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Carbon Frontiers 2025 | Episode 1
Mark Lewis, Head of Research, Andurand Capital

We kick off *Carbon Frontiers 2025* this week with Mark Lewis, Head of Research at Andurand Capital. David Greely sits down with Mark to discuss the leading role that the EU ETS may play in moving carbon markets forward as it's forced to balance carbon emissions reductions with keeping its industry competitive in a world where the U.S. is no longer in the Paris Agreement.

Mark Lewis (00s):
Trump is making no secret of his desire to see more European industry than has already relocated to the US, do it over the next four years, and he is out to see European industry relocate to the United States. Europe has got to get smart, and it's got to get smart quickly.

Announcer (17s):
Welcome to SmarterMarkets, a weekly podcast featuring the icons and entrepreneurs of technology, commodities, and finance ranting on the inadequacies of our systems and riffing on ideas for how to solve them. Together we examine the questions: are we facing a crisis of information or a crisis of trust, and will building Smarter Markets be the antidote?
This episode is presented by Base Carbon, sensible carbon investing. For more information, visit basecarbon.com.

David Greely (57s):
Welcome to Carbon Frontiers 2025 on SmarterMarkets. I am Dave Greely, Chief Economist at Abaxx Technologies. Our guest today is Mark Lewis, Head of Research at Andurand Capital Management. We will be discussing the leading role that the EU ETS may play in moving carbon markets forward as it's forced to balance carbon emissions reductions with keeping its industry competitive in a world where the United States is no longer in the Paris Agreement. Hello Mark. Welcome back to SmarterMarkets.

Mark Lewis (01m 27s):
Hey Dave, it's a pleasure to be back with you.

David Greely (01m 29s):
Well, it's a real pleasure to have you here. It's been far too long. You are here for our first Carbon series a number of years ago and each year since we have done what we call our Carbon Frontiers podcast series where we try to give our listeners a better sense of where the leading edge of the development of the carbon markets is. Now, it's not always easy and I am glad you are here to help us find where that leading edge is. And I wanted to talk with you at the start of this year's series because my sense is that market participants are turning more and more to compliance markets to lead the way forward. We are seeing more national compliance markets and schemes forming and more and more focus on the Paris Agreement Article six markets. And at the forefront of a lot of these schemes is the EU ETS and no one understands the EU ETS better than you. So maybe we start there. What is the EU ETS's place in the world right now and what role do you see it playing either on its own or as a model for how carbon markets may move forward?

Mark Lewis (02m 35s):
Thanks Dave, and thanks for having me back on the show and for the kind introduction. I mean it's a great question and it's a very, very topical question and I guess if you'd asked that question only three months ago before the US election, you would have got a different answer because I think we are going into a different world now with Donald Trump back in the White House and we'll get onto that no doubt a little later on. But before we get into that, that and the kind of general geopolitical backdrop that we now face to come back on some specifics to your question, right? So I think the EU ETS is still very much the global benchmark compliance market, still the largest market, the most liquid daily auctions. So pricing in real time with very decent liquidity, 35,000 to 40,000 lots traded every day on the EU ETS across the strip.

Mark Lewis (03m 27s):
Still mostly in that front year contract, but you know, that's 35 to 40 million tons a day being traded notional in the carbon futures market. So it's a very sophisticated deep liquid market with a very wide range of players, the compliance players, obviously the power

companies and the industrial companies that have compliance obligations under the scheme and then different kinds of financial players, banks who are in there on behalf of industrial companies very often than hedge funds and speculative funds such as ourselves who are looking to trade the pricing arbitrage opportunities and look for opportunities whether across the curve or between EUAs and other carbon markets and we will certainly get into that later in the conversation because at the moment, well right now I think probably the most interesting opportunity in compliance markets is, is in the UK and narrowing the discount to EUAs and we will come back on that, but that's kind of the state of the nation in terms of why the EU ETS is still very much the benchmark market for compliance schemes globally, the one that people look at.

