

# Global Environmental Markets

January 2009



## TFS Green London

Tel: +44 207 198 1600

## TFS Green New York

Tel: +1 212 943 2883

## TFS Green Beijing

Tel: +86 10 8800 3721

## TFS Green Melbourne

Tel: +61 3 9614 2700

[www.tfsgreen.com](http://www.tfsgreen.com)

## Announcement



### TFS Green would like to wish our readers a very Prosperous Chinese New Year

**DISCLAIMER:** This document is made available for general information purposes only and does not constitute investment advice or an offer, or solicitation of an offer, to buy or sell any securities, commodities, derivatives or any other financial product.

While every effort has been made to verify the accuracy of the information appearing in this document, no representation or warranty is made as to its validity, timeliness, completeness, accuracy or reliability and it should not be relied upon as such. All information is subject to change without notice at any time and markets can be subject to rapid, unexpected movements. All information contained in this document is indicative only and may not be suitable for valuing positions.

No liability whatsoever will be accepted for any direct, indirect or consequential loss arising from any use of the information contained in this document or any omission from this document.

This document is directed at Market Counterparties and Intermediate Customers as defined by the FSA. This document is not for distribution to nor should it be relied upon by Private Customers as defined by the FSA. This document is not intended for distribution to, or use by any person or entity in any jurisdiction or country where such distribution or use would be contrary to any applicable law or regulation.

Tradition Financial Services Ltd is authorised and regulated by the Financial Services Authority.

NOT ALL ENVIRONMENTAL BROKERS ARE THE SAME

 **TFS Green**  
Part of Tradition

### Primary Market

The Chinese floor price for CERs has been closely followed by market participants since the onset of the financial crisis, especially as the secondary CER price has dropped significantly. There had been suggestions that the Chinese government was to lower the floor price. However, a letter was released by the NDRC which indicated that the floor price will not follow the trends on the secondary market.

Towards the end of 2008, there were several tenders held by Chinese state-owned enterprises. These tenders yielded a wide range of CER prices from €8.75 to €12.20.

Despite market conditions at the end of last year, many Chinese project developers remain overly optimistic in regards to CER prices. This was particularly the case with wind project developers who continually press for prices above €13. With secondary prices coming down below that level, developers have had to adjust their expectations significantly.

### Secondary Market

Near-end secondary CER prices remained stable as buying interest escalated on anticipated supply concerns based on the the suspension of Det Norske Veritas as a DOE. This resulted in a tighter CER/EUA spread for Dec08. Latter year CERs remain marginally in contango.

The Dec08 cleared CER contract opened at €14.15 as of 1<sup>st</sup> December and weakened to a closing level of €13.40 as of 15<sup>th</sup> December. The intra-month low was marked on 9<sup>th</sup> December at €12.95 while the intra-month high was marked on 13<sup>th</sup> December at €15.80. The Dec08/12 strip ranged from €2.55 to €4.30 and the CER/EUA spread for Dec08 widened from €1.20 to €2.30.

### Voluntary Markets

As a result of the Christmas and New Year's holidays, December is often reduced to two or three weeks of trading with limited activity in most markets and the VER markets would typically be no different.

However, with prices for renewable energy VCUs between €4.25 and €4.75, buyers took the opportunity to enter the market and procure reasonably priced units. As a result, there was a great deal of activity in December. This was welcome news after limited trading at the beginning of the final quarter of 2008 as the economic slowdown weighed heavily on the market.

Notwithstanding this point, for pre-CDM registration VERs, buyers have reduced their appetite for registration and verification risk. As a result, spot VER trades have become the most common type of transaction. This is because buyers became unwilling to put the delivery date and volumes of their VER transactions at the mercy of the Executive Board and DOEs.

This is a complete change in approach for many buyers who, at the right price, were happy to buy forward VERs prior to verification. The reasoning was that by taking these risks they would be procuring the most recent vintages available.

It is expected that this reduction in risk appetite will continue for the coming months. This means that those VER sellers who are able to pay the costs of verification and sell their units on a spot basis will be at an advantage. Further, prices for renewable energy VCUs are expected to remain in the €4.25 to €4.75 range with energy efficiency VCUs priced between €2.75 and €3.50.

