

Speaker notes

For Petter Longva representing IFIEC
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Goals and Objectives

1. Within national markets, **the geographical movement of electricity is done by the TSO**, not involving market participants. By extension, this should also be the case within integrated market areas.
2. The ultimate goal for the internal market in electricity should be full integration: **Electricity markets operating seamlessly across national borders**. The present long-term model proposed by AHAG/ASEAG provides a weak link between separate national markets, not full integration.
3. The target model lacks a vision of how a single pan-European market should be organised. Its main fallacy is the **implicit acceptance of national “market silos”**: The basic unit is a country for all time frames: balancing, day-ahead, intra-day, and forward.
4. The overall objective of the on-going reform process should be to develop efficient, well-functioning markets, providing **effective hedging instruments** enabling market participants to manage their risk associated to price variations.

The Market Model

5. **The proposed long-term market model is not a good solution for consumers.**
We would prefer a forward market solution based on a "hub" (system) price with swaps (CfDs) between the different geographical layers of the price.
6. This proposal is comparable to both by **the Nordic electricity market model and the gas market model** that is developing in Europe:
 - The market is divided into a number of fairly homogeneous market areas in which there a common reference price index for the forwards (system/hub price).
 - The forward is linked to the physical delivery price through financial products linked to the difference between the reference price index and the day-ahead price (CfDs/spreads).
7. European harmonisation toward the AHAG/ASEAG model would not support the development of a pan-European electricity market. Ideally, it should be seen as a **voluntary transition arrangement**.

The NC in our Model

8. **IFIEC has questioned the necessity of having this Network Code.** After the phase-out of Physical Transmission Rights, the forward market should essentially be financial. Trading should answer their needs in a competitive environment, and be organised by market participants themselves, not by TSOs.
9. We accept that the **present process is bound by the Framework Guidelines**. The present model is however at best suitable as a first step for immature markets. Implementing it across the market will mainly **serve the interests of traders and large, dominant generators**.
10. In the future, **power flows and the demand for grid capacity will be very unstable** due to an ever increasing share of power from intermittent sources. Forward capacity calculation is therefore not going to have significant value for market participants.
11. **Creation of one or more virtual hubs for electricity in Europe and calculation of one or a number of unconstrained day-ahead prices for given market areas** should be the main issue in the NC. This would serve as the basis for financial markets covering large trans-national areas.
12. **The main requirement on TSOs would be to promote and enable financial markets to develop.** Only if this is not successful, a number of actions, supporting the liquidity of certain instrument etc. should be required.

Market Development

13. **FTRs at borders will not promote cross-border competition.** On the contrary, they will cement national borders as the main division between market. FTRs at borders should be seen as a transitory solution towards a pan-European electricity market, mainly applicable in less developed markets.
14. **Cross-border instruments may prevent liquidity from developing:** Players from a market with illiquid forward continue to trade the neighbouring market as a proxy for their own market, sometimes using transmission products, sometimes not.
15. **Cross-border instruments cement the silo.** Changing market structure, day-ahead bidding and price zones, etc. becomes much more difficult due to the commercial interests linked to the FTRs.
16. **FTRs Options or FTR Obligations will not provide arbitrage of forward prices.** On the contrary, if forward markets on both sides are liquid, FTRs are rendered completely useless as hedging products.

Hedging Needs and Cross-border Instruments

17. The simplest hedging of opposite long and short positions in two markets would be to hedge each of them in their own market. **Our main target is thus liquidity in all markets.**
18. In the “energy only” European market, market participants want to hedge long or short positions in energy in the various market/price areas. Hedging capacity between areas done through for example **FTR Options** thus only has a very indirect value as a hedge. This is the kind of instrument that TSOs could offer without significantly increased risk.
19. **FTR Obligations** move a fixed quantity from one market to an adjacent to other, adding to the length in on and reducing it in the other. Such instruments may in principle offer a “bridge to liquidity”. However, issuing such an instrument will involve unlimited risk exposure, and it is hard to believe that TSOs or any other player would issue such instruments, and make the trading of them liquid.
20. As I mentioned, FTRs **may to a certain extent help market players in illiquid markets** next to a liquid one hedging opposite positions across borders. This is however only possible for generators and a few very large consumers with significant trading capability. Furthermore, it is of no practical use in hedging in liquid markets, on national borders where both or none of the markets are liquid, or on price area borders inside a country.
21. **Consumers will not be much supported by FTRs** in their procurement or hedging of electricity. This is in particular true for small or mid-sized consumers that are not active in trading markets. Such consumers will not be able to create international competition for their supply without significant support from a trading company.

Conclusion

22. Energy intensive consumers believe that their interests are better served in a market where the price in each price zone is linked to a hub price through swaps (CfDs). In this model, there is no need for **cross-zonal or cross-border instruments**.
23. Cross-border instruments may possibly be seen as a **transitory measure in immature markets**. In Northwest Europe, implementation of FTRs has no value for market development. In the Nordic market, implementation will force development of market liquidity into reverse.
24. **Trading FTRs may be an attractive value proposition for traders**, in particular if TSOs are forced to sell them to the highest bidder. Value lost by too low auction prices would have to be covered by the consumers through increased grid tariffs.