2. Delivering the new electricity market design and gas liquid markets – two case studies

Individual Policy Developments: Showcases from the electricity and gas markets

- *Mr Dennis Hesseling, Head of Gas Department, ACER*
- *Mr Fernando Hernández, Chair, ACER Electricity Working Group*

"A BRIDGE TO 2025"

24 SEPTEMBER 2015

ONE YEAR ANNIVERSARY EVENT

Implementing the Gas Target Model

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IN COOPERATION WITH

ACER Agency for the Cooperation of Energy Regulators

CEER Council of European Energy Regulators

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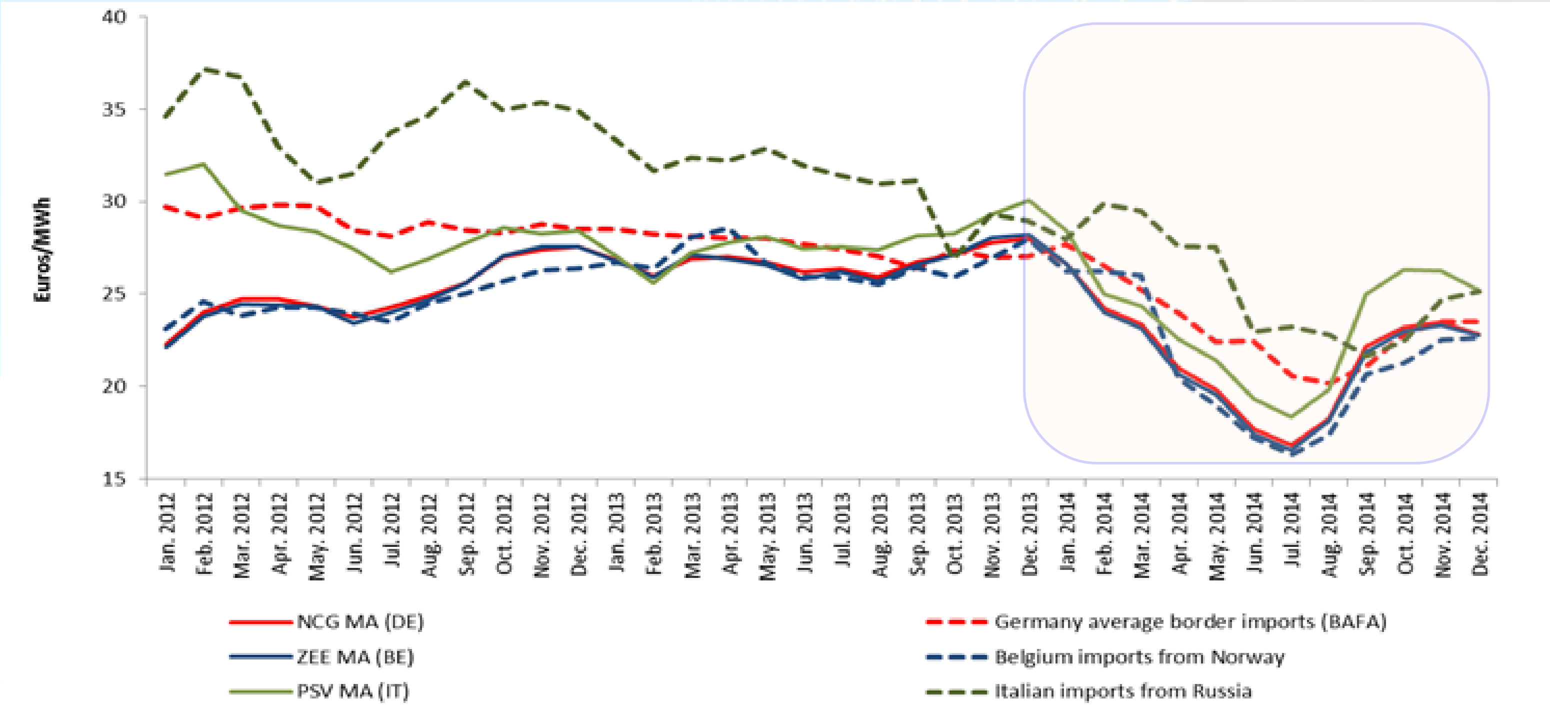
Gas Target Model stresses importance of liquid hubs - Price gap between long term contracts and hub prices gradually diminishing

