

# ANALYSIS: Europe's CO2 trading scheme faces crunch 48 hours

14 Dec 2011 14:05 CET Last updated: 14 Dec 2011 15:41 CET

Europe's carbon market will next week face a crunch 48 hours that will either heap more pressure on prices already stuck at record lows, or resurrect faith in what once was the bloc's main weapon to combat climate change.

A committee of 64 MEPs will on Tuesday morning vote on an energy efficiency directive that could include a measure to withdraw up to 1.4 billion EU Allowances from supply in the third phase of the bloc's carbon market, starting 2013.

Just a day later, the European Court of Justice is to give its final ruling on whether the European Commission was within its powers to include airlines in its Emissions Trading Scheme.

While the parliament's environment committee vote is just the first step in a six-month lawmaking process to resurrect prices languishing below 7 euros by creating scarcity of permits, it could send a political signal that the Commission has been waiting for.

"They (the EC) are waiting for sufficient political support before proposing these things. It is only the environment committee in the parliament, but it would be the very first step in that direction," said Isabelle Curien, an analyst with Deutsche Bank.

If the proposal clears next week's ballot it will need to pass votes in the industry committee on Jan. 24 and the full parliament in April or June after EU leaders have agreed to the measures in the European Council.

"I think, if positive, next week's vote will support prices, although I am not sure whether it should, given the lengthy process to get these things confirmed," said Stig Schjolset, a senior analyst with Thomson Reuters Point Carbon.

Curien agreed: "It could very well support prices, and at the moment prices could only be supported by political intervention."

## DANISH COUNCIL

Bas Eickhout, the Dutch green MEP that tabled the set-aside amendment, told Point Carbon News in an

interview last week that if the bill comes out of the industry committee it should pass parliament, but a lot will depend on talks with the Council, which will be chaired by Denmark from January.

“The Danes are for it, there is no doubt about that. But unless they think they have a reasonable chance of getting it through, I don’t think they will push it too hard,” said Schjølset.

In traditional horse-trading fashion, one possible deal would be to let Poland bank some of its government carbon permits into a second round of targets under the 1997 Kyoto Protocol in return for its consent to let the Commission withhold EU ETS permits, Schjølset.

Earlier this year, Poland, the current holder of the six-months rotating presidency, delayed discussions on the set aside until 2012, saying high carbon prices could cripple its economy.

But green groups claim politicians could have a direct impact on the market much earlier by giving traders faith that they will intervene.

Such a move could drive prices up and spur investment in clean technology.

Tomas Wyns, director at the Center for Clean Air Policy-Europe, said it was a political “embarrassment” that carbon prices are so low and urged European leaders to take action.

“European leaders need to come up with a declaration in the European Council to urgently intervene on the demand side to create more scarcity,” he said, adding that are five or six different ideas about how this could be done.

A political declaration, under the Danish presidency “would see an immediate effect on carbon prices.”

## GOD HELP US

While most analysts agree Tuesday’s vote could only have a neutral or positive impact on the market, the ECJ ruling in the court battle between U.S. airlines and the Commission could have the opposite effect.

Europe’s top court will deliver its verdict on Wednesday on whether the 27-nation bloc broke international law by forcing all airlines to comply with emission limits under its cap-and-trade scheme.

The decision will be announced at 1000 GMT and the market is expecting a ruling in favour of the Commission after the court’s advocate general said in an opinion that the EC’s directive was legal.

“I think that is the only way (the ECJ verdict) will impact prices is down,” said Curien.

“With regards to a positive ruling most of it should be factored in, but a negative ruling will be bearish for sure as you would take away the second biggest buyer of credits behind the power sector,” said Schjølset.

Airlines are expected to make a massive dent in supply of carbon permits for the third phase in 2013,

buying around 700 million permits from 2013 through 2020, according to Thomson Reuters Point Carbon data.

If airlines are excluded from the scheme the overall scarcity of permits would fall from more than 1 billion over the eight-year trading phase to 333 million.

“If that happens, God help us,” said one observer, who declined to be named.

The committee vote is on Dec. 20 and the court ruling on Dec 21.

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