

4 April 2008



**CARBON MARKET
SOLUTIONS**

Carbon Market Workshop

**Town Hall , Wellington
4 April 2008**

**Brokerage Experiences in Trading Carbon
Internationally**

**Wayne King
Carbon Market Solutions Ltd**

Wayne@carbonmarketsolutions.com

- New Zealand carbon advisory, brokerage, and trading company
- Founded in 2003
- Offices in Auckland, Hamilton, Wellington, Moscow, London, Paris
- Key personnel with over 35 years of commercial experience related to climate change, trading, and corporate finance
 - ❖ Richard Burns – Ex Senior Partner , PwC London (Corporate Finance)
 - ❖ John O'Brien – Carbon finance specialist with extensive experience in trading in Europe (London & Moscow)
 - ❖ Wayne King – Forestry background. Over 12 years climate change experience in Asia-Pacific with World Bank/Asian Dev Bank

CMS has a successful track record in carbon deals from New Zealand



The CMS track record includes:



2005 – Sale of 149,000 ERUs from PNCC to Austria – 2nd ever Kiwi JI deal



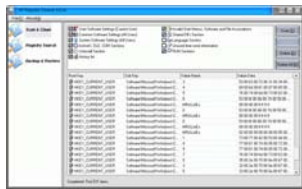
2006 – Sale of 200,000 ERUs from Christchurch City Council to British Gas



2007 – Sale of up to 650,000 ERUs from Meridian Energy to Switzerland



2007 – Sale of VERs to Pacific Blue to offset air-travel between NZ and Aus



2008 – World's first ever transaction between National Kyoto Registries from Switzerland to New Zealand for Indian Gold Standard CERs.

What makes CMS unique?

- We have been doing carbon deals since 2005, gives us unique experience in NZ;
- We do not represent brokers in Europe we work directly with companies;
- We do not represent international oil companies, large corporates or foreign governments;
- We are in the business of carbon trading to get the 'best deal' for New Zealand companies. When you win, we win.

What brokerage role does CMS have:

- Has specialist knowledge and experiences in the carbon markets both internationally and domestically
- Provides a clear and focused benefit only to a New Zealand client
- Maximises an opportunity to the NZ client
- Provides for a cost effective service in a new industry in NZ
- Brings credibility and recognition to the table for engagement, ie, we have a track record
- Provides risk analysis and advice on the international or domestic carbon markets, including a carbon perspective on policies, methodologies, validation/verification
- Provides analysis and advice on counterparty risk

Experiences in Advising JI deals from New Zealand



Issue	
Country Risk	New Zealand country risk generally viewed as low. Leads to a pricing premium.
Project Risk	Buyers prefer purchasing from projects with project finance in place and with strong counterparties with strong balance sheets
CDM v JI	Many companies prefer CERs over ERUs as they are better understood and viewed as less risky
Guaranteed Delivery	Buyers generally prefer guaranteed delivery of a firm volume and with projects with approved UN methodologies
Time Frame	It can take a long time to close deals up to 12 months due to time needed to prepare PDD, undertake validation (previously only 1 validator), obtain government approvals, and for buyer due diligence
Governing Law	Governing law of the contract is often an issue. New Zealand companies often want New Zealand law whereas international buyers do not. UK law is often a good compromise.

Why do NZ companies forward sell ERUs & not wait for the Spot Market

- Companies needing cash today can sometimes secure an up-front payment of up to 50% of the transaction value
- A forward sale locks in a forward price over a period of 5 years with secure cash flow every year;
- Companies whose core business is not carbon trading can focus on their core business;
- Spot-market for carbon very volatile and risky with prices ranging from Nz\$1.00 to Nz\$60 for EU Allowances (for example) so to wait until delivery and sell everything is a very risky strategy;

What are the lessons then for New Zealand companies who want to buy units in the international market?

- Great deals take time and require a lot of due diligence
- Price is not everything: You need to also examine the counterparty credit risk. What is the risk of the counterparty not delivering guaranteed CERs?
- Over 120 companies in London are selling guaranteed CERs. How many will be around in 2012? Know your seller is critical.
- Share prices of AIM listed carbon trading companies such as EcoSecurities, Trading Emissions plc, Econergy, and Camco are all down significantly.
- One AIM listed company which used to sell guaranteed CERs (Agcert) from pig-farm projects is now bankrupt.

