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CLARIFICATION: EUAs to feature in new hybrid voluntary carbon contract

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EU ETS allowances will be used as a substitute for removals units in a new global “hybrid” credit for the voluntary carbon market (VCM) until the removals market develops enough liquidity, the contract's developers said on Thursday.

(Clarifies that the EUAs traded as part of the GER are issued at the point of trade and not retired as previously suggested)

EU ETS allowances will be used as a substitute for removals units in a new global “hybrid” credit for the voluntary carbon market (VCM) until the removals market develops enough liquidity, the contract’s developers said on Thursday.

The Global Emission Reduction (GER) offset will launch Friday (https://carbon-pulse.com/162715/) on Singapore-based AirCarbon exchange (ACX) for spot contracts, and US-based Nodal for futures transactions, and will be made up of four separate tradable sub-contracts or ‘buckets’ spanning renewables and energy efficiency, forestry, credits with added social and development benefits, and removals.

The Carbon Capture Contract (CCC) meant to encompass removals that keep carbon out of the atmosphere for at least a 100-year period, will initially be made up from EUAs “as long as there isn’t a liquid market for removals,” Louis Redshaw, CEO and founder at UK-based NetZero Markets told a press briefing in London.

With removal credits priced at a substantial premium to other offsets partly due to the sheer lack of supply, NetZero Markets said that it would be best to look to the EU ETS as the first step as a “proxy for removals”.

The justification for this was that the EU has a binding net zero emissions target by 2050 through which the EU ETS compliance carbon market is expected to play a crucial role. The scheme currently caps the emissions of the bloc’s power stations, factories, and intra-EU flights and covers around 40% of its total greenhouse gas output.

"What we wanted to achieve was an exchange-traded price for removals," Redshaw said.

The EUAs included as part of the GER are issued allowances. Users of the GER on ACX can then request for the allowance to be retired via their ACX account, a spokesperson for the exchange explained to Carbon Pulse.

The ACX spokesperson added that the exchange does not tokenise any retired carbon credits or allowances and the GER does not include retired EUAs.

"Only unretired credits and allowances are featured in the GER," the spokesperson said.

The tokenisation of the GER and its sub-contracts via AirCarbon would be the equivalent of a "digital warehouse receipt", Redshaw said.

He cited the price of biochar credits as generally changing hands for around the $100 per tonne mark, a comparable price with EUAs that settled on ICE on Wednesday at €86.20 ($90.32).

Direct air capture credits, a very nascent technology on which several multinationals have committed huge funding (https://carbon-pulse.com/160227/) to scale, can go for as much as twice the value of current EUA prices.

The impact on the EU ETS of the "proxy" use of the market for the GER is likely to be minimal given the European market sees trade well in excess of 20 million allowances a day and the share of removals will initially comprise just 1% of the standardised voluntary contract.

The EU ETS emissions cap stood at 1.25 billion tonnes of CO_2 a year in 2021, while a little over 160 mln carbon credits issued by the four main VCM standards were retired last year.

Three of the GER buckets, those not concerning removals, will assume a share of the hybrid contract based on offset retirement volumes via registries over the previous year. For 2023, NetZero Markets will apply 2022 retirements for example to calculate the share of each contract bucket.

However, the share of removals in the GER will be determined on a more discretionary basis by the contract's supervisory committee, which will not include Redshaw.

The idea is to consistently scale up from 1% to ensure a net zero pathway by mid-century, meaning that by 2050 100% of the GER will be comprised of removals credits.

At some point over the coming years, it is likely that the GER will no longer use EUAs as this proxy given the expected rise in the supply of removals credits.

OTHER DETAILS

Other updated details from the press briefing included more clarity on the launch of GER futures on Germany-based exchange EEX – Nodal's parent company – a move set to take place in the second half of the year.

EEX and Nodal are said to be looking at a five-year curve for the GER futures, with initial December-expiring products to aid corporates comply with annual targets, but also potentially monthly products if the demand is there, Redshaw said.

The bucket containing offsets with additional benefits, called the Prime Carbon Contract (PCC), will contain credits that have at least three UN Sustainable Development Goals (SDGs).

Redshaw also described the exchange fees as "very, very low" when compared to some of the fees charged by VCM intermediaries, and hopes that by moving to an exchange-traded product will drive greater price transparency in a current "opaque" market.

THE VISION OF SUCCESS

When asked by Carbon Pulse what success in a year's time might look like, Redshaw responded that he hoped the GER would see significant trade every day via the exchanges, and a high multitude of underlying trades like any other market.

The overarching purpose of the GER is to boost demand and liquidity in the VCM by creating greater confidence in the price of carbon credits and to clear up current confusion in the space, Redshaw explained in a webinar earlier in the week.

NetZero Markets' founders believe that challenges with a lack of liquidity, transparency, and the wide range of moving parts in the VCM mean that buyers are more often than not confused by the market, which is crimping demand.

By Roy Manuell – roy@carbon-pulse.com