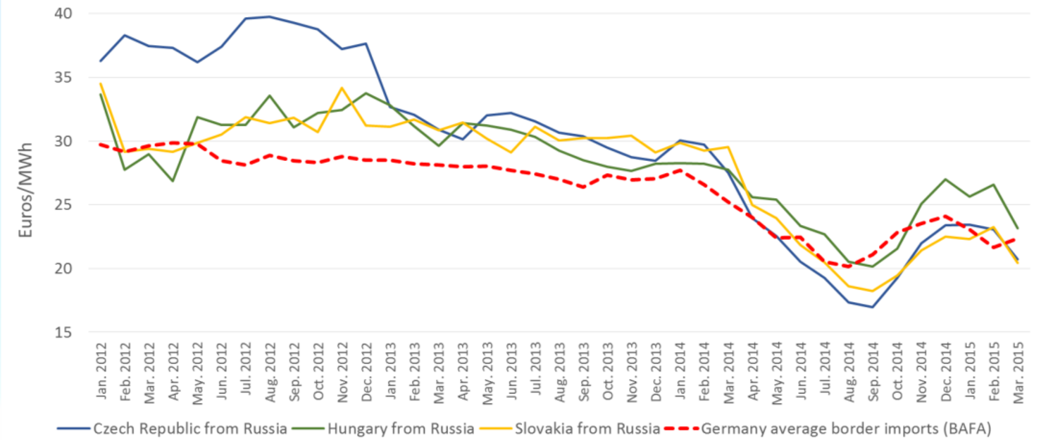
Comparison of selected hub and border import prices – 2012-2014 (euros/MWh)

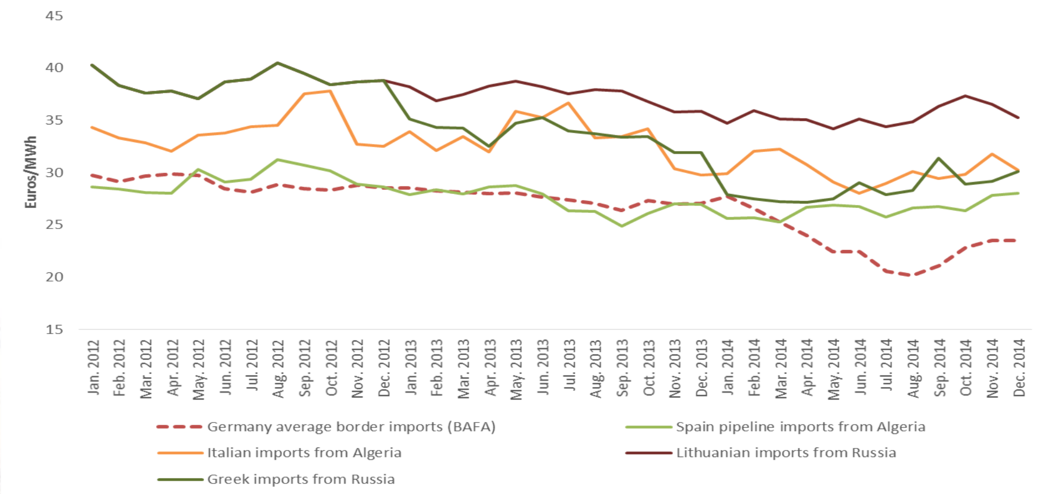


- NWE region hub prices were in 2014 on average almost 4 euros/MWh lower than in 2013.
- Reducing price gap due to renegotiation of contract terms and drop in oil prices (further observable in 2015)

