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Quarterly Report

Report 57

February 2013

The Marketplace for PRNs and WENs



November 2012 to January 2013

By Ian Andrews

As we entered the final quarter of the compliance year genuine fears regarding non compliance were at the forefront of everyone's mind. The year had got off to a bad start with early supply figures identifying issues with the plastic and glass markets. In the end both of these markets remained fully stocked right up to the close of the year. While some complaints were to be heard from glass buyers regarding the associated costs of complying when entering the market at the last minute, the higher costs seen in the second half of the year, provided the market with the extra boost in supply which in turn enabled most if not all UK businesses to comply. Further evidence of the remarkable turnaround in glass was provided when buyers holding transitional tonnage started to accept it against 2013 obligations after being previously asked by the agencies to release the tonnage back into the market.

If we are to take anything from the previous compliance period, it has to be that when the chips are down and prices start to increase to close the gap in supply side, the UK method of compliance addresses the shortfalls swiftly and puts the system back on track albeit at increased costs to the producers. While higher prices are never palatable for business, the UK is unique in that the higher values are never sustained and periods of high values tend to be followed by extended periods of lower values.

Trading for the quarter equated to 292,136 tonnes with 197,846 tonnes trading in the Spot 2012 market, 26,403 tonnes trading in the Spot 2013 market and 64,888 tonnes trading in the Forward markets.

Market Material Analysis

Paper – Paper traded in strong volume throughout the quarter with very little variation on prices. Good supply remained in the market right up to the close with some higher values being achieved from last minute buyers.

Plastic – After a sustained period of increasing values resulted in excellent growth in supply, the final quarter saw prices soften back down into single figures. It has been a remarkable turnaround in plastic this year with supply outstripping demand in the last month of the compliance year. Prices subsequently fell to close at the lowest price for the year of £2.00.

Glass – The glass market remained active right up to the year end. Prices held firm as the majority of late selling came from the December transitional pot meaning that anyone holding this tonnage had flexible delivery options against 2013 contracts and were under no pressure to drop prices against 2012 buying interest.

Steel – Strong demand in the final quarter resulted in the price holding firm. Prices started to soften toward the end of the year when it became evident that strong supply was still being offered to the market. At the end of the year some tonnage remained unsold and will have been returned to the agency marking a turnaround in fortunes for this market.

Wood – This market continued to hold its price premium above paper and although this meant that it subsequently lost out to some volume trading opportunities in general buying, by the end of the compliance period tonnage became so scarce the price rebounded for last minute buyers.

Aluminium – A slow quarter for aluminium sales resulted in very little movement in prices. Sellers in this market took the early decision to write back unsold tonnage rather than devalue the note to incentivise sales.

Recovery – Prices for recovery remained unchanged from the previous quarter. Supply in this market continued to outstrip demand by a large margin.

	High this quarter	Low this quarter	Traded this quarter	Quarter average traded price	YTD average traded price	YTD aggregated traded
PAPER MARKET						
Spot 12	£2.20	£0.50	93,278	£0.74	£0.83	170,103
Spot 13	£0.85	£0.85	1,319	£0.85	£0.85	1,319
Dec Fwd 2012	£1.15	£0.65	13,554	£0.73	£0.81	64,380
Jan Fwd (Trans)	£1.15	£0.85	11,177	£0.88	£0.88	11,177
Apr Fwd 2013	£1.00	£0.90	1,142	£0.91	£1.05	2,142
PLASTIC MARKET						
Spot 12	£12.00	£2.00	45,965	£7.66	£13.98	104,095
Spot 13	£18.00	£12.50	9,610	£14.50	£14.50	9,610
Jan Fwd (Trans)	£18.00	£15.00	3,250	£16.09	£16.09	3,250
Apr Fwd 2013	£16.00	£16.00	2,500	£16.00	£16.00	2,500
GLASS MARKET						
Spot 12	£85.00	£60.00	30,809	£73.42	£40.87	104,039
Dec Fwd 2012	£75.00	£75.00	16,435	£75.00	£56.64	65,135
Jan Fwd (Trans)	£75.00	£75.00	5,425	£75.00	£68.27	7,425
Oct Fwd 2013 (Agg)	£45.00	£45.00	222	£45.00	£45.00	222
Oct Fwd 2013 (Rem)	£55.00	£55.00	220	£55.00	£55.00	220
STEEL MARKET						
Spot 12	£55.00	£7.00	14,164	£35.43	£24.44	37,736
Spot 13	£15.00	£13.00	1,489	£14.56	£14.56	1,489
Dec Fwd 2012	£36.00	£35.00	3,800	£35.21	£22.49	6,400
Jan Fwd (Trans)	£38.00	£35.00	500	£36.20	£36.20	500
Apr Fwd 2013	£28.00	£20.00	750	£23.74	£24.24	1,250
Jul Fwd 2013	£20.00	£20.00	650	£20.00	£20.00	650
WOOD MARKET						
Spot 12	£5.00	£1.15	9,009	£1.28	£1.40	17,817
Spot 13	£1.60	£1.60	160	£1.60	£1.60	160
Dec Fwd 2012	£1.15	£1.15	3,000	£1.15	£1.18	5,500
Apr Fwd 2013	£1.60	£1.60	3,000	£1.60	£1.60	3,000
ALUMINIUM MARKET						
Spot 12	£10.00	£4.00	638	£5.71	£8.33	4,568
Spot 13	£7.50	£4.95	119	£5.30	£5.30	119
Dec Fwd 2012	£7.00	£4.95	1,260	£6.30	£6.30	1,260
RECOVERY MARKET						
Spot 12	£0.35	£0.30	3,985	£0.31	£0.33	23,667
Spot 13	£0.25	£0.25	13,706	£0.25	£0.25	13,706
Jan Fwd (Trans)	£0.30	£0.30	1,000	£0.30	£0.30	4,000



