

Carbon Market Australia-New Zealand

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NEWS

Energy companies gear up for allocation scrap

As international negotiators labour over a new global climate agreement in Germany, Australian energy companies are preparing to battle for more free permits under the country's proposed emissions trading scheme.

In the past two weeks, major energy firms such as Rio Tinto, Shell Australia, Woodside Energy and Caltex have all argued for more permits to be issued to their businesses, claiming are under threat from Asian competition.

In a submission to a senate committee, Rio Tinto reiterated claims made by the Australian Coal Association that the CPRS would lead to job losses, and estimated that it would cost the company alone A\$90 million in 2010/2011 and A\$430 million over the first 10 years.

"Being trade-exposed with major competitors not subject to a carbon price, our businesses will not be able either to pass through these higher costs to our customers or to absorb such and impost in today's difficult economic environment," said Stephen Creese, managing director of Rio Tinto Australia.

What the company wants is to maintain free allocation of permits until 80 per cent of all carbon emissions globally are covered by a comparable scheme.

As China accounts for more than 20 per cent of global CO₂ emissions, what Rio Tinto is implying is that China should regulate emissions before it should take a lower allocation.

Meanwhile, refiner Caltex has warned that a planned increase in refining capacity in the region, coupled with the economic slowdown, is already squeezing margins, something the bill would make worse.

Caltex wants to amend the bill so it will receive 100 per cent of its permit needs to protect its business from competition from refineries in Singapore and Korea.

"The need to purchase 40 per cent of permits would cost Caltex's two refineries about \$25 to \$40 million annually at the carbon prices in the White Paper," the submission said.

"Under the proposed CPRS legislation, the cost of these emissions will be borne by Caltex," it said.

Shell Australia is also keen on making changes. Instead of phasing out free allocation of permits after 2020, Shell wants a guarantee that a phase-out will not occur until companies can pass costs on fully to the consumer.

At the same time the oil giant wants refineries to get 90 per cent of emissions permits for free, far higher than the 60 per cent it thinks it will receive.

Without the additional free permits Shell said local production would be replaced by imported refined products. It claimed this would reduce economic activity and costs jobs in Australia while having no net impact on global emissions.

But it is not just energy companies that are queueing up to slam the emissions bill.

The Australian food industry claimed that food prices would rise by 3-5 per cent under the new bill, threatening to force the country into a mass importer and again costing Australia jobs.

Observers say criticism of the bill means that it will likely be delayed from its scheduled start date of 1 July 2010.

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Market comment

One trade and one put option for delivery in 2012 dominated the fledgling AEU market during the first nine days of the month.

A 50,000-trade at A\$22.65 on 2 April was followed one week later by a put option for the same volume at a strike of A\$19.00 for October 2012 delivery with a premium of A\$2.20. Newedge and Nextgen brokered the deals.

Bids and offers narrowed for the 2012 contract, while price indicators remained wide for others.

Sources said trade was being strangled by ambiguity over the scheme, especially with regards to the start date - one reason why liquidity was being pooled in the 2012 as opposed to the 2011 contract.

"The AEU market is really illiquid at the moment, so when it trades there is a lot of fanfare around. Deals being done have caveats and can be cancelled if the scheme doesn't emerge," one participant said.

"Things will change when legislation is passed but there is increasing doubt now over the start date for the scheme. A lot will depend on political horse trading and how much the government will change the bill to get it over the line," he said.

Observers agree AEU should be priced around secondary CERs, which were pegged at €10.90 (A\$20.33) for 2012 delivery, notwithstanding forward exchange rates.

"We expect there may be some changes to scheme commitment dates, but I don't think the liberal import limits would change," another trader said.

AEU OTC closing prices (A\$/t)

Delivery	Bid	Offer	Close
AEU 2010/11	20.00	22.25	21.75
AEU 2011/12	22.50	22.90	22.65
AEU 2012/13	22.50	24.50	23.50

The prices reflect OTC levels on 26 March. AEU's are quoted in A\$. Prices provided by brokerages Newedge, Nextgen and TFS and market traders. For methodology, see www.pointcarbon.com.

New Zealand to allocate 8m permits

New Zealand is to allocate 8 million NZ units (NZUs) to forest owners for the year 2008.

