

Tuesday 20 January 2026

A turbulent year for EU ETS

- **ETS price:** The ETS price fell from a level of EUR 92/ton to around EUR 85/ton as a result of risks surrounding reciprocal trade tariffs between the US and EU Member States.
- **Frontloading:** The targeted EUR 20 billion in REPowerEU financing is expected to be raised in the coming months, bringing an end to frontloading volumes.
- **ETS Phase 5 proposal:** The European Commission will publish a proposal next year for the EU ETS from 2031 onwards.
- **CBAM:** The ETS border levy entered into force (partially) as of 1 January this year, while both internal and external pressure on the mechanism continues.
- **Electricity price:** The Dutch electricity price (baseload, active month contract) is following price movements on the TTF gas market, where a multitude of factors have led to sharp price increases in recent days.

The ETS market prices in the risk of trade tariffs

The December contract of the European Union Emissions Trading System (EU ETS) is currently trading at around EUR 85/ton. This means the ETS price has fallen by more than 7% since last Friday's closing price (EUR 92/ton). The price movement this week is the result of (limited) profit-taking on excessive long positions. The price decline followed the announcement of US import tariffs over the past weekend. Trump threatened import tariffs of 10% as of 1 February (and 25% as of 1 June) in response to military exercises by a number of NATO Member States in Greenland.

If these import tariffs materialise, EU exports of industrial products to the US would become financially less attractive. As a result, expected emissions and demand for emission allowances would decline. Whether the import tariffs will actually enter into force remains to be seen. What is clear, however, is that geopolitical interests and economic measures and impacts are becoming increasingly intertwined.

ETS-price



Source: LSEG Eikon

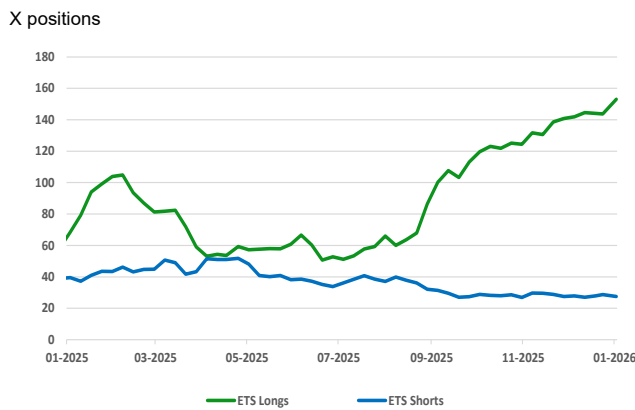
The upward trend in the ETS market

The price correction resulting from risks surrounding trade tariffs is taking place amid the current upward trend in the market. Last week, the ETS price settled above EUR 90/ton for the first time in 2.5 years. The upward trend that led to this price level started in September 2025, but accelerated in particular after breaking through the EUR 80/ton level a few weeks ago.

This trend is largely related to the activity of speculative market participants. On Wednesday 14 January, the Commitment of Traders report showed that the net position of speculative investors had risen to a record level of more than 125 million tons. In the preceding week, the largest increase in the

net position in four months was also recorded. It is clear that sentiment around the ETS market in recent months has been dominated by expectations of a tighter market balance and rising prices.