Managing Director's Report

A final quarter filled with the unexpected as the realisation came about that not only was it possible for everyone to comply in the Glass PRN market but also the flexibility of the PRN system had stimulated the solution with the glass industry responding to the high prices to deliver the requisite number of PRNs. Slightly less spectacularly so too had compliance been delivered in the plastic and steel sectors where some uncertainty had previously existed. A quarter of strong demand saw the fourth highest volume ever of trading in a quarter.

Reviewing the year the high prices and uncertainty saw a shift in trading from the forward to the spot markets with 47.6% traded in the spot, a level not seen since 2009 and the first time that the trend of growth in trading forward contracts has slipped. Something in hind sight that many buyers will have regretted. Disappointingly with trading slowing up in materials other than glass in January we missed the magical million mark in 2012 PRNs by a meagre 30,000 tonnes. Nevertheless a growth of 20% and 22.5% respectively in transactions and traded volume was achieved over the previous compliance year!

2013 has started more slowly as obligated companies and compliance schemes are licking their wounds a little from the high prices in 2012, something that was not anticipated at the start of the year, are revisiting their obligations, checking their budgets, planning their strategies and hoping that prices might fall. This is a difficult prediction to make. On the demand side it is to be anticipated that a modest Christmas and the impact of the Courtauld agreement will have a downward pressure on packaging handled in 2012. However there remains a significant gap in the key materials of glass, steel and plastic between the

tonnage of packaging reported as placed on the market by obligated companies and by the material obligations. Until this is sorted out there is should be a resistance to increasing the de minimis tonnage or turnover.

On the supply side carry forward at 263,155, the lowest since 2001, was some 60,000 tonnes less than what was brought into 2012 and comparable to the figure carried forward from 2008 which many will recall as a difficult year. Very little Recovery was carried forward from 2008 whereas this time some 40,000 tonnes has been. Of interest, against a backdrop of a flight of wood to biomass projects, is that carry forward of both paper and wood is at the lowest level since 2001. Of possibly greater significance, given the traumas of last year and the uncertain consequences of splitting the obligation, is 16,674 is the second lowest figure ever carried forward in glass.

The carry forward in plastic is up as is their material specific target. The plastic industry although they have expressed concern about the feasibility of achieving their target and what they perceived as a lack of consultation on it had anticipated that the target was challenging but achievable. But as a sector that has relied on exports to meet almost 65% of its PRNs they will view China's declared hard stance on 'foreign waste' imported through Hong Kong, the route followed by a substantial proportion of UK plastic for recycling with concern. As a result there has been an upward correction in price.

2013 looks as though it could develop into as interesting year as 2012. Thank you to all those who supported us through 2012. We look forward to being of service to you in 2013.

