The NZ – ETS, Forestry and Carbon Market Opportunities

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Outline

- Introduction – Kyoto, where it all began
- New Zealand’s unique situation
- Opportunities for Sellers and Buyers
- Risk is Everything
- Beyond 2012
CMS is a New Zealand advisory & brokerage company with a successful track record in carrying out carbon deals with clients domestically and internationally

- Sale of over 4.0 million ERU/NZU/AAU from NZ sellers to domestic and international compliance buyers.
- Prepared carbon strategies for Iwi/incorporations and Trusts with carbon assets
- Working with partners and clients to originate and secure ERU/CERs from Eastern Europe, Africa, and Asia
- Working with partners in developing REDD projects in the Asia-Pacific, and Africa regions
- Working on an investment portfolio comprising, renewable energy and forestry for participation in the carbon markets

UN CLIMATE CONVENTION AND KYOTO PROTOCOL – WHERE IT ALL BEGAN

Provided basis for market mechanisms as a way to achieve emission reductions globally

- Defined targets for countries who are responsible for historical emission increases, although many are going to be in compliance
- Attempted to provide a one-size-fits-all approach, which is not working
- Ongoing negotiations for a new draft international climate treaty, fraught with politics
- Possible alternative is an amendment to the existing Kyoto Protocol, only one group likes this
- Calls for engagement in new treaty with US, as well as larger developing countries, eg, China, Brazil, India, to also take on commitments, not all are in agreement
UN CLIMATE CONVENTION AND KYOTO PROTOCOL
WHERE IT ALL BEGAN

- A view that CDM should continue although needs to be more robust rules and may cover sectors rather than projects
- A view that projects which Reduce Emissions from Degradation and Deforestation (REDD) should be a part of a new international treaty, voluntary markets at present
- A view that carbon markets be promoted as most effective means of emission reductions, with focus on regional and national ETS
- A view that Land Use and Land Use Change will play a more significant role in emissions reductions
- Nuclear energy still outside new treaty discussions and may remain so, for some time to come

New Zealands Unique Situation
The Emission Trading Scheme

- In operation since late 2008, but still an illiquid, non-transparent, small scale market
- The current Review may continue the existing uncertainties around parts of the ETS, impeding increased investor interest
- Agriculture may not participate for sometime yet, thus exacerbating current market conditions
- Agriculture sector should become participants as planned initially with reporting, but as a Voluntary Opt-In phase
The ETS - New Zealand Situation

- Submissions to the current Review also outlined that a projects window should be promoted to incentivise small scale innovation and participation
- Current market conditions highlight its out of balance nature (approx 2000 sellers and approx 25 active emitters) which impedes investment and market expansion
- Market size is so small that it can be manipulated by a large participant
- Many participants do not understand the linkage of the NZ market to other markets eg, EU-ETS

ETS Demand and Supply 2010 - 2012

All the demand figures are derived from projected annual emissions in industrial sectors from the May Kyoto Net Balance Report, issued by the NZ Ministry for the Environment. Supply figures are based on the following assumptions: that 58% take up of eligible forestry into the ETS; 60% of pre 1990 NZUs are put to market; surplus from previous year being carried over.
Who is participating in the ETS-2011

Mainly Selling
- Brokers
- Banks
- Forest Investors
- Forest Managers
- Forest Owners

Mainly Buying
- Brokers
- Banks
- Companies with obligations

NZ-ETS – Outlook
2012-2015

- Higher supply volume, increased NZU availability,

- Downward pressure on price, driven by supply and international conditions

- Clearer linkage to offshore market prices, development of ETS in Korea, Japan, US states, Australia, China

- New market developments, such as investment projects, emergence of ethical funds, renewable energy projects
Opportunities for Sellers

• Relationships for selling medium – long term, ie, spot vs forward

• Other markets such as Japan, Korea, and Australia,

• Portfolio approach, some forests for wood production, others for carbon, ie, viability and rate of return

• Government incentives, is the ETS enough?

• Public participation, how can public engage in forestry and ETS?

Opportunities for Sellers

• Carbon forestry provides added value to other core wood production activities

• Provides advanced income streams for reinvestment in forestry which may have been more difficult to achieve previously

• Strengthens existing wood production industry by encouraging investments through additional revenue streams
Opportunities for Buyers

- Chance to establish relationships with forest owners for medium to longer term supply, both in spot and Forward

- When international price closes gives ability to source alternative units

- Companies now engaging in a Portfolio approach, and moving away from large volume purchasing to more frequent smaller volumes

- Some companies have international subsidiaries operating in emerging ETS countries, maybe easier to source carbon

Risk is everything

- Political risk carries a high uncertainty rate for investors

- Currently there are a range of options for buyers to purchase compliance units

- Short to medium term downward price pressure adds risks to sales strategies

- Medium to longer term issues around retaining a skilled forestry workforce and viable nurserymen

- An NZU is not an NZU, unless its on the spot market, and there is not, to date, in the general carbon market, a premium for PFSI over ETS NZU’s
Beyond 2012 – New business
or more of the same

• International treaty – if there is a gap post 2012 what effect will this have on the international market, and the NZ market

• Fungibility – while there is an option to convert NZU, why would NZ sellers want greater linkage with other markets. Beyond 2012 what happens to a Commitment Reserve if there is no agreement on a amended Kyoto Protocol

• Additionality – is this concept outdated? Where GHG of a project is lower than those that would have occurred in a business-as-usual case

• Commodity – Is the carbon market dealing with just another commodity, such as a barrel of oil, if not, what’s so special about carbon

• Speculation around future carbon price trends internationally have looked increasingly attractive, yet why is there not so much activity post 2012

• Clearly post 2012 is risk takers market
Thank You

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