ETS specs



Source: LSEG Eikon

End of frontloading impacts the supply of emission allowances

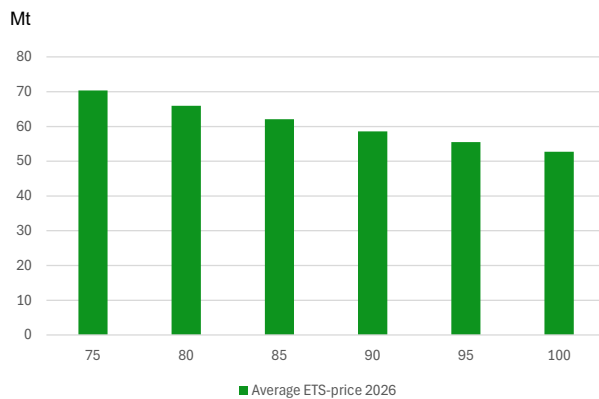
That sentiment is underpinned by a number of fundamental drivers. One of these relates to REPowerEU financing. Following Russia's invasion of Ukraine, the European Commission (EC) decided to frontload ETS allowances. This means that emission allowances are auctioned earlier than originally planned. Strictly speaking, the multi-year supply of emission allowances remains unchanged, but there is a shift in the timing of supply. In this way, the EC aimed to free up cash resources to roll out policies that would make the EU energy-independent from Russia more quickly.

As a result, from 2023 onwards a temporarily looser market was created by bringing forward the sale of allowances from the 2027–2030 period. The EC had announced in advance that it aimed to raise a total of EUR 20 billion through this mechanism. It has since become clear that this total amount is likely to be reached sometime in the coming months. At that point, frontloading will, as planned, be halted immediately. The exact timing, however, depends on the level of the ETS price.

Initially, frontloading led to a temporarily looser supply, resulting in downward price pressure. Now that the required financing target of EUR 20 billion is coming into sight, the relationship between the financing target and the ETS price has come firmly to the fore. After all, at a higher ETS price, fewer allowances are needed to raise the required financing, and vice versa. This creates an upward price effect. Pushing up the ETS price, as a result of the build-up of the net long position, leads to faster achievement of the required REPowerEU financing. In short, a higher price leads to a smaller supply.

The chart underneath shows the frontloading supply in 2026. At an average ETS price of EUR 75/ton, around 70 million additional emission allowances will be offered this year. In that case, frontloading will end in July of this year. At an average ETS price of EUR 100/ton, the frontloaded supply this year amounts to around 50 million emission allowances. In that case, the auctioning of these additional allowances will stop around April. Out of a total supply of around one billion allowances this year, the difference amounts to only a few percentage points. However, relative to the required annual cap reduction — around 90 Mt — the difference is significant.

Frontload supply 2026



Source: EqoLibrium

CBAM and benchmark adjustments contribute to upward sentiment

As of 1 January 2026, the Carbon Border Adjustment Mechanism (CBAM) has come into effect (more on this later). The introduction of this mechanism coincides with a reduction in the allocation of free emission allowances to industry. In addition, EU benchmarks, which are also relevant for the allocation of free allowances, are being tightened this year. The publication of these new benchmarks is expected in the first quarter of this year.

Both developments mean that industrial companies will need to cover a larger portion of their allowance requirements through auctions or the market. On an annual basis, this does not lead to a higher structural demand for allowances, since the portion that was previously allocated for free now needs to be purchased. However, it is reasonable that companies anticipate these changes by bringing forward their required purchases and (partially) hedging in advance. This has therefore also been a factor contributing to upward price pressure in the market over the past weeks and months.

The 2026 revision of the EU ETS

With the start of 2026, the fourth phase of the EU ETS (2021–2030) is now halfway through its lifespan. An important revision of the emissions trading system is planned for the second half of this year. The European Commission is reportedly set to publish a proposal in July, which will define the EU ETS in Phase 5, from 2031 onwards. This proposal will need to be aligned with the recently adopted EU-wide target of a 90% greenhouse gas reduction by 2040.

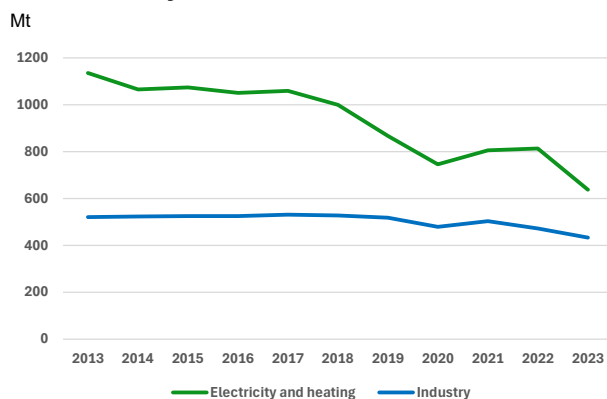
Developments regarding public acceptance and potential adjustments to ETS2 are also relevant in this context. From 2028 onwards, ETS2 will apply mainly to emission reductions in the road transport and buildings sectors. Both the EU ETS and ETS2 together account for the bulk of the emission reductions required under the 90% target. In other words, the emission reductions enforced by the EU ETS effectively ease the burden in ETS2, and vice versa.

