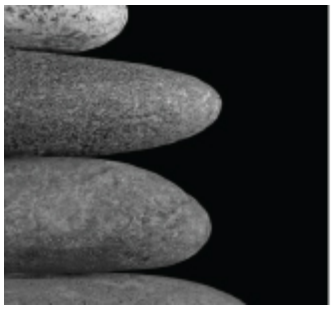


EVOLUTION MARKETS

The Intersection of Energy, Environment, and Finance™

MARKET UPDATE

September 13, 2016

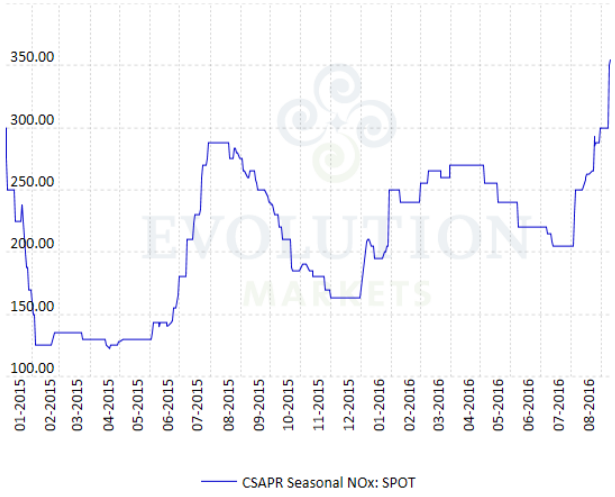
Cross State Air Pollution Rule

Market Status

On September 7th, the U.S. Environmental Protection Agency (EPA) finalized an update to the Cross-State Air Pollution Rule (CSPAR) Seasonal NOx Program. Starting May 2017, the final rule will reduce seasonal NOx allocations by approximately 48%. The final rule covers 22 states and includes an allowance trading program for implementation. The rule also allows Georgia to voluntarily opt into the state trading program.

The 2015/2016 Seasonal Allocation was approximately 628,000 tons and 603,000 tons, respectively. The new 2017 allocation is 316,000 tons. Actual 2015 emissions were approximately 463,000 tons, which represents a 165,000 ton 2015 bank. The EPA estimates the 2015/2016 bank to be approximately 350,000 tons. In the final rule, the EPA will apply a one-time ratio to the 2015/16 bank, reducing it to around 99,700 tons. Although the exact ratio is not known, the EPA will take the full bank and divide it by 99,700 tons. Based on the EPA's 350,000 estimated bank, the ratio is expected to be around 3.5.

With a 2017 allocation of 316,000 tons – and a bank of allowances of 99,700 tons – the available allowances for compliance in 2017 is approximately 416,000 tons. With 2015 (and anticipated 2016) Seasonal NOx Emissions around 460,000 tons, the 2017 market is short and reductions will have to occur.



Future Outlook

Seasonal NOx prices for 2016 jumped from $300 to $350 the day after the EPA announcement, and prices so far have stayed there. Applying a 3.5 ratio to this $350 Allowance Bank price, an implied 2017 Seasonal NOx price is $1,225. As market participants digest the new information, 2016 compliance Buyers will have to purchase any anticipated short fall. This may push prices higher if Sellers become too conservative with their Allowance Bank. Based on the 2017 final allocation and 2015 emissions data, every state in the program is short allowances.

However, with 2017 prices above $1,000, one can anticipate that electric power generation units will reduce their emissions by either running pollution controls more aggressively, switching to a lower NOx emitting fuel when possible, or retiring some units. Either way, reductions in emissions will have to occur. If control measures occur, prices may drop as the demand drops, however this may not take place until mid- to late-2017 as participants assess actual emissions relative to their allocations.

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