Reflections on 2012 RGGI Review

RGGI stakeholder meeting, New York, September 19, 2011

Olga Chistyakova, Thomson Reuters Point Carbon
Today: RGGI over-allocated through 2018

- RGGI emissions to stay below the cap through 2018
- Cap would need to be lowered to incentivize additional emission reductions
- Accumulated surplus of allowances could be many times the annual cap

Source: Thomson Reuters Point Carbon 2011
The problem with the allowance surplus

- Surplus of allowances from Phase 1 could thwart efforts to make program short
- If cap lowered to 2009 emissions as a baseline, program is short - on paper
- But in reality surplus of allowances could keep program long through 2018

Source: Thomson Reuters Point Carbon 2011
Who holds the surplus allowances?

- **Private bank = emitters or financials**
  - allowances purchased by market participants over and beyond what is needed for compliance
  - We estimate to date only 10 Mt banked

- **Unsold allowances = states**
  - allowances not allocated for free and not sold
  - 4 out of last 5 auctions were undersubscribed: 93 Mt unsold to this date
  - We assume not all set asides have been distributed: 24 Mt
  - Total: we estimate to date, states have 117 Mt unsold allowances

- **What to do with unsold allowances?**
  - State regulations differ with regard to retirement of, or auctioning of unsold allowances
  - For simplicity in our modeling, we assume that unsold allowances don’t come to market
Remaining uncertainty: what about the next auctions?

- What will happen at next auctions?
  - We assume final decision on 2012 Review happens late 2012
  - Policy uncertainty creates uncertainty on auction subscription rate
  - Market participants could bank an additional 62 Mt maximum if all auctions (Dec 2011-Dec 2012) are fully subscribed

- “Low banking case”
  - low subscription rate (10%) at Dec 2011 auction
  - Emitters buy only what they need for compliance in 2012
  - only 27 Mt banked by end 2012

- “High banking case”
  - emitters/financials buy all available allowances at Dec 2011 and 2012 auctions in anticipation of tighter cap
  - up to 91 Mt banked by end 2012
Revising the cap: scenarios

- We construct two scenarios:
  1. Use 2009 emissions as a baseline for 2013-2014
  2. Cut 2013-2014 cap level by 50%
- 2.5% annual decline 2015-2018 in both cases

Source: Thomson Reuters Point Carbon 2011
Scenario 1: Adjust cap to 2009 baseline

- Lowering cap to 2009 baseline works well if private participants don’t bank too much in 2011 - 2012
- Market remains long if emitters build a large bank

Source: Thomson Reuters Point Carbon 2011
Scenario 2: Lower cap by 50%

- Program sure to be short even if private participants build a large bank in 2011 - 2012
- Large volume of emission reductions required through 2018

**Source:** Thomson Reuters Point Carbon 2011
Conclusion

• RGGI faces a serious over-allocation problem
• Over-allocation can only be addressed by combination of two actions from regulators:
  – Withhold unsold allowances
  AND
  – Lower cap
• Short market could lead to high prices
  – Limited abatement options in RGGI
  – Few offsets allowed, insufficient to keep prices low
  – Consider other price containment mechanisms, possibly using unsold allowances for back up (Price Containment Reserve)
Questions?

Olga Chistyakova – olga.chistyakova@thomsonreuters.com
Emilie Mazzacurati – emilie.mazzacurati@thomsonreuters.com

www.pointcarbon.com
Disclaimer and copyrights

• A THOMSON REUTERS PUBLICATION

• Copyright © 2011 All rights reserved. No portion of this publication may be photocopied, reproduced, scanned into an electronic retrieval system, copied to a database, retransmitted, forwarded or otherwise redistributed without prior written authorisation from Thomson Reuters. See "Terms & Conditions" at pointcarbon.com

• The data provided in this report were prepared by Thomson Reuters Trading Analytics and Research division. Publications of Thomson Reuters Trading Analytics and Research division are provided for information purposes only. Prices are indicative and Thomson Reuters does not offer to buy or sell or solicit offers to buy or sell any financial instrument or offer recommendations to purchase, hold or sell any commodity or make any other investment decision. Other than disclosures relating to Thomson Reuters, the information contained in this publication has been obtained from sources that Thomson Reuters believes to be reliable, but no representation or warranty, express or implied, is made as to the accuracy or completeness of this information. The opinions and views expressed in this publication are those of Thomson Reuters and are subject to change without notice, and Thomson Reuters has no obligation to update either the opinions or the information contained in this publication.

• Thomson Reuters Trading Analytics and Research division receives compensation for its reports. Thomson Reuters Trading Analytics and Research division reports are published on a subscription basis and are not issued at the request of any client of Thomson Reuters.