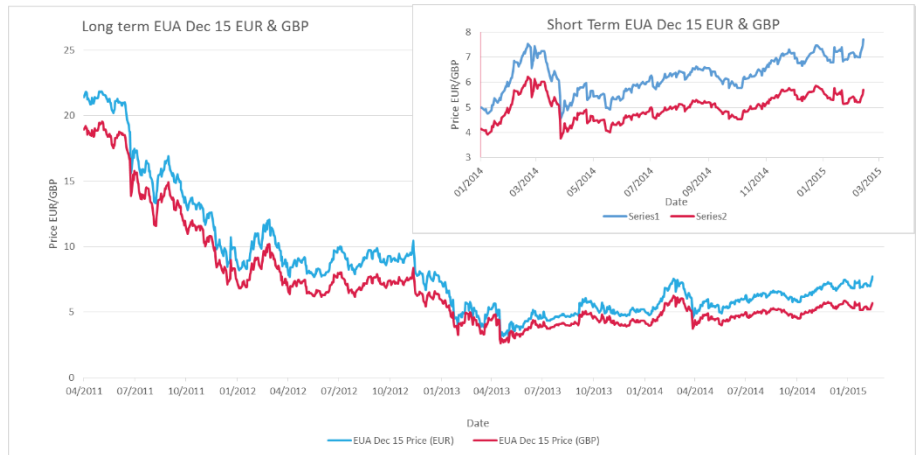


WEEKLY CARBON TRADING MARKET UPDATE – 16TH FEBRUARY, 2015

Market Development

- Near 10% jump in carbon prices last week.
- Prices rise on Tuesday afternoon as EPP said to have agreed 2019 start as a compromise.
- Gas & power climb adding to upward pressure on carbon as clean dark spreads strengthen.
- Ivo Belet, who is steering the MSR process, advocates 2018 start and backloaded allowances AND all other unallocated volume (from NER and derogated volumes) into the reserve.
- Friday's push through technical resistance level of €7.50 sees a close at €7.71, crucially above last year's high of €7.66.



Auction Overview

- Full week of auctions, 15.075 mt will be sold

Price Action

What a difference a week makes. Last Monday we saw little positive news for carbon save for the chance of news from Brussels and a change in fuel prices. Cue carbon prices jumping 9.83% (69c) amid 'perfect storm' conditions. 2 unexpected factors came together to influence the carbon price and push it up to its highest close for more than 2 years at €7.71. Prices started the week where they left off the previous week, languishing around the €7.00 mark with price falls looking more likely than rises as German power started the week down, clean dark spreads hovered at recent lows and with coal prices in the ascendancy. Gas outages in the Netherlands, cutting production capacity by up to 50%, were revealed Monday evening which helped push the gas price up over 6% early on in the week to leave power produced from coal looking relatively more profitable when adjusted for carbon. Tuesday saw reports circulated on an agreed stance from the EPP on the MSR amendment proposal (we reported this in last Monday's weekly). It wasn't especially bullish news so carbon price rises that day were most likely driven by the fuels. The rise probably smoked out a few carbon shorts to help things on their way. Power prices eventually climbed (more than coal) posting a 3.37% week-on-

Weekly Price Changes (EUR)				
Product	06/02/2015	13/02/2015	Change	% Change
EUA Dec 15	7.02	7.71	0.69	9.83%
DE Power Cal 16	32.6	33.7	1.10	3.37%
API2 Cal 16	55.24	56.01	0.77	1.40%

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Friday's EUA Implied Funding Rate			
	Price	Annual Rate	Total Return
Spot	7.63	0.00%	0.00%
Dec-15	7.71	1.05%	1.05%
Dec-16	7.84	1.69%	2.75%
Dec-17	7.99	1.91%	4.72%
Dec-18	8.16	2.13%	6.95%
Dec-19	8.39	2.82%	9.96%

Annual Rate is calculated by dividing the relevant forward price by the relevant prompt price. The Total Return is calculated by dividing the relevant forward price by the spot price. Note: these rates do not include transaction costs.

week gain which strengthened the clean dark spread and provided more bid side support for the carbon market (gains in gas and stronger clean dark spreads create demand for carbon as utilities sell power and buy back the resulting carbon exposure). On Thursday, with carbon having retraced most of the previous day's gains, Ivo Belet's surprise MSR proposal (more on this below) broke cover sending prices right up to €7.52 where it was capped, as it has been 4 times before in the last 12 months. On Friday a nudge by buyers through €7.50 saw a scramble for more volume as carbon market participants took advantage of new price territory. Friday saw an intraday high of €7.73 and the week closed at €7.71. *Price Impact: The close above €7.66 confirmed the case for the bulls, it is the highest for more than 2 years and will likely entice additional speculative buying interest from outside the normal market. With a combination of positive sentiment and strong fuel prices creating large upward momentum in carbon, it is possible we see further gains. The €8.10 technical level is achievable to the upside. Volatility will likely remain high as we*

approach the 24th February vote. All things being equal, to the downside €7.50 should now provide solid support. We are in new price territory.

Market Stability Reserve (MSR)

As we reported on Thursday, lead MSR lawmaker, Ivo Belet, released a compromise MSR proposal that will go before the Environment Committee for a vote on 24th February that has tacit support from the EPP. The proposal put forward is for a 2018 start to the MSR with all the backloaded allowances going straight into the reserve. Under the proposal the backloaded allowances would be joined by any unused NER (New Entrant Reserve) allowances and other allowances not allocated due to installation closures and significant capacity reductions. The start date and the future of the backloaded allowances were always going to be the big negotiating points. Adding in un-allocated allowances is a new twist that is, bullish for price.