Climate Change Minister Nick Smith asked for the 8 million permits to be transferred to the crown's registry in late March and the credits will be given to owners of forests established after 1989.

Forestry is currently the only sector covered by the New Zealand emissions trading scheme.

Participation is voluntary for post-1989 forest owners, and those who wish to be included in the scheme must apply for NZUs.

Officials reckon that foresters that are able to claim 8 million credits for their forests' carbon storage will apply.

In total, post-1989 owners in New Zealand are expected to have prevented 16 million tonnes of CO₂ equivalent from being emitted in 2008.

The 8 million allowances will be transferred to foresters' accounts before 1 April, according to the Ministry of Environment.

However, the 2008 allocation plan for forestry will not be finalised for some time yet. The government will take submissions on the plan until the end of this month.

Last week, the NZ ETS saw the first-ever trade with an unnamed forestry firm selling 50,000 NZUs at a price of NZ\$20 per tonne.

New Zealand ETS hearings to close in May

Final parliamentary hearings on emissions trading in New Zealand will be held on 11 May.

The feedback is meant to help the government implement changes to the country's emissions trading scheme before 1 September this year.

New Zealand has named 108 individuals and organisations to comment on the proposed cap-and-trade scheme, which is currently being reviewed by a parliamentary committee.

MPs wants to hear a wide range of views from different economic sectors, including the opinions of science and non-governmental organisations, said Peter Dunne, committee chairman.

When the government established the committee in December, its terms of reference said it should also review the scientific warnings against climate change.

The terms were included following pressure from the Act party, a small member of the governing coalition.

Rodney Hide, Act party leader and member of the review committee, has several times said publicly that climate change is a hoax.

While the reference terms to science have since been removed, the list published today includes some outspoken sceptics of climate change science, according to Dunne.

However, he did not say whether this means the committee will report on climate change science and the need for adaptation and mitigation policies, or whether the committee will focus on emissions trading.

The ETS, which currently only covers the forestry sector, started on 1 January 2008 and was approved by parliament in September 2008.

It is scheduled to be expanded to stationary energy sources and industrial facilities 1 January 2010, with other sectors gradually phased in by 2013.

Australia selects areas for carbon storage plan

Australia has defined 10 offshore areas for carbon capture and storage (CCS) development.

Since March, companies can apply to the government for rights to explore and develop CCS projects as part of the country's efforts to slash greenhouse gas emissions.

"The first ever release of exploration areas for greenhouse gas storage sites forms an important part of the government's commitment to reducing Australia's carbon emissions while maintaining economic growth," Energy and Resources Minister Martin Ferguson said.

"Advancing storage technology and capacity is vital to the

future of Australia's coal industry and to coal's future as part of the world's transition to cleaner energy pathways," he said.

Coal accounts for 80 per cent of Australia's electricity generation, and the coal sector represents half of the country's carbon emissions.

As a result, Australia is among the world's biggest per capita emitters of greenhouse gases, alongside South Africa, another mining giant.

Meanwhile, Australia's liquefied natural gas (LNG) sector has a huge untapped potential, even though only two projects are operational so far.

"Projects such as Gorgon LNG in Western Australia have enormous potential to create jobs, exports and long-term economic growth at a time when we need it most, but CCS technology is crucial to its success," Ferguson said.

Geoscience Australia has contributed to providing the science behind last month's announcement.

The 10 areas chosen are located in the Gippsland basin, the Otway basin, the Petrel sub-basin, the Torquay sub-basin and the Vlaming sub-basin.

Five of the selected areas are off the coast of Victoria, four are offshore from the Northern Territory and Western Australia and one area is off the coast of South Australia.

Australia aims to drive 20 CCS pilot projects by 2020, and last year established an international institute for the development and deployment of CCS technologies – which are currently not economically viable.

"I am pleased to say the institute now includes dozens of countries and companies around the world and I welcome the announcement that the United States will also participate in the institute," Ferguson said.

Australia opposes border adjustment tariffs: minister

Giving free permits to Australian industry is better than imposing import tariffs, Australian Climate Change Minister Penny Wong told a conference in Washington DC last month.

Wong said the Australian carbon trading bill avoids imposing tariffs on imported goods from countries with less stringent carbon regulations.

