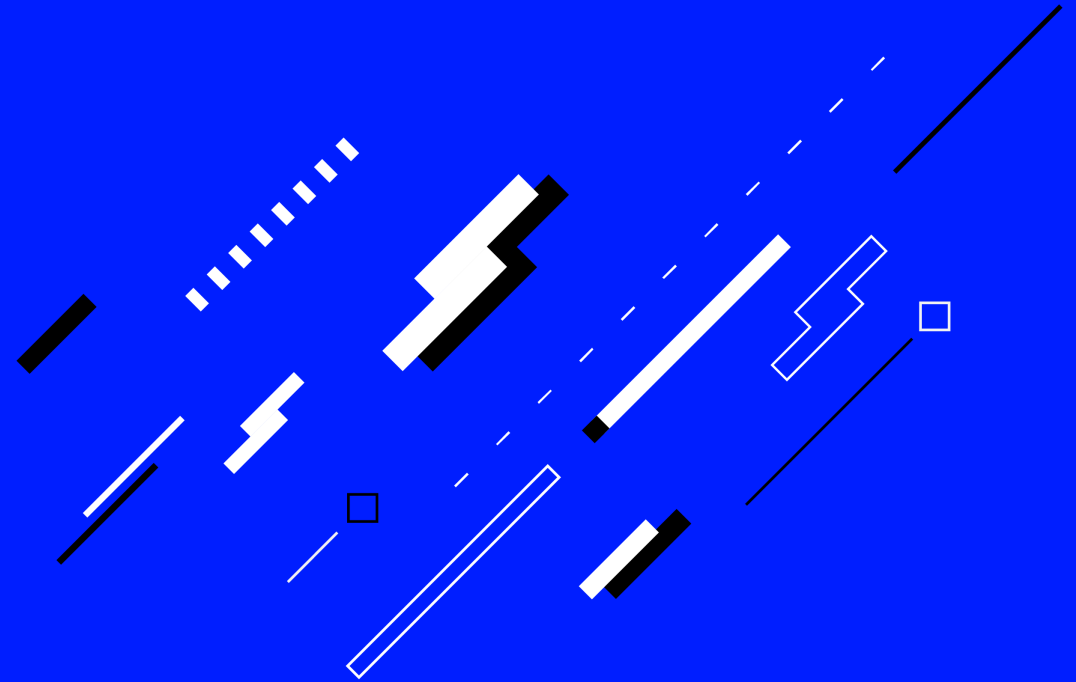


# What role for the MSR under a more ambitious climate target?

Market outlook and interplay of policy design options

ERCST 16 December 2020

Hæge Fjellheim, Refinitiv Carbon Research



# Agenda



Carbon market outlook under a ‘fit for 55’ EU ETS

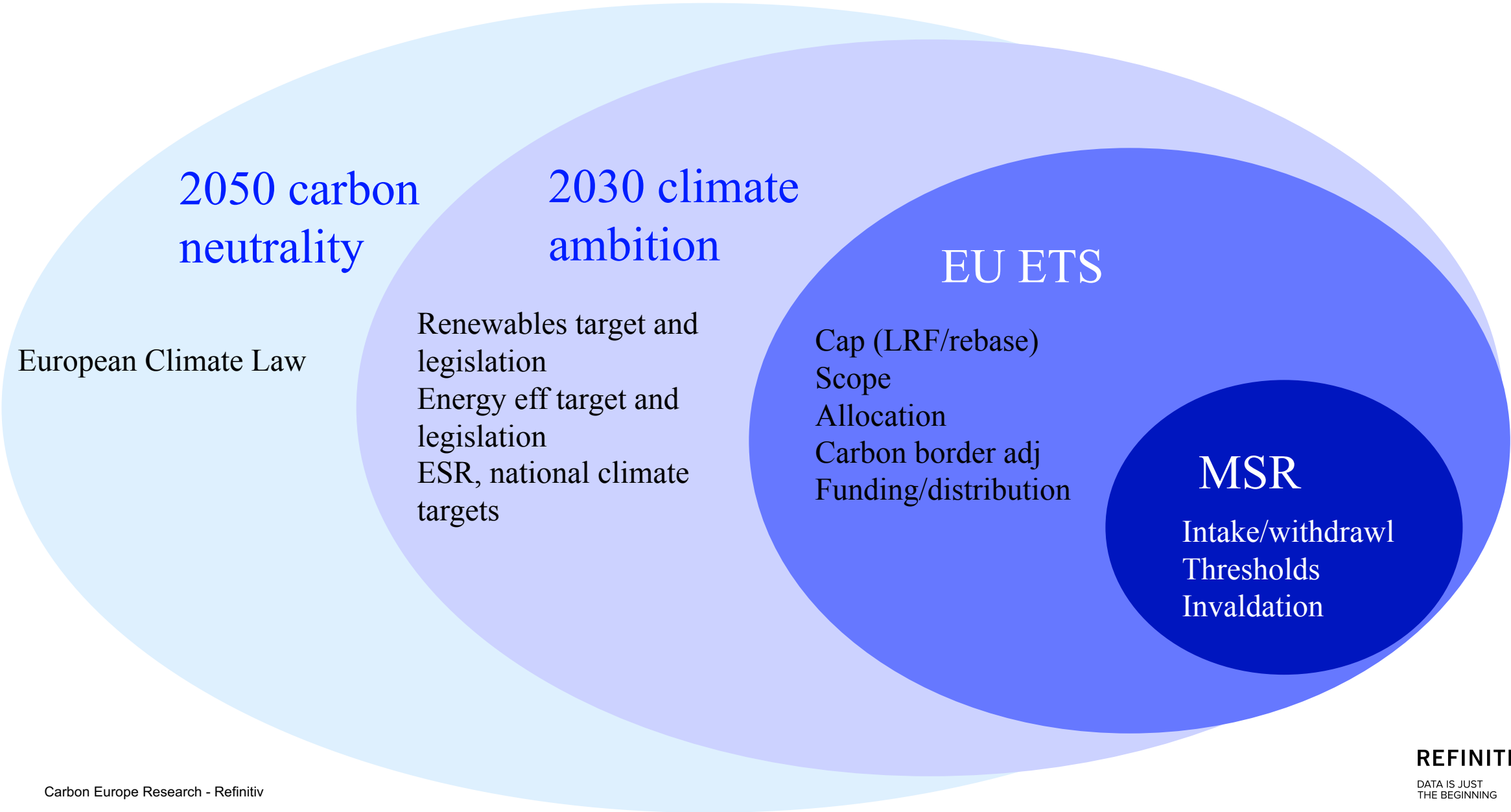


Significance of MSR and interplay with overall ETS policy design



MSR invalidation – embedded ambition

# It's all connected – MSR revision in context



# EU ETS and MSR reveiw - a complex puzzle....

## 1. Choose ambition



## 2. Start to puzzle



- Burden between ETS and non-ETS?
- How fast will ETS cap be reduced?
- Timing of implementation?
- Size Innovation fund?
- Split auctioning of EUAs and free allocation to industry?
- New sectors?
- Market Stability Reserve?
- Cancellation of EUAs?
- Transition fund?
- Flexibility EU ETS/non-traded sector?
- Border tax adjustment
- New renewable target?

## 3. Legislation ready



# ....and a long haul from agreement to implementation

## 1. Choose ambition

## 2. Start to puzzle

## 3. Legislation ready



**Dec 2020?**  
EU Council  
2030 target  
agreement

**June 2021**  
Commission  
proposal

**2021-2023/4?**  
Council and  
Parliament legislative  
process

**2024/5?**  
Implementation of  
legislation



- Burden between ETS and non-ETS?

- How fast will ETS cap be reduced?
- Timing of implementation?
- Size Innovation fund?
- Split auctioning of EUAs and free allocation to industry?

- New sectors?  
- Market Stability Reserve?

- Cancellation of EUAs?
- Transition fund?
- Flexibility EU ETS/non-traded sector?
- Border tax adjustment
- New renewable target?



