ClimateWire
THE POLITICS AND BUSINESS OF CLIMATE CHANGE

An E&E Publishing Service

MARKETS: World Bank and exchanges work to keep CDM trades going after 2012 deadline *(Monday, March 7, 2011)*

Nathanial Gronewold, E&E reporter

UNITED NATIONS -- Carbon market proponents are fast at work ensuring that the Kyoto Protocol's emissions offsetting systems survive longer than the treaty itself.

Governments have been put on notice that if they fail to either renew or replace the 1997 global warming agreement by Dec. 31, 2012, a huge part of the global emissions trading regime will be disrupted. The Clean Development Mechanism (CDM), a U.N.-connected system for generating greenhouse gas abatement credits from the developing world, would be most affected -- reviewers say no new CDM projects could be conceived from 2013 onward under the current rules.

But carbon allowance and credit exchanges have extended their product offerings into 2013 futures contracts, citing interest from traders. And the World Bank has explicitly told the projects it supports that funding will be available to purchase credits well into the post-2012 period, despite the fact that there may be no buyers then.

The World Bank is actually leading the effort to guarantee the CDM's survival. It recently announced new funds allocated for post-2012 carbon credit purchases, which are made available to member countries and companies facing reduction requirements. Officials at the bank say they are very actively working to ensure that the CDM survives even if the Kyoto Protocol dies, focusing their expansion efforts on the poorest nations and Africa.

"This is to provide certainty to any potential regime," said Eduardo Dopazo, an administrator of the World Bank's Carbon Finance Unit. "We did it in the past, and we're doing it now."

Last year, the offices of the U.N. Framework Convention on Climate Change (UNFCCC) conducted a legal study of the Kyoto Protocol in an effort to tell nation members what to expect should the treaty be allowed to expire with no replacement. The study assumes there will a "gap" between Dec. 31, 2012, and when a new arrangement can be agreed upon over the course of slow and painful negotiations.

The world's largest carbon market, the European Union's Emissions Trading System (ETS), would continue -- countries are committed to operations until at least 2020. But carbon market analysts have pointed out that there should be enough projects existing today to keep the ETS well supplied with CDM credits, or Certified Emission Reductions

(CERs), up to that end date.

Will there be enough projects to continue?

Fresh demand would come online should the European Union raise its emissions reduction target from 20 percent to 30 percent, but that's unlikely to happen, experts say. The United States shows no interest in importing CERs since its withdrawal from the Kyoto pact, and other potential buyers like Japan, Australia and Canada have also been turning away from the CDM lately.

A flood of new CERs into the market in recent months backs up the analysts' assertions of robust supply lasting to 2020, although the CDM office is projecting very low CER issuance as the end of 2012 draws near. The reason, say the International Emissions Trading Association (IETA) and many of its member companies, is that investors have begun to sharply curtail their spending on new projects, shrinking the future pipeline.

But Dopazo and his team are behaving as if there are only sunny days ahead for the CDM, even as most market players are predicting its slow death.

The bank's Carbon Finance Unit made news when it announced from Washington, D.C., one month ago that it had allocated €105 million ($147 million) to "Tranche 2" of its Umbrella Carbon Facility, a fund for purchases of CERs from projects backed by the World Bank. The funds are earmarked specifically for CERs generated from 2013 to 2018.

The bank is also moving forward with projects that generate CERs from avoided or reversed deforestation and even from so-called "soil carbon" projects, even though the current CDM system doesn't allow those.

Dopazo said the post-2012 efforts, approved by the World Bank's board of directors, are simply an extension of the Carbon Finance Unit's history of laying the groundwork for offsets projects even before there is any clear demand for the credits, assuming all the risk in the interim. Carbon project funding at the bank was set up in 1999 and launched in 2000 -- well before the Kyoto Protocol entered into force -- to help create a critical mass of CERs that nations and large corporate buyers could draw from.

Current efforts like the Tranche 2 funding are just an extension of that, Dopazo said in an interview.

"At this time, I would say we are at a similar environment," he said. "We don't have a regime post-2012, there is a lot of uncertainty, so this is precisely for us the moment of opportunity to demonstrate the role of the market mechanisms and carbon finance in helping to mitigate climate change."

Exchanges offer futures trades beyond 2012

The private sector is beginning to mimic the bank's efforts.

At the end of January, InterContinental Exchange (ICE), which operates the European Climate Exchange and the Chicago Climate Futures Exchange, began offering trades in CER futures for delivery from 2013 to 2020.

ICE's main competitor quickly followed suit. Green Exchange (GreenX), which has only begun very recently to expand its share of ETS trading activity, launched its "CERplus" futures contracts at the end of February. December 2013 was set as the initial delivery date, though officials there added that "it is GreenX's intent to offer additional vintages, options and spread contracts associated with the CERplus at a later point."

Brookly McLaughlin, a spokeswoman at ICE, declined to specify why her firm decided adding post-2012 CER futures contracts was a good idea, even though the CDM itself may abruptly come to a halt. She said contracts are normally added to the exchanges after consultations with trading members.

"We assess what services and contracts will best meet the market needs of our customers and consult with market participants on product demand," said McLaughlin.

Mixed outlook at U.N. agencies

ICE data show that trading volumes for the 2013 and onward contracts has been weak, but this could just be reflecting the focus of traders on the current ETS compliance period, which also closes on December 2012.

Actions by the World Bank and the exchange platforms that assume the CDM will continue post-2012 stand in sharp contrast to the sentiments of the CDM's own administrators and the Kyoto Protocol's regulators. UNFCCC chief Christiana Figueres recently warned the CDM's Executive Board that its system faces extreme challenges in the months to come.

Foremost among their worries is the slow pace of negotiations and Japan's very public effort to turn its back on the CDM and establish its own bilateral offset trading system, a scheme that Tokyo authorities hope to link into the greater global carbon markets. U.N. carbon trading regulators fear other nations will follow suit.

Meanwhile, regulators of the CDM's sister institution, the Joint Implementation (JI) system, are as upbeat as ever.

"Actually, I'm quite more confident that there will be a JI post-2012 than I am for the CDM," said Benoît Leguet, current chairman of the Joint Implementation's supervisory committee.

Leguet recognized the UNFCCC's determination that the rules would not allow new CDM projects from 2013 onward, but he sees nothing in the legal terminology that wouldn't let the JI continue its current expansion, even after the Kyoto treaty period ends. During international climate change negotiations in Cancun, Mexico, last year, his supervisory committee asked delegates to confirm their findings, and Leguet expressed confidence that they would agree.

"We're quite confident that we can do it," he said. "We asked the [delegates] to clarify that we can do it, and not whether we can do it."

About ClimateWire

ClimateWire is written and produced by the staff of E&E Publishing, LLC. It is designed to provide comprehensive, daily coverage of all aspects of climate change issues. From international agreements on carbon emissions to alternative energy technologies to state and federal GHG programs, ClimateWire plugs readers into the information they need to stay abreast of this sprawling, complex issue.

E&E PUBLISHING, LLC www.eenews.net	E&E Publishing, LLC122 C St., Ste. 722, NW, Wash., D.C. 20001.Phone: 202-628-6500. Fax: 202-737-5299.www.eenews.net