

Vision for a European Gas Target model State of discussion

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Context

- About 65 % of demand is produced outside EU (2009 demand)
- Long-term supply contracts (typically 25 years) with Take-or-Pay obligations and certain flexibility do exist in many Member States
 - Underpin investment in long-distance pipelines and production sites
 - Often seen as guarantee for SoS
- The tariffs for transporting the gas out of these contracts are often still set out in separate 'transit contracts' which is not in line with EU legislation, e.g.
 - Based on distance
 - Different from the arrangements for 'domestic' transmission networks serving end-users
- The current arrangements for gas trading are on a long-term contractual basis with producers outside of the EU rather than on wholesale gas markets in the EU.

What are the challenges?

- How to achieve a more 'hub-based' trading on both long and short-term basis?
 - Almost no trading activities, except for NW Europe in recent years.
- The 20-20-20 obligations will most probably lead to much greater within-day fluctuations in gas demand than previously has been the case.
- Removing contractual paths for transporting gas and creating E/E zones requires changes to the current contractual arrangements for network access.
 - How many E/E shall exist in Europe?
 - Will 25 or even more E/E zones lead to sufficient liquidity?
 - Will 25 or even more E/E zones facilitate cross-border trade and market integration?
 - How shall the trading arrangements between E/E zones look like?

