



POTSDAM INSTITUTE FOR
CLIMATE IMPACT RESEARCH

Will markets take over Merkels when it comes to linking?

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German coal-phase out a lesson for linking



Bloomberg



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Climate Changed

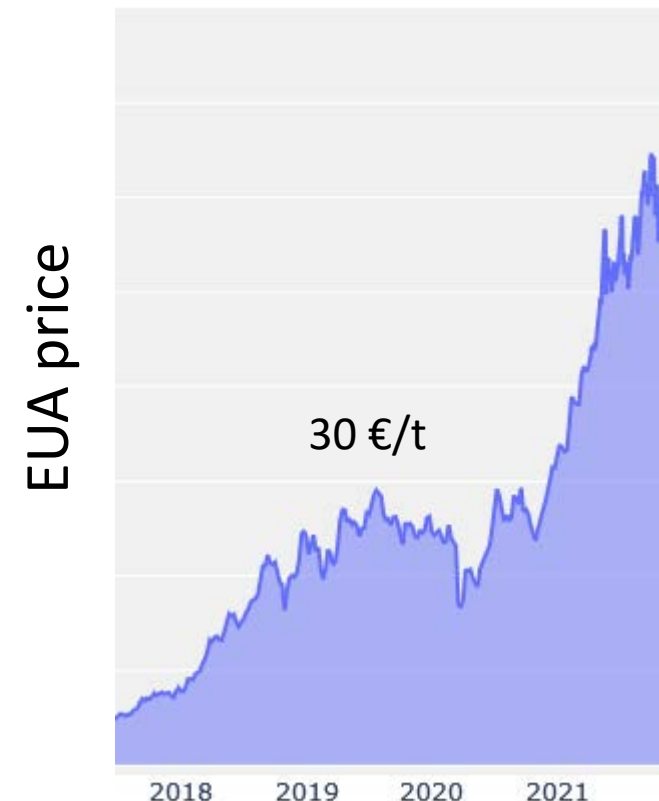
Markets Drive Germany's Exit From Coal Much Harder Than Merkel

By [William Wilkes](#) and [Brian Parkin](#)

5 July 2019, 14:57 CEST

Updated on 6 July 2019, 07:00 CEST

- ▶ BNEF study shows coal losing out to natural gas, renewables
- ▶ Plants powered by imported gas cheaper to operate than lignite



Regulators



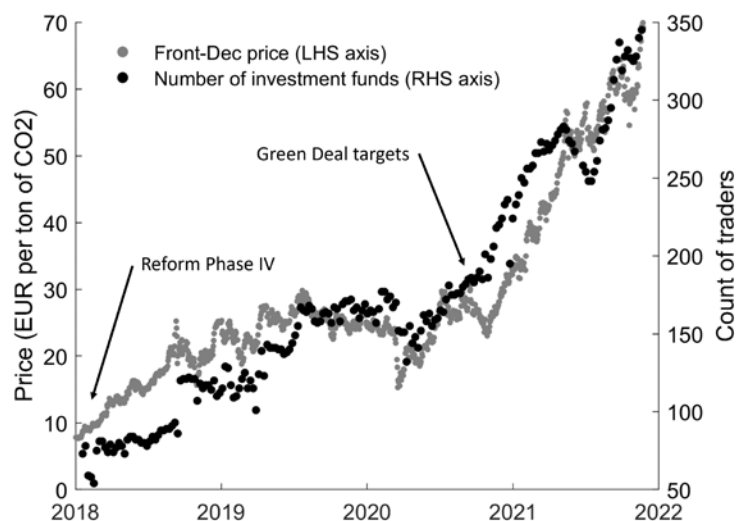
- *Washington state carbon market **will not be linked from outset** [to WCI] -govt official ([Carbon Pulse](#), Nov 21).*
 - *The Parties shall [...] give **serious consideration** to linking their [...] systems in a way that **preserves the integrity** [...]. (EU-UK Agreement, April 21)*
 - *Any possible merger of the two systems should be assessed **only after a few years of the functioning** of the new emissions trading system. (EU FF55 package, ETS reform proposal, July 21)*
- Cautious for good reasons, e.g. delinking of NZ ETS from Kyoto markets in 2013 (Kerr et al. 2021), **conditions need to be met** (→ Stefano)

Markets



- Voluntary carbon market put pressure on Article 6 agreements (cp. TSCVM)
- *“UK utilities are widely believed to have continued hedging their forward power sales with EUAs. [...] The growth of the **UKA premium** has begun to **trigger calls for the market to be linked to the EU ETS**”* ([Carbon Forward 2021](#))
- *“[Financial participants are] just **trying to anticipate** where we’re going next. That’s what has been going on with the EU ETS since the announcement of the MSR a few years ago.”* (Rob Pulleyn, Morgan Stanley, [Carbon Forward 2021](#))
- *“If allowance prices in either [EU] system are considerably lower than the **anticipated future single allowance price** in an integrated system, market participants might buy and bank lower-priced allowances for future use, driving up short-term prices.”* (Edenhofer, Kosch, Pahle & Zachmann 2021)

Prepare for financials in the linking driving seat!



Source: Quemin & Pahle (forthcoming)

EXHIBIT 4: GOVERNANCE BODIES

		Supply	Market intermediaries	Demand					
Governance roles		Project design & development	Verification/Validation	Supply side financing	Trading (pricing, execution)	Risk management	Settlement & retirement	Market & reference data	Voluntary
Underwrite oversight	CCPs: Core carbon principles	Establish, host, and curate the Core Carbon Principles and additional attributes							
	Adherence to CCPs	Develop guidance for any required guardrails or exclusions of project types							
	Participant eligibility	Assess validity of methodologies against the CCPs							
	Participant oversight	Set principles for what suppliers, market intermediaries, and buyers must adhere to in order to participate in voluntary carbon markets							
Market integrity principles	Participant oversight	Set guidelines on supply commitments (i.e. templates for suppliers' pledges)	Provide accreditation, guidance, and oversight over the VVBs (incl. spot checks)	Increase VVB capacity if needed				Establish principles for commodity trading regulation (e.g. derivatives / futures regulation), combating money laundering, fraudulent transactions and excessive speculation	Set guidelines on buyer commitments (i.e. template for buyers' pledges)
	Market functioning	Develop mechanisms against supply-side fraud (e.g. double counting, misrepresentation)							
Legal and accounting rules	Legal	Develop necessary principles for an accelerated and digital MRV project cycle							
	Accounting	Host / refine standardized contracts for OTC and exchanges and for securitization (with appropriate legal underpinnings)							
		Provide financial accounting guidance for off-takers							
		Provide carbon accounting guidance relevant to off-taking							

Source: TSVCM (2021), Phase 1- Final Report

- Acknowledge “emission market as financial market” (→ talk by E. Cantillon), with financials (always) a step ahead of regulators
- Strengthen & harmonize governance (→ talk by R. Betz)