

### 2005 compliance: Official shoot, shaky references

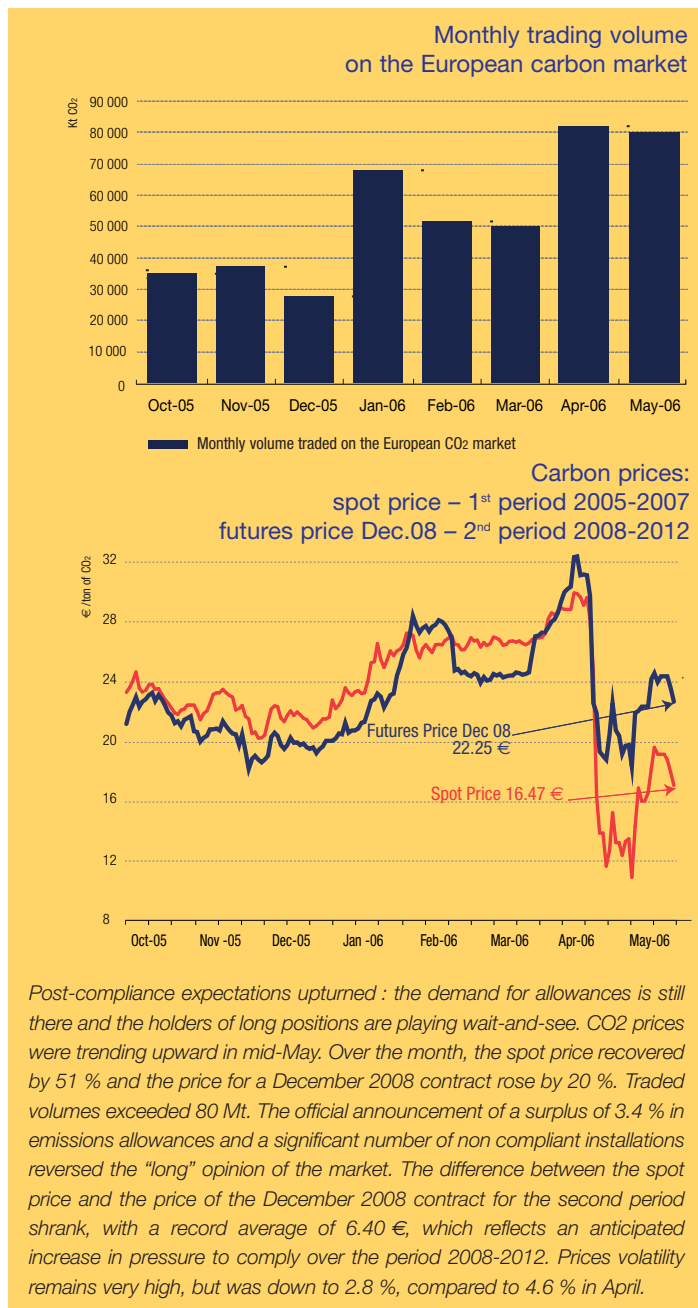
On May 15, after two weeks of waiting and numerous statements concerning the compliance of nine countries, the European Commission made public the 2005 emissions of installations for twenty-one of the twenty-five member States, as four countries still do not have an operational register. For these twenty-one countries, owning 88% of the European allowances, the market proved to be long overall by 62.8 Mt. These surplus allowances represent only 3.4 %, which is less than initially projected.

The allowance price reacted very strongly to the anticipated disclosure of compliance data by some countries. Within ten days, nine of the twenty-one countries reported their overall positions before the official deadline of May 15: the allowance spot price dropped by 65 % between April 24 and May 12, and the price of the 2008 contract fell by 42 %. This decline must also be considered in the context of international financial markets, where investors turned away from numerous commodities considered "risky".

Since May 15, and for the first time since the market was created, players had common access to the carbon emissions data of installations, which resulted in a partial recovery in prices. The spot price rebounded almost 50 % from its lowest level, and the price of the 2008 contract recovered by 25 %. Short traders were still able to buy the allowances they needed to certify their first compliance, and other traders took advantage of low prices to ensure their second compliance. Symmetrically, the structurally long traders had an incentive to wait for a recovery in prices to sell their allowances. However, the disclosure of compliance data did not give the market sufficient information to limit its instability. Price volatility in late May was significantly greater than observed over the first eleven months.