At the same time as the EU ETS revision, the European Commission will publish an extensive regulatory package next year regarding Carbon Capture and Storage (CCS). The fact that these two policy packages are published simultaneously illustrates the interconnectedness of the two types of climate policy. This connection becomes clear when looking at the (historical) emission reductions of the EU ETS.

The total emissions under the EU ETS are largely attributable to the energy sector (electricity and centralized heat) and (large) industry. The emission reductions achieved by the EU ETS to date — around 50% compared to 2005 — have mainly come from the energy sector. The growth in renewable

energy capacity, such as solar and wind, has played the largest role in this. This growth has resulted in reduced electricity generation from fossil sources such as coal and natural gas.

Emission reductions are occurring primarily in the electricity sector



Source: European Union Transaction Log

Impact of decarbonization on ETS price differs between East and West

It is understandable that historical emission reductions within the EU ETS have taken place mainly in the electricity sector, as the costs for doing so are lowest. This changes when looking toward the future. In Western European countries, annual electricity consumption is already around 50% renewable. Further expansions of solar and wind capacity in these countries generally result in smaller emission reductions than in the past.

Newly built solar panels and wind turbines will generate renewable energy at the same times as the existing capacity. Due to insufficient use of storage options, this can lead to periods of necessary curtailment. In addition, it reduces the business case for new projects. Partly as a result, the government revised its offshore wind target downward last year.

The situation is different, particularly in Eastern Europe. Many countries there still have a high dependence on hard coal or lignite in their electricity mix. An increase in solar and wind production capacity in these regions could potentially lead to a substantial reduction in demand for emission allowances. Coal-fired power plants are roughly twice as emission-intensive as gas-fired plants. In short, the greening of electricity generation in Eastern Europe has the potential to significantly impact the ETS market in the coming years.

The impact of CCS in the coming years

The chart above shows that the relevance of industrial decarbonization for the ETS market is steadily increasing. While emissions from the energy sector in 2018 were roughly twice as high as those from industry, the emissions of both sectors are rapidly converging. This is changing the nature of demand for emission allowances in the ETS market. Unlike emissions from the energy sector, industrial emissions are generally less influenced by weather patterns. Over time, this should reduce the impact of weather on the ETS market — at least on an annual basis.

At the same time, attention on the demand side of the market will increasingly shift to the implementation of CCS projects. The CCS policy package, which will be published later this year, is intended to help the sector achieve the target of 50 Mt of CO₂ reduction through capture and storage by 2030. The current linear reduction factor of the EU ETS requires a CO₂ reduction of around 90 Mt per year. In this context, the CCS target accounts for more than 50% of the required CO₂ reduction in the EU ETS by 2030.

Moreover, the development of CCS projects can have a significantly more abrupt market impact than the rollout of solar and wind projects seen in recent years. Emission reductions in the electricity sector result from a large number of renewable energy generation projects. CCS, on the other hand, typically involves a few large-scale projects that only become viable once all necessary parties can make a positive Final Investment Decision (FID). For example, the Aramis project will ultimately need to provide capacity equivalent to over 20 Mt of emissions per year. The success or failure of a single CCS project like Aramis therefore has a relatively large impact on the ETS market.

