

PART B: DETAILED QUESTIONS FOR RESPONSE

Please indicate your preference by providing comments as appropriate. Where there is insufficient space, please attach additional pages as necessary.

- (1) The first commitment period of the Kyoto Protocol will expire in 2012. The continuity of CERs as recognized carbon emission offsetting credits under the Kyoto Protocol is subject to a new international framework for the second commitment period under negotiation with a target completion in the United Nations Climate Change Conference in Copenhagen in December this year. Meanwhile, the US appears to be committed to develop a US emission trading scheme, but the details of the scheme are subject to further announcement and the relevance of CERs is uncertain. Against this background, do you think CERs should be the core carbon emission product to pursue in Hong Kong now or in a few years' time?

Historically the CDM has been the most widely traded international carbon offset. Given the established mechanisms for approval and the number of experienced carbon players involved in the creation and sale of CERs, it would make sense for this asset class to become the "linking" currency of choice between the ETS and future cap-and-trade markets in the US and Australia and New Zealand.

However this is somewhat speculative as the current bottlenecks at the CDM EB and the potential divergence in criteria for offset types accepted in the US market could determine the attractiveness of the CDM as a US driven international offset.

- (2) At this stage, the global CER market is dominated by European participants connected to the EU ETS and the delivery of CERs is based on the EU standard. Mainland China is the major supplier of CERs, which focuses on clean development projects and CER origination. Under Mainland China's policy, CERs are usually engaged by foreign investors based on forward sale agreements before they are issued by the United Nations. As such, the secondary CER trading market is not developed. European participants are using CER markets in Europe to manage their carbon emission trading needs and risk exposure. Under the existing market conditions, in what way can Hong Kong add value to the business process of the CER market and attract carbon emission trading participants to the Hong Kong marketplace? What are the success factors for Hong Kong to develop a commercially viable CER trading platform that can attract trading activities and develop trading liquidity? Do you think Hong Kong possesses the success factors? Please explain your view.

The liquidity of CERs is linked to demand from the compliance buyers under the ETS. As such European participants are the main players driving demand, but the Japanese buyers are increasingly significant players as well. With the emergence of demand from Australia, New Zealand and potentially Korea, this could create the necessary conditions for an Asian secondary market. Similar to London, despite not being the country where majority of the demand originates from, Hong Kong could establish itself as the primary trading centre provided its able to build the appropriate infrastructure that encourages the relevant parties to base themselves there and create the greatest amount of liquidity. E.g. while the Bluenext is based in Paris, and Nordpool is in Norway, the ECX based in London continues to be the preferred exchange for most players.

- (3) Do you consider Hong Kong investing communities have sufficient knowledge in carbon emission trading and are they ready to participate in trading CERs products? Please explain your view.

We don't have a very informed view in this regard. From our limited perspective, Hong Kong participants have so far been limited to participating in the CER market indirectly as service providers in the CERs market, mostly in China, but with some foray in Southeast Asia. This is mostly due to the limitations imposed on HK companies owning assets in China PR to participate in and trade the CERs that could be generated by such assets. This is expected to change with expected updates in China CDM regulations and could lead to deeper involvement in CDM trading.

- (4) If you are a financial intermediary, please respond to the following questions:

- (i) Do you see any potential in the asset class of carbon emissions and how would you rank the priority of carbon emission trading business among your other business initiatives? (high, medium or low)?

Carbon Emissions is a growth area within our Global Commodities group which is expected to become strategic to our clients as regulatory uncertainty is removed and environmental decisions become mainstream.

(ii) How would you assess your clients' interest in carbon emission trading? Do you have the know-how and expertise in handling carbon emission trading related operations and providing advisory services to your clients?

[REDACTED] is a market maker in trading emissions across all asset classes, including voluntary carbon units. In addition [REDACTED] is experienced in advising, structuring and buying offset-generating projects to enable clients to monetize the embedded carbon in their project portfolio. We observe increasing interest and concern among our clients with regards to managing carbon emissions depending upon the sector they are in and their geographical footprint.

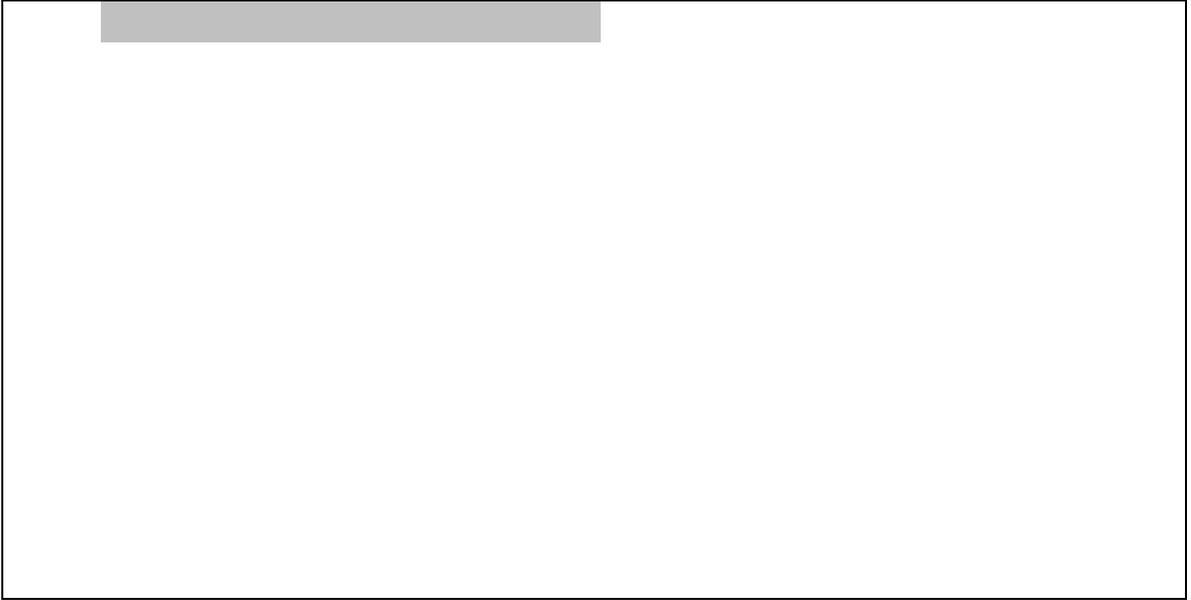
(iii) Are you located in Hong Kong and if so are you an Exchange Participant of Hong Kong Futures Exchange?

[REDACTED] through its subsidiaries and affiliates is an Exchange Participant in HKFE and has a major presence in Hong Kong.

(5) Are there any other issues regarding the introduction of CER futures not mentioned in this consultation paper that we ought to consider? Please explain your view.

Large proportion of CER business is voice brokered and then given up to exchange (both ICE and Nymex) so need to make sure that this model can be followed for any HK exchange, otherwise will not succeed. Also need to have robust and simple delivery mechanism with central clearer. Should consider spot market also.

(6) Do you have any other comments in relation to the overall development of emissions or pollutants trading markets in Hong Kong?



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