The compliance figures reflect sharp disparities among countries and sectors: according to our initial estimates in the 5 largest countries (excluding Poland), representing more than 65% of the first period allowances cap, the electric power sector was short overall by 7 %, i.e. 45 Mt, principally in the United Kingdom and in Italy. The steel sector was long by 38 %, i.e. 35 Mt, essentially in Italy and in Germany. The oil sector was long by 16 %, i.e. 15 Mt, mainly in Germany. These different positions among countries and sectors may fuel certain tensions in the present preparation of the second national allocation plan.

Finally we can derive two major lessons from this first experience in the compliance verification. On the operational level, the operation has been successful. More than 95 % of



*Post-compliance expectations upturned : the demand for allowances is still there and the holders of long positions are playing wait-and-see. CO<sub>2</sub> prices were trending upward in mid-May. Over the month, the spot price recovered by 51 % and the price for a December 2008 contract rose by 20 %. Traded volumes exceeded 80 Mt. The official announcement of a surplus of 3.4 % in emissions allowances and a significant number of non compliant installations reversed the "long" opinion of the market. The difference between the spot price and the price of the December 2008 contract for the second period shrank, with a record average of 6.40 €, which reflects an anticipated increase in pressure to comply over the period 2008-2012. Prices volatility remains very high, but was down to 2.8 %, compared to 4.6 % in April.*

Source: Powernext Carbon, ECX, Pointcarbon

the 9,420 installations in question have in fact measured and declared their actual 2005 emissions last April 30, the market reacting to this information. On the level of the information communicated to the market, improvements still have to be made both in the publication process and in the clearness of the information published. It is essential to provide uncontested data on emissions, and we can only hope for the future greater transparency and harmonization between countries in their methods of reporting.

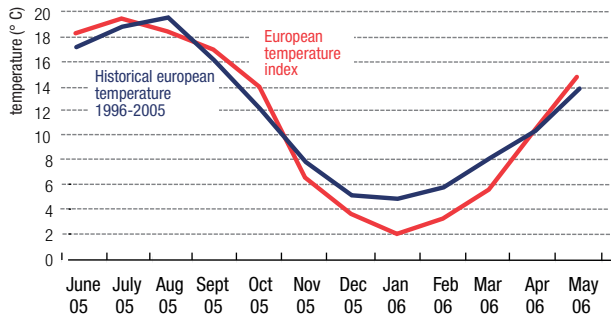
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## European temperature index (°C)

Average of Powernext Weather indices\* – France, Germany, UK and Spain – weighted by the allowances allocated to each country.

	April	May
Monthly average (°C) - 2006	10.4	14.8
Monthly average (°C) - 1996-2005	10.4	14.0
Monthly maximum (°C) - 2006	6.3	10.8
Monthly minimum (°C) - 2006	14.7	17.4

Source: Climat Task Force - Caisse des Dépôts

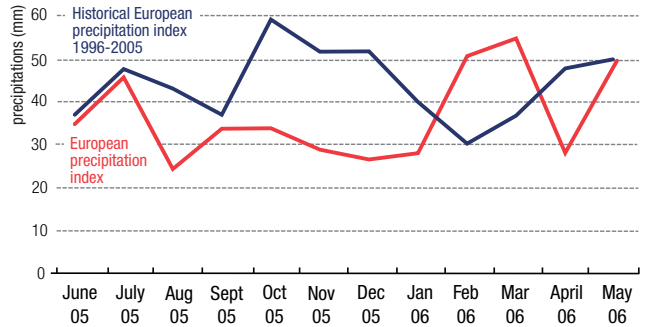


## European precipitation index (mm)

Average of precipitation indices for Paris, Berlin, London and Madrid, weighted by the hydroelectric share in each country's electric power mix.