However differences in long-term contracts prices persist across geographies even though these are reducing

Comparison of CEE region MSs Russian supplies (above), Mediterranean, SSE and Baltic region (below) vs German average import prices – 2012 – 2014, (euros/MWh)





Reasons for divergence:

- Market competitive frames
- Role of hubs
- Bargaining powers
- Diversity and origin of supplies
- Interconnection infrastructure availability

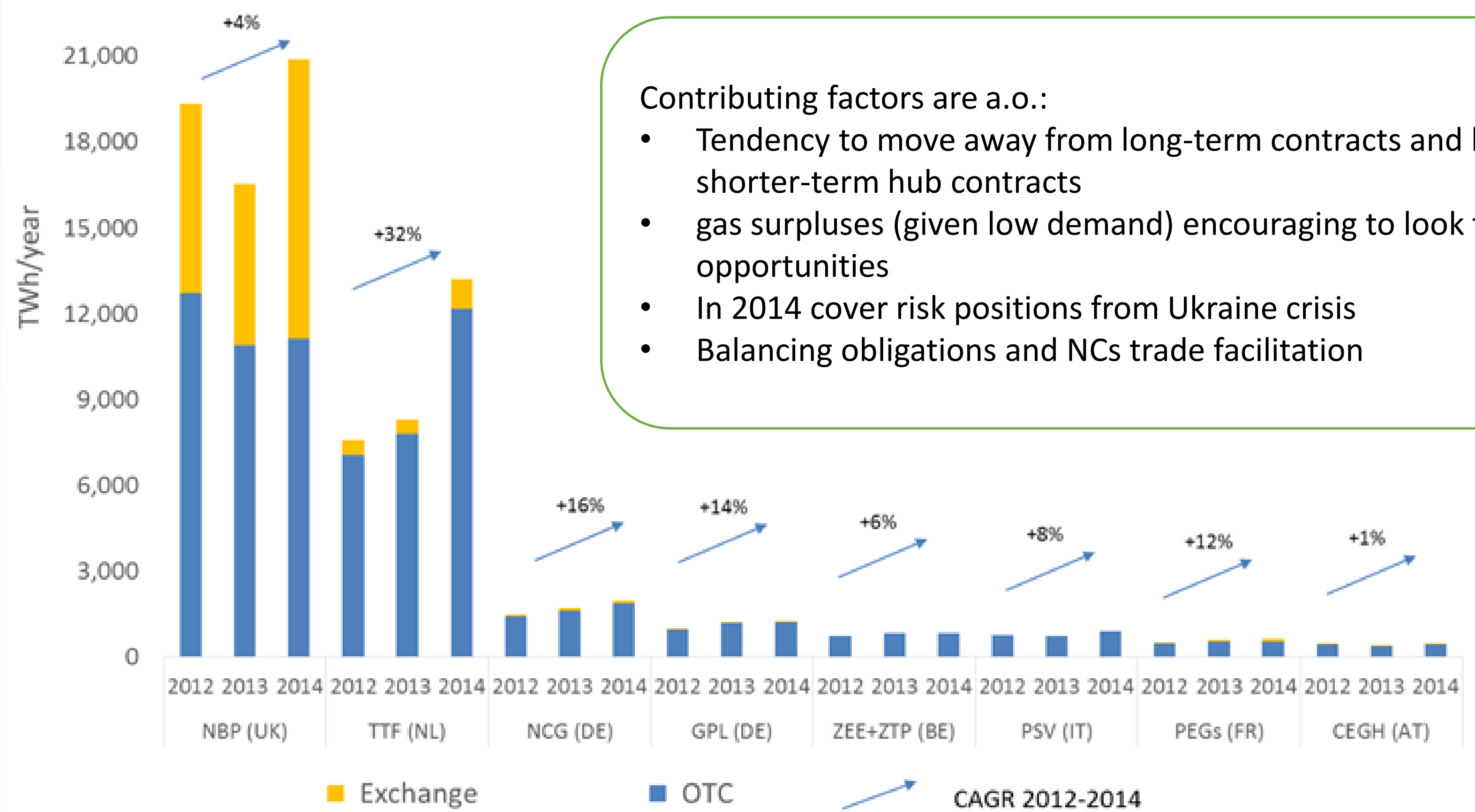
Large Western European gas markets

- Except UK and NL, liquidity below target churn rate and uncertainty regarding further evolution of liquidity
- But liquid and transparent gas trading in large market zones
- Several supply sources, also thanks to LNG, and diverse market stucture with imports from multiple firms and production by multiple firms (where applicable)
- But dependence on large suppliers may increase again should gas demand pick up
- ➢ **Many consumers (mostly large consumers in largest markets) already benefit from wholesale gas competition**

Central and Eastern Europe

- Most gas markets without transparent hub trading and – according to GTM criteria – relatively small to develop into competitive wholesale markets
- Often high concentration on the supply side
- Potential competition in some Central European Member States
- But often large reliance on largest supplier, i.e. Gazprom
- ➢ **Lack of competition in smaller Member States should not be ignored**

Traded volumes at main EU hubs – 2012 to 2014 (TWh/year) and CAGR (%)

