EU ETS: delivered results and challenges to face

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Enel Group overview
2011

- 40 Countries in 4 continents
- 97 GW of installed capacity
- 61 million customers
- 2nd European largest energy utility
- 4th compliance player in the EU ETS
- Leader in the international carbon market
Successes of the EU ETS

- **CO₂ has a price**
  - The EU ETS is working, delivering a price signal based on market fundamentals and expectations of future price
  - CO₂ price has become a key driver for long term investments and business decisions, engaging directly the private sector

- **Setting the example**
  - Pioneered carbon emissions trading schemes around the world

- **Foundation for an international carbon market**
  - Instrumental to the development of Kyoto mechanisms, providing support to sustainable development in developing and emerging countries while increasing cost efficiency and market liquidity

- **Cost effective**
  - The scheme is allowing to achieve the cap at the lowest cost
“Emission Trading” a world overview

- At time about 20 Countries around the world are considering the option to adopt a “cap and trade” scheme to reduce carbon emissions (following the example of EU ETS)
- The widespread of Emission Trading systems creates opportunities for “linking” different regional schemes all over the world (following the principle “a ton is a ton”) with vantages in terms of cost efficient abatements and market liquidity
A critical context
CO₂ price forecast to 2020

- Current low prices are undermining ETS’s credibility as the driver of the transition to a low carbon economy

Expected carbon price trend for Phase 3 of EU ETS

- In case of “no intervention” prices are expected to remain low until 2020
- Forecasts are widely subject to regulatory decisions: according to analysts the average price for Phase 3 can vary between 10 and 20 €/tCO₂

Source: Point Carbon 2012
Lack of scarcity of emissions allowances

- With the carry-over of unused phase 2 allowances and international offsets, phase 3 of the EU ETS (2013-2020) is now expected to be largely oversupplied.
- Market is **not expected to self-adjust**: an annual average GDP growth of around 4.3% would be requested to restore balance.

EUA balance: market long up to 2020

Source: IETA based on Deutsche Bank, Barclays, Point Carbon, European Commission;
Challenges to face

• The EU ETS is not aligned to expectations
  - Current prices are well below expected levels, unable to stimulate low carbon investments
  - ETS objectives are not coherent with long term targets agreed at international level and recommended by 2050 Low Carbon Roadmap

• The economic recession exacerbated the existing weaknesses of the scheme
  - Lack of flexibility to adapt to short term contingencies. The rigidity of the scheme conflicts with a flexible market and unpredictable economic cycles
  - Lack of policy coherence with other instruments implemented at EU and national level

Possible risks
  - The adoption of more expensive alternative measures
  - Increasing marginalization of EU ETS
  - Insufficient support for low carbon investments
Open issues

✓ What is the right price? ...is there a right price?

✓ Shall the ETS truly be the cornerstone of EU climate policy? ...if so, how to ensure it?

✓ How to increase clarity on long term policy framework?
What investors need

Enabling the EU ETS to accommodate for swings in the economic cycles and delivering a clear CO₂ price signal

Intermediate CO₂ emission reduction target for 2030

Stable regulatory framework for the development of energy market

Policy actions

- Restoring the effectiveness of the EU ETS, introducing flexibility with predictable and transparent rules

- Improving clarity on post-2020 targets

- Investigating how to optimize policies for CO₂ reduction by coordinating systems for the development of renewables and energy efficiency with the ETS
“Doing nothing” is not an option

“Do nothing” solution could lead to the failure of ETS scheme, increasing the likelihood of alternative more expensive measures such as the strengthen of RES incentives or the introduction of a carbon tax

Expensive alternative measures

- Risk of more ambitious targets on complementary policies such as renewables incentives

Additional cost on electricity price of different measures of CO₂ emissions reduction (2012, €/MWh)

26
7,2
2,9

RES Incentives (1)
ETS (2)

(1) A3 component of electricity fee
(2) Expected impact on CO₂ price on electricity price (CO₂ specific emission factor of CCGT plant- 0,36 tCO₂/MWh)
(3) Average carbon price (Dec. 2011)

Back to taxation

- Introduction of a unilateral carbon tax based on the difference between expected price and market value of EUAs. The tax is estimated to be around £5/tCO₂ for 2013
- The carbon tax will be applied only to national utilities covered by ETS
- Dutch parliament voted for a tax on coal for electricity
- The coal tax is expected to be equal to €5 per tCO₂
- Norwegian government committed to almost double the carbon tax on the country’s offshore oil and gas sector because the ETS was not driving clean investment quickly enough.

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The impact of carbon price varies among sectors

Source: EEA, 2012
The EU ETS protects the competitiveness of EU industry

Free allocation - EU ETS Phase 3

Sectors “highly exposed to carbon leakage”

• 77% of EU industry will receive 100% of free permits until 2020 (based on pre-defined benchmarks) for an expected total allocation of 500 MtCO₂/yr*

Other industrial sectors

• 23% of EU industry will receive 80% of free permits in 2013 (based on product benchmarks). The percentage of free permits will decrease until 30% in 2020

Allowed measures to compensate the increase in the electricity prices

• Art. 10a(4) of EU ETS Directive allows Member States to adopt financial measures in the form of State aids to mitigate the increase of the electricity bill in sectors exposed to carbon leakage

• Such measures need to be coherent with EU provisions on State aids

• Such measures can be funded with revenues of EU ETS auctions

* REF data – Point Carbon, 2011
Enel view on how to restore the effectiveness of the EU ETS

- **Clear post-2020 targets** coherent with long term objectives, and intermediate milestones
- **Flexibility** to adapt to short term contingencies under clearly pre-defined rules

Quick fix

- As structural fixes will likely require 2-3 years to be implemented, a **quick intervention** is needed to **restore credibility**
- A measure of **set-aside**, or at least **the reschedule of auctions’ profile for phase 3** (“backloading”), should be implemented before the end of the year in order to provide an immediate signal to market participants

Policy coherence

- **Policy coherence among different policy instruments** implemented both at national and EU level in order to avoid policy fragmentation and overlapping effects with complementary policies
Thank you!

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