

Carbon Trading: The state of the [global] union

January 30, 2010

Obama is still committed to a climate bill, but his ambitions are being diluted. This reinforces the opinion of the BRAVE partners that carbon emission prices will remain suppressed from the true cost of implementing low carbon technologies for many years.

Reality

Now into his second year in office, President Obama is running into some realities of the American psyche and politics. As BRAVE Partners has stated before in commentary, it was surprising to see Obama hold on to climate change as part of his political agenda soon into his term of office.

The reality is that healthcare reform is proving a tougher challenge than anticipated and it is becoming tougher. The election of Republican Scott Brown to the late Edward Kennedy's Senate seat for Massachusetts only a year after mid-west states went blue (Democrat) for Obama is a clear sign that the inherent conservatism of Americans is showing through again. Massachusetts had not elected a Republican senator since Edward Brooke in 1972. There are no Republicans in the state's congressional delegation and no Republicans holding statewide elected office in the traditionally Democratic-leaning state.

BRAVE Partners found the lack of American leadership in Copenhagen most informative. The Waxman-Markey Bill was stalled in the Senate. Although rising, the vote on the Senate website showed very low support. In the opinion of the BRAVE partners, America had sided with the Republicans on the energy agenda and emission caps and carbon trading did not feature high on their agenda.

The energy agenda

The Republicans fought hard on energy policy in the Presidential election campaign. The Republican message was clear. Under the slogan: 'drill baby drill' the Republicans promoted the notion that cheap energy was essential to the US economy. Renewable energy was clearly a factor in developing a sustainable supply of cheap

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energy – but all energy was important to Republicans, including oil, coal and nuclear.

Shifting sands

In the State of the Union address, Obama did throw his weight behind a climate bill, but he also emphasised the need for bipartisan support – a need ever more necessary with the arrival of Scott Brown in the house.

In this address, Obama put forward a new energy agenda. This agenda looks a lot more like the Republican agenda. Clean coal and nuclear got a nod. The President even admitted that there were tough decisions to be made on offshore drilling – a ban that even George W. Bush did not lift. Energy policy in the USA is moving away from carbon pricing and reduction.

Clean tech economy

Moreover, the language that Obama used about clean tech was that of economics, not the environment. The Republican attack on Obama's energy policy had focussed on the economic impact of increasing energy prices. The President had always countered with the promise of technological leadership and job growth. The change this time was that this tenet was the core of Obama's argument. He admitted that many were sceptical of global warming, but urged them to build a world-beating clean-tech industry. The two do not fit comfortably together. If there is not an environmental issue from hydrocarbons and adequate pricing of carbon, then it is tough to see how a clean tech industry will thrive.

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The BRAVE approach to carbon

As one of the largest emitters of carbon dioxide and one of the largest and most sophisticated financial markets, whatever happens in the USA will drive carbon markets and carbon pricing around the world. The content of the State of the Union address has reinforced the view at BRAVE Partners that, whilst Obama himself is committed to cap-and-trade, he has too great a challenge to implement his policy. The firm believes that the USA will not have a robust carbon policy for the foreseeable future.

The impact of a non-capped USA

If the USA does not implement a cap-and-trade policy this will provide it with a short term economic competitive advantage if other countries maintain or implement carbon pricing. The disincentive for China and India to cut carbon is huge. It even has to put into doubt whether the EU and Japan will maintain their Kyoto cap-and-trade schemes post 2012.

The impact will be twofold. Firstly, carbon prices will remain depressed from that which BRAVE Partners believes is the true cost of carbon reduction. Simply put: carbon technologies will be less profitable and more marginal. Secondly, the futures market for carbon credits will not trade much beyond 2012. As time marches on this means that there will not be a forward and futures market for carbon. Many

renewable energy projects have looked at financing by selling forward carbon credits. Whilst an excellent idea, this has always been hard to achieve due to a number of uncertainties, including those described here. A lacklustre approach to carbon trading and carbon markets by the USA will shut this opportunity completely.

Business and investment choices

BRAVE Partners believes that the knock-on impact of the clear step back from carbon trading in the USA will be for investors to switch from pure carbon driven energy projects to those that create efficiencies. Efficiency can either be created by using what was previously a waste product, as in methane to methanol conversion, or simply using less – as in insulation and other similar ideas. This has already been happening, but it will now accelerate.

BRAVE Partners services

BRAVE Partners monitors the major developing factors that impact the carbon credit markets. BRAVE Partners can assist companies in assessing the future developments in carbon markets and the strategic impact that this will have on their business.

Interaction

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- BRAVE Partners believes that the US Administration gave a clear signal that it has stepped away from a cap-and-trade policy in the State of the Union address.
- BRAVE Partners can advise companies on their carbon credit strategy.

enquiries@bravepartners.com

www.bravepartners.com