# European Markets

## EU Emissions Trading Scheme

In December 2008, the EU ETS market maintained a general bearish sentiment as recession concerns reduced demand and EUA prices declined with other commodities, particularly oil

The value of carbon continued to fall largely due to heavy forward selling of EUAs in anticipation of further reduced industrial output. Concerns in relation to escalating credit issues and the subsequent impact on OTC transactions led to an increase in broker-cleared transactions. Volumes for December totalled in excess of 215 million allowances.

The benchmark Dec08 contract opened at €15.50 on 1<sup>st</sup> December with a cleared contract expiring on 15<sup>th</sup> December at €15.30 and with intra-month low registered on 9<sup>th</sup> December at €14.20

Phase 2 EUA spreads ranged from €0.65 to €0.55 during December. The Dec 08/12 spread remained stable trading in a €0.30 range from €2.55 to €2.85 which reflects the cost of carry.

## EU Emissions Trading Scheme (continued)

The EUA strip strengthened marginally during the month ranging between a low of €14.75 on 5<sup>th</sup> December to an intra-month high of €16.95 on the 22<sup>nd</sup> December.

## Emissions Options

EUA option volumes rose in early December as the EUA Dec08 contract expired. Over 21 million tonnes traded in total, of which the Dec08, Dec09 and Dec10 constituted 15%, 75% and 10% of the volume, respectively.

Dec09 puts are still the main focus of attention with 10 million tonnes traded and 6 million calls. ATM volatility slipped in Dec09 from 54% fair value at the end of November, to 52% for the Straddle.

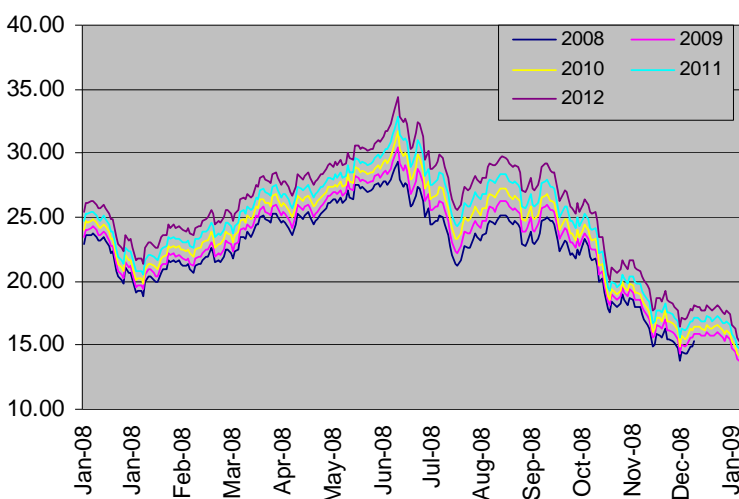


Figure 1: 2008 EUA performances

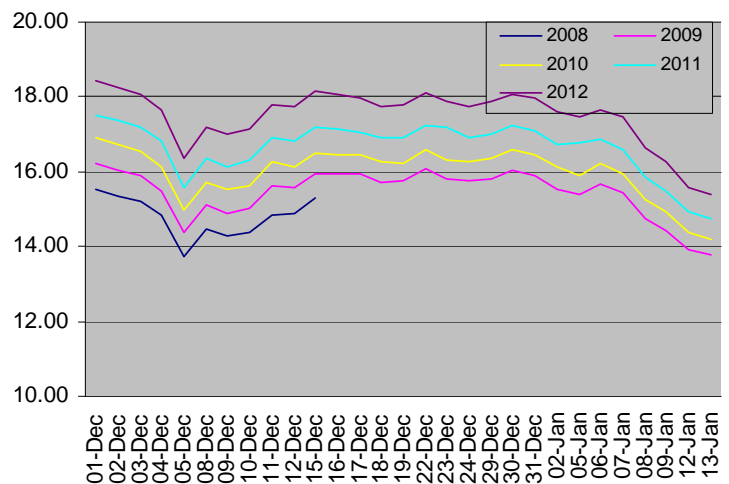


Figure 2: EUA performance since October

## US Markets

---

### SO<sub>2</sub>

SO<sub>2</sub> rocketed upward on the news that the District Court reinstated CAIR, immediately trading up to the \$240 level. The December 2008 contract retreated to \$215 by year end. There continues to be sporadic interest in forward streams throughout the curve from Vintage 2010 to 2038. The January SO<sub>2</sub> contract last traded \$187.50, with a current bid/ask of \$185 - 195.