# Agenda



Carbon market outlook under a ‘fit for 55’ EU ETS

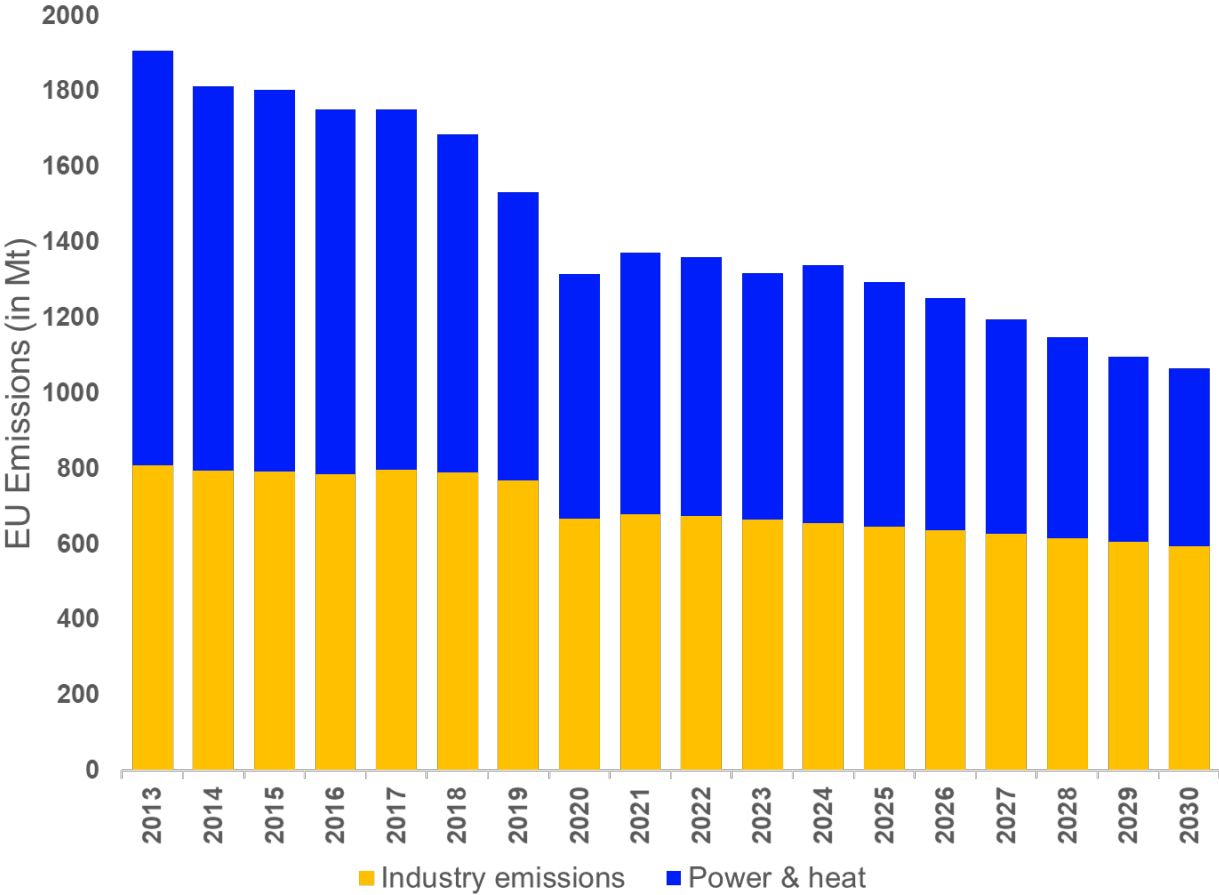


Significance of MSR and interplay with overall ETS policy design



MSR invalidation – embedded ambition

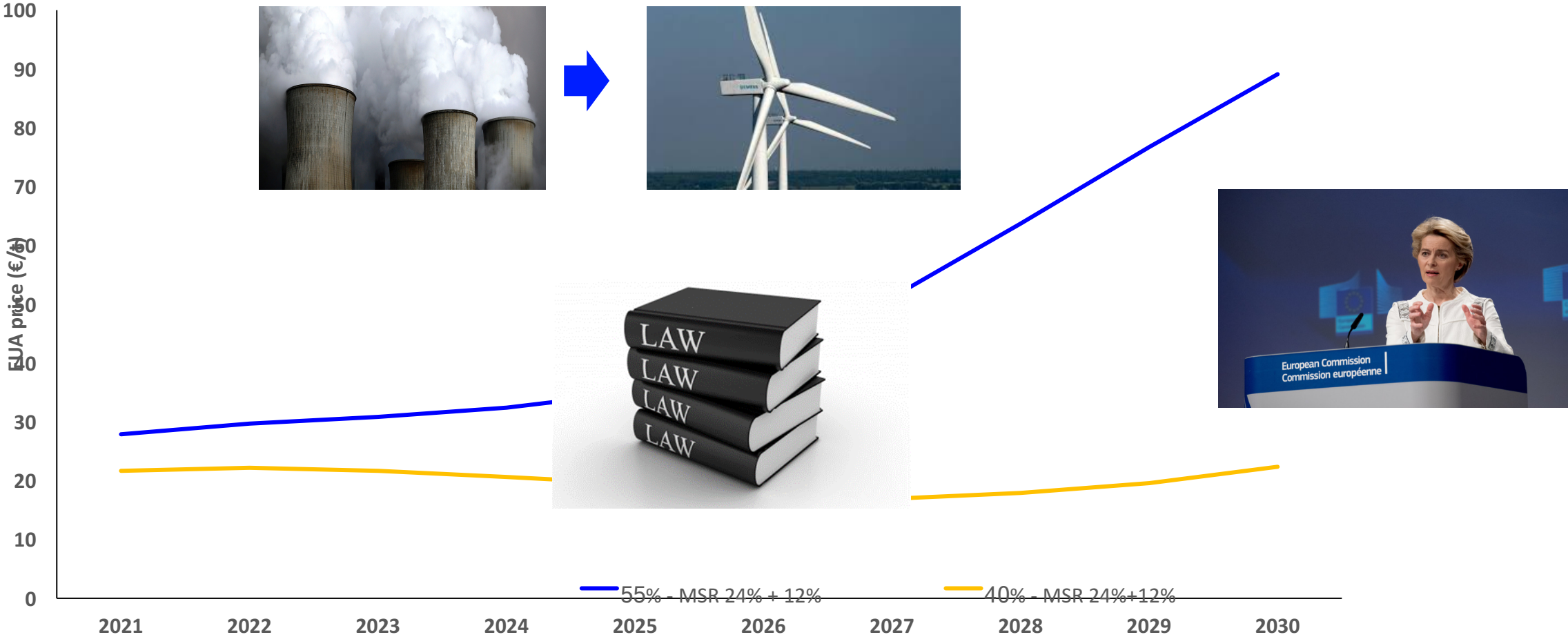
# Rapid greening of the power sector pushes abatement role onto industry sectors



2019-2030:

- Share of renewables in power generation nearly doubles (35% → ~70)
- Power sector emissions down 60%
- Assumes RES target 32% → 38%

# Carbon price forecast: €48/t average phase 4, €89/t in 2030





# Agenda

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Carbon market outlook under a ‘fit for 55’ EU ETS