Mark Lewis (04m 37s):
And one other feature of it, of course that I should have mentioned in that summary is it's the longest in existence. It's been going since 2005. And crucially Dave, and I think this is a point that is often easy to forget in the day-to-day excitement of trading this market. We are now halfway through the lifetime of this market. It started in 2005, the cap is falling to zero by 2040. So this is a market that's been up and running for 20 years and basically it's only got another 15 years to go, at least as the legislation is currently written. We will see what happens as these geopolitical pressures from Donald Trump kick in and tariffs potentially kick in. But right now we are over the halfway mark in the lifetime of this market and the rubber is about to hit the road in a big way because coming back to your question, just trying to set the scene again where we are in terms of the development of the market, a very, very key development next year we have the CBAM, so-called CBAM carbon border adjustment mechanism, which is effectively a carbon tariff that the European Union will place on imports of goods covered by the scheme to ensure that European producers are not at a disadvantage in their own market from foreign producers of steel and cement and so on.

Mark Lewis (06m 04s):
And this is going to change we think market participants' behavior. And perhaps just to step back a little and explain to our audience the significance of this, I mean this is a market that from day one, so from the 1st January, 2005 where price formation has been driven by the power sector, the power generation sector, right? They have always had this obligation, certainly from 2008 they have been under an obligation to buy all of their allowances at auction. Whereas the industrial sector receives still a very significant share of their overall allocation for free precisely because of this problem of competitiveness with countries outside the EU who produce the same goods. And what that means is it's been the power sector that has driven price formation. They are the ones who have had to hedge forward and take carbon pricing into account when they're selling their power forward. It's, it's essentially just another commodity like coal or gas that they are using for their power generation.

Mark Lewis (07m 06s):
They buy coal and they buy carbon, they buy gas and they buy carbon and because they hedge forward, typically they sell their power on a rolling three year forward basis. That's why they have always been the main driver of prices. Now of course, Europe is decarbonizing in the power sector very quickly. We have renewable energy capacity coming onto the system every year and it is displacing the older fossil fuel generation capacity and what this means structurally, the European power industry is reducing its emission from year to year simply by virtue of the fact that more and more renewable capacity is coming onto the system and what that means in turn is we need the industrial sector to step up and start hedging their forward liabilities in the same way that the power sector in the past did, but in the future will not be doing because they have less and less of a requirement to do that because more and more of their generation collectively is coming from renewable sources.

Mark Lewis (08m 06s):
So I think this is an absolutely crucial moment in the development of the EU ETS which will be watched very closely by other jurisdictions that have compliance markets because the EU ETS as we have known and loved it since its inception, is going to go through a big identity change as industrials step up to take over from utilities as the main driver of prices. I liken it Dave, to a relay race where the power generation sector has been running the first lap or the first few laps around the stadium and we are now getting into the box where they hand over the baton to the industrial sector and they have to step up and take responsibility for driving prices. So that's a long answer to your question, but just to give a flavor of, you know, where we are in the market, the day-to-day liquidity, the main participants and how we're thinking about these significant structural changes that are coming and the pricing opportunities that inevitably will arise from that.

Mark Lewis (09m 05s):
Because what we are looking at now between now and the end of this decade, and in fact all the way down to 2040 now is annual deficits where demand is outstripping supply. So we should start to see prices move structurally higher over the next five years,

between now and 2030 as we find that abatement price point for industry. What's the price at which industry can reduce emissions? That's logically that's where the price has to go Now, is it a 100, 150, 200? That's what the market will have to figure out over the next two to three years.

David Greely (09m 45s):
There is so many great things for us to dig into and threads to pull upon. Thanks, for setting the, the frame for us. And I wanted to dwell for a moment just to pick out a few things that you said. And one really importantly I think is when you said the EU ETS is about halfway through its mission, right? To get to the lower carbon reductions. And I think that's important for people to hear because often in carbon markets people hear net zero commitments or caps and they seem to perpetually be floating out in the future 10, 20, 30 years. So to understand that in the EU market there have been the reductions, as you said, the rubber is hitting the road where our generation sector alone isn't enough but it has to pass that baton and now industrial users needing to change their behavior as well.

David Greely (10m 35s):
And I want to get into all the geopolitics and how that affects outside of the EU as well and one thing I wanted to come to you before turning to the US and some of the change in policy direction under President Trump is think often people have had a sense that the path to a more global compliance market may arise eventually from kind of a growing patchwork quilt of regional compliance markets. It's interesting that it's about five years post Brexit and there's discussion of reintegrating the great ETS with the EU ETS. So I was just curious that probably one of the earliest steps we might see of new emissions trading systems merging. So I was curious what's happening there?

