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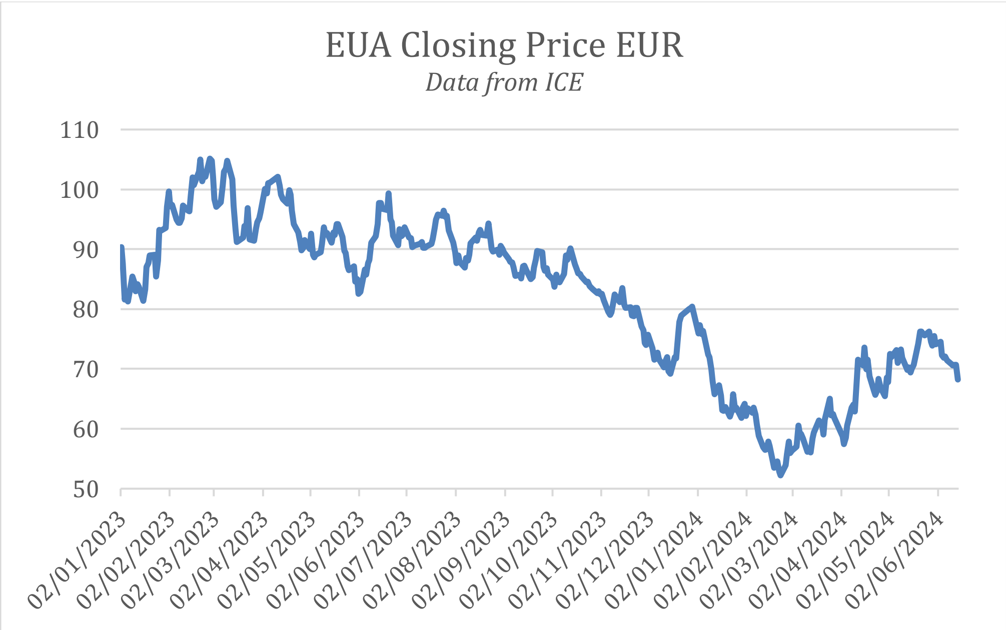
FIS Consultancy for Shipping in the EU Emissions Trading System (EU ETS)

EUA WEEKLY REPORT 17/06/24

In brief: Emissions decouple from gas on options pin

The Dec24 contract closed the week down EUR3.11 (4.4%) at EUR68.28. Open interest climbed to 684k nearing its year-to-date peak of 705k on 18 December. Volume came in at 182k up from 171k the week prior. The slide in EU emissions occurred despite EU gas (TTF) prices rising 6.8% following ongoing supply concerns. This represents a significant break from what has typically been a correlation of over 90% in recent months. Traders speculate the break in correlation owes to the June options expiry on Wednesday, with the EUR70 and EUR65 call options pinning the market as traders unwind hedges. They further speculate, that should TTF prices remain high, we could see a surge in EUA prices to resume the correlation following the options expiry. Tapering this, we have also seen slower growth in long positions by investment funds over past two weeks. Moves to the right in EU politics appear to have impacted sentiment, but any real impact could be limited in the medium term (more below). Our outlook for the second half of the week is bullish.



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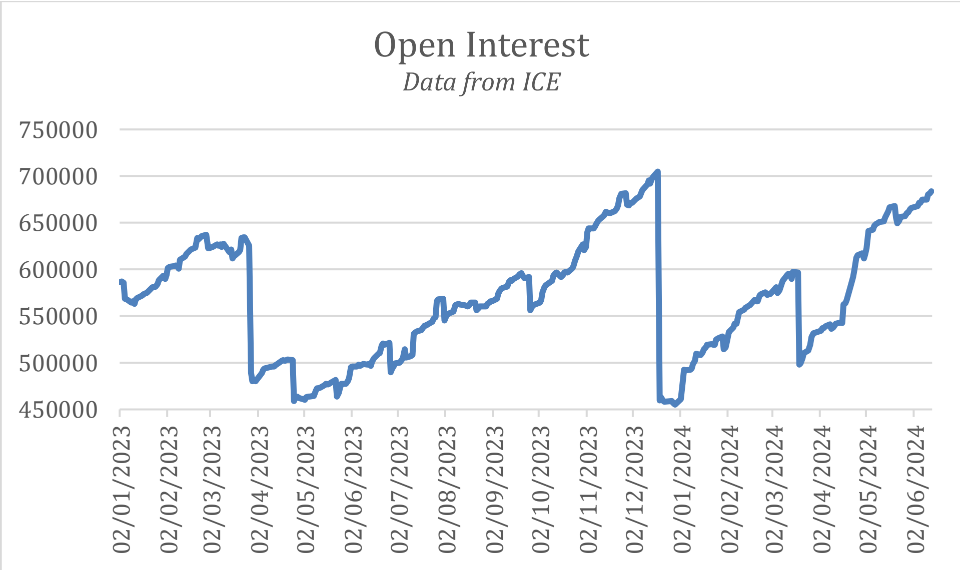
What happened? (Price movements)