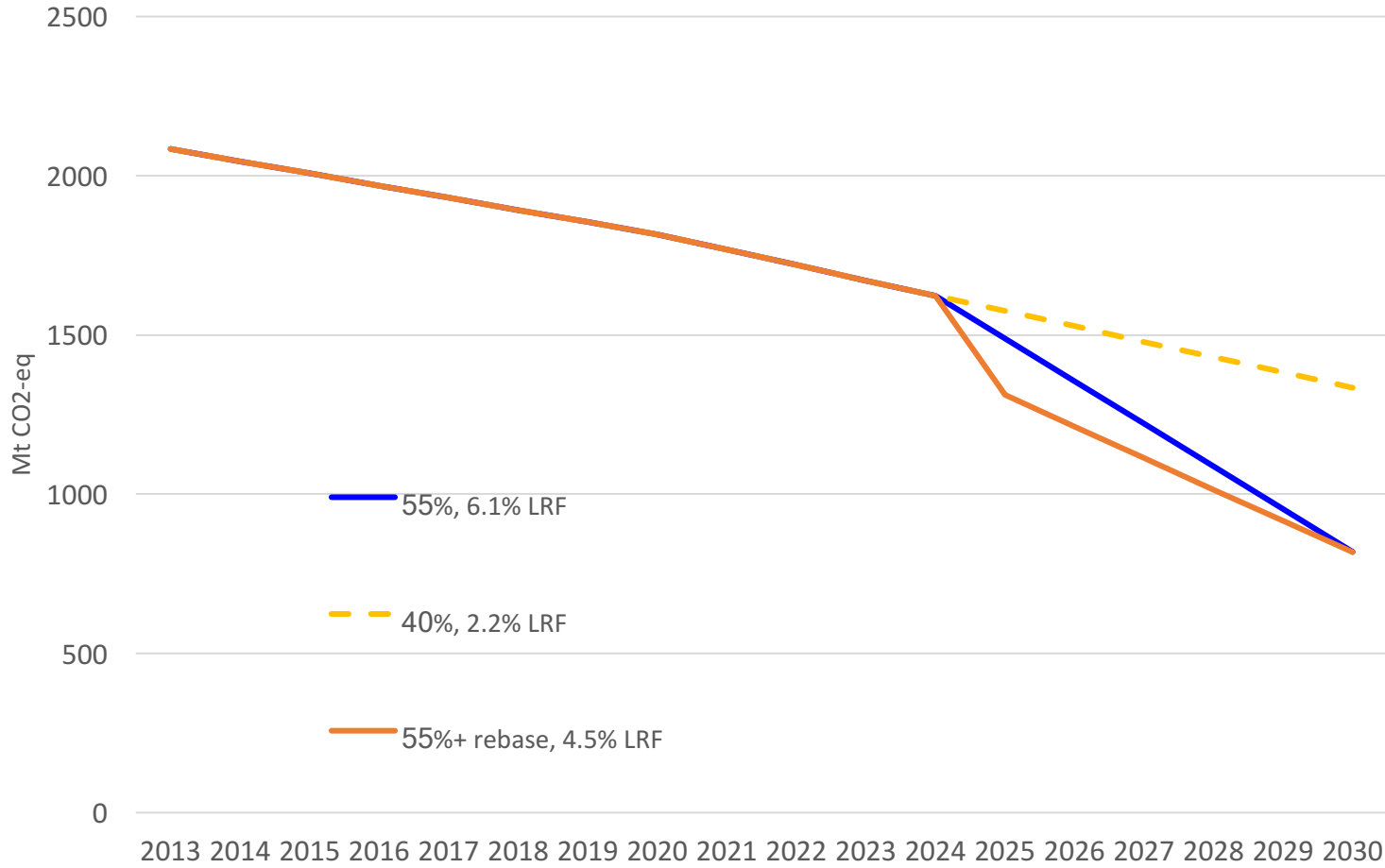


Significance of MSR and interplay with overall ETS policy design



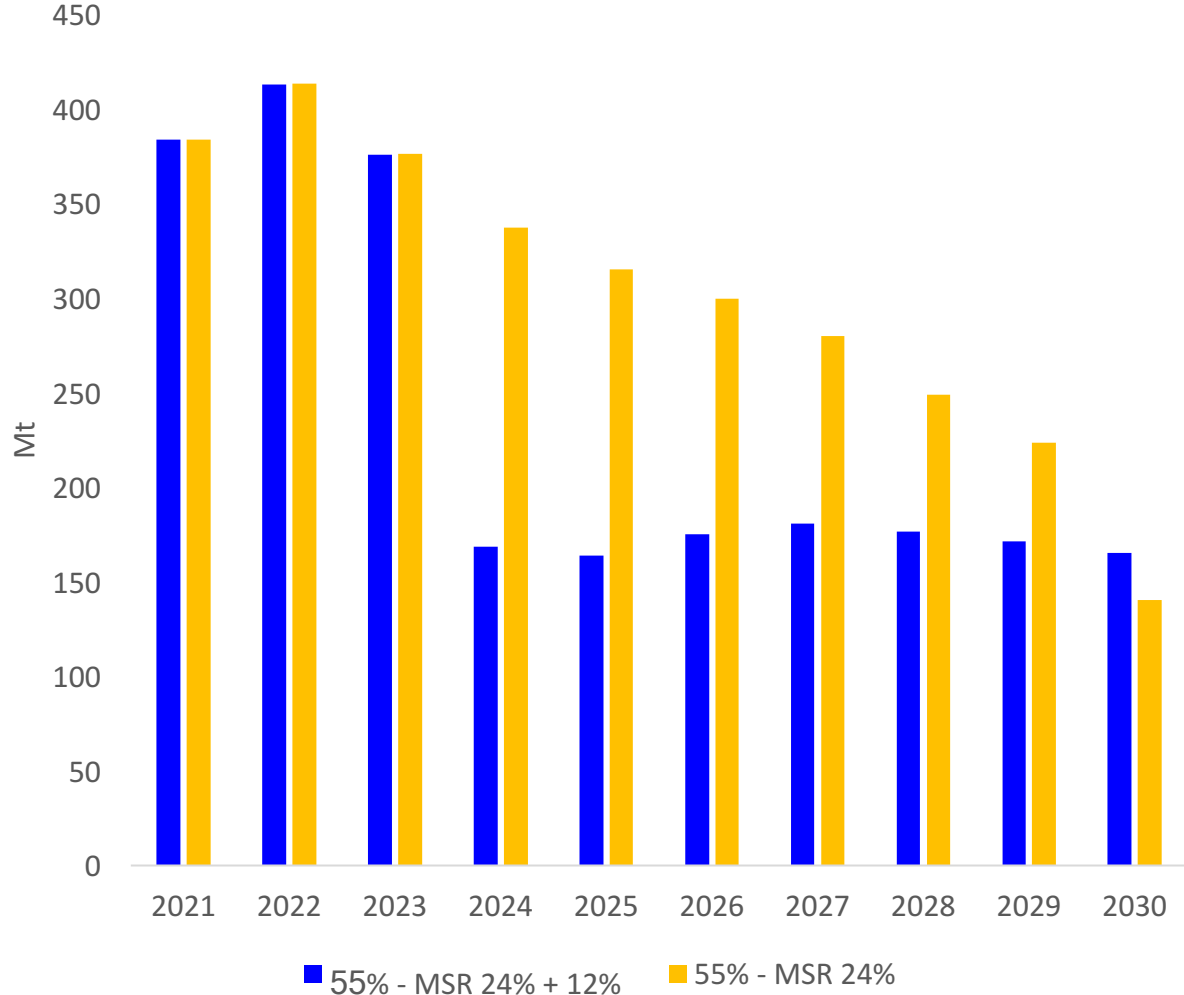
