



# Ninepoint Carbon Credit ETF

## May 2022 Commentary

### The Ultimate Uncorrelated Asset Class

Throughout the month of May, the global carbon market demonstrated robust performance in a time of heightened volatility in the broad market - CCA (California Carbon Allowances) posted a 7.2% monthly return while UKA (UK Allowances ) generated a 2.3% gain. EUA (European Union Allowances) and RGGI (Regional Greenhouse Gas Initiative Allowances) posted small losses, -0.5% and -1.3% respectively. During the same time, S&P 500 finished the month almost flat with a total return of 0.2%

In Europe, home to the largest carbon market by trading volume, EUA price experienced some volatility in the month of May. On May 18, the European Commission set out its full REPowerEU Plan that included multiple proposals with the aim to reduce the EU's dependence on Russian fuels. European Commission also plans to raise €20 billion for the plan with the sale of EUAs out of its Market Stability Reserve. Market Stability Reserve (MSR) was established in 2014 to maintain the long-term price stability of EUA – the reserve conditions the availability of allowances to respond to overall economic conditions and supply/demand dynamics from world events such as the pandemic.

EUA prices fell as much as 7% from €92 to €85 amid this proposal. In the two weeks following this, EUA has been trading sideways. The best performing carbon market is CCA, which has been trading up steadily throughout the month, settling at 7.2% monthly return, following its bullish Q2 auction result.

In the asset management world, American investment management firm VanEck filed an application to launch Australia's first carbon ETF. The ETF will track the ICE Global Carbon Futures Index.

### Investment Team



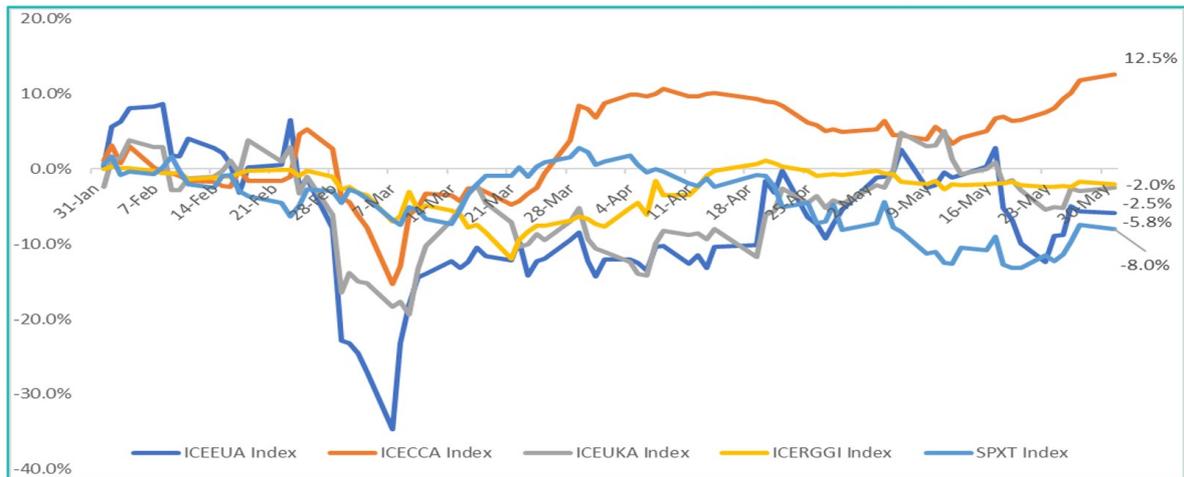
**John Wilson, MBA**  
Co-CEO, Managing Partner,  
Senior Portfolio Manager

### Performance of Major Carbon Markets (May 2022)

	Cumulative Return (May)	Daily Volatility (May)
ICE EUA Carbon Futures Index (ER)	-0.5%	3.0%
ICE CCA Carbon Futures Index (ER)	7.2%	0.9%
ICE UKA Carbon Futures Index (ER)	2.3%	2.1%
ICE RGGI Carbon Futures Index (ER)	-1.3%	0.5%
S&P 500 (TR)	0.2%	2.0%

Source: Bloomberg

Global Carbon Markets – Cumulative Returns (Feb'22 – May'22)



Source: Bloomberg

### What does Ninepoint Carbon Credit ETF invest in?

**The Ninepoint Carbon Credit ETF** invests in **carbon credit futures** – futures that track the prices of carbon in compliant carbon markets globally. Unlike the conventional equity funds which invest in traditional stocks.