	April	May
Monthly precipitation - 2006	29	50
Monthly precipitation - 1996-2005	49	50
Cumulative over 12 months	436	447
Cumulative over 12 months 1996-2005	541	540

Source: Climat Task Force - Caisse des Dépôts



On average, European climatic conditions in May were in line with seasonal normals, although the latter part of the month was characterized by surprisingly low temperatures. Overall, precipitation came back. The water situation in Europe is therefore improving slowly, but remains, in terms of annual totals, far below the ten-year average. The monthly European precipitation index, however, masks some diversity in trends, since precipitation has been heavy primarily in the Alps and over the Balkans, where snowfall and rainfall have swollen rivers and lakes. In Scandinavia, the reservoirs' level rose slowly, reaching 45 % at the end of the month. On the other hand, precipitation has been below seasonal normals in Spain for the second consecutive month, which may threaten the country's hydro-electric production.

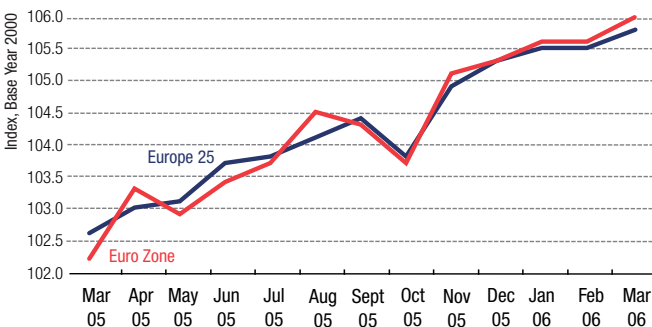
\* The Powernext Weather indexes are defined on the basis of average temperatures, weighted by the population of the representative regions that make up each country.

## European industry production index

Index of production of all industries, excluding construction (Base Year 2000)

	March index 2006	Monthly variation (%)	Variation/12 months (%)
Europe 25	105.8	+ 0.3	+ 3.7
Euro zone	106.0	+ 0.4	+ 3.8

Source: Eurostat

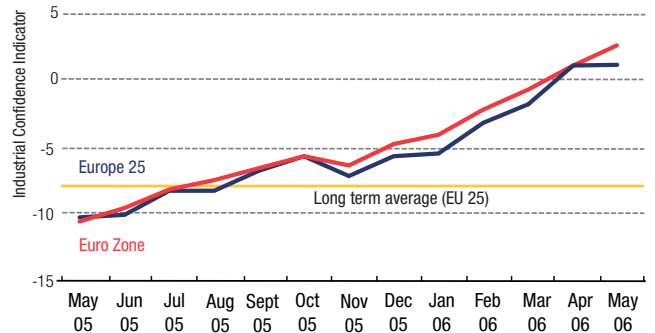


## Opinion of Business Leaders (Balance of responses)

Industrial Confidence Indicator  
Balance of responses

	April 2006	May 2006
Europe 25	1	1
Euro zone	1	2

Source: Eurostat



The recovery signs noted in the first quarter remain steady, with a further increase in industrial production in March, by 0.4 % in the Euro Zone and +0.3% in the EU of 25. The declines in industrial production recorded in Germany (-1.7 %) and in Italy (-0.1 %) do not appear to have had an adverse affect on the morale of European industrial leaders. The European industrial confidence index remains positive, and was even up for the Euro Zone, returning to its May 2000 level. The decline in new orders for European industry overall observed in March, by 2.4 % in the Euro Zone and 1.7% in the EU of 25, does not appear likely to hold back the upward trend of industrial production. In May, production forecasts improved and inventories of finished products were being re-absorbed. This projected growth of industrial production should have consequences on the demand for allowances and especially by electric power companies, whose output increased by 3.2 % in the Euro Zone and 1.4 % in the EU of 25 over the past twelve months.

