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Demand shock déjà vu: how resilient is the EU ETS this time around?

The coronavirus pandemic has dealt a severe blow to European economies by forcing industrial plants to shut and sharply cutting demand for energy. The result is a predicted slump in demand for emissions allowances in the world's largest carbon market - and a key driver of coal-to-gas switching in Europe - the EU Emissions Trading System (ETS).

If that sounds familiar it is because this, or some iteration of it, has happened before. In the aftermath of the global financial crisis of 2008, an economic slump caused a chronic oversupply of EU carbon allowances and a dwindling price that dogged the market for years, and from which it only recently staged a recovery.

This time around, the price of EU carbon permits slumped from a pre-pandemic peak of around EUR 24/tonne (USD 26/t) to a low of EUR 14.34/t (USD 15.53/t) on 23 March 2020 as investors liquidated positions. Prices have since rallied slightly to around EUR 20/t as of 24 April, on the back of two major auctions absorbing supply and the news from EDF of revised maintenance outages at its nuclear facilities in response to the pandemic.

Analysts suggest that companies who need to buy EU Allowances for compliance have yet to sell any of their holdings, but caution that this may happen as the need to raise cash increases.

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