In short, the factors influencing demand for emission allowances are slowly changing in the coming years. The rollout of solar and wind in Western Europe has played an important role in recent years. Going forward, the market's focus on decarbonization in the electricity sector will increasingly shift eastward. Regarding industrial emissions, attention will focus on the progress of CCS. Both developments may follow a bumpier path than the rollout of solar and wind in Western Europe over the past years.

CBAM will undergo a practical test

In addition to decarbonization in the energy sector, emission reductions in industry will play an increasingly prominent role in the ETS market in the coming years. The entry into force of CBAM on 1 January this year is illustrative of this. This CO₂ border levy is intended to ensure that industry within the EU — which faces higher ETS costs — remains competitive with industry elsewhere in the world. The question to be answered over the coming years is the extent to which the implementation of CBAM aligns with its political intentions.

Currently, ETS-industry receives a relatively large portion of its emission allowances for free. This free allocation largely ensures a level playing field between EU industry — which faces ETS costs — and industry outside the EU. The political concern is that this free allocation does not sufficiently incentivize companies to reduce emissions. As a result, it has been decided to phase out the free allocation of allowances so that the assumed financial incentive for decarbonization is increasingly felt.

However, phasing out free allowances would also create an unequal playing field. EU industry would be exposed to ETS costs, while industry outside the EU would not, or only to a lesser extent. CBAM has therefore been introduced. CBAM is being phased in simultaneously with the reduction of free allowances. However, CBAM cannot fully prevent an unequal playing field for the export of industrial products to countries outside the Union. Moreover, its scope is limited, as the mechanism primarily covers basic industrial products, while imported finished products are mostly excluded.

CBAM therefore fails to fully compensate for the cost disadvantage in the export of industrial products from the EU. This limitation is particularly problematic for sectors and companies that are highly dependent on exports, such as the chemical and steel industries. These sectors are still awaiting policies that provide a solution to this issue.

CBAM from a geopolitical perspective

The characteristics of the mechanism outlined above are well known and have already led to criticism within the EU. But parties outside the EU have also voiced their objections. CBAM is, de facto, an import levy that affects exports from non-EU countries to the EU. For example, on Thursday 1 January, the Chinese Ministry of Commerce labeled CBAM as unfair and announced that it would take countermeasures.

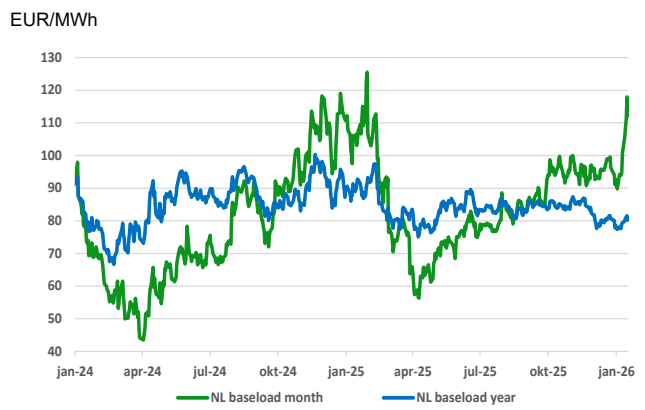
Although the Chinese countermeasures remain uncertain at this time, they come at a moment when European industry is struggling. In addition, restrictive trade measures from the US also threaten to emerge. At the same time, the European Commission has, in the spirit of the Draghi report, set out a policy path intended to address industry concerns.

The question, therefore, is whether the CBAM “soup” is as hot as it is currently being presented. The phased introduction of CBAM provides both industry and policymakers time to let that “soup” cool. For instance, in Q1 or Q2 of this year, an EC proposal is already expected that will expand the scope of CBAM to downstream goods. In short, the entry into force of CBAM marks a new phase of the EU ETS, in which industry is increasingly exposed to costs. Nevertheless, the policy will continue to be fine-tuned throughout the duration of this new phase.

