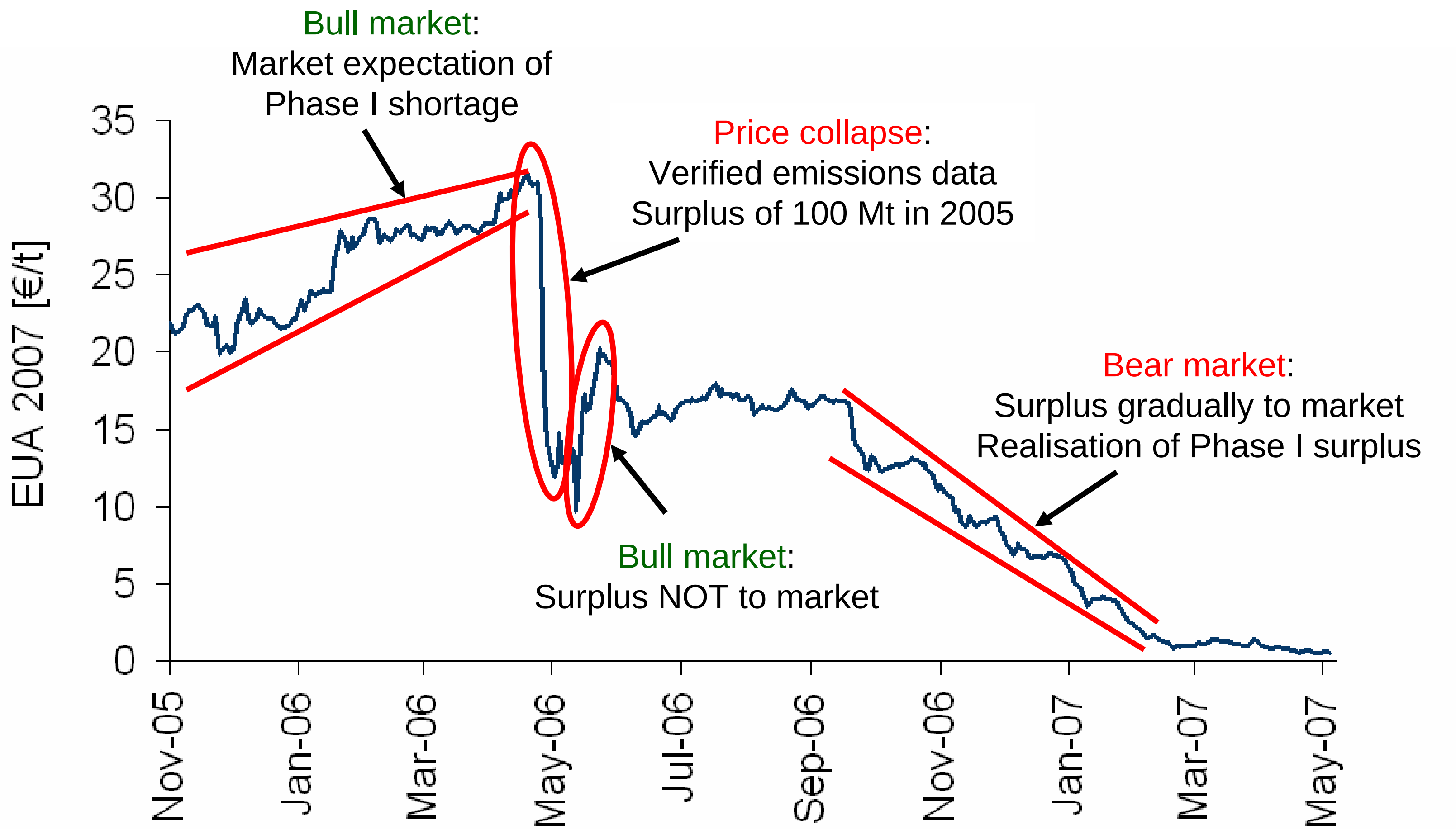
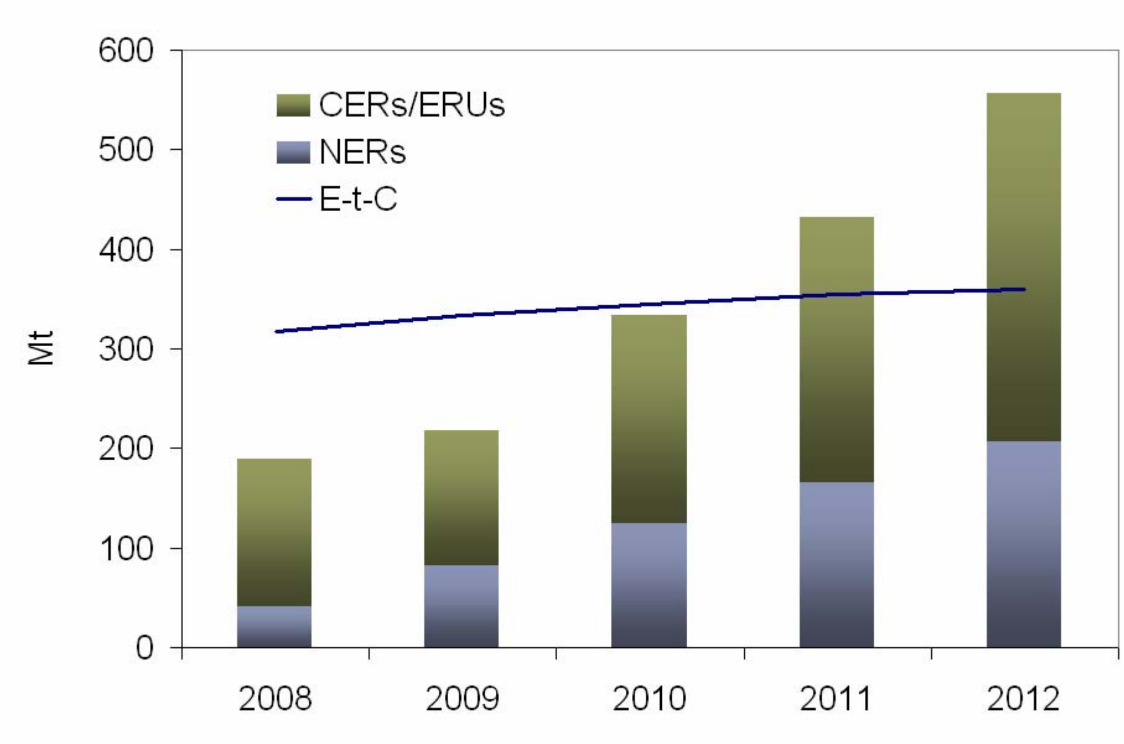
Why is market behaviour important?



Source: Point Carbon

Why is the timing of auctions important?



- Phase II supply and demand looks balanced overall
- But, annual shortage until 2011
- Timing of credits/NERs to market is critical!
- Late auctioning may exacerbate demand squeeze

How much to be auctioned?

- Direct auctioning according to NAPs (Mt/year)
  - UK 17.0 Mt (7.0%)
  - ITA 12.0 Mt (5.7%)
  - NLD 3.9 Mt (4.3%)
  - POL 2.6 Mt (0.9%)
  - HUN 1.3 Mt (4.2%)
  - LTU 0.5 Mt (2.9%)
  - AUT 0.4 Mt (1.2%)
  - ...
  - Total 38.4 Mt (1.9%)

- Germany contemplates 5-7% (25-35 Mt)

- Auctioning of surplus NERs (and other reserves)?
  - Most Member States plan to auction surplus NERs
  - Estimated Phase I surplus of 60%