Green Trading Markets: Will 2005 Be The Breakthrough?

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Environmental financial risk is rising as an issue in corporate America as well as throughout the world. Environmental financial liabilities and the emergence of climate change risk have made companies extremely nervous on proceeding forward in market development with such near term uncertainty. For the past several years, corporate America has been trying to figure out the business case for GHG reductions. The business case is fairly simple either pay less now or pay more later. So we have companies beginning to analyze their risk and realize that there is a global issue and that they have got to do something about it.

Moreover, another driver behind the GHG market is that we now have institutional shareholders forcing corporations to acknowledge the environmental risk on their books. This has been done by pension funds mostly and is similar to the strategy that was taken in tobacco litigation. In effect, climate risk is rising as corporate financial issue and is becoming a fiduciary responsibility of corporates.

Emissions trading is one mechanism to accomplish much of these goals in a cost effective manner.

Green Trading is the triple convergence of capital markets and the environment and has come into the mainstream as a corporate financial issue. The intent was to capture both the problem and the solution as a financial trading means to ameliorate pollution. Building on the successful almost 10 year program in sulfur dioxide emissions trading in the US, Green Trading is the financial bridge to reduce greenhouse gas (GHG) pollution, increase renewable energy credit trading and the increase the use of energy efficiency (megawatt) trading through the use of financial markets. The long-term impact would be to reduce pollution in a cost effective manner and accelerate the introduction of more environmentally benign technologies. This would cause minimal economic disruption to the capital intensive energy industry as well as other industrial and agricultural sources of pollution.

In the US, we are getting an uplift from the marriage of CO2 injection for enhanced oil recovery and carbon sequestration. And the launch of the Chicago Climate Exchange (CCX) in September 2003 has seen over 60 companies sign up on a voluntary basis with many companies outside of CCX starting to look seriously at self-imposed caps.

In Europe, the EU ETS beginning January 1, 2005 will have close to six thousand facilities in the EU emissions trading system. Transactions have already occurred. represents both the participation of energy companies and banks, the key financial market makers that are needed.

We are witnessing a market transformation as the risk manager in some major corporations is now handling the GHG issue. While only about 200 trades with a notional value of $500 million have taken place globally for carbon trading, we are now positioned for the beginning of a liquid spot market instead of one off trades. Next year will be the breakthrough year with spot trading, high volumes, price indices, and advanced brokerage, similar to the power and gas markets, and we will see a growth in carbon finance.

Renewable energy credits (RECs) are going from promise to reality. The Texas REC market has been extremely active. But we are starting to see real market growth throughout the US, EU and Australia. There is also rising demand for green power among consumers which is driving this market forward.

Green Trading markets are now entering the hockey stick phase of market development with next year promising to accelerate the financial commoditization process. The US is well positioned to lead on environmental financial market development with its entrepreneurial culture, risk capital and knowledge base in trading. Don't count us out yet!

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