Instead, a draft of the country's carbon pollution reduction scheme (CPRS) bill will award 25 per cent of revenue generated by carbon auction sales to "energy-intensive, trade-sensitive" companies, such as steel and cement manufacturers.

Wong said she hopes the bill will pass parliament in June.

"We consider providing permits significantly preferable to approaches such as border tax adjustments," Wong said at a seminar in Washington DC.

The award of free permits to emit greenhouse gases would help prevent the phenomenon of "carbon leakage" and aid in the transition to carbon caps, she argued.

Several cap-and-trade bills that had been introduced in the US Congress over the past two years have contained language to create a system of border adjustment tariffs to protect US trade-exposed industries under mandatory carbon caps.

With the US economy floundering and unemployment levels on the rise, policy analysts predict future climate change legislation will contain such provisions.

Australia, like the US, is dependent on fossil fuel energy and has major industries vulnerable to competition from the likes of China and India.

But Wong warned that such measures are not in the interest of a smaller country such as Australia.

"We are a small and open economy. We don't believe it's in our economic interest to argue for more or different types of protection, and particularly in the current climate there is benefit in continued and open trade," she said.

More than 30 industries have been identified as "emission intensive trade exposed" (EITE) industries by the government, and will be awarded compensation to cover up to 90 per cent of their added cost from the CPRS.

Wong addressed another feature of the CPRS, such as permission for companies to use credits from global emission trading schemes and programmes for compliance with Australia's carbon caps.

The draft bill allows the use of an unlimited amount of Kyoto credits for domestic compliance but falling international prices for certified emissions reductions (CERs) has led to speculation that a quantitative limit might be introduced.

"We decided that qualitative rather than quantitative control is more important," Wong said.

She added that enabling Australian companies to buy credits stemming from emission-reduction projects is a good way for them to invest in developing countries.

Wong said that the majority of reductions that the CPRS will stimulate would come from domestic actions, not actions overseas.

Post-2012 targets should be based on cost: Australia

Australia said it should have a lower-percentage carbon reduction goal than other rich countries.

In a document published by the UN last week, Australia argued that cutting carbon emissions is more expensive in Australia than in the EU and Japan - and therefore it should have an easier target to cut emissions.

Australia's abundance of cheap coal for electricity generation means using alternative energy sources would come at a much higher cost than in some other countries.

The report, submitted to the UN in late March, argued that the economic cost of cutting emissions should count as an important indicator for 'comparative efforts' - a key issue in ongoing international climate change talks.

Negotiators are currently debating emission obligations for the period after the Kyoto protocol runs out in 2012 at UN climate talks in Bonn.

A working document is supposed to emerge in the second round of talks in the German city in June.

But so far, talks have primarily focused on the different targets that developed countries should take on, compared to poorer nations.

The Australian report hints that talks ahead of the December UN climate conference in Copenhagen will also focus on which of the developed nations should do most - and how

this should be measured.

Australia has said it is willing to cut emissions 5 per cent below 2000 levels by 2020 – 15 per cent if a solid international treaty is in place.

In comparison, the EU has said it will unconditionally cut its emissions 20 per cent below 1990 levels, and up the target to 30 per cent if UN talks succeed.

“While the reduction from 1990 is a convenient common way to express an emission target, it is not necessarily informative about the degree of effort required to achieve that target,” the report from the Australian government said.

It presented findings by modelling led by the Australian Treasury showing that its national income would take a 1.6-per cent blow annually if it carries out its 15-per cent reduction target.

The reports claimed the EU’s income would only drop 0.6 per cent, even if it cut emissions to 41 per cent below 1990 levels.

Japan would see its income pared back 0.4 per cent if it reduces emissions 29 per cent below 1990 levels, the report said.

Only Canada and Russia among developed countries would face similar costs to Australia when cutting emissions, it said.

But even this 15-per cent reduction target to cut emissions falls way short of the demands of both scientists and developing countries such as China and India.

Instead at UN talks in Bonn this week, developing nations said that all industrialised countries should cut emissions by at least 45 per cent under 1990 levels.

The Australian government vowed to keep the issue of emission reduction costs on the agenda.

“During the course of 2009, Australia intends to provide further input on the matter of comparable effort by all countries, including all advanced economies, as part of a comprehensive, effective and fair post-2012 outcome,” it said.