MSR invalidation – embedded ambition

# From 40% to 55% – what implications for the EU ETS cap?



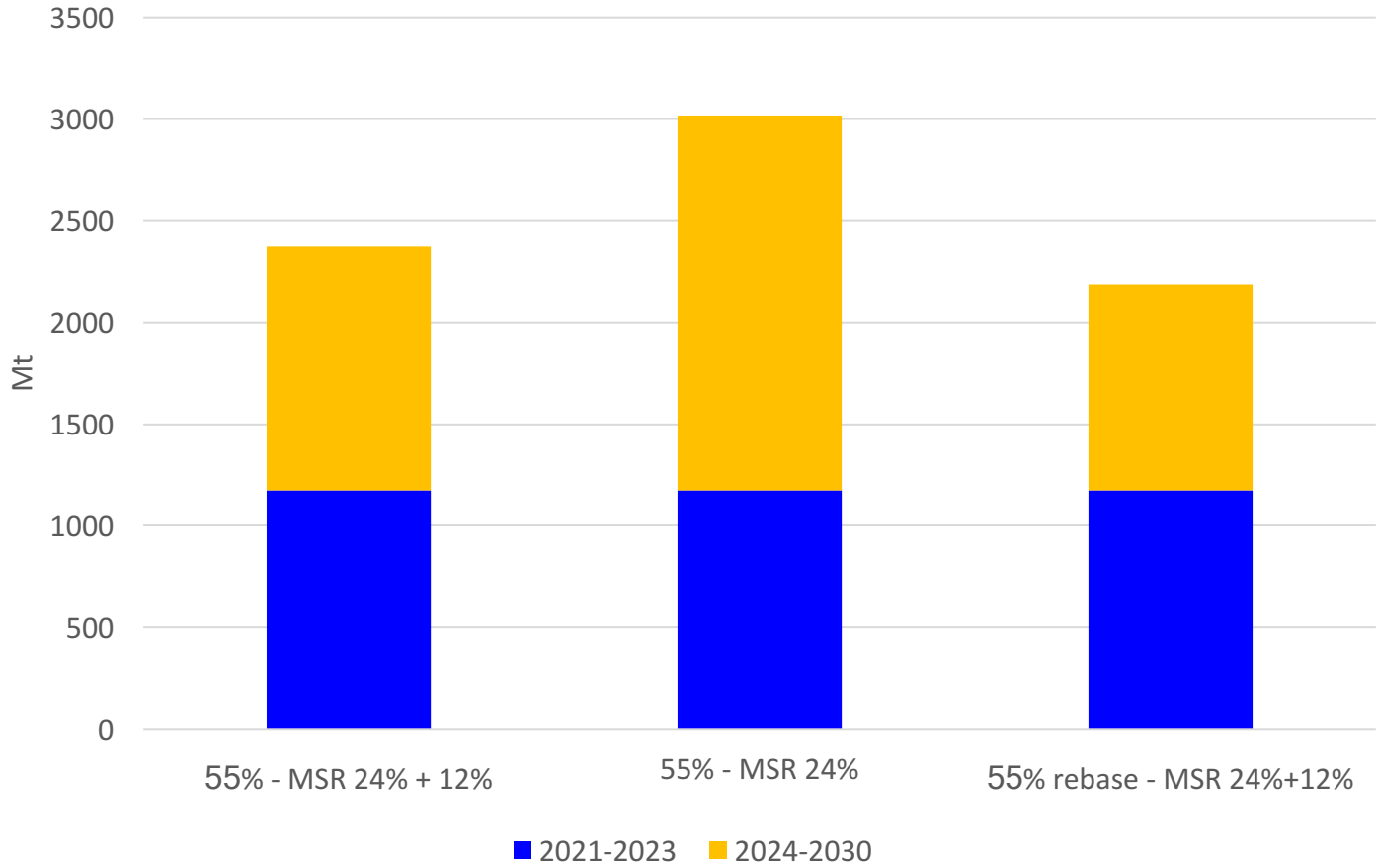
- How to tighten the cap?
- Linear Reduction Factor only or combined with one-off reduction of the cap?
- Mind the interplay with the MSR!

