

Ariadne @ Brussels 9 December 2024

A NEED TO MEND THE BEND? INDUSTRY DECARBONIZATION AND MARKET STABILITY IN THE YEARS AHEAD

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GEFÖRDERT VOM

Time	Activity (both sessions under <u>Chatham House rules</u>)
11:00 – 13:00	<p>Session I: Prices and industry demand for allowances through 2030</p> <ul style="list-style-type: none"> • Welcome and setting the scene, M. Pahle (10 min) • Overview of price scenarios/forecasts, S. Osorio (5 min) => elaborations by teams (3 min each) • Overview of developments of industry EUA demand, S. Osorio (5 min) => reactions and comments by teams (3 min each) • Open discussion with following guiding questions: <ul style="list-style-type: none"> • Will a price bend come, and if so: when and how strong will it be? • What would happen if industrial production would decline further?
13:00 – 14:00	<p>Light lunch</p>
14:00 – 15:30	<p>Session II: Potential implications for ETS design, with a view to long term needs</p> <ul style="list-style-type: none"> • Connecting short term prices and the long term needs: the role of flexibility and stability, M. Pahle (5 min) • Inputs by H. Fjellheim, J. Delbeke and O. Edenhofer (5-10 min each) • Open discussion with following guiding questions: <ul style="list-style-type: none"> • Do we need more <u>flexibility</u> in the ETS, and what are suitable options? • Are the <u>stability</u> rules in place generally fit for purpose, or is it necessary to more radically rethink them and potentially also ETS governance more broadly?

ETS IN LIMBO, BETWEEN SERIOUS MYOPIA AND PANICKING ABOUT “ENDGAME”?



The image shows a screenshot of a Financial Times article. At the top, there is a navigation bar with a hamburger menu icon, the text "FINANCIAL TIMES", and the "myFT" logo. Below this, the article is categorized as "Opinion Lex" with a button that says "+ Add to myFT". The main headline reads "Europe's carbon price crash looks like serious market myopia". A sub-headline below it states "The emissions trading system is too clunky to deliver the required impetus to decarbonisation".

Short term fundamentals (gas price, industry production, additional REPowerEU supply) all bearish though

CFEL24: No need to panic about end of EU ETS allowances in 2039, says Commission

Published 18:59 on October 9, 2024 / Last updated at 18:59 on October 9, 2024 / Rebecca Gualandi / Aviation/CORSIA, EMEA, EU ETS

A European Commission official said there is “no need to panic” about running out of EU ETS allowances in 2039, due to the expansion of the system’s scope to include additional sectors and auctioning of allowances for aviation.

Damien Meadows, carbon markets and clean mobility adviser at the European Commission’s directorate general for climate action, said the EU ETS cap on emission allowances will rise in 2026 and 2027 because of shipping, and other sectors such as waste and incineration, may be added to the scheme.

With the revision of the ETS directive in 2023, the rate at which the emissions cap is reduced has been increased by 4.3% per year over the period 2024-27 and to 4.4% per year from 2028, which implies the original cap will reach zero by 2039.

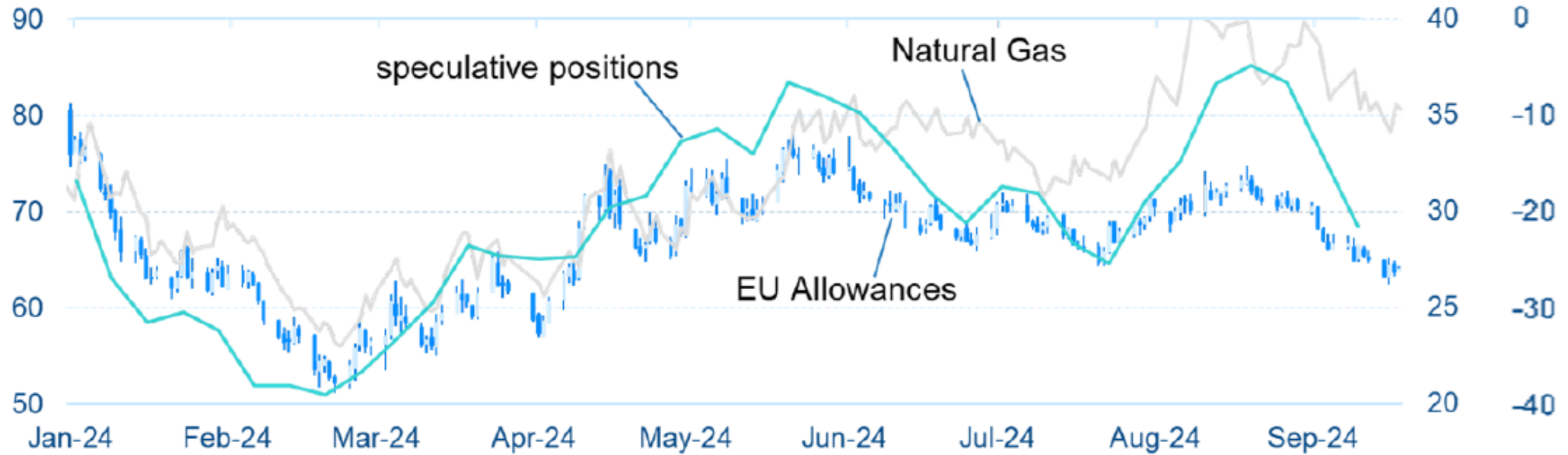
But “we don’t need to panic” when 2039 comes around, Meadows told the Carbon Forward Expo 2024 in London on Wednesday, because allowances for the aviation sector will be auctioned until 2044.