Electricity price rises following gas price

The active month contract of the Dutch electricity price (baseload) is trading around EUR 110/MWh. This means the price of the month-ahead contract has risen by approximately 15% compared to a month ago. This development is largely linked to the increase in gas prices on the TTF market. On Friday 16 January, the TTF month contract closed at just over EUR 37/MWh, more than 30% higher than the closing price a week earlier.

Electricity price



Source: LSEG Eikon

The sharp price increase on the TTF market over the past week is the result of a combination of risk factors coming into play. First, large parts of Europe and Asia experienced a cold wave, while the EU gas storage level was only 50%. This is about 15 percentage points below the five-year average.

In addition, France is dealing with the outage of the Flamanville nuclear power plant, at least until 31 January. This plant accounts for 7% of the country’s nuclear capacity. The outage therefore increases pressure on gas demand for electricity generation in Western Europe. Geopolitical tensions surrounding the situation in Iran have also raised the risk premium on gas prices.

Finally, the market had taken on a significant number of short positions. In other words, in recent weeks and months there had been heavy speculation on price declines. When the fundamental price drivers mentioned above created upward price pressure, this prompted the closing of short positions (and the opening of long positions). The closing of short positions thus added further momentum to the upward price movement.

In short

Negotiations on linking the EU and UK ETS – This week, negotiations begin between the United Kingdom and the European Commission on linking the European and UK emissions trading systems. This follows a mandate approved by the European Council on 12 November. Once the two parties reach an agreement, the UK will also be exempt from CBAM, which

could reduce administrative costs for the UK. British industries had sought an exemption from the border levy due to these costs, but Brussels has decided that this exemption will be granted before the link is finalized.

The European Commission expands the Indirect Cost Compensation (ICC) – To prevent carbon leakage in energy-intensive sectors, the EC is expanding the ICC to include 20 new sectors. This increases the compensation intensity from 75% to 80%. The ICC reimburses a portion of the additional electricity costs that companies incur due to the EU ETS. In addition, large recipients of the compensation are required to invest part of the reimbursement in reducing their electricity costs.

Energy agenda

Organisation	Date	Event
US Supreme Court	21-1-2026	Follow-up lawsuit Fed Gov. Lisa Cook
International Energy Agency (IEA)	21-1-2026	Publication <i>Oil Market Report</i> January
International Energy Agency (IEA)	23-1-2026	Publication Gas Market Report - Q1 2026
Federal Reserve (FED)	28-1-2026	Interest rate meeting US
European Commission	29-1-2026	Publication <i>Competitiveness Package</i>
European Commission	29-1-2026	Publication Industrial Accelerator Act
OPEC+ (V8 landen)	1-2-2026	V8-meeting
European Central Bank (ECB)	5-2-2026	Follow-up lawsuit against Fed Gov. Lisa Cook
International Energy Agency (IEA)	12-2-2026	Publication <i>Oil Market Report</i> February
OPEC	12-2-2026	Publication <i>Oil Market Report</i> February
International Energy Agency (IEA)	19-2-2026	IEA Ministerial Meeting
European Commission	10-3-2026	Publication Energy Package
Federal Reserve (FED)	18-3-2026	Interest rate meeting US
European Central Bank (ECB)	19-3-2026	Interest rate meeting Eurozone
Federal Reserve (FED)	15-5-2026	End of term for Fed-chair Powell
OPEC+	7-6-2026	Vienna-meeting on i.e. production quota
European Commission	jul-26	Publication proposal EU ETS phase 5

For more information about this update or other services offered by EqoLibrium, please contact:

Hans van Cleef – hans.vanCleef@eqolibrium.com / 0031- 6 30 90 33 76

Bart van der Pas – bart.vanderpas@eqolibrium.com / 0031 – 6 36 52 95 51

Fabian Steenbergen – fabian.steenbergen@eqolibrium.com / 0031 - 6 18 55 34 46

Marije Willigenburg – marije.willigenburg@eqolibrium.com / 0031 – 6 21 91 83 03

Guusje Schreurs – guusje.schreurs@eqolibrium.com

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