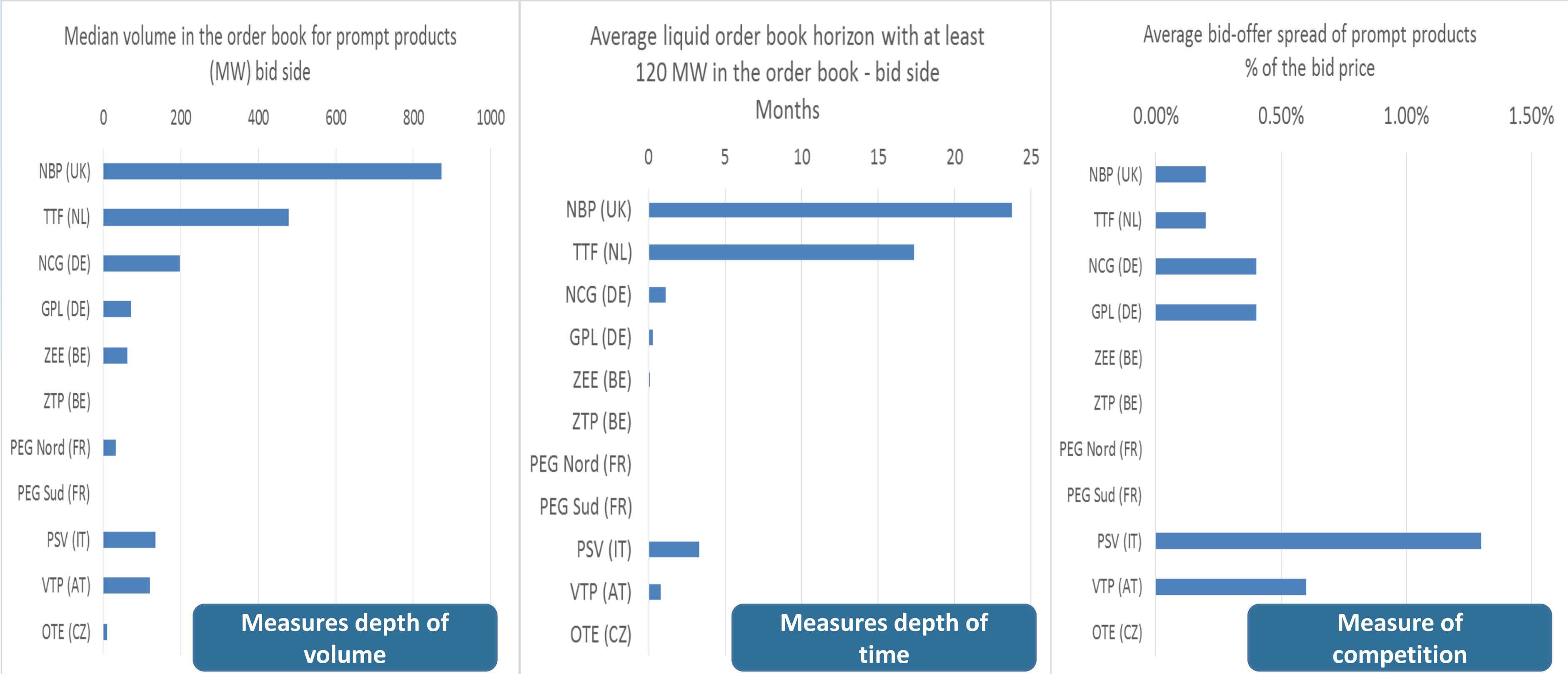


Contributing factors are a.o.:

- Tendency to move away from long-term contracts and hedging to shorter-term hub contracts
- gas surpluses (given low demand) encouraging to look for trading opportunities
- In 2014 cover risk positions from Ukraine crisis