- The week opened with bearish sentiment in EU carbon following strong results for far-right parties in the EU parliamentary elections. EUAs lost 0.8% through the day to close at EUR70.80. Meanwhile, TTF settled up over 3% on the day and after losing over 2% in the morning
- Tuesday saw a continued gentle downward trend. The front-December contract dropped below the EUR70 mark in the morning before rebounding and settling at EUR70.63, marking a 0.2% loss on the day
- On Wednesday December EUAs again dropped below EUR70 before climbing modestly through the day tracking TTF natural gas. Prices ebbed back a touch before close to gain 0.2% on the day at EUR70.74. On Wednesday, the Commitment of Trader's (CoT) report revealed funds increased their net short position for the second week. This time by 22.6%
- Thursday saw prices fall back just three cents to close at EUR70.71. While TTF prices gained, EUAs rose through the day before falling off into close
- Friday saw heavy selling through the afternoon, which many speculated to be hedge-unwinding ahead of Wednesday's June options expiry. Prices were pushed down to EUR68.28, a 3.4% loss on the day and 4.4% on the week.

Why? (Market drivers)

- Commitment of Trader's (CoT) Report: CoT data last Wednesday revealed investment funds increased their net short position by 1.8 Mt (22.6%) to 9.9 Mt the week ending 7 June. This marked the second week in a row of rebuilding the net short position
- TTF gas:
    - EU natural gas prices saw a further bump following news Uniper formally ended ties with Gazprom. The news comes amid a rise in European imports of Russian gas despite several EU countries pushing to impose sanctions on them
    - Demand for gas in Europe remains relatively weak, with storage levels near record highs for this time of year
    - An outage at Chevron's Wheatstone facility in Australia was extended to 27 June

- TTF price further spiked on Friday following news of a Russian attack on a Ukrainian gas transshipment point
- Concerns over strong Asian LNG demand persist and continue to drive EU gas prices. Asian spot LNG prices hit a six-month high today following reduced demand in India, higher forecast temperatures in north-east Asia and suspended production at the Chevron Wheatstone facility.



- The expiry of the June options on 19 June is playing a strong role on the direction of carbon, with traders speculating the EUR65 and 70 call options are pinning prices
- Recent EU parliamentary elections saw gains in right wing parties and losses in green representation. The result was perceived as a reduction in climate ambition. However, analysts point out that many current EU climate laws run to 2030 and are unlikely to be easily amended in the short term, if at all.

What's coming up? (Trends and key developments)

Macro: The outlook for EUAs in the coming months is influenced by stable Eurozone economic growth projected at 1.6% for 2024, increased industrial output, moderated inflation, and stable energy prices, particularly natural gas. Despite some global economic headwinds, such as disappointing factory output from China and falling U.S.

consumer sentiment, the Eurozone's industrial production is expected to rise, driving higher EUA demand. Geopolitical tensions, especially involving Russia-Ukraine and the Middle East, continue to impact energy supplies, but Europe's diversification efforts are providing some stability. Overall, the combination of these factors suggests a potential increase in EUA demand as the Eurozone economy recovers and industrial activities expand

EU Gas: Dutch TTF gas prices are expected to remain stable to slightly bullish in the coming week due to rising Asian LNG prices, driven by strong cooling demand in India and higher temperatures forecasted in northeast Asia. European gas prices are supported by supply disruptions from Chevron's Australian facility, but high storage levels and low European demand may temper price increases. Additionally, increased LNG freight rates and an open inter-basin arbitrage drawing LNG to Asia further influence the market. While global economic factors and warmer European weather could impact demand, stable industrial activity in Europe supports continued gas consumption.

Weather: In the coming weeks, Europe is expected to experience unusually high temperatures and potential heatwaves, particularly in Germany, the Nordics, and southwestern regions like Spain. This weather pattern is influenced by the transition from El Niño to La Niña conditions, as well as record-high sea surface temperatures in the North Atlantic, which may enhance heatwaves and drive stable high-pressure systems. These factors suggest a continuation of the recent trend of warmer-than-average conditions across the continent.

Sources
All pricing data taken from Intercontinental Exchange (ICE) and European Energy Exchange (EEX)

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