

THE PARIS CLIMATE AGREEMENT AND COAL: RELEVANT, BUT NOT DEFINITIVE

In Brief:

The Paris Climate Agreement has been variously hailed as bringing about the 'death of fossil fuel' and alternatively has been called a 'sham' for relying on national government promises without binding commitments. It has tremendous importance for all involved in the energy sector, but, considering its call for action (contributions) to be decided and taken at the national level, may be all things to all nations, but not always the same things. While coal markets will undoubtedly be impacted by the Agreement, the current coal market slump is unrelated; rather, this can be attributed to the slackening coal demand in China and, to a lesser extent, the plentiful supply of energy substitutes, most notably natural gas.

A Few Details:

There is no doubt these are challenging times for most parts of the international coal sector. In New York, 175 countries have joined on the opening day to sign the Paris Climate Agreement, hailed as "game changing" for the shaping the structure of global natural resource production and consumption, and more specifically, for how governments and corporations address climate change. Not surprisingly, many journalists and analysts have linked coal markets with Paris. While the long term future of coal is severely threatened by the climate change agreement, there is little linkage between it and today's dismal coal markets.

Gone are the days of "top-down" global targets (that didn't do much to slow the growth of greenhouse gas emissions), replaced by "Nationally Determined Contributions" (NDCs) for almost all countries worldwide. This new paradigm also brought over 11,000 commitments from companies, investors, cities, regions or other groupings. And the Agreement sets an objective to keep temperature increase "well below" 2°C. Nevertheless, several studies indicate that the existing NDCs are far from meeting the critical target of maintaining temperature increase below two degrees. In fact, most analyses believe they are likely to result in warming of between 2.7 and 3 degrees.

What might this mean for coal? To start to understand the potential impact, let's consider how much greenhouse gas emission reduction a two degree target entails. The International Energy Agency calculated emissions trajectories for a 450 ppm CO₂ scenario, which approximates this target. It estimates that between 2013 and 2030 energy-related CO₂ emissions must decline from 32.2 Gt to 25.6 Gt, and further decline from then.

In contrast, the IEA's scenario for energy-related emissions is considerably less ambitious if the Paris Agreement's initial Nationally Determined Contributions are taken to be the limit of future ambition. IEA's Energy and Climate Change Special Report estimates that energy-related emissions could increase from 32.2 Gt in 2013 to 34.8 Gt in 2030. How the emission budget is allocated between fuels and nations could be significant. There are extremely wide differences in the anticipated coal demand between countries; coal in the EU, for instance, is likely to decline to a relatively small share of all fuels consumed by 2030 in either IEA scenario, whereas coal consumption in countries like India will likely expand, albeit at a slower rate than non-fossil sources.

Yet a linkage of the slump in coal prices, and associated coal bankruptcies and mine closures, to the Paris agreement, is most likely wishful thinking, and again illustrates different approaches and priorities between the US and Europe on the one hand, and rapidly growing Asian economies on the other. The latest IEA World

Energy Outlook (considering a scenario similar to adoption only of the initial Nationally Determined Contributions) foresees that even by 2040 the world's energy supply mix divides into four almost equal parts: oil – gas – coal – low-carbon sources, with coal still accounting for 30% of electricity generation.

So why is coal currently seeing such a dramatic downturn? The mundane answer is all about supply and demand balances and, as is the case with so many other commodities, the slowdown in China. With only around 15% of coal being internationally traded and with China alone responsible for around 50% of world coal supply and demand, even a small rebalancing in Chinese coal market dynamics can have a massive impact – and this is what is happening. Meanwhile, the travails of the US coal industry are almost entirely the result of the shale gas revolution. The question is whether coal prices can ever recover as supply and demand is rebalanced.

So what can we conclude from the above for the future? Very little, except that coal consumption will face further constraints as each five years, parties to the Agreement need to recommit and strengthen their targets. Interestingly, different nations could come up with very different emission reduction targets and policies, as ultimately national politics will play the dominant role in NDC target setting. For instance, if carbon capture and storage is a strategy that is both feasible and embraced by policymakers and energy consumers in a growing number of countries, then the position of coal could be much brighter, at least for the next several decades.

The COP21 outcome seems to mean different things to different continents. In Europe it is, uniquely, a binding commitment and opportunity to be World leaders. In India and South East Asia the NDCs foresee further rapid construction of coal stations; not only are they unabated – some are not even HELE (high efficiency low emissions) partly because of entirely perverse consequences of the divestment campaign. In America COP21 will be treated differently depending on the results of the upcoming elections, and, possibly linked to them, on the future make-up of the Supreme Court. However, whilst COP21 does not herald the end of coal, which will be with us for decades to come, it may mark the beginning of the end.

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Nigel joined the coal industry in 1977 after graduating in Physics from Cambridge University. He moved to UK Coal in 1995 on privatisation of the industry and was Marketing Director until end-2005. Since 2006 he has developed his consultancy business in the coal and energy field, and is founder and Managing Director of CoallMP, the Association of UK Coal Importers and Producers.