EWEA position on solutions to a low CO_2 price
Delaying allowances auctions and ensuring removal of surplus

EWEA recommends immediate action to address the now proven oversupply of credits resulting from the crisis and depreciating the price of carbon as well as lower emission projections to 2020. Delaying auctions is a welcomed first step, but we consider that at least 2.6bn surplus credits must be permanently removed from the market in order to provide scarcity and visibility and avoid merely pushing back oversupply.

The economic crisis has severely undermined the ability of the ETS to reduce emissions and promote investments in renewable energies, including wind power. Figures released recently by the European Environment Agency[1] show that in the last four years heavy industry sectors in the ETS received 34% more free carbon allowances than their real emissions. This oversupply threatens the very idea of carbon pricing. The carbon price is currently around €7/tCO_2, too low to move investments away from fossil fuels, too low to reduce emissions, as recently confirmed by Commissioner Oettinger in a Reuters interview.

Raising the carbon price to continue creating EU growth and jobs

While renewable targets will continue to drive investments in the wide range of existing renewable energy technologies, a high carbon price is key for EU companies to move away from fossil fuels and continue on a renewable path. As overall EU employment fell by 9.6% from 2007-2010, wind energy jobs in Europe went up 30% to 238,000[2]. Over 50 new jobs were created in the sector daily. The sector's contribution to GDP went up by 33%, reaching €32.4 billion. Wind energy and other renewables represent already today more EU jobs than several other electricity sectors, and more than heavy industry under the ETS[3]. As such, a higher carbon price will benefit, and not harm, the overall EU economy.

Delayed auctioning as the only swift option to increase scarcity on the market

The best solution to raise the carbon price is a move to 30% GHG emissions reduction across the EU. However, alternative options can also increase scarcity. Increasing the 1.74% linear factor is compatible with reaching 80%-95% domestic reduction in 2050, but requires re-opening the ETS directive. The only swift option is to prevent too many auctioned allowances from reaching the marketby delaying auctions of EU Allowances (EUAs).
This implies an agreement by all Member States, or by a coalition of the willing, to withhold some allowances, to auction less than they would otherwise have. The modelling done by the EU Commission as part of the "Low carbon roadmap 2050" suggests that the price would increase enough to offset the loss in auctioning revenue resulting from selling less credits.

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[1] EEA ETS Data Viewer, update from May 2012
[2] EWEA report "Green Growth", April 2012
[3] According to their representative bodies, job figures for ETS sectors in 2010 are as follow: wind 238 000, solar PV 265 000, coal 330 000, gas 270 000, nuclear 500 000, steel 350 000, cement 48 000, refineries 100 000.

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Providing visibility on the market by ensuring total removal of withheld credits

Withholding EUAs to be auctioned is the first step to re-establishing scarcity on the carbon market. The second step is to give operators certainty about what will happen with the EUAs withheld. The impact of withholding EUAs will be greatly diminished should any uncertainty remain, as operators will speculate to get ulterior access to delayed EUAs.

EWEA favours an outright removal of these credits from the auctioning books. This will give the strongest signal and certainty to the market about quantities available and quickly restore the price. A second-best option could be considered, in the form of a conditional auction of these withheld allowances, in case the carbon price reaches a certain level of i.e. 50€/tCO_2. This would enable withholding an ambitious share of EUAs without risking a price spike in the future in case of better than expected economic recovery.

Lower demand projections and industry oversupply justify removing a minimum 2.6bn EUAs

Today's projections for emissions to 2020 are significantly lower than in 2008 scenarios. Carbon analysts estimate the existing supply of EUAs to be about sufficient to cover actual emissions to 2020, without resorting to overseas credits (CERs/ERUs) from CDM and JI projects[4].
While this means 1.7bn CERs/ERUs allowed into the System are not needed, an outright ban of CDM credits is not necessarily desirable or possible. Hence, EWEA calls for the withholding and subsequent removal of the same quantity of EUAs from auctioning books. This will not establish scarcity, but merely remove forecasted surplus supply.

Additionally, the EUA supply/demand balance hides both a shortfall and an oversupply: from 2008-2012, heavy industry sectors in the ETS will have received for free ca. 900M more EUAs than needed to cover their real emissions - a consequence of the economic downturn rather than company investments. This oversupply consistently reduced the carbon price, hampering investments in emissions reductions technologies and allowing for more emissions in the power sector. This must be corrected to reward investments already made (lower CO_2 price means lower return and longer payback), address what is in essence a public subsidy[5] and re-establish some scarcity on the market.

➔ Addressing both weaker demand and heavy industry oversupply means withholding at least 2.6bn EUAs from auctioning, or a 325M yearly average.

Exceptional circumstances warrant exceptional intervention on the market.

Some actors have criticised delayed auctions as intervention on the market. But exceptional events call for exceptional measures and the current economic crisis, the toughest since the 1920s, certainly is an exceptional event.
When the climate package was agreed in 2009, investors were expecting a carbon price above 20€/tCO_2. As such, one can consider that the crisis itself, and not a potential intervention on the market, increased uncertainty by lowering these price expectations. Intervention is hence required to re-establish a path in line with investors' initial price previsions. Early movers in industry and power sector will be hence rewarded.
Finally, the ETS is a regulatory market, delimited by regulatory boundaries (others directives, the cap itself, etc…). It serves a purpose, reducing emissions through a market signal, and must be re-tailored if it doesn't achieve its objective as planned.

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[4] For 2008-2020, Point Carbon foresees 1.7bn market surplus and Deutsche Bank foresees 2.2bn lower demand
[5] The power sector can pass 100% of the carbon price to consumers in the electricity price, so that consumers have paid for EUAs bought by the power sector from heavy industry, creating a hidden subsidy.