- Balancing obligations and NCs trade facilitation

NBP and TTF hubs play leading roles, particularly on forward liquidity, by attracting hedging risk and financial trading

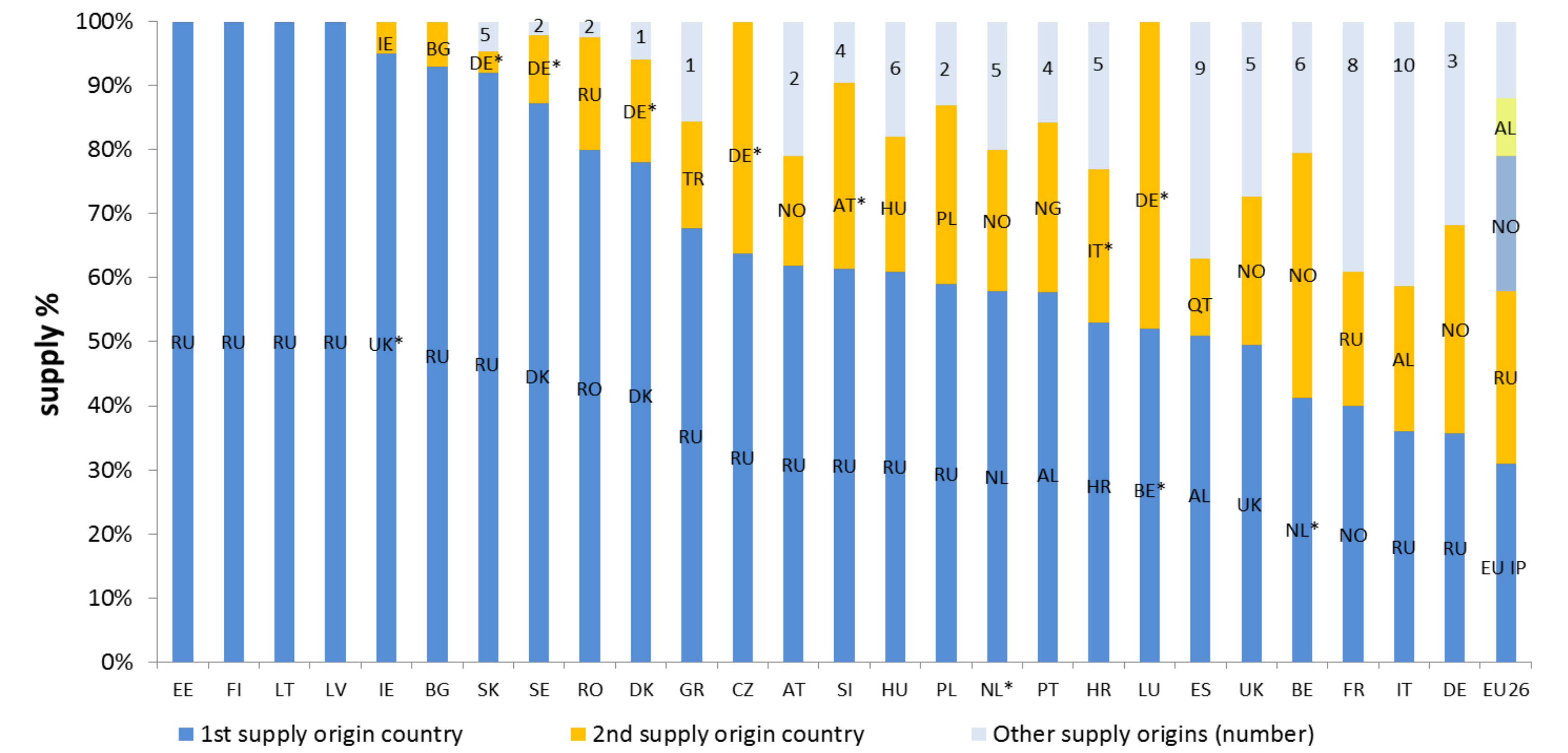
Hub comparison for a selection of GTM parameters related to functioning degree of hubs.