NZ businesses back multi-party carbon law

Almost half of New Zealand business leaders want politicians to agree a deal on emissions trading.

According to a poll conducted by the New Zealand Business Council for Sustainable Development, 48 per cent of decision makers want all parties in government to agree on an emissions trading bill before it becomes law.

This is needed to ensure long-term policy stability, the poll found.

But 17 per cent of respondents opposed a multi-party deal, while 20 per cent were neutral and 11 per cent didn’t know.

The poll was launched after Climate Change Minister Nick Smith accepted an offer from Labour’s climate change spokesperson, Charles Chauvel, to discuss a multi-party ETS agreement.

“It’s quite clear business people would like a deal on an ETS which sticks. We need a scheme which lasts for another 30 parliaments, not just one,” said Business Council Chief Executive Peter Neilson.

A review of emissions trading law is expected next month, and politicians are seeking to align the carbon scheme with Australia’s Pollution Reduction Scheme, a bill which has not been passed.

New Zealand’s law currently only regulates forestry but is scheduled to expand to all sectors over the next few years.

Some 50 per cent of business people said it was important that an agreement is reached in the short term (i.e the next six months).

The poll found 37 per cent said isn’t important to agree a deal quickly, while 13 per cent said they didn’t know.

“A clear signal on emissions pricing is also needed to make sure the right decisions are made on billions worth of major infrastructure projects, specially in the energy sector,” Neilson said.

Aussies see future in CDM

By Sally Burns, Sigma Global

Following Australia's ratification of the Kyoto protocol and the announcement of the proposed Carbon Pollution Reduction Scheme (CPRS), Australian companies and investors are increasingly gaining interest and preparing for trade and compliance under the scheme.

Furthermore, they are exploring the opportunities offered by the CPRS acceptance of CERs and preparing for investment, trade and project development in the CDM market.

Many are currently establishing the internal processes required to enter the CDM market in a range of ways, although the ongoing uncertainty surrounding the implementation of the CPRS has slowed progress for some.

The downturn in economic activity has curiously offered a prime opportunity for strategy development and process change, as well as for gathering the range of approvals and structural adjustments for engaging in a new and relatively poorly-understood commodity.

Those companies that move decisively at this stage are likely to reap the benefits offered in the initial phase of the CPRS in a similar way to those forward thinking companies that profited in the EU emissions trading scheme. They did this by taking advantage from the year on year backwardation in the scheme by selling EU allowances for short term delivery and buying them back at a lower price prior to compliance requirements.

There are three drivers for Australian companies who have had previously no interaction with the CDM market to develop strategies.

Firstly, companies with compliance requirements under the CPRS may be able to reduce their costs through generating their own, cheaper, fungible carbon assets.

Secondly, those providing trading services may wish to increase the range of commodities they are able to provide as well as to offer structures built around correlated products such as emissions allowances and electricity.

Finally, many Australian companies are holders of innovative, low carbon technologies that may become economic to implement in developing countries with an added CER kicker.

The Australian government has opted for a 'soft start' to the CPRS as is reflected in the cap and the price ceiling. As a result of this it is likely that in the lead up to and during the first phase of the scheme Australian investors will need to source CERs only within the primary market, as Australian Emission Unit (AEU) prices are unlikely to be high enough to warrant purchases on the secondary market.

Fortunately, the opportunities for Australian companies within the primary CDM market are vast. Of particular note are the many companies with global operations in CDM-eligible countries, but those that are not already active in these locations also have ample scope to engage.

The secondary markets may also have their attractions and prove useful for companies looking to forecast prices and assess the bankability of CERs for later phases.

The proposed provision for unlimited use of Kyoto units including CERs, affords Australian companies much flexibility and many advantages. The opportunity to meet compliance at a cost lower than that of AEU's, while improving operational efficiency in developing country operations is one that can not be shunned lightly.

By allowing unlimited use of Kyoto units the government has recognised the challenges faced by compliant companies in a largely industrial and often highly-efficient economy and provided a mechanism through which to potentially lower substantially compliance costs. It also allows a form of linking with other emissions trading schemes via the common fungibility.

Linking schemes (even partially) is likely to lead to further market efficiencies and drive the markets to find the lowest cost emissions abatement. This will bolster the effectiveness of the Kyoto protocol to reduce global emissions and contributing to the sustainable development of developing countries.

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