As of May, the fund allows market participants to access a basket of four of the world's most liquid carbon futures markets by traded volume: the **European Union Allowances (EUA)**; the **California Carbon Allowances (CCA)**; the **UK Allowances (UKA)**; and the **Regional Greenhouse Gas Initiative Allowances (RGGI)**<sup>1</sup>. As the global carbon credit market grows, the fund will evaluate and invest in additional carbon allowance futures contracts.

World Carbon Markets – Total Value by Segment



Refinitiv, January 2022

Source: Refinitiv

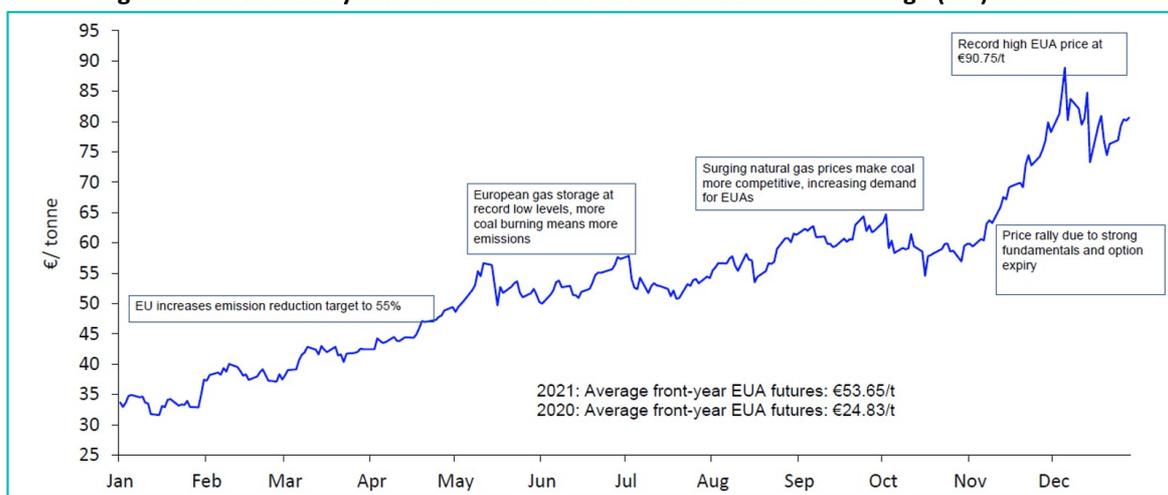
### 1. EUA- European Union Allowances

European Union Emissions Trading Scheme is the world's first major carbon market and a

cornerstone of the EU's policy to reduce greenhouse gas emissions cost-effectively. It is the largest carbon market by traded volume<sup>2</sup>. Approximately 11,000 installations are covered across European Union, plus Iceland, Norway, and Liechtenstein. The sectors covered under the system include power generation, energy-intensive industrial sectors and aviation within Europe, covers ~40% of the EU's emissions<sup>3</sup>.

Since 2021, the price of the December 2022 futures increased from €35/t in January 2021 to €85/t in May 2022. As we discussed in our [April commentary](#), three factors drove this persistent price increase since 2021. Firstly, more aggressive EU-wide climate policies including "Fit for 55" and phase 4 of the EU ETS starting from 2021 further limited the amount of EUA supply available in the market. Secondly, high gas prices made the demand for more carbon-intensive energy sources such as coal very high, especially during Q4 of 2021. Finally, extreme weather in Europe since 2021 led to surged energy demand, and thus translated directly into an increase in demand for EUA<sup>4</sup>.