The start date was seen as a contentious issue with the original commission plan proposing a 2021 start which many said was too little, too late. The Green party had lead calls for an introduction in 2016/2017 with the EPP seemingly stuck on a 2021 start. The EPP is the largest party within the EU parliament and therefore holds a fair amount of power at the negotiating table. A 2018 start was seen at the bullish end of the likely compromises.

The future of the backloaded allowances was another of the major negotiation sticking points. The 900Mt of withheld allowances were due to be auctioned to the market in 2019 & 2020, swamping demand in the carbon market and pushing prices from a projected €15 in 2017 back down towards the €5 level by 2020. With these allowances now set to go straight into the reserve there will be support at the back end of the curve, where previously, there was none. Treating backloaded allowances in this way is no particular surprise, the MSR is supposed to be about Stability so reducing volatility at the end of Phase 3 is a key outcome of its implementation and makes planning for emissions cuts by market participants easier.

So what has the EPP gained out of this compromise? Belet's proposal calls for the commission to review carbon leakage provisions. It is likely that the EPP have maintained a strong position on implementing the carbon leakage list which is designed to protect industry covered under the EU ETS who are deemed to be especially at risk of re-location to areas without similar pollution costs. These installations are protected by greater free allocations than they would otherwise have received to protect them from the costs of compliance within the emissions markets.

The remainder of the proposal largely followed the commission's original plan with the threshold levels remaining the same but the time lag for surplus calculations shortened to one year.

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The Environment committee will vote on the proposal on the 24th February and assuming a positive outcome the proposal will still need the backing of a majority in parliament as well as member states. *Price Impact: bullish in the short term as traders expect the proposal to pass through ENVI committee. Continued volatility, as the package makes its way (or otherwise) through the legislative process, is highly likely. If adopted as currently proposed then very bullish for the long term.*

Important MSR dates are:

- 24th February, 2015 – Environment Committee vote

The week ahead

With prices finishing at the week's high last week it is possible the bull run will continue into the early part of this week. A test to the upside at €8.10 is a distinct possibility. A close eye will need to be kept on power, coal and gas prices as they were the catalyst for the original upward momentum last week. As always, volatility can be expected around any MSR announcements.

Auction Timetable 09th February 2015 - 20th February 2015						
Date	Volume('000 tonnes)	Auction Platform	Allowance Type	Clearing Price (EUR)	Cover Ratio	Total Bid Quantity
09-Feb-15	2,918	EEX	EUA	6.86	5.87	17,126,000
10-Feb-15	2,918	EEX	EUA	6.88	6.79	19,805,500
11-Feb-15	1,494	EEX	EUA A	6.87	2.51	3,750,000
12-Feb-15	2,918	EEX	EUA	7.29	4.00	11,666,500
13-Feb-15	3,198	EEX	EUA	7.35	2.65	8,464,000
16-Feb-15	2,918	EEX	EUA			
17-Feb-15	2,918	EEX	EUA			
18-Feb-15	3,123	ICE	EUA			
19-Feb-15	2,918	EEX	EUA			
20-Feb-15	3,198	EEX	EUA			

Registry shortcuts

As the 30th April deadline for compliance and the 31st March deadline for CP1 CER use approaches, have you logged onto your registry account recently? Bookmark [this](#) page to easily check your account status.



Upcoming Conferences

- Platts Central and Eastern European Power Feb 17th-18th 2015 (Prague) – **REDSHAW ADVISORS SPEAKING**
- Europe: Argus Emissions Mar 4th-5th 2015 (Amsterdam) - **REDSHAW ADVISORS SPEAKING**
- Europe: IETA's Business Partnership for Market Readiness Workshop (London) - **REDSHAW ADVISORS SPEAKING**
- Europe: Carbon Expo May 27th-29th 2015 (Barcelona)

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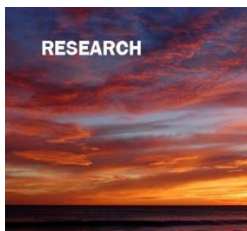
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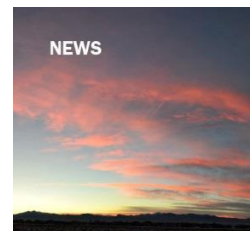
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EU-ETS Compliance: preparing for position management, allocation and completing verification

For those of you who have not read it yet, check out our report on EU ETS Compliance. Please find it briefly below and in full [here](#):

- 1. Preparing for position management** - Towards the end of February, after verification has been finalised, companies will come to market to balance their carbon books for 2014. Getting on top of this activity early is essential to avoid a rush as we get closer to 30th April and to make sure transfers of EU Allowances go smoothly.
- 2. Allocation** - Most companies will know exactly how much they can expect to be allocated already, this is prescribed to 2020. However some uncertainty exists for companies in Eastern Europe (those in the power sector entitled to 'derogated' volumes), for some new entrants and for companies with significant capacity increases or decreases. In addition, companies often don't know what their emissions will be in 2015. Regardless of what you know about your allocation or future emissions, the biggest exposure is not what overall carbon position you are likely to have but what happens to the price of carbon while your position evolves over the course of the year.
- 3. Verification** - The process by which companies achieve compliance with their EU-ETS obligations can be a long and complex one. New entrants in 2014 have a particularly steep learning curve and the first thing to get right is to appoint an *appropriately accredited* verifier. However all installations should take note of the things they themselves must do that may fall outside of their verifier's responsibilities.

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