## Energy prices

	April 2006	April 2006
Average closing price		
British natural gas NBP ICE Futures Month Ahead	59.92 €/BTU	52.91 €/BTU
Amsterdam coal CIF ARA Month Ahead	51.25 €/t	46.67 €/t
Powernext Futures™ month ahead	Base	39.29 €/MWh
	Pointe	58.74 €/MWh
Difference between the price of electricity and the price of natural gas, corrected for the price of CO <sub>2</sub> : Clean Spark spread	15.24 €/MWh	22.10 €/MWh
Difference between the price of electricity and the price of coal, corrected for the price of CO <sub>2</sub> : Clean Dark spread	10.57 €/MWh	24.24 €/MWh
Price of the CO <sub>2</sub> quota that establishes equilibrium between the prices of coal and natural gas	21.17 €	18.02 €

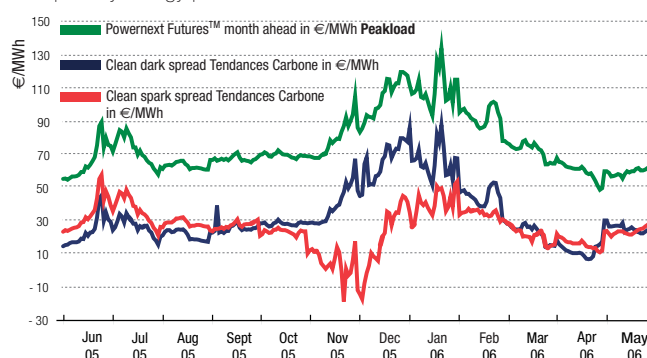
Source: Reuters, Powernext, Climat Task Force - Caisse des Dépôts

Electricity prices tracked the ups and downs observed in the price of allowances only to a very limited degree. Although the spot price of CO<sub>2</sub> fell by 47 % between April 24 and May 15 following the announcements of surplus allowances by the member States, peak prices of electricity held steady over the same period: +0.10 %. As the month neared its end, the difference between 2007 and 2008 electricity futures contracts decreased, and the price of 2008 CO<sub>2</sub> futures contracts recovered pending the more restrictive national allocation plans for the second period. Primary energy prices were not as volatile. In May, the price of natural gas fell by 12 % and the price of coal fell by 8 % while the price of Brent crude remained stable. The drop in the price of allowances contributed to a reversal of clean spreads in favour of coal, as the difference narrowed because the drop in natural gas prices was greater than the drop in the price of coal.

Primary energy prices



Price of electricity and price difference between electricity and primary energy prices



## European Union: National Allocation Plans, National Registries and CO<sub>2</sub> Allowances

Country	National share of EUAs allocated in Europe	No. of 2005 EUAs in MtCO <sub>2</sub> (excluding réserves)	Announced 2005 emissions (1) (Mt CO <sub>2</sub> )	2005 Position	2005 Position (relative value)
Germany	23.6 %	495.0	473.7	21.3	4.3 %
Italy	10.3 %	215.7	215.4	0.3	0.1 %
<b>United Kingdom</b>	<b>9.8 %</b>	<b>206.0</b>	<b>242.4</b>	<b>- 36.4</b>	<b>- 17.7 %</b>
<b>Spain</b>	<b>8.2 %</b>	<b>172.0</b>	<b>181.1</b>	<b>- 9.1</b>	<b>- 5.3 %</b>
France	7.2 %	150.2	131.1	19.1	12.7 %
Nordic Countries (2)	4.9 %	104.2	78.5	25.7	24.7 %
New EU Member Countries (3)	3.5 %	73.3	56.0	17.2	23.5 %
<b>Austria</b>	<b>1.6 %</b>	<b>32.4</b>	<b>33.4</b>	<b>- 1.0</b>	<b>- 3.0 %</b>
<b>Ireland</b>	<b>1.0 %</b>	<b>19.2</b>	<b>22.4</b>	<b>- 3.2</b>	<b>- 16.4 %</b>
Other States (4)	18.1 %	380.1	351.3	28.8	7.6 %
<b>TOTAL (5)</b>	<b>100 %</b>	<b>1,848.1</b>	<b>1,785.3</b>	<b>62.8</b>	<b>3.4 %</b>

(1) Source: CITL (Community Independent Transaction Log) or European Commission press release.

(2) Finland, Denmark, Sweden.

(3) Estonia, Latvia, Lithuania, Slovakia, Slovenia.

(4) Czech Republic, Netherlands, Greece, Belgium, Portugal, Hungary.