# Role for the Market Stability Reserve - a case for further tightening?



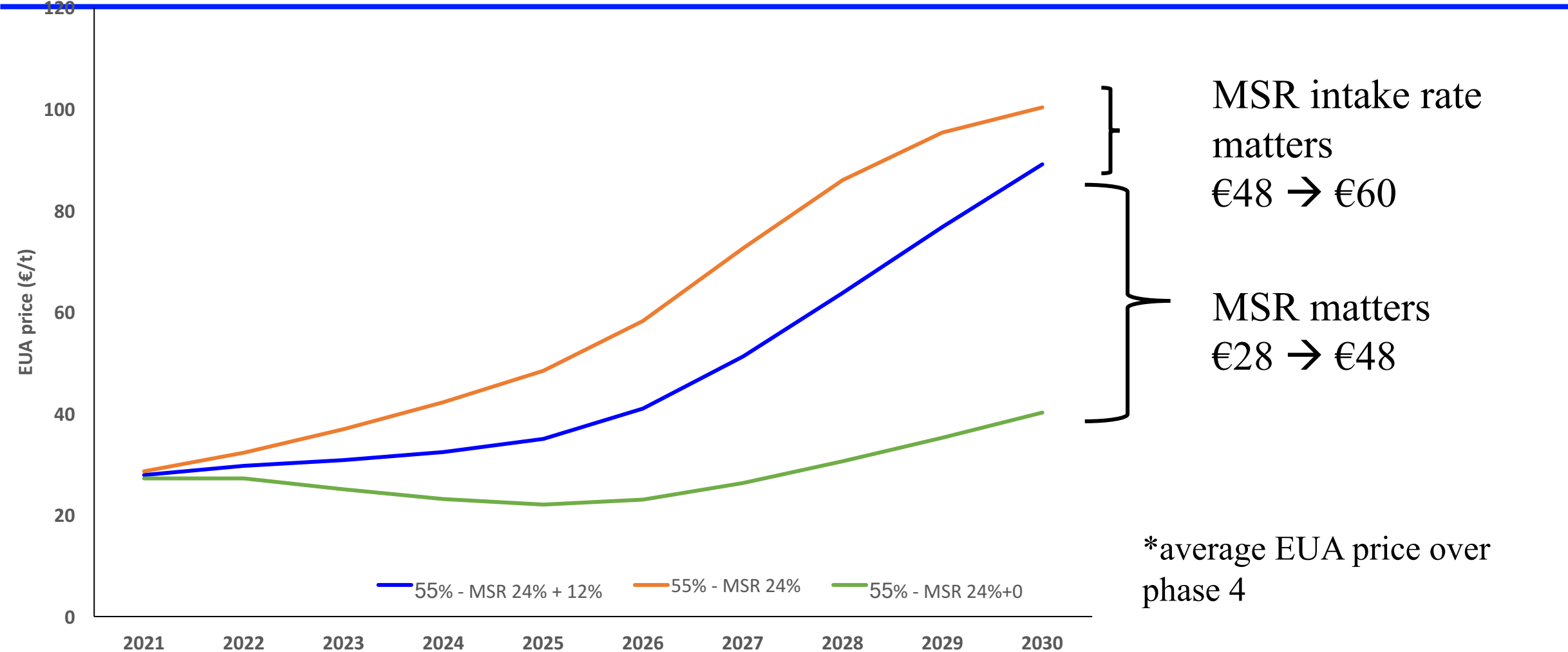
- MSR intake: 24% of surplus for five years, then 12% intake rate
- 2.4 Gt intake to MSR under current set-up, with 24% intake all the way 3 Gt soaked up by the reserve
- Market surplus stays above threshold level in all years
- MSR remains active and is an important balancing tool throughout hase 4