NBP and TTF show larger volumes availability, at longer time horizons and lower trade operations ask-bid price spreads

Large disparity in number of gas source access in Europe

Estimated diversity of gas supply origin (country) in EU MSs (2013)

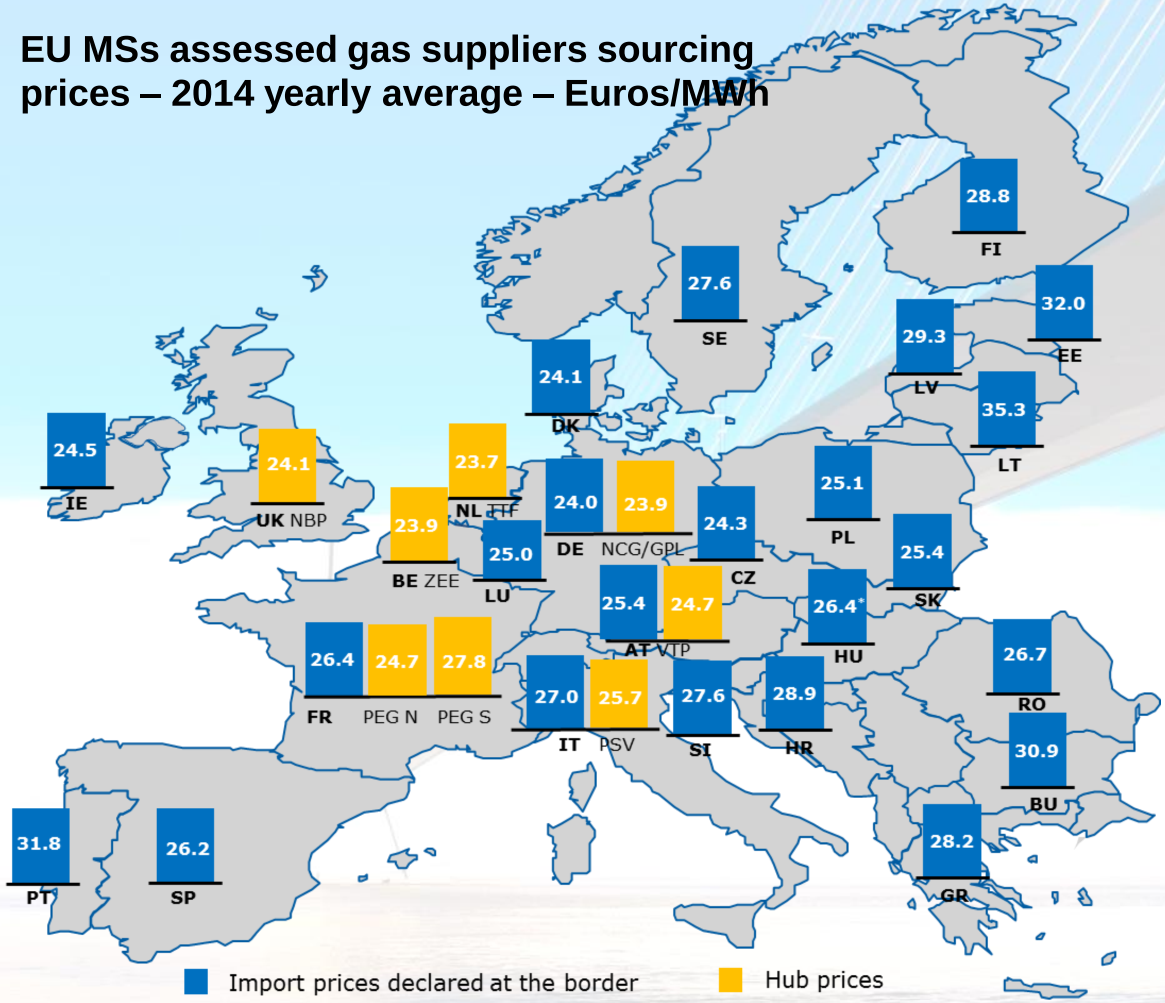


Note: Supply origins indicate the upstream gas producer state or, in those origins marked with an asterisk, a MS featuring an organised market where gas has been purchased.

SOURCE: Eurostat Comext, BP Statistical Report, Eurogas, MSs' National Reports (2014) and ACER calculations

Result is that countries with limited sourcing options and less developed hubs tend to have higher sourcing costs

EU MSs assessed gas suppliers sourcing prices – 2014 yearly average – Euros/MWh



- Differences in suppliers' sourcing prices result in relevant gross welfare losses: MMR 2013, 7 billion euros
- Welfare gains to be obtained from further market integration

* Assessments work in progress pending final input/validation from some NRAs

SOURCE: Eurostat Comext, BAFA, NRAS, ACER methodology

Wholesale market development: self-evaluation process

Analysis	• Periodic analyses by National Regulatory Authorities (NRAs) of market development • Periodic analysis also to review achievements against commitments and proposals
Assessment	• Criteria not met: NRAs assess whether natural evolution is sufficient to meet criteria within 3-year period or more active intervention is required (incl. Network Code implementation)
Plan	• Where more active intervention required: NRAs propose – based on assessment – a plan to achieve target criteria (with Member States and stakeholder involvement, consultation, Cost Benefit Analysis-CBA)