Mark Lewis (11m 16s):
This is a, a very, very topical question Dave, because last week we had a story in the Financial Times saying that the UK government is now formally working behind the scenes with a proposal in concert with the European Union to link the UK ETS back to the EU ETS as you rightly say because only five years ago there was not a separate UK ETS, all the UK compliance players were, were part of the EU ETS and I think before we get into where we are on that because I think there is a very exciting story there which I would like to bring to the attention of our audience. But before I do that, this makes a lot of economic sense, right because you know, Europe is still the UK's largest market and we mentioned CBAM and we will probably get into it in greater detail later in the show.

Mark Lewis (12m 05s):
But the EU's CBAM is meant to come into force from the 1st of January next year 26, the UK which is also going to put in place its own version of CBAM but that won't come into effect until the 1st January, 2027. So there is a year's discrepancy and that can cause all kinds of further disruptions to trade between the UK and the EU or find that the UK some of its exports to the UK are negatively impacted by that. So it makes a lot of sense to align the carbon pricing schemes of the UK and the EU in economic terms and I would argue it makes a lot of political sense as well because we don't need to go into great detail on Brexit. But you very rightly mentioned the point, it's five years, it was five years to the day on Friday of last week, 31st of January is when the UK formally left five years ago in 2020.

Mark Lewis (12m 58s):
And if you look at the opinion polling on that now, there was one opinion poll published on Friday the 31st January showing that only 11% of the UK public think that Brexit has gone well. I think that kind of says everything. So I think there is political mileage for the government in finding ways to cooperate with Europe where it makes sense and the other thing I would say is this is quite a technical market. This is not something that gets the UK tabloids and the UK media generally excited. It's a technocrats market and so politically the UK government can afford to take a risk. They are nervous about being seen as going back on Brexit. Like it's still a politically toxic thing to be seen to be doing in the UK. Although personally I think that that is changing but you know, there's a lot of pragmatism bonus points to be won on pragmatism here if they can get this over the line and certainly it makes sense economically.

Mark Lewis (13m 51s):
So coming back to what this means and the opportunity here, trading opportunity, investment opportunity for a fund like ours, the crucial point is that UK allowances, UK carbon allowances, UKs are trading at a discount still even though they rallied very sharply following the publication of that FT article last week. Well let's move, let me put it this way, the night before that article was published, UKs were trading at a 42 euro per ton discount to UAs, right? It doesn't make sense. The UK market is as tight if not slightly tighter than the EU market if you look at the balances to 2030. So UK is a very ambitious emissions reduction trajectory, slightly more ambitious even than the EU. So that's why the UK market will get tighter than the EU market later in this decade. So on a fundamental basis it doesn't make sense but it's less liquid market, it doesn't get traded anywhere near as much.

Mark Lewis (14m 52s):
I think we do 3,000, 4,000 lots a day compared with what I mentioned the size of the European market. So that's also from a trading perspective makes sense to encourage the two schemes to merge because it would create more liquidity in the four UK compliance players. They would have a bigger pool in which to fish as it were for their compliance allowances. But here is the thing, UK allowances have rallied very sharply already. They were trading around €33, €34 a ton when the FT article was published or before the FT article was published and then on the Tuesday of last week, the day it was published, they rallied all the way up to €40 a ton. So you know, it was a 16% rally on the day and subsequently they have continued to push up and I think we have closed today at around €45, €70, so up very, very substantially from where we were before this story was published.

Mark Lewis (15m 52s):
And yet they are still trading at a €27, €28 Euro discount, right because the UAs have been trading water and trading above €80 still. So if we get political confirmation and that will come when the UK and the EU hold their long awaited trade and cooperation talks, which I think are scheduled for late March. So six, seven weeks from now we could find ourselves in a situation where there is an announcement from the UK and the EU that they are agreeing to have discussions on all kinds of things. And one of them is they want to formally align the UK ETS with EU ET now. There will be political and no doubt legal obstacles to be overcome, but if the political will is there, you can be pretty sure that they will find a way of doing that. Now what do you think happens if such an announcement is made?

Mark Lewis (16m 44s):
I think you know, the market will push UKs much higher very quickly, not necessarily closing the discount completely with UAs because of these residual political and legal barriers that will have to be jumped over at some point. But I would expect that discount to narrow to something like €10 euros a ton instead of close to €30 where we are at the moment. So that's a very exciting potential opportunity for anyone looking at investment opportunities in global carbon markets at the moment and I think it's important also symbolically, I mean the way you framed the question was absolutely spot on. This is a way in which we can show the world that separate compliance trading schemes can be linked and what does it mean? What does that look like? What it means is, you know, UKs still exist independently of UAs but there are fungible articles.

