The Exchange: How carbon is traded on an Exchange and in the OTC Market

Manuel Moeller
European Energy Exchange
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Market places

• Three routes to market
  – Bilateral trades
  – „Over the counter“ (OTC) brokers
  – Exchanges

• Different characteristics with regard to:
  – Liquidity & number of participants
  – Transparancy
  – Level of regulation
  – Management of credit risk
Share of market places in EU ETS

Trading alternatives – Exchange, OTC, bilateral

Source: Point Carbon, Reuters, LEBA

*World Bank estimate: Bilateral amounting to 15% of total volumes – shown for illustrative purpose
Trading sectors

• Primary auctions
  – Primary allocation of allowances

• Spot
  – Meets short term needs, deals are completed „on the spot“ and settled quickly (<2 days)

• Futures/Forwards, Options
  – Management of price risk or speculative bids; Transactions with delivery in the future (eg December 2013)
Emissions Trading on the Exchange

Trading Platform
Trading in standardized contracts on emission allowances
Order matching through continuous trading or auctions

Clearing & Settlement (Clearing House)
Clearing house guarantees payments and physical delivery of allowances as well as anonymity of trading

Emissions Registry
All transactions are settled through the Registry infrastructure

Exchange member A (seller)
Clearing agreement
Clearing member (Bank)
Euros
Registry Account
Exchange member A
CO2

Exchange member B (buyer)
Clearing agreement
Clearing member (Bank)
Euros
Registry Account
Exchange member B
CO2
Emissions Trading on the Exchange

• Trading on an electronic platform at standardized terms and conditions
  – Exchange rules and clearing conditions
  – Trading hours (8-18h CET)
  – Contract Specifications (define eg quantity/quality, contract size, place of delivery, delivery period,...)

• Access to the exchange
  – Direct exchange membership
  – Via financial intermediaries
Emissions Trading on the Exchange

• Trading
  – Bid/ask orders can be entered/modified/cancelled in the order book directly through trading screens or „on behalf“ (via phone/mail/fax)
  – Order matching: Auctions vs. continuous trading

• Clearing & Settlement
  – Clearing house steps in-between buyer and seller, thus becomes direct counterparty of buyer/seller
  – Covers counterparty risk, guarantees all payments, depositing of collateral and deliveries as well as anonymity
Order book (Example)
Questions?