# Mind the interplay!



- MSR operation and role sensitive to how cap is set
- MSR operation in combination with rebasing:
  - Somewhat less prominent role
  - Avoid ‘double squeeze’ in year of rebase

# Climate ambition matters....but so does MSR design



\*average EUA price over phase 4

# Agenda



Carbon market outlook under a ‘fit for 55’ EU ETS

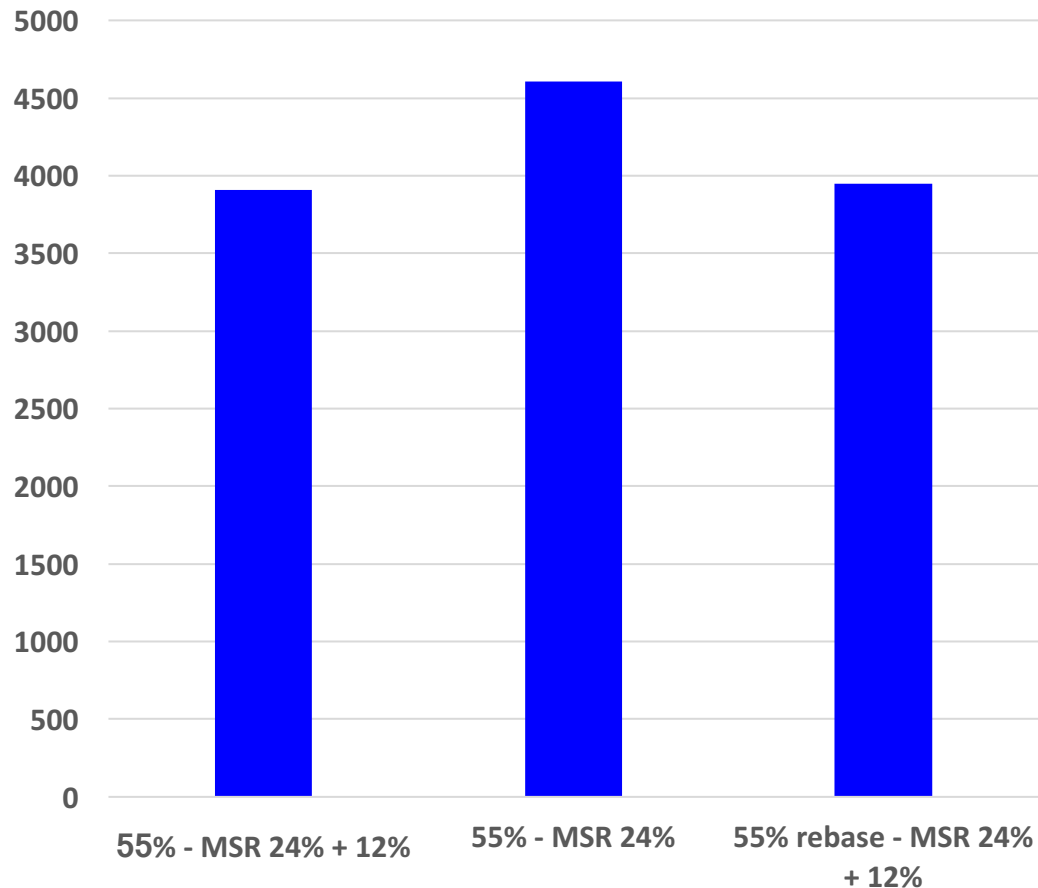


Significance of MSR and interplay with overall ETS policy design



MSR invalidation – embedded ambition

# MSR as a vehicle for higher ambition



- § Invalidation provision: From 2023 the reserve should not hold more than the previous year's auction volume.
  - Embeds higher ambition - MSR no longer a cap neutral instrument.
  - Invalidation volumes vary with different ETS and MSR set-up.
- Task for ETS review: Consider how invalidated allowances are treated in respect to a more ambitious climate target.



# Reflections on the future role of the MSR

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- Still a **significant role for MSR** as a market balancing tool until 2030 → What role for the MSR in a revised EU ETS, front or back seat?
- Market significance of the MSR **vary with policy choices for cap-setting** → Mind the interplay!
- Invalidation provision calls for **clarification on the purpose of the MSR** → Cap neutral market balancing tool or also a vehicle for higher ambition?
- KISS-principle at the heart of the review → Ensure **transparency** on interplay between MSR purpose & design and the broader ETS review.



# Thank you!

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