Mark Lewis (17m 41s):
A European compliance player can use the UK a for compliance with the EU ETS obligations and similarly a British compliance entity can buy EUAs to meet their compliance obligations in the UK. So it would be a very exciting thing to happen. I think it would be incredible if they could choreograph this to coincide with COP 30 in Brazil in November as a way of showcasing this to the world. Hey look, this is how you link carbon markets. This is how you drive forward the decarbonization of major jurisdictions through corporation via carbon markets. So an awful lot of exciting stuff I think to come there.

David Greely (18m 29s):
Very exciting and an important and interesting model of potential integration in Europe, potentially profitable opportunity for people trading markets. Maybe I will take the other direction and go across the Atlantic now to get on an example of movement in the other direction, notably President Trump once again pulling the US out of the Paris agreement. How are you thinking about the implications of that exit?

Mark Lewis (18m 54s):
There is so much to say here, right? My first observation would be of course this is not a surprise he did it. It was essentially the first thing he did when he took off his last time in 2016 and it was one of the many executive orders he signed on the day right after the inauguration this time round. So I think everybody was expecting it. So in that sense, disappointing of course. I mean nobody wants to see the United States pull out of the major global agreement on climate change. So disappointing but not a surprise. What does it change on the ground and I think in terms of what it changes on the ground, we will have to wait and see now how he deals with the IRA legislation and whether the many and varied subsidies and incentives and tax exemptions for renewable energy and hydrogen and other forms of low carbon energy, whether those are retained or rejected because that has been a very strong driver of decarbonization if it's in the United States under the Biden administration, even though there is no federal cap and trade scheme.

Mark Lewis (19m 59s):
But we do have obviously regional cap and trade initiatives in the US and California, Washington, Reggie, New York coming in soon. So the point is there is never been a federal cap and trade scheme. So it will all be about how he approaches the IRA. I think we for the

time being at least are relatively sanguine about the prospect of the compliance markets in the US under President Trump because again, we have already lived through Trump 1.0, this is Trump 2.0. My personal observation from the other side of the Atlantic is that he seems to be approaching this period in office how to put it in a more organized way than he was the first time round. He has hit the ground running very, very hard across a, a whole range of issues. So there seems to be a greater degree of organization and coordination about what he is doing and what he wants to do.

Mark Lewis (21m 00s):
But I am not feeling yet any sense of threat or concern about his wanting to go after any of the compliance markets. I say that Dave, because I do hear from time to time people wondering whether he will set his sights on California in particular, which of course he did try and do in his first term and that he wasn't successful in doing that. So maybe he will think, well we tried that once we have got other things, other priorities, but you know, you never know. I think the jury is still out it's early days and we will see what happens on a case by case basis. But clearly, obviously if you take at face value so many things that he has said over the years around wind power in particular where he feels very critical of wind power and very negatively disposed towards wind power, that's obviously not something that anybody concerned with decarbonization of the power sector can look at comfortably. So let's wait and see what happens.

David Greely (21m 59s):
And I am curious what it may mean for Europe and the EU ETS in light of, you mentioned earlier now the batons being passed to industrials who in the past were given allowances so that they could remain competitive and we have the carbon border adjustment mechanism coming in. So now you have US industry that already has access to much cheaper energy through natural gas not potentially being subject to the same emissions constraints as Europe. And you have President Trump's proclivity to using tariffs as a way to push back against trade policies from others that he disagrees with. So I am curious how you see that angle, you know, affecting the ability of Europe to continue with its carbon policies and its carbon market.

Mark Lewis (22m 51s):
Again, you know, you are hitting all the topical questions very much on the head here. Look, I don't think you can look at this completely comfortably, you know, in terms of what the implications for the EU ETS are going to be and one reason I say that, and there are a few straws in the wind here about this, but last week there were press reports that and we wait and see how if and how this gets formalized but the largest grouping of political parties in the European Parliament, the so-called European peoples Party, which is really the center right grouping. So these are conservatives, but centrist conservatives, generally Christian Democrats in Germany for example, they are the largest party within that EPP grouping and the EPP is the largest single grouping in the European Parliament. They have I think 188 MEPs out of a total parliament representation of 720, something like that.