(5) Excluding Poland, Cyprus, Luxembourg and Malta, which have not yet made public their emissions.

Source: Climat Task Force - Caisse des Dépôts

The 2005 emissions of the twenty-one States were announced on May 15, with a surplus over 3.4 %. The allowances allocated to these countries were 62.8 Mt higher than the declared emissions. The positions are not uniform: the United Kingdom, with its strict national allocation plan, is very short in allowances (-36.4 Mt), and is followed at some distance by Spain (-9.1), Ireland (-3.2) and Austria (-1.0). The countries with the longest positions are the group of Nordic countries (25.7), which benefits a strong hydroelectric production, Germany (21.3), France (19.1), the new member States (17.2) and the Czech Republic (14.6) which took advantage of their hot air situation. The degree to which the market is long remains uncertain, however, because 12 % of the European allowances have still not been issued on some national registers, especially in Poland (11 % of the allowances).

# Dashboard

## CO2 Markets

			Dec - 05	Jan - 06	Feb - 06	March - 06	April - 06	May - 06	
Spot market (Powernext carbon)	Average closing price in €	Low price traded	19.80	21.77	25.25	26.00	13.19	10.14	
		Average price traded	21.11	23.92	26.19	26.37	26.71	14.81	
		High price traded	22.40	26.23	26.97	26.68	29.75	19.10	
	Volume in t	Daily average	64,810	89,364	84,350	100,304	115,778	143,158	
		Total monthly	1,361,000	1,966,000	1,687,000	2,307,000	2,084,000	2,720,000	
Futures market (ECX)	Dec 2006	Average closing price in €	Low price traded	20.35	22.30	26.15	26.70	13.55	9.30
			Average price traded	21.66	24.70	26.88	27.07	27.18	15.09
			High price traded	22.80	27.10	27.95	27.50	30.45	19.65
	Dec 2007	Average closing price in €	Low price traded	20.55	22.75	27.15	27.60	14.25	9.80
			Average price traded	22.07	25.34	27.80	28.03	28.14	15.73
			High price traded	22.90	27.90	28.85	28.45	31.50	20.45
	Dec 2008	Average closing price in €	Low price traded	18.25	19.70	24.20	23.55	18.80	17.80
			Average price traded	19.24	21.58	26.60	24.33	28.09	21.26
			High price traded	20.10	24.65	28.15	26.80	32.25	24.20
	Volume in t	Daily average	615,400	1,618,619	1,331,900	970,913	2,285,889	2,426,409	
		Total monthly	12,308,000	33,991,000	26,638,000	22,331,000	41,146,000	53,381,000	
	Total european market volume in t (Pointcarbon)			27,900,000	67,851,000	51,598,000	50,167,000	81,881,000	80,605,000

Source: Powernext Carbon, ECX, Pointcarbon

## Climate

> Temperatures (°C)	June-05	July-05	Aug-05	Sept-05	Oct-05	Nov-05	Dec-05	Jan-06	Feb-06	Mar-06	April-06	May-06
Germany - monthly average	17.4	19.3	16.9	16.3	12.1	5.0	1.4	-1.6	0.6	2.6	9.1	14.1
Germany - difference monthly and decennial average	0.3	0.9	-2.3	1.5	1.8	-0.1	-0.3	-2.7	-2.1	-3.1	-0.3	0.1
Spain - monthly average	24.0	25.2	24.7	21.6	18.5	12.2	9.1	8.4	9.2	13.4	15.9	19.8
Spain - difference monthly and decennial average	1.5	1.0	0.0	-0.1	0.5	-0.7	-1.3	-1.6	-1.5	0.1	1.0	1.8
France - monthly average	20.1	20.9	19.3	18.0	15.7	7.3	3.4	3.4	3.8	7.4	11.3	15.4
France - difference monthly and decennial average	1.3	0.8	-1.6	0.9	2.3	-0.6	-1.9	-1.5	-2.0	-1.5	0.2	0.1
UK - monthly average	15.9	17.0	16.5	15.6	12.6	6.1	4.5	4.4	4.0	4.9	8.5	12.0
UK - difference monthly and decennial average	0.9	0.2	-0.9	0.8	1.4	-1.4	-0.6	-0.6	-1.6	-2.3	-0.5	-0.1