Carbon Credit Units and Difficulty to Get Hold of Them



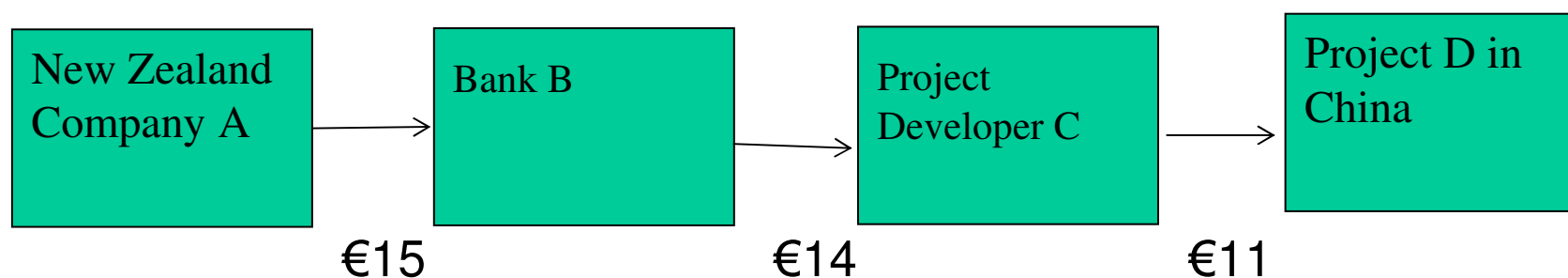
Units	Price Range Today	Main Countries	Ease to Obtain
NZUs	To be determined *	New Zealand	Difficult as not yet issued
AAUs	€10-16	Russia, Ukraine, Eastern Europe	Extremely Difficult
CERs (guaranteed)	€15 - 16	China, India, Brazil	Easy
CERs (not guaranteed)	€8 – 13	China, India, Brazil	More Difficult
ERUs	€7 – 10	Russia, Ukraine, Eastern Europe	More Difficult

What will the price of an NZU be? NZU price should not be higher than international price or else companies would simply source the Units from the overseas market. We expect Nz\$15-30 per NZU.

Who you buy from is critically important:



Here is a hypothetical example of a carbon deal gone badly wrong:



- New Zealand company A buys guaranteed delivery from Bank B
- Bank B buys guaranteed delivery from Project Developer C
- Project Developer C obtains guaranteed delivery from Project D
- Project D fails to deliver
- Result: New Zealand Company A has a problem. Bank B's guaranteed delivery was contingent on the guarantee from Developer C whose guarantee was contingent on Project D. A litigates B for non-delivery, B litigates C, C litigates D and D claims 'force-majeure'.

What about the Carbon Exchanges being developed in New Zealand? (TZ1 and Regi)

- Exchanges are important as they bring liquidity and price discovery to the market.
- However, exchanges need large numbers of participants and standardized commodities to work properly
- In the EU ETS, approximately 50% of the carbon transactions are bi-lateral deals whereas the other 50% are through exchanges. We expect something similar to develop in New Zealand.
- 81% of trades in the European Union went through one exchange, the European Climate Exchange. Is New Zealand big enough for more than one exchange?

In Conclusion what are the key lessons for New Zealand companies?

- ✓ Good carbon deals take time to negotiate;
- ✓ Price is Not Everything;
- ✓ Understanding counterparty credit risk in contracts and what happens when there is failure to deliver is critical;
- ✓ Exchanges play an important role in bringing liquidity to the market;
- ✓ The New Zealand carbon market is growing and is here to stay!

Thank You!

Contact Information

- Wayne King
- Carbon Market Solutions Ltd
- Main Office: KCSM House
- 187 Peachgrove Road
- Hamilton
- New Zealand
- Tel 07 853 6220 (Hamilton Office)
- Email: Wayne@carbonmarketsolutions.com