Mark Lewis (23m 47s):
And the EPP came out with a policy suggestion that the introduction of CBAM be delayed by two years, or in fact I think they said at least two years. Now, if we go back to everything we said at the top of the show about the importance of passing the baton and having industry drive price formation if, and it's still a very big effort at this stage, but the question is going to be put on the table. I believe, you know, I think this is coming, if CBAM were to be delayed by two years with a view more than anything else, I think to preempting anything that Donald Trump might want to do in terms of tariffs on European industry, I mean, hey those are probably coming anyway, right? Whether the EU proceeds with CBAM or not because CBAM even in the best case scenario, won't take effect for another year.

Mark Lewis (24m 44s):
And I think President Trump wants to act long before that, probably within the next couple of weeks. I think Europe is going to be hearing something on tariffs, but if they were to delay it then free allocation would obviously continue for another two years. And the impetus for European industry to be in the market buying allowances or hedging future obligations would not be as great. So that's a negative reading of, you know, the impact on price formation in the market. That being said, unless or until there were a much, much bigger existential question around the survivability of the EU ETS itself, and we are a very, very long way away from that. So as long as the scheme itself continues and I think that is absolutely going to happen, imagine what this means. If you remove the incentive on industry to actually start hedging their future obligations, you don't change the supply and demand balance.

Mark Lewis (25m 47s):
That remains what it is. So all it means is you probably have another 18 months, two years of industrial companies not hedging their future liabilities very much all the time while the deficits are growing. And what that means is, I think the risk you would get yourself into is that all of a sudden, two years down the line, two and a half years down the line, industrials would be panicked into buying

because the speculators would've still been playing in the market and they will be trading the fundamental balances. And if the fundamental balances are saying the outstanding market inventory is declining rapidly, which is what we expect to happen, certainly from next year, there will be a small decline in the inventory this year. There's gonna be a small supply demand deficit on our numbers this year that grows more substantial next year, the year after, and the year after that. And as with any commodity market, we've discussed this before, right Dave, in any commodity market, if inventory is falling, prices are going up. That's commodities 101, right? So I think there is a risk that if CBAM is delayed, it's actually on the one hand it's a recipe for future price volatility because all you are doing is delaying the moment of truth for industry and probably what will happen is you know, speculators will step in to fill the void and because they will be reading the ballots.

David Greely (27m 14s):
And I wanted to ask you, maybe we could then also look at bringing in the Article 6 markets. So there's been a lot of focus there on that development, people looking at that being a new way, you know, potentially bringing some more voluntary carbon market projects into the mix. I am just curious, how do you see all this affecting the development of the Article 6 markets?

Mark Lewis (27m 35s):
I think this is crucial and I do think there is now an opportunity here. Europe realistically is going to have to lead the way on this, right? I mean for all the reasons we mentioned at the beginning of this conversation, that it's the benchmark compliance scheme globally the longest established and it's the one where the rubber is now hitting the road. So they really have to find a way of squaring the circle, which is circle and when I say squaring the circle, I mean how do you ensure that European industry remains competitive when energy prices are already much higher than they are in much of the rest of the world and certainly a lot higher than they are in the United States and North America. Generally, how do you avoid putting even more competitive pressure on European industry whilst at the same time ensuring the carbon price is high enough to send a price signal that decarbonize industry without forcing industry out of Europe?

Mark Lewis (28m 32s):
That's the stark choice, that's the circle that has to be squared and in particular that debate which is coming I believe in probably 2026 because in 2026, you know there's a review of a number of features of the EU ETS and very much on the table will be the question of what kinds of offsets or removals will be allowed into the EU ETS beyond 2030 because from 2030 onwards the cap is declining in linear fashion to hit zero by 2040 and today in 2025 the cap is around 1.1 billion. So we are going from 1.1 billion tons of allowed emissions to zero tons of allowed emissions. People often forget whilst the EU headline target is a net zero target, the EU ETS falls to zero in absolute terms in terms of the cap by 2040, this is an absolute zero as it is written at the moment.

Mark Lewis (29m 34s):
Now I don't think that's going to be possible to retain. I think if you did not allow European industries somehow to have a safety valve in terms of pricing, you would see huge dislocation in European industry and you would see a huge amount of offshoring European industry just leaving Europe. Nobody wants that. So to me, the obvious solution is to allow credits that can be generated at scale and credits that are compatible with the accounting framework of the UNFCC's Paris Agreement into the EU ETS beyond 2030 and we can debate the volumes and how much of the abatement that needs to happen should happen domestically and how much should be offset via the use of Article 6 credits with corresponding adjustments but in my view, I am not aware of any other instrument that is gonna be scalable and that will have by definition the environmental integrity that will allow Europe to say yes, we're allowing offsets in, but the fact that the only offsets allowed in are Article 6 credits with corresponding adjustments.

