What's Hot: EUA prices nearing €100/tonne

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The front December European Union Allowance (EUA) futures price hit an all-time high of €98.36 per tonne intraday on Tuesday, 8th February 2022. Although its prices pared back to €91.16 per tonne at the time of writing (Thursday 10th February 2022), €100 per tonne is easily within sight as the market closes in on a compliance deadline. Operators must have their greenhouse gas (GHG) emissions for 2021 verified by the end of March 2022 and then surrender the appropriate number of EUAs by the end of April 2022.

Figure 1: December 2022 EUA Price

Source: Bloomberg. Data from January 2017 to February 2022.

Historical performance is not an indication of future performance and any investments may go down in value

Fundamentals driving the price rise

High GHG emissions from electricity production and reduced Allowance supply are helping EUA prices. Elevated European natural gas prices due to the NATO-Russia sabre rattling is driving a greater reliance on electricity production through higher greenhouse gas emitting sources of energy, thus increasing reliance on EUAs.

Why a high EUA price is consistent with policy goals

Reducing greenhouse gas emissions by 55% by the year 2030 (relative to 1990), as stipulated in EU law, is a difficult task and will require the adoption of more pollution abatement technologies. However, many technologies are expensive. A higher carbon price is thus required to make these technologies viable. For example, Bloomberg New Energy Finance estimates that a carbon price of $145/tonne would be needed to incentivise the initial phases of decarbonising global steel production over the next ten years . Heavy polluting industries need clean electricity, green hydrogen and carbon capture technologies to reach net-zero emission by 2050.

Path to net zero requires more

The European Union is the only continental scale economy with a well-articulated pathway to reach Net-Zero by 2050. But unless it fully adopts the "Fit for 55" legislative package , it will fall short. Negotiations are currently taking place, but this could be a multi-year process. However, what is clear is that the direction of travel is one of tightening emission standards and putting in the incentives to accelerate decarbonisation. A greater focus on European Union's Emissions Trading System (ETS), which is already the centrepiece of the EU's climate policy, is highly likely.
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Press reports indicate that Peter Liese, a Member of European Parliament, will propose some changes to reduce price volatility of EUAs in the coming week. Under Article 29a of the ETS Directive, the European Commission is required to hold a committee meeting to discuss the possibility of increasing the supply of allowances if, for more than six months, the EUA price is more than three times the average price from the previous two years. Despite the strong price gains we have seen in the past year, this meeting has not been triggered (as the conditions have not been met). We agree that the Article is poorly worded and could do with clarification. However, prices are an important signalling mechanism and any measures that delink EUA supply from fundamentals could be a mistake. The climate goals are tough to achieve. To blunt the tools to get there would make it even tougher. We note that Peter Liese agrees that prices have been driven by fundamentals and any changes her proposes (which are not known yet) will require circa 65-70% approval at the Council, Parliament and then with the Commission. So, the price-drop in recent days (December 2022 EUA price fell to €90.50 at the time of writing, Friday 11th February) seems premature and possibly indicates an attractive entry point.

1 Decarbonizing Steel: A Net-Zero Pathway, BloombergNEF, December 2021

2 https://www.wisdomtree.eu/en-gb/blog/2021-10-14/fit-for-55-legislation-going-harder-deeper-faster-with-the-eu-emissions-trading-system

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