Market integration tools	• Where market integration is considered the preferred option: GTM market integration tools (detailed CBA)
Surrogate measures	• Where none of these market integration options deliver a positive CBA: NRAs to propose equivalent surrogate measures

In all cases – regardless whether the market functioning criteria have been met – steps to **improve hub functioning** should be pursued

Implementation of self-evaluation process

ACER supports the GTM implementation and has developed a template to facilitate NRAs’ self-evaluation work

Self-evaluation in two phases

- Phase 1:
  - Assessment of the current state of wholesale market functioning based on GTM metrics
  - Identification and description of the key drivers towards improved wholesale market functioning
  - Expected state of wholesale market functioning in 2017
  - Consultation
- Phase 2:
  - Identification and description of potential structural market reforms
  - Consultation

First movers

CZ, AT and DE as first movers in self-evaluation

- CZ and AT conduct respective self-evaluations in line with bilateral market integration project
- DE: commissioned study to assess the potentials for further market integration on the basis of criteria

Other NRAs welcome to join

ACER will continue to monitor GTM indicators as well as implementation plans

Conclusion

- Liquid hubs bring clear advantages
- NWE hubs show that good levels of liquidity can be achieved (under right conditions)
- GTM promotes liquid hubs throughout EU
- NRAs with less liquid hubs to do self-evaluation
- If prospects of hub becoming liquid stand-alone limited, structural measures should be envisaged