



MARKET UPDATE

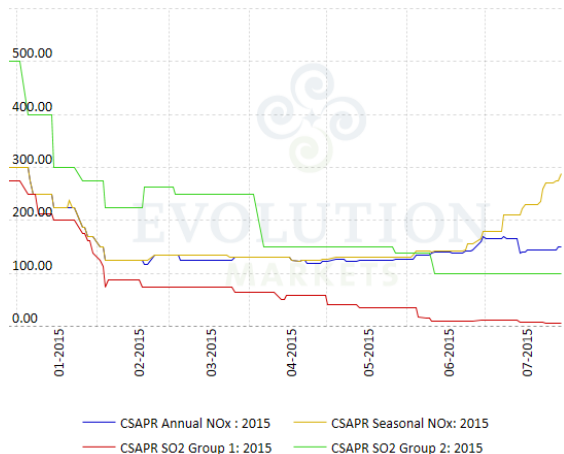
July 31, 2015

Cross State Air Pollution Rule

Market Status

The US Court of Appeals for the District Court of Columbia Circuit ruled this week that the EPA must reconsider the 2014 Budgets for SO₂ and Ozone NO_x in several states because they required the States to reduce beyond the points necessary to achieve air quality improvements in downwind areas. The rule follows the Supreme Court decision last year upholding CSAPR. Importantly, the Court did not vacate the rule, and the 2014 budgets impact Phase 2 of the program, which starts in 2017. The Court urged the EPA to move promptly in its reconsideration of the Rule. CSAPR NO_x prices moved up in mid-July as market participants came in to hedge their summer emissions. However, prices were unaffected after the Court decision. Prices for Seasonal NO_x saw the biggest jump as prices increased 75%, to \$275 as offers were hard to come by in mid July. Prices settled at the end of the month as participants digested the contents of the Court decision. SO₂ Group 1 prices have settled between \$5.00 - \$10.00 and were not affected by the news. SO₂ Group 2 Market Participants were looking to see if Texas would remain in the program, and although the Court decision seems to resolve that issue, the reconsideration affects SO₂ emissions budgets for Alabama, Georgia, South Carolina and Texas, all of which are covered by the Group 2 SO₂ cap.

Term (2015)	Bid	Offer
Annual NOx	\$145.00	\$155.00
Seasonal NOx	\$275.00	\$300.00
SO2 Group 1	\$ 4.00	\$ 10.00
SO2 Group 2	\$50.00	\$100.00
Acid Rain SO2	\$0.25	\$0.75



Future Outlook

Although we finally heard from the D.C. Circuit Court resolving the remaining issues with CSAPR, as in life, the Court ruling does not finalize all issues and there are still unanswered questions. Although the CSAPR rule was not vacated, market participants will still need to see how the EPA resolves the budget reconsideration in Phase 2. Some States can see their budgets increased, decreased, or some state could be removed from the program altogether. This uncertainty will hinder future hedging and the market will most likely still be a spot traded market until future budgets are known

Fundamentals

Current Emission vs. Allowance Allocation estimates show that all four CSAPR markets are long in Phase 1 (2015 – 2016). The tightest markets being both Annual and Seasonal NO_x where there are several states projected to be short Allowances, but as a whole the markets is long. SO₂ Group 1 is long in Phase 1 but reductions in the Allocation in Phase 2 can make the SO₂ Group 1 market short. Since this is the start of the program, there is no bank of allowances to draw upon in 2015. If projected surpluses do not come to market for a variety of reasons, it may affect the market demand supply picture.