Mark Lewis (30m 49s):
And that means that if we are buying from Brazil or Mexico or India or whoever they are having to reduce their emissions further so that they comply with their Paris obligations, then it's a win-win. You are reducing the overall cost of compliance in Europe whilst ensuring the global agreement on emissions reductions through the Paris agreement is respected. Now that's how I think in an ideal world, Europe should approach the question of Article 6 and the other thing that would do of course is it would give a great momentum to generating supply if Europe gives a signal ahead of time next year or the year after, we will allow in this volume of Article 6 credits between 2030 and 2040. So because scaling up is gonna be really important, but the idea that Europe can do this by allowing some carbon removal credits within Europe itself and at the same time allowing some direct air capture, which is the other, not silver bullet, but it's a solution that is often talked about.

Mark Lewis (31m 54s):
I mean I am not a great expert on direct air capture technologies, but what I do know is that at the moment the cost of direct air capture technologies is anything between $501,000 a ton and secondly, there is just nowhere near enough supply and there will not be enough supply by 2030 either. So, you know, these are the very real challenges that have to be met, have to be faced and the clock is ticking and it's ticking very loudly because all of this policymaking in Europe takes years to get onto the books. So you have to start legislating for this, as I said, 26, 27, so that everything is in place for offset credits to be allowed in beyond 2030 from 2031 onwards. So that's how I view it personally. I don't see any other solution because if you don't do that and you're just allowing a small amount of removals and direct air capture credits to be used, then carbon prices in Europe between 2030 and 2040 are going through the roof and European industry will not be able to handle that and it will become politically totally unmanageable for European policy makers.

David Greely (33m 08s):
And to me this seems to be such an important opportunity for the markets as a whole where, you know, for a long time the EU ETS as you said is the benchmark kind of the gold standard. Absolute zero is what we are aiming for. And at the same time in the voluntary markets, what I often hear is people saying, just tell us what's okay to do. You know, we need a standard, we need someone. And so it seems like the EU ETS could offer that imp premature of this is quality, this is equal to a EU ETS ton, and now we can potentially get the economic force to create a moment of pragmatism to move the market that way.

Mark Lewis (33m 51s):
I think that's absolutely right. And as I say, it's not on the agenda at the moment, but however, think of this, I always make this point, I made this point at a seminar I attended yesterday, which is this, although there is a lot of political opposition in Europe to the idea of allowing Article 6 credits in. And by the way, you know, again for the benefit of our audience, that resistance stems from what many people in Brussels regard as an overgenerous quota of offset credits under the Kyoto protocol. So CDM credits and J credits that were allowed to be used in the EU ETS between 2008 and 2020, which that was done with the best of intentions is that we will allow 1.6 billion tons more or less into the market over that period, 2008, 2020, that was all agreed again, and this is the whole point I made about timing and how everything needs to be queued up ahead of time.

Mark Lewis (34m 49s):
And 2008, people forget, you know, the world changed radically in 2009 with the global financial crisis in 2008 the carbon market had a deficit in Europe and prices doesn't seem a very high price today, but you know, prices went above €30 euros a ton. It was a very exciting moment and we were looking at deficits all the way through to 2020 back then in 2008. But then what happened, the global financial crisis happened. Emissions in Europe collapsed European and GDP collapsed because of the global financial crisis. And all of a sudden we have got this huge volume of cheap offsets coming in from outside Europe under the Kyoto protocol mechanisms and carbon prices crashed. So there is this, and I understand resistance in Brussels in some quarters simply from the scars on policymakers backs that were caused by that unfortunate turn of events with the global financial crisis and the flooding of the market with these cheaper credits as it turned out with the benefit of hindsight.

