EUETS:
Short-term fixes, long-term solutions

Grzegorz Peszko
Lead Energy/Environmental Economist,
European Bank for Reconstruction and Development

CEPS, Second Meeting of the CCMF Task Force on “EU Emissions Trading”
Warszawa, Monday, 23 July 2012
Historical emissions and growth in EBRD countries: Decoupling

Index (1990=100)

GDP (PPP)

CO2 emissions (energy related)

UNFCCC adopted
KP adopted
US pull-out
KP effective

0 10 20 30 40 50 60 70 80 90 100 110 120 130 140
Trend in energy intensity in Poland

Decomposition Poland

Energy Intensity of VA

KP adopted
US pull-out
KP effective

European Bank
for Reconstruction and Development
...driven both by more efficient processes and structural changes.

Decomposition Poland

Structural Change
Efficiency
Energy Intensity of VA

- KP adopted
- US pull-out
- KP effective

Years: 1995 to 2009
High gross costs of mitigation depend on access to intl emissions trading.

All scenarios based on a global stabilisation at 500ppm. Diamonds refer to emissions reduction targets of 30, 40, 50 or 80 per cent for the energy exporters in the EBRD region. Delayed CCS refers to a 15 years. Limited carbon trade requires that all regions achieve at least 80 per cent mitigation domestically.
The up-side of mitigation

- **Benefits**: Avoided cost of climate change impact and adaptation
- **Faster growth**: economies that are not resource-based tend to grow faster
- **Competitiveness**: retaining economic competitiveness in a low-carbon world requires decarbonisation (comparable efforts required in all major countries)
- **Faster technological progress**: participation in global mitigation efforts is likely to accelerate technological spillovers

![Average real growth rate 1981-2000](chart.png)
Phase III will be long

Source: IETA based on Barclays, Deutsche Bank, Point Carbon.
Reasons for oversupply in EUETS

- Economic slow-down and financial crisis
- Overlapping policies (RES, EE)
- Overhang of free allocations in phase 2
- Import of project-based credits (CERs and ERUs)
- NER 300
Has market worked correctly?

- Fundamentals are right!
- EUETS responded efficiently to changed market conditions
- Allowance price will (and should) follow economic cycles
- Emissions within the cap at the least cost
- Were phase 2 caps too generous? (large volumes accumulated by some companies, inefficient outcomes, windfall profits)
• Low carbon prices = more cash but low returns, less willingness to innovate, invest and improve efficiency
• Price outlook more important than spot price of the day
• Too many uncertainties created by policy makers (including Poland - e.g. derogations, 2050 roadmap)
• Difficult to treat EUA related revenues as security in project finance (value and risks)
• EC accelerates the EUETS review to reduce risks
Ad hoc interventions increase investment risk

- Set-aside looks like the short-term necessary fix
- Back-loading (delaying auctions) can help short-term prices and finance, but less impact on investment decisions and long-term price visibility
- Back-loading may undermine principle of predictability of auctions as required by the ETS Directive
- Adjusting the phase III cap would require amendment of the Directive
- Cancellation of allowances not allowed under the Directive (allowances can be allocated free of charge or auctioned)
- **Overall: Set-aside would increase political risk without increasing long term visibility of prices**
Sustainable, market friendly solution needed

Increase long term visibility of phase 4 and beyond by:

- Consensus on the 2050 Road Map with visible cap trajectory and interim targets for 2020-2050 (can be quick)
- Stringent caps for EUETS phase 4 (also crisis-adjusted baseline + recalibration of ETS linked to effectiveness of RES and EE policies)
- Banking to future phases

Expected demand from phase 4 should suck-up phase 3 surplus and should influence long-term investment decisions. But it will not solve short term liquidity.
Mixed blessing of high carbon prices to Poland

Benefits

• More attractive investments in CCS, nuclear, shale gas, renewables
• Accelerated efficiency and innovation
• Development of new competitive high value added industries
• More revenues from 300NER for CCS and innovative RES
• Higher value of allowances transferred to lower income/most reducing member states

Concerns

• Cash out-flow from auctioned sectors (mitigated by state aid)
• Loss of comparative advantage in energy intensive industries
• Increased dependence on imported fuels
Acknowledging and addressing concerns

- **International competitiveness and emission leakage – mitigants (in addition to 10a):**
  - More effective EU in UNFCCC negotiations
  - Bilateral agreements, linking ETS
  - Energy markets (gas and electricity)
  - Appropriate proposals Art 10b.1
    - Art 10b.1(b) Inclusion of importers of products
    - Art 10b.1(c) energy security and import of electricity

- **Competitiveness within the Union - mitigants:**
  - Transfer of allowances (Art 10.2)
  - State aid,
  - Domestic offsets (Art 24a), AAU revenues for non-ETS installations
  - Tailored approach depending on carbon dependence? Will it encourage emission reduction and structural changes?
Civilizational choices:

What vision of Poland in 2050?
What role of market instruments?