Source: [Carbon Pulse](#)

MARKET IN "PRICE DISCOVERY MODE": TO BUY AND HOLD, OR NOT?

Figure 1

After a drop in 1Q, EU Allowances are in price discovery mode, mirroring energy prices and investor short positioning

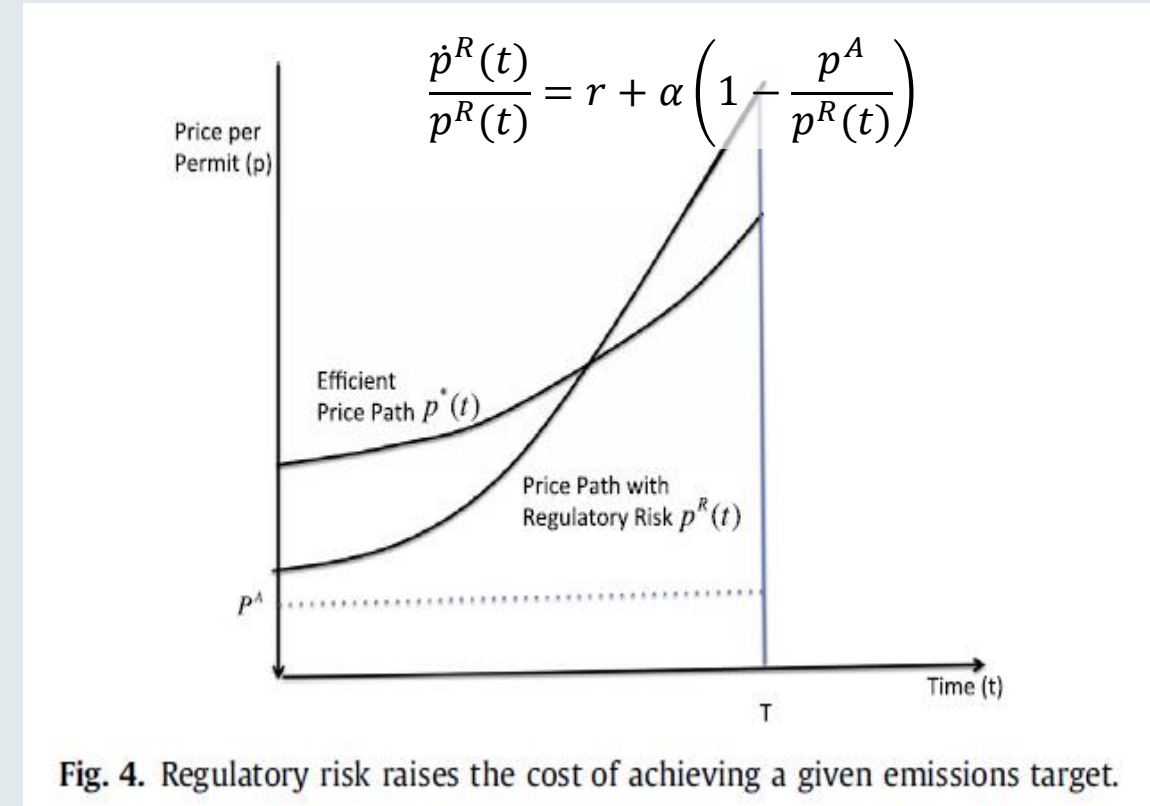


Source: Bloomberg, own illustration; EU Allowances as Dec 2024 EUA in EUR per tonne (left scale), Natural Gas as next TTF Future in EUR per MWh (right axis, first column), speculative positions as net positions by investment funds in ICE Index in million tonnes (right axis, second column)

Source: BBVA (2024)

DOES PRICE DISCOVERY BREAKS DOWN TO DISCOVERING CREDIBILITY OF CAP?

- Question if **ambitious timeline** to tighten cap will be politically sustainable is becoming more and more pertinent
 - If(!) commitment to long term cap is **not deemed credible**, theory suggests this **should depress short term prices**
- 1) Do currently relatively low prices reflect low credibility?
- 2) Credibility hinges on prices & state of industry that can be expected for coming years...



Source: Salant (2016)