**Figure: Price of front-year EUA contract on the Intercontinental Exchange (ICE) in 2021**



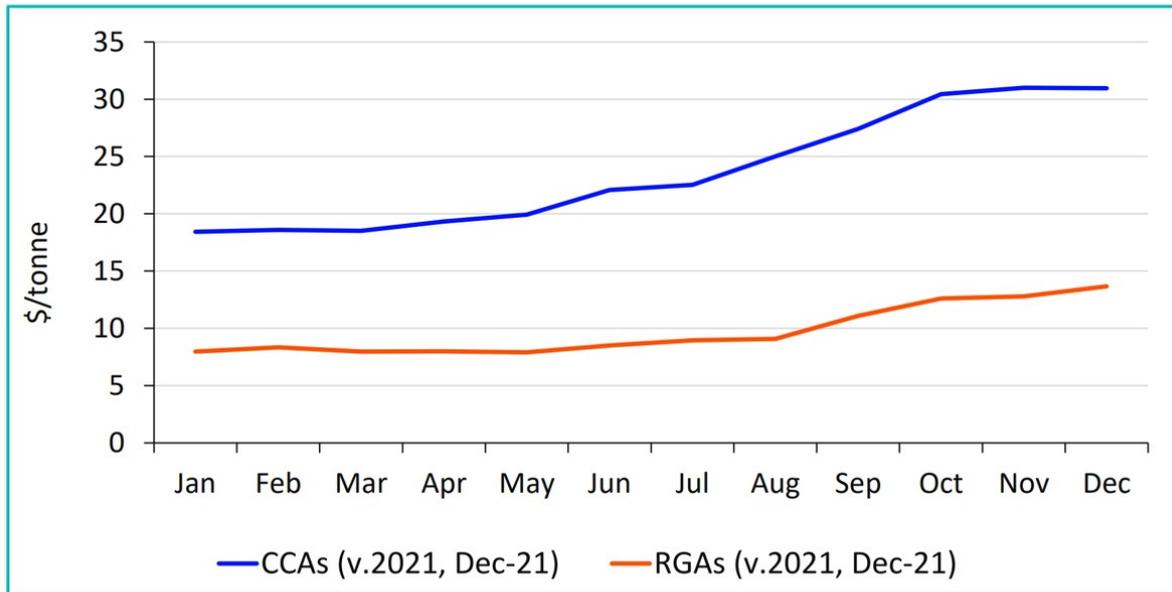
Source: Refinitiv

## 2. CCA- California Carbon Allowances

The California Air Resources Board (CARB) and the Ministry of the Environment and Climate Change of the Canadian Province of Quebec have collaborated to form a single cap and trade market to govern emissions in their respective territories. In California, approximately 400 institutions have compliance obligations while an additional 200 are required to report their emissions, covering ~74% of California's carbon emissions<sup>5</sup>. California has a series of longer-term climate targets including a 2030 state reduction target of 40% below 1990 levels and an objective of carbon neutrality by 2045.

Price rose steadily over the course of 2021, from \$18 in Jan 2021 to \$31 in Dec 2021<sup>6</sup>.

### CCA and RGGI (RGA) monthly closing prices in 2021



Source: Refinitiv, Intercontinental Exchange (ICE) and Nodal Exchange

### 3. UKA- UK Allowances

As a replacement for the UK's participation in the EU emissions trading system (ETS), the new UK emissions trading system came into operation on January 1, 2021. The allowances trading under the UK ETS are referred to as United Kingdom Allowances (UKA). The first UKA auction took place in May 2021 and sold more than 6 million allowances at a market clearing price of GBP £44<sup>7</sup>, since then, the UKA has been frequently trading at a premium to EUA.

The UK ETS currently covers approximately 2,000 installations in the power generation sector, aviation, and other energy intensive industries, similar to the scope of the EU ETS. According to Refinitiv, a total traded volume of 335 Mt UKAs transacted in 2021, making it the third most liquid ETS market globally, after EUA and CCA<sup>8</sup>.

During the Brexit negotiations, the UK government indicated that it would be open to consider the possibility of linking UKA with EUA. However, such idea has not been moving further since 2020 - It is worth noting that the linkage between Swiss ETS and EUA took almost a decade.