Source: Powernext Weather

> Precipitations (mm)	June-05	July-05	Aug-05	Sept-05	Oct-05	Nov-05	Dec-05	Jan-06	Feb-06	Mar-06	April-06	May-06
Berlin - monthly precipitation	29.0	142.9	57.1	55.0	35.0	21.8	49.5	20.4	43.8	33.5	12.8	62.5
Berlin - difference monthly and decennial precipitation	-20.9	80.0	-3.3	9.5	-16.1	-15.3	9.6	-22.6	-1.3	-4.6	14.3	9.9
Madrid - monthly precipitation	13.1	0.0	0.4	4.3	64.4	45.1	10.2	37.4	35.0	45.8	13.6	7.4
Madrid - difference monthly and decennial precipitation	-1.3	-10.1	-11.9	-18.3	19.3	-5.1	-34.9	5.6	8.2	15.6	-25.3	-32.1
Paris - monthly precipitation	48.0	35.8	23.2	39.9	17.8	25.2	25.8	28.8	62.2	68.8	31.0	60.4
Paris - difference monthly and decennial precipitation	6.0	-26.0	-28.5	-1.4	-50.4	-31.8	-34.0	-14.3	34.8	28.0	-28.4	6.0
London - monthly precipitation	31.6	40.6	48.4	46.8	70.8	29.8	45.4	16.4	40.4	37.0	27.8	99.8
London - difference monthly and decennial precipitation	-27.7	5.1	-2.5	3.0	-2.8	-38.7	-8.4	-32.4	1.9	2.2	-20.9	58.7

Source: WeatherOnline UK

## Economic activity

	June-05	July-05	Aug-05	Sept-05	Oct-05	Nov-05	Dec-05	Jan-06	Feb-06	Mar-06	April-06	May-06
Total industry production index (excluding construction and seasonally adjusted), base = 2000												
Europe 25	103.6	103.8	104.1	104.4	103.8	104.9	105.3	105.5	105.5	105.8	-	-
Euro zone	103.4	103.7	104.5	104.3	103.7	105.2	105.4	105.6	105.6	106.0	-	-
Industry confidence indicator												
Europe 25	-10	-8	-8	-7	-6	-7	-6	-6	-3	-2	1	1
Euro zone	-10	-8	-8	-7	-6	-7	-5	-4	-2	-1	1	2

Source: Eurostat

## Energy prices

	June-05	July-05	Aug-05	Sept-05	Oct-05	Nov-05	Dec-05	Jan-06	Feb-06	Mar-06	April-06	May-06
Natural gas, NBP ICE Futures, 1 <sup>st</sup> maturity date, in €/BTU	41.86	47.60	47.09	56.43	67.48	116.62	133.00	103.97	84.84	73.17	59.92	52.91
Coal CIF ARA, 1 <sup>st</sup> maturity date, in €/tonne	50.76	51.78	47.77	47.14	45.16	43.86	44.42	45.29	50.79	53.54	51.25	46.67
Powernext Futures™ month ahead, in €/MWh	Base	45.42	51.63	46.82	48.88	51.89	56.40	74.94	68.76	54.83	46.11	39.29
	Peak	65.42	72.51	62.67	67.06	69.25	79.50	103.72	109.56	93.48	59.64	58.74
Difference in prices of electricity and of natural gas, corrected for the price of CO2: Clean Spark spread in €/MWh	33.55	36.01	27.43	26.09	21.88	3.20	18.33	39.97	33.68	20.54	15.24	26.10
Difference in prices of electricity and of coal, corrected for the price of CO2: Clean Dark spread in €/MWh	23.12	25.75	20.46	25.03	27.40	38.83	65.11	66.41	44.02	22.47	10.57	24.24
Brent crude oil, 1 <sup>st</sup> maturity, in \$/baril	55.42	57.91	63.62	63.80	59.50	56.23	57.23	63.86	61.14	63.03	70.57	70.98

Source: Reuters, Powernext, Caisse des Dépôts



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