

IIGCC Response to EU Commission Consultation on structural options to strengthen the EU Emissions Trading System

The Institutional Investors Group on Climate Change (IIGCC), representing around 80 investors, with EUR7.5trillion in assets, is concerned about the potential for climate change to have major negative impacts on the economic systems in which we operate in and, in turn, on the assets in which we invest. We believe that clear, credible and long-term domestic and international policy frameworks are needed in order to shift the balance in favour of low-carbon investment opportunities, and generate a return on investment competitive with hydrocarbon-based alternatives.

We strongly support the EU's ambition to reduce carbon emissions as set out in its 2050 Roadmap. However, we are concerned that the current policy architecture established to deliver this ambition may not deliver the desired outcomes.

Our role as investors

The members of IIGCC are a major source of capital for investment in low carbon infrastructure, both directly through project finance, and indirectly through our investments in utility and infrastructure companies. The possible withdrawal of the banks from long-term risk finance only increases this role. We welcome the opportunity to invest in support of the EU 2050 Roadmap, but are concerned that we will not be able to do so because of inadequate policy support.

A central goal of EU climate policy in the coming decade should therefore be to ensure that low carbon projects, particularly in the electric power sector, generate a return on investment competitive with hydrocarbon-based alternatives. If the EU ETS is to be the central mechanism to achieve this, investors must be confident that it will provide a carbon price that is consistently high enough. Unfortunately, it looks unlikely to do so, and so structural reform is urgently required.

The current situation in the ETS

There is now a structural oversupply of permits which looks set to persist throughout Phase 3 and remain high up to 2020 and beyond. As a result analysts project a carbon price of €10 or less for this period. This is well below what is needed to make low-carbon power infrastructure investment competitive. Uncertainty about Europe's longer-term goals for the ETS and wider climate policy after 2020, further undermines confidence in the ETS's ability to provide the required price support.

Given the long-life time of infrastructure investment decisions, particularly in the electric power sector, investment decisions made in the next 15 years will have a decisive effect on Europe's ability to hit its 2050 targets. Uncertainty about climate and energy policy could have a chilling effect on all kinds of energy infrastructure investment, with energy security and economic growth implications.

The options proposed by the EU Commission

From an investor perspective, the ETS has not yet provided investors with the strong, long-term price signals that are necessary to commit to long-term low carbon investments.

Uncertainty that carbon prices will be sufficient to offer a competitive return on investment in less carbon intensive technologies is hampering major investment in these assets. The six options proposed by the EU all have some merits in this regard, and are, to varying extents, complementary with one another.

Many of the options proposed in the consultation, however, raise questions about the longer term design of the EU climate policy. It is difficult to discuss these options in isolation from the wider discussion about the EU's ambition post 2020. We look forward to discussing these and other options in the context of the wider debate on post 2020 ambition commencing with the publication of the Green Paper in April.

A reformed ETS is the most cost-effective approach

We believe that an effectively functioning ETS is the most cost efficient mechanism for achieving the low carbon transition in Europe and that it is compatible with a globally competitive European manufacturing sector.

The importance of post-2020 policy

Moving quickly to agreeing longer-term ambition is very important. While structural changes to the scheme in Phase 3 are necessary to restore investor confidence in the ETS, they are not sufficient. Given the investment time horizons for energy infrastructure, it is necessary to develop a clear view of shape of the ETS and wider EU ambition post-2020 before the middle of this decade.

IIGCC Membership February 2013

Amundi	HSBC Investments
AP1 (First Swedish National Pension Fund)	Hudson Clean Energy Partners
AP2 (Second Swedish National Pension Fund)	Impax Asset Management
AP3 (Third Swedish National Pension Fund)	Insight Investment
AP4 (Fourth Swedish National Pension Fund)	Joseph Rowntree Charitable Trust
APG Asset Management	Kent County Council Pension Fund
ATP	Kleinwort Benson Investors
Aviva Investors	Legal & General Investment Management
AXA Real Estate	London Borough of Hounslow Pension Fund
Baptist Union of Great Britain	London Borough of Islington Pension Fund
BBC Pension Trust	London Borough of Newham Pension Fund
Bedfordshire Pension Fund	London Pensions Fund Authority
BlackRock	Low Carbon Investors Pte Ltd
BMS World Mission	Mayfair Capital Investment Management
BNP Paribas Investment Partners	Merseyside Pension Fund
BT Pension Scheme	Mercer Global Investments Europe Limited
CB Richard Ellis	Mn Services
CCLA Investment Management	Nordea Investment Funds
Central Finance Board of the Methodist Church	Osmosis Investment Management
CF Partners (UK) LLP	PGGM Investments
Church Commissioners for England	PKA
Church of Sweden	Platina Partners
Climate Change Capital	PRUPIM
Co-operative Asset Management	Railpen Investments
Corporation of London Pension Fund	Robeco
Dragon Capital Group Ltd.	Sampension
Earth Capital Partners	Sarasin & Partners LLP
Environment Agency Pension Fund	Scottish Widows Investment Partnership
Environmental Technologies Fund	South Yorkshire Pensions Authority
ERAFP	Temporis Capital
Ethos Foundation	The Church of England Pensions Board
F&C Management Ltd	The Church in Wales
Five Oceans Asset Management	The Roman Catholic Diocese of Plymouth
Generation Investment Management LLP	The Roman Catholic Diocese of Portsmouth
Greater Manchester Pension Fund	The Roman Catholic Diocese of Salford
Grosvenor Fund Management	United Reformed Church
Henderson Global Investors	Universities Superannuation Scheme
Hermes	West Midlands Metropolitan Authorities Pension Fund
Hermes GPE LLP	West Yorkshire Pension Fund
HgCapital	William Leech Charitable Trust