Angus Macpherson
Managing Director

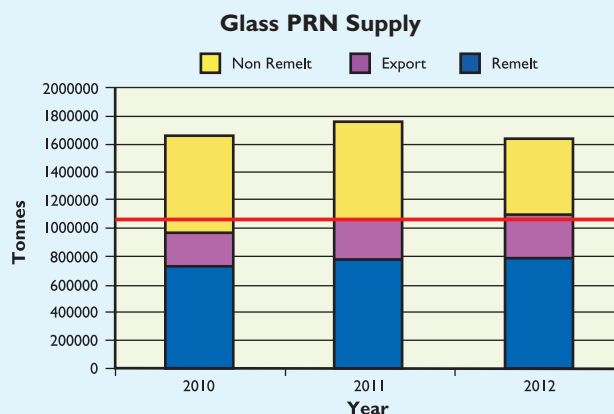
2013 Glass

Many are still trying to digest the price implications of this split. There is no cap on aggregates, solely a target for re-melt Glass PRNs and a target for total Glass PRNs. Obligated businesses have to acquire a minimum percentage of their glass obligation as re-melt glass PRNs and a minimum percentage of their general recycling obligation as glass, aggregate or re-melt, PRNs. While there will undoubtedly be many variations on a theme the split glass PRN is anticipated to work as follows:

If there is a:

- surplus of Glass PRNs in each category, re-melt and aggregate, their price will tend towards the general recycling price which is fixed by the surplus PRNs available in other materials predominantly paper and wood, although as I mentioned the extent of the latter surplus is reducing due to the dash for biomass.
- shortfall of total Glass PRNs, re-melt and aggregate, their price will rise and tend to drift together.
- surplus of Glass PRNs but a shortfall of re-melt PRNs but a surplus of aggregate PRNs, the re-melt price will rise but the aggregate price will tend to drift towards the general recycling price.
- shortfall of aggregate PRNs but a surplus of re-melt PRNs, the re-melt price will move towards the aggregate price, the overall direction of the glass PRN price will be determined on whether there is a net surplus or deficit of Glass PRNs.

It is unlikely that an aggregate PRN will ever exceed the price of a re-melt PRN because it can always be substituted by it. So why buy a more expensive PRN when a less expensive one will do the same job?



Note: The red line represents glass remelt obligations when calculated against 2012 demand figures



2012 Annual Review

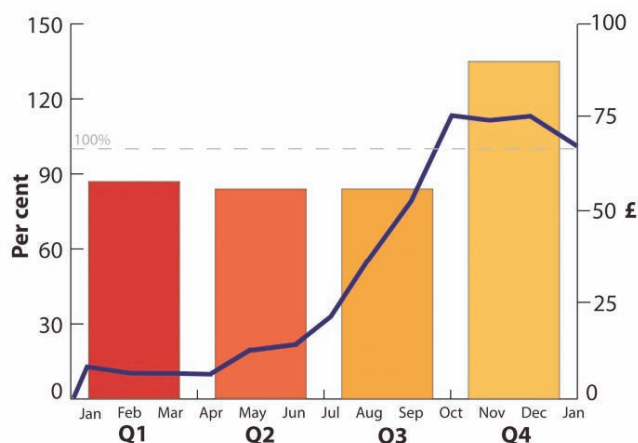
By Tom Rickerby

As the dust settles on the 2012 compliance year, The Environment Exchange takes a look back on a turbulent year of trading that saw the PRN system tested to the brink of collapse but ultimately emerge a more robust and credible system.

Wind the clock back 14 months and the climate of the PRN system was very different to now. A freeze on targets and an abundance of PRNs had left the markets flat and in some materials PRNs had become almost worthless. Whilst producers were enjoying their cheapest compliance in years (far cheaper than their European counterparts), accredited sellers were growing increasingly disillusioned by the increased administrative demands of the system coupled with limited financial rewards. This situation had led many to question the value of the market based system to drive UK recycling targets.

On paper, 2012 looked to be an administrative formality. Targets had been comfortably met in 2011 and PRN prices were showing no sign of recovery. 2012 opened as a strong buyers market but all that was about to change...

Glass Quarterly Supply vs Demand/Price



In the story of 2012, Glass will be remembered as the main protagonist. In 2011, the market was rocked by two separate investigations into the fraudulent issue of Glass PRNs. This fraudulent element had left the supply side of the market heavily distorted, however it wasn't until April of 2012 that the full ramifications of this were felt. Large PRN surpluses in 2011 saw Glass PRN prices fall to unprecedented levels. The 2012 market opened trading at £9 per tonne – the lowest opening price since 2000. At this stage, few would have predicted the storm that was coming.

