



*****PRESS RELEASE*****
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European Commission's carbon market fix could face ten year setback

In a new report published today, Sandbag finds that the European Commission's proposal to tackle the oversupply of 2 billion allowances in the EU carbon market, could take a decade to get supply below current levels.

The report, "[Avoiding the Avalanche](#)"¹, finds that that previous forecasts published by the Commission and the UK government, underestimated the extent to which unassigned carbon allowances will hit the market in 2020. Sandbag estimates, roughly 750 million unused allowances will be auctioned in 2020, adding to 900 million "backloaded" allowances that are already due to flood the market in 2019 and 2020. This will see an acute increase in the supply just before the Commission's proposed market stability reserve is supposed to start reducing it. By allowing the oversupply to worsen in this way, Sandbag estimates the Commission proposal could take a decade or more to get supply back to current levels.

The unused allowances are expected to come from a reserve for New Entrants, which is being used at a slower rate than anticipated, and from factories which have closed or reduced activity levels and no longer need some of their scheduled free allowances.

Sandbag's report makes three key recommendations for improving the Commission's original MSR proposal when the Parliament's Environment Committee votes on it next Tuesday (February 24th):

- 1. Start the MSR as early as possible**
- 2. Prevent 900 million backloaded allowances from flooding the market**
- 3. Prevent unused allowances from flooding the market**

Damien Morris, Sandbag's Head of Policy and the author of the briefing, commented:

"Parliamentarians in Europe's Environment Committee face a simple question when they vote next week: are they going to let things go backwards? Are they going to accept a proposal that takes a decade to start getting oversupply below today's levels? If policymakers are serious about rescuing the EU carbon market, they need to start the stability reserve immediately and prevent the market being hit by this avalanche of unused and backloaded allowances."

Labour MEP and ENVI committee member Seb Dance, hosted an event in the European Parliament in Strasbourg last Wednesday, where Sandbag and environmental consultancy Ecofys both presented some of their latest analysis on unused allowances. Ecofys presented similar findings to Sandbag,

¹ http://www.sandbag.org.uk/site_media/uploads/Avoiding_the_avalanche.pdf

estimating that 500-900 million unused allowances will be released at auction in 2020 unless somehow addressed.²

Seb Dance, Labour MEP (S&D UK) and ENVI committee member commented:

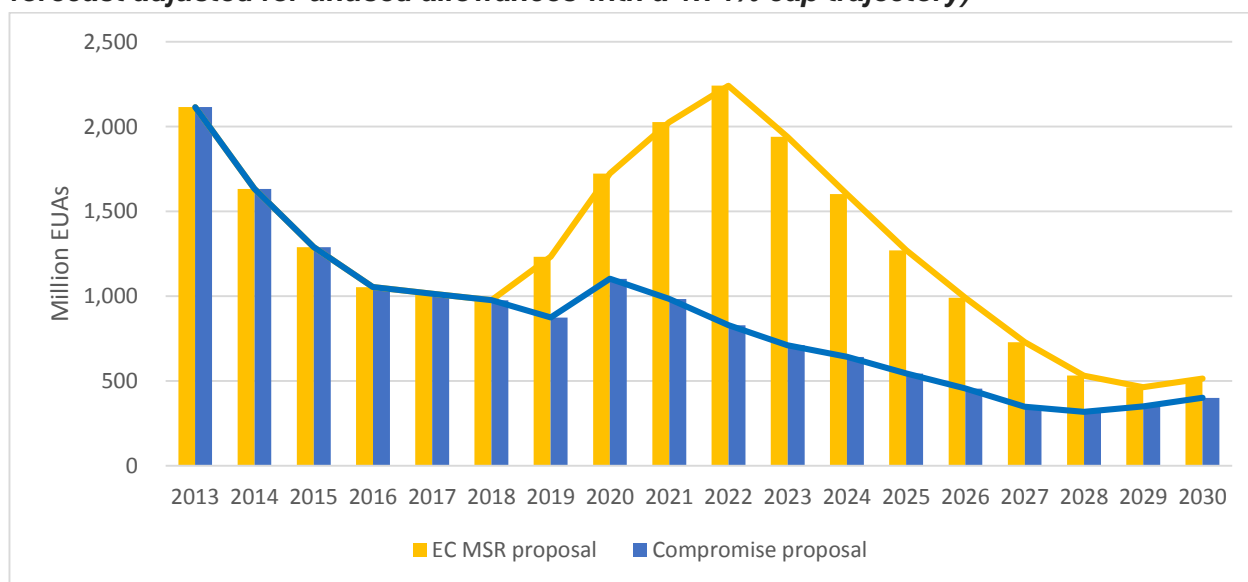
"The issue of unallocated allowances has taken something of a backseat in the debate around the Market Stability Reserve with discussions about the start date, what to do with the backloaded allowances, and carbon leakage dominating the agenda."

He continued:

"With up to 900 million unused allowances potentially returning to the market in 2020, increasing the surplus and destabilising the price of carbon even further we, as policy makers, have a duty to find a solution if we are to fix our carbon market once and for all".

Last Friday's announcements from the political groups show positive signs of a compromise that improves substantially on the Commission proposal by implementing the market stability reserve from December 2018, and by placing backloaded and unused allowances into the reserve.³ In the chart below, Sandbag adjusts the Commission supply forecast to include unused allowances, and illustrates how this compromise would regulate supply in a more stable and controlled fashion compared against the Commission's original proposal. However, Sandbag notes that by failing to start the MSR earlier, and by auctioning 300 million of the backloaded or unused allowances towards an industrial innovation fund, oversupply will still be allowed to worsen before it improves. This will be especially problematic, if emissions turn out to be lower than the Commission forecasts, as Sandbag strongly suspects they will be.

Figure 1: The Commission MSR proposal vs. the ENVI compromise (Commission supply forecast adjusted for unused allowances with a 1.74% cap trajectory)



² <http://www.ecofys.com/files/files/ecofys-2015-working-paper-leftover-allowances-phase-3-eu-ets.pdf>

³ See draft compromises here: <http://www.changepartnership.org/wp-content/uploads/2014/10/Provisional-draft-of-ENVI-compromise-amendments-12-February-2015.pdf>

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