### NO<sub>x</sub>

Interest in CAIR Annual has increased dramatically now that the CAIR will be in place. Vintage 2009 rallied from approximately \$1,500 to a high of \$6,250 on the court ruling. Annual has decreased to \$4,000 over the first week of 2009 trading as sellers who were previously on the sidelines during the regulatory uncertainty have rushed in to take advantage of the prices. The market is still thin on counterparties with many natural players still sitting inactive and waiting for the market to reach a stable level. V10 Annuals have traded at \$2,250 and remain in the \$2,100 - \$2,400 level.

CAIR Ozone NO<sub>x</sub> has been slower to react. That market was due to be in effect as a continuation of the SIP Call program if CAIR was not in place. Since there was decent liquidity leading up to the court ruling on 23 December we did not see the same price spikes as was witnessed in the Annual program. Prices did tick up slightly from \$550 to approximately \$650.

### CAIR

On 23<sup>rd</sup> December the US Court of Appeals reversed its previous ruling from July 11 that vacated the CAIR Rule. They have remanded the rule back to the EPA for revision but declared CAIR will be in effect while the EPA revises it to address the concerns of the court and the plaintiffs.

### Federal Developments

With President-elect Barack Obama continuing to tout his plan of a green investments initiative to create three million jobs over the next two years, there are whispers in the Senate that Joe Lieberman (I., Ct.) plans to introduce a new climate bill in 2009. In 2008, the Senator's co-authored Lieberman-Warner Security Act failed to garner enough support to resist a filibuster, owing much of its defeat to interests in the coal-heavy Midwest. Senator Barbara Boxer (D., Cal.), chair of the Senate Environment and Public

Works Committee has also expressed plans to introduce a bill early this year. Few other details of the Lieberman bill are available at this time.

### The Regional Greenhouse Gas Initiative (RGGI)

On 17 December, RGGI Inc. held its second quarterly auction, the turnout of which auditor Potomac Economics described as "robust". Sixty nine entities submitted bids for 31.5 million allowances ranging from the reserve price of \$1.86 up to \$7.20. The \$3.38 clearing price, within close range of the OTC price at the time, raised \$106.5 million for use by the 10 RGGI states. Since that point, contracts for the 2009 vintage allowances have traded up 23% to \$4.15 on 12<sup>th</sup> January 2008.

The OTC RGGI market is currently seeing an average of 500,000 allowances traded per day. The option market is also seeing high volume, with implied volatilities currently in the 60% to 80% range. Most OTC transactions are submitted for block clearing on either the Green Exchange or CCFE.

At publication, the Dec09 Future was trading at \$3.90.

## US Markets (continued)

---

### California and AB23

On 11 December, as a requirement of AB32, the Global Warming Solutions Act of 2006, the California Air Resources Board (CARB) approved California's scoping plan to reduce greenhouse gas emissions in California to 1990 level by 2020. CARB Chairman Mary Nichols proclaims that the step "will guide capital investments into energy efficiency to save us money, into renewable energy to break our dependence on oil and promote a new generation of green jobs for hundreds of thousands of Californians." The blueprint will also set up a cap-and-trade mechanism covering 85% of the state's emissions and encompassing 21% of the state's planned reductions. All California businesses subject to reporting in 2009 have been notified. The plan in its entirety can be viewed at [www.arb.ca.gov/cc/scopingplan/document/scopingplandocument.htm](http://www.arb.ca.gov/cc/scopingplan/document/scopingplandocument.htm)

### California Climate Action Registry (CCAR)

In the coming year, CCAR plans to explore protocol developments in the following sectors: Bus Rapid Transit, N<sub>2</sub>O Reduction at Acid Plants, Tidal Wetland Restoration, Blended Cement, Truck Stop Electrification, Boiler Efficiency and Bus Fleet Upgrades.

Additionally, public comments for the updated Forest Project Reporting Protocol are due by 19<sup>th</sup> February 2009.