With the fraudulent element removed from the market, coupled with a downturn in the aggregates market and less price support from the PRN, Glass recycling figures were hit hard. The release of the Q1 data in April was first clear cut indication of this with PRN generation falling 15% from the peak in 2011. This triggered a dramatic upward trend in the PRN price that would last for the next 7 months. However, despite the rising PRN price, recycling rates failed to improve for the following 2 quarters and as fears grew over mass non-compliance, distressed buying pushed spot prices to a record £75 per tonne. By October the glass market was over 15% undersupplied (138,000 tonnes) and was facing a severe uphill battle to achieve not only UK compliance but minimum European targets too. But just as people were beginning to right it off, the Glass market responded.

The high PRN price had started to have a major influence on activity right through the glass supply chain. Recycling activities that would previously have been uneconomical were now made viable by the £75 PRN subsidy. 1000s of tonnes of 'dirty' mixed glass were able to be cleaned, sorted and recycled, glass export increased by 77% in Q4 as new markets were 'unlocked' and fresh impetus was provided to stagnant markets in the glass aggregate sector.

In one of the tightest year ends in PRN history (Glass continued to trade at £70+ right up to the final minutes of the compliance year) and against all the odds, enough PRNs were generated in the final 3 months to meet demand.

In all 561,521 glass PRNs were generated in the final quarter, (an increase of 35% on the quarterly average for 2012).

Glass was not the only material to experience extreme volatility in the 2012 compliance year. Plastic also

Plastic Quarterly Supply vs Demand/Price

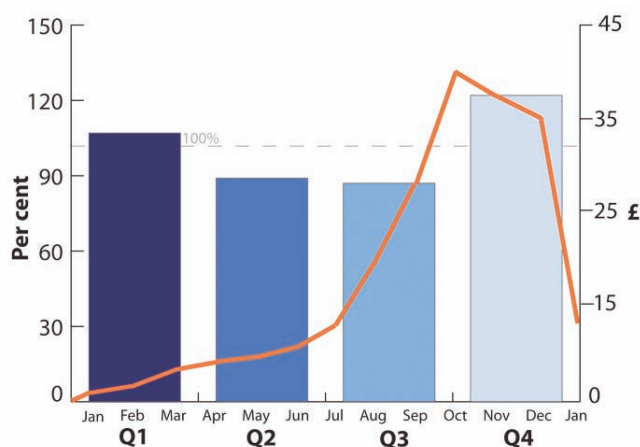


MRW 2012 review - continued

experienced 6 months of undersupply that saw prices go from £4.50 in January to a peak of £30.50 in October. A slow down in the plastic export market was the main cause of this, with export activity falling 15% on the same period the previous year. PRN supply was initially reported as being 13% (39,000 tonnes) undersupplied for the half of the year but this was revised upward by 28,000 tonnes, reducing the undersupply to 3%. This would ultimately turn out to be the tipping point in last year's market and brought 6 months of price increases to an end. In a complete reversal of fortunes, the 2nd half of the compliance year saw Plastic PRN generation surge to all time record levels in back to back quarters. The dramatic improvement to the availability of PRNs saw prices plummet with 90% of the value wiped out in final 3 months. The year closed at £2 per tonne with over 3000 tonnes of unsold evidence. Record supply figures were matched by record trading on t2e with 1 in 4 plastic PRNs trading through The Environment Exchange in 2012.

The rise and fall of the plastic price was matched by a similar trading pattern in the steel. A weak export market, falling scrap prices and a general lack of material in the market resulted in a significant drop off in PRN generation for the first 9 months of the year. The recovery in the Steel price began in subdued fashion; trading up from an opening price of £3.50 to £9 by early June. However an increasing shortage in supply final caught up with the market in the 3rd quarter. In a period of highly volatile trading, PRN values increased by 500% - trading up to a year high of £55 in late October. However, a substantial growth in exports in the 4th quarter (in part stimulated by high PRN prices) bought relief for late buyers as prices fell to a year close of £15 per tonne.

Steel Quarterly Supply vs Demand/Price



Whilst higher prices in Glass, Plastic and Steel had pushed compliance costs up as much as 10 times for many producers, the story elsewhere was less volatile. At the other end of the price spectrum, the paper and recovery markets recorded their lowest ever average PRN price. The average price on t2e for these materials was £0.88 and £0.34 respectively.

2012 was a year of extremes for PRN prices but many would argue this is a sign of the PRN system working. As a market based system it offers low cost compliance in times of plentiful supply but is designed to provide price support and help restore balance when markets show signs of underperforming. Although many producers may be 'licking their wounds' from higher prices in 2012, the PRN system has yet again proven it is up to this task.

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