### 4. RGGI- Regional Greenhouse Gas Initiative Allowances

The RGGI is a cooperative, market-based effort among the US states of Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, Vermont, and Virginia to cap and reduce carbon emissions from the power sector, covering ~16% of RGGI's total emissions<sup>9</sup>. Price rose steadily over the course of 2021, from \$8 in Jan 2021 to \$14 in Dec 2021<sup>10</sup>.

### Why do we need a secondary carbon market?

Compliant companies (e.g. O&G companies), policymakers, and the general public participate in the carbon credit futures market for different reasons. Below are some of the key benefits of carbon credit futures trading:

- **Provide Flexibility** - Give compliant companies flexibility to decide how and when to manage

carbon emissions

- **Manage Risk** - Transfer risks (e.g. price risk) between counterparties
- **Enhance Transparency** - Help the carbon price discovery which in turn helps compliant companies' strategic planning and policymakers' decision making
- **Promote Innovation** - Encourage carbon market participation, incentivizing businesses to discover more sustainable business models

## Why Ninepoint Carbon Credit ETF?

For an emerging asset class like carbon credit, volatility management is at the heart of our fund strategy. Currently, the **Ninepoint Carbon Credit ETF** invests equally in the four major ETS markets globally with quarterly rebalancing. This strategy has demonstrated resiliency in the unprecedented recent carbon market volatility.

## Reasons for investors to consider Ninepoint Carbon Credit ETF

- **Diversification** - Balanced exposure to all carbon credit markets can help minimize single jurisdiction risk by eliminating over-concentration to any single market, as recent market action has demonstrated. Having a diversified underlying portfolio is important for an emerging asset class with volatile price patterns, like carbon credits
- **Global Exposure** - The fund provides investors with access to a US\$851 billion global carbon credit market which has grown by 18x since 2017<sup>11</sup>. Compared to volume-weighted fund or funds that invest in one single market, we believe that our equal-weighted fund strategy has a better value proposition, over the long-term, given its overweight to the under-represented and rapidly growing carbon credit trading markets
- **Core Value** - As a Canadian fund, by overweighting the North American market relative to its total index weight, we align the fund's strategy with our values and our society
- **Easy Access** - The fund is structured as an alternative mutual fund offering Series A, F, Q, QF, D on Fundserv and as an ETF series on the NEO Exchange (NEO:CBON / CBON.U)

## References

<sup>1</sup>Refinitiv, Carbon Market Year in Review 2021

<sup>2</sup>Refinitiv, Carbon Market Year in Review 2021

<sup>3</sup>International Carbon Action Partnership, Emissions Trading Worldwide: Status Report 2022

[https://www.ecb.europa.eu/pub/economic-bulletin/focus/2022/html/ecb.ebbox202203\\_06~ca1e9ea13e.en.html](https://www.ecb.europa.eu/pub/economic-bulletin/focus/2022/html/ecb.ebbox202203_06~ca1e9ea13e.en.html)

<sup>4</sup>International Carbon Action Partnership, Emissions Trading Worldwide: Status Report 2022

<sup>5</sup>Refinitiv, Carbon Market Year in Review 2021

<sup>6</sup>International Carbon Action Partnership, Emissions Trading Worldwide: Status Report 2022

<sup>7</sup>Refinitiv, Carbon Market Year in Review 2021

<sup>8</sup>International Carbon Action Partnership, Emissions Trading Worldwide: Status Report 2022

<sup>9</sup>Refinitiv, Carbon Market Year in Review 2021

<sup>10</sup>Refinitiv, Carbon Market Year in Review 2021

<sup>11</sup>Global carbon markets value surged to record \$851 bln last year-Refinitiv (Reuters - January, 2022).

**The Ninepoint Carbon Credit ETF is generally exposed to the following risks See the prospectus of the Fund for a description of these risks** **Absence of an active market for ETF Series risk, cap and trade risk, collateral risk, commodity risk, concentration risk, cybersecurity risk, derivatives risk, foreign currency risk, foreign investment risk, Halted trading of ETF Series risk, inflation risk, interest rate risk, liquidity risk, market risk, regulatory risk, securities lending, repurchase and reverse repurchase transactions risk, series risk, substantial securityholder risk, tax risk, trading price of etf series risk.**

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