Mark Lewis (35m 53s):
But that was originally, those credits were there to act as a safety valve on pricing, which is what we have just been discussing. And let me say one other thing here, which I think is crucial, and this is the point I've been making a lot over the last 18 months. The fact of the matter is, again, it's easy to forget, European Union is already allowing Article 6 credits to be used for compliance in the EU ETS on a de facto basis, not yet on a de jure basis, but on a de facto basis and let me explain what I mean. So we have the CORSIA scheme for aviation. The CORSIA scheme for aviation is this voluntary mechanism set up by the ICAO to enable the global aviation industry to buy offsets against their emissions between now and 2035 and really that whole course scheme came into being because the European Union originally and is still in the directive actually because we are under the so-called stop the clock provision at the moment, whereby in 2012 the European Union under pressure from the United States, from Russia, from China, from India, agreed to suspend the compliance obligation on airlines operating flights between the EU and third country jurisdictions.

Mark Lewis (37m 16s):
Because originally the, the directive states that if United Airlines is flying between Washington, DC and Paris, all of the emissions on that flight should be subject to a compliance obligation under the EU ETS but there was huge pushback from these other countries and in the end, the European Union said, okay, you know what, we will stop the clock on that obligation as long as the global aviation industry gets its act together and establishes a credible offsetting scheme that will ensure that these emissions are be in fact being offset and what are the credits that are eligible for inclusion in CORSIA well, it's Article 6 credits with a corresponding adjustment. So if

you think about it, this is why I say where the EU is effectively already allowing compliance with the directives obligations in the form of Article 6 credits with corresponding adjustments. That's exactly what CORSIA is.

Mark Lewis (38m 13s):
And course here only exists because of the European Union stopping the clock. So therefore, I don't think this is a very big intellectual step to take for the European Commission to say, well effectively we're already allowing the use of Article 6 credits with corresponding adjustments for compliance with the European ETS obligations. So why don't we simply formalize that beyond 2031 and allow industrial companies to use them and enshrine that in the law and indeed, you could go, you can start taking this further, right because if you are a lawyer acting for the European industries, you might be tempted to argue that, wait a minute, this is not fair. The airline industry is getting a pass. They are allowed to use these cheaper credits, these Article 6 credits for compliance with effectively for compliance with EU ETS obligations and we are not. So you could find that there are legal cases, and by the way, if CBAM is up and running, you might find Chinese steel makers saying, this is not fair.

Mark Lewis (39m 15s):
We are subject to CBAM we are not allowed to use Article 6 credits for our European compliance obligations, but China Airlines is allowed to use those credits. So you can see how this very quickly could become very messy if you don't formalize it legally. So I am optimistic that, you know, the economic pressure of the need for a safety valve on pricing beyond 2030 and the realization that actually it's a small step from formalizing de facto what is already the case to making de jure. So, so I am hopeful that ultimately that argument will gain traction. And we will see Article 6 credits used,

David Greely (39m 56s):
As you said, it's already messy on the side of what's allowed de facto between industries and I could also see if you are a policy maker who is looking at the choice of, well we either continue to just give allowances to industrials instead of the passing of the baton versus well maybe we let industrials finance and offset that is doing something more than getting it for free. That's a, at least a step in the proper direction for them.

Mark Lewis (40m 26s):
I think. So, you know, the EU probably still wants also to see a thriving global carbon market and you know, why wouldn't you want to see that and therefore I think this would be a great way also of providing huge impetus to the establishment of other compliance schemes globally and Article 6 credits would then somehow become, if you like, the glue that binds these different compliance markets. That's how I kind of think about this, but it's going to take a little bit of imagination in Brussels, certainly on the part of those who are skeptical about allowing the use of offset credits from outside Europe into the EU ETS again. But you know, that's maybe the optimistic reading of how Donald Trump is going to affect things in Europe. Europe's going to have to reinvent its thinking on trade policy, on economic policy, on industrial policy and I think it's going to have to reinvent its carbon policy and climate policy to reflect these new realities and this is one way you can do it because Trump is making no secret of his desire to see more European industry than has already relocated to the US do it over the next four years. And he is out to see European industry relocate to the United States. Europe's got to get smart and it's got to get smart quickly.

David Greely (41m 44s):
Thanks again to Mark Lewis, Head of Research at Andurand Capital Management. We hope you enjoyed the episode. We will be back next week with another episode of Carbon Frontiers 2025. We hope you will join us.

Announcer (41m 59s):
This episode is presented by Base Carbon, a financier of projects involved primarily in the global voluntary carbon markets. Base Carbon endeavors to be the preferred carbon project partner in providing capital and management resources to carbon removal and abatement projects globally and where appropriate will utilize technologies within the evolving environmental industries to enhance efficiencies, commercial credibility, and trading transparency. For more information, visit basecarbon.com. Base Carbon, sensible carbon investing.
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