Carbon slide will not halt Kyoto projects: UN
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By Gerard Wynn

LONDON (Reuters) - Solar, wind and other green energy projects based in developing countries and funded under the Kyoto Protocol will survive the plunge in the European carbon market, which underpins project investment, the UN says.

A 65 percent collapse in European carbon prices in the past two weeks has slashed the cost to European industry of buying pollution permits, or carbon credits.

This in turn cuts the cash that clean energy projects in developing countries can expect for carbon credits they sell into the EU market, under a Kyoto Protocol process known as the Clean Development Mechanism (CDM).

But the United Nations, which brokered the Kyoto Protocol, does not see such market fluctuations stifling what is hoped to fan up to $100 billion inward investment in developing countries by 2012.

"Decisions on CDM projects are unlikely to respond to short-term fluctuations like this," said Kai-Uwe Schmidt, UN Manager of CDM projects.

"It takes a long time to prepare and implement a CDM project, and such decisions will be based on longer term trends."

A tally of 156 countries last year ratified the Kyoto Protocol -- which sets for some 40 developed countries targets to cut emissions of heat-trapping carbon dioxide, widely blamed for climate change.

The EU plans to meet a large chunk of its Kyoto commitments through its carbon trading market, which it set up last year.

The EU then handed its polluting firms a certain quota of carbon credits. But they can get more by funding pollution cuts in developing countries, under the CDM, at a discount to the European price.

That alternative route -- to buy so-called Certified Emission Reduction units (CERs) -- has flourished in the past year, as a vogue market prospered playing the price difference between Europe and Latin America and elsewhere.

COLLAPSE

A slew of European countries last week announced lower than expected carbon emissions in 2005, implying a surplus of pollution-permitting carbon credits and prompting the price dive.

Traders say no CER deals have happened since that collapse, which flushed out losers including brokers that guaranteed CERs at prices indexed to the European price, the European Union Allowance (EUA), and project managers that did not get such guarantees.

"(CER) Deals will continue to happen. (But) people who have negotiated deals at higher price levels may want to take a break," said Edwin Aalders, a Manager at the International Emissions Trading Association.

"CDM projects indexed to the EUA are sweating at the moment. (But) Realistically there are very few projects which rely on CER revenues. I'm not sure many will go belly up."

SILVER LINING

The carbon price dive has also potentially wiped out the CER discount -- which allows for project uncertainty and risk.

Last month CERs traded at up to 22 euros ($27.80) compared to a European carbon credit price of some 30 euros, but European credits were trading at just 12 euros on Wednesday.

"No-one will pay 20 euros for a CER now when the EUA is at 12 euros," said James Emanuel, Head of Carbon Trading at brokers CO2e.com.

Carbon market players are hoping that the European Commission will use the credit surpluses to enforce stricter pollution targets from 2008, the second phase of the EU's carbon market, reviving demand for and the price of credits.

"We think the EC will fix (the surpluses) and create a shortage. There will be a regulatory backlash," said Laurent Segalen, investment manager at the European Carbon Fund, a non-governmental fund investing in CDM projects.

"Our strategy is buy (CERs) in phase 1 and sell in phase 2."