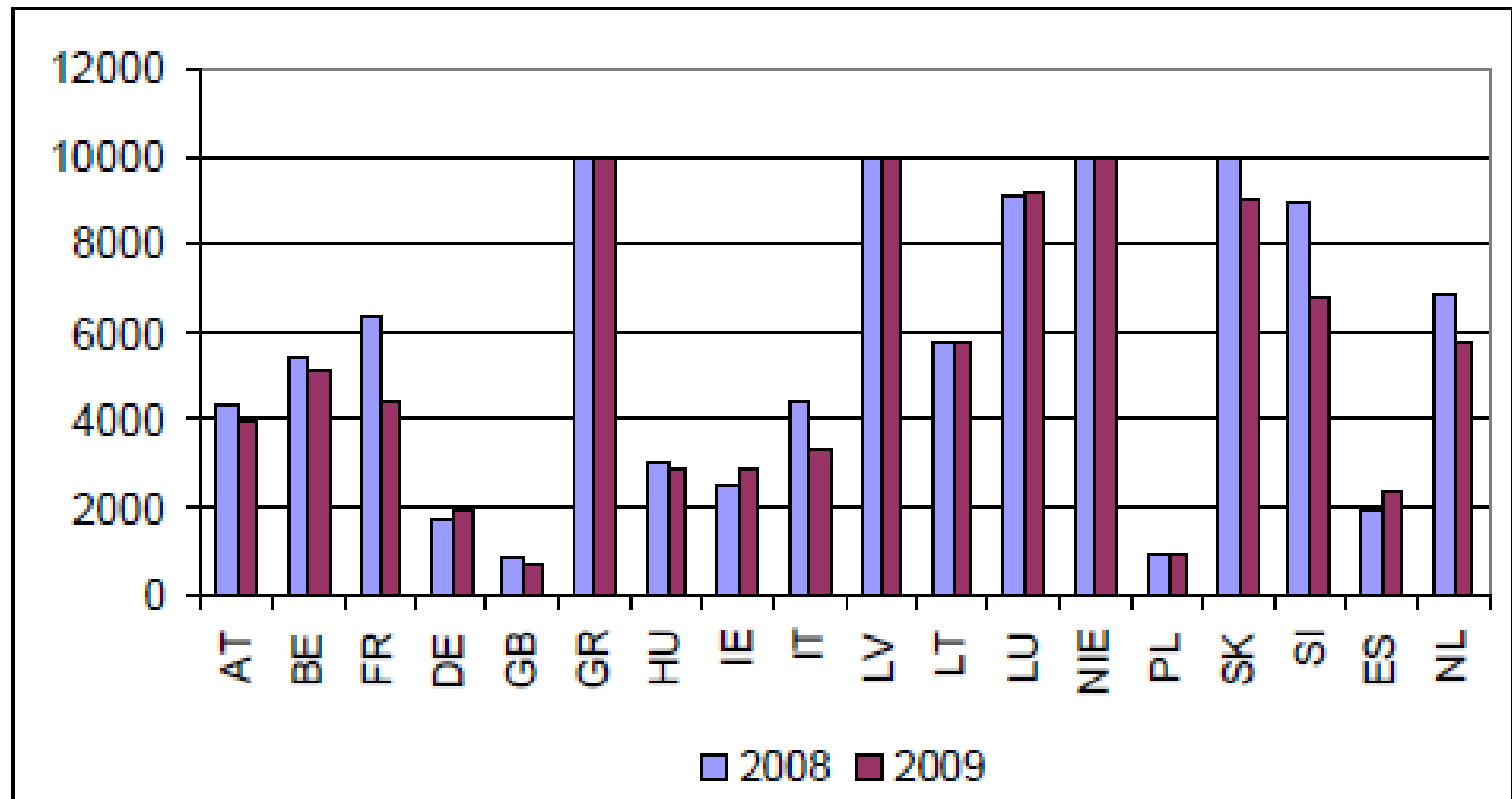
Internal EU gas market

- What do we want to achieve?
 - Internal EU gas market
- What do we have to consider?
 - Legal framework
 - The political goals of the EU, as to
 - Deliver real choice for all customers of the European Union;
 - Achieve efficiency gains,
 - Achieve competitive prices, and
 - Achieve Higher standards of service, as well as, to
 - Contribute to SoS, and
 - Sustainability.
 - The fundamentals of the value chain
 - Reasonable balance between cost and benefits

Basic conditions need to be established in all countries
No one size fits all solution possible

Functioning markets in Europe?

Figure: HHI in national gas wholesale markets

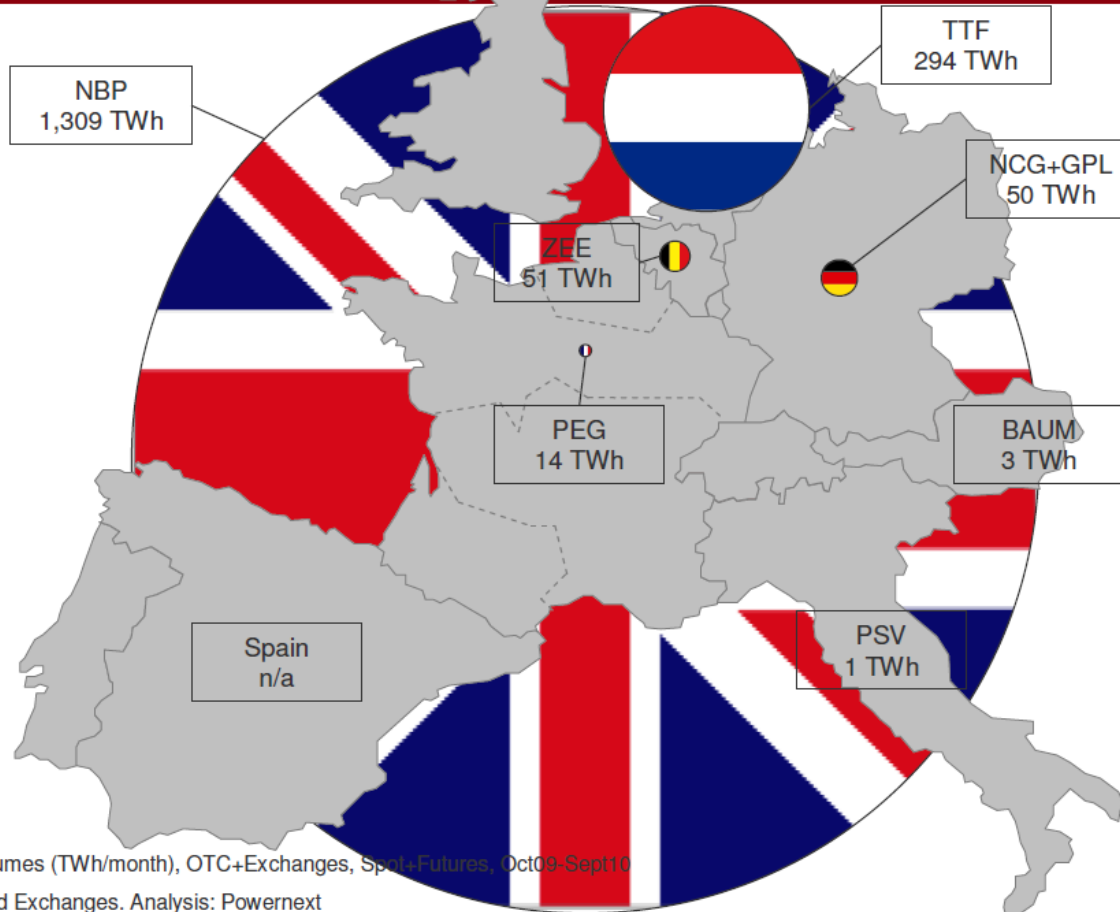


Source: Regulators data

Source: EC 2011 Report on progress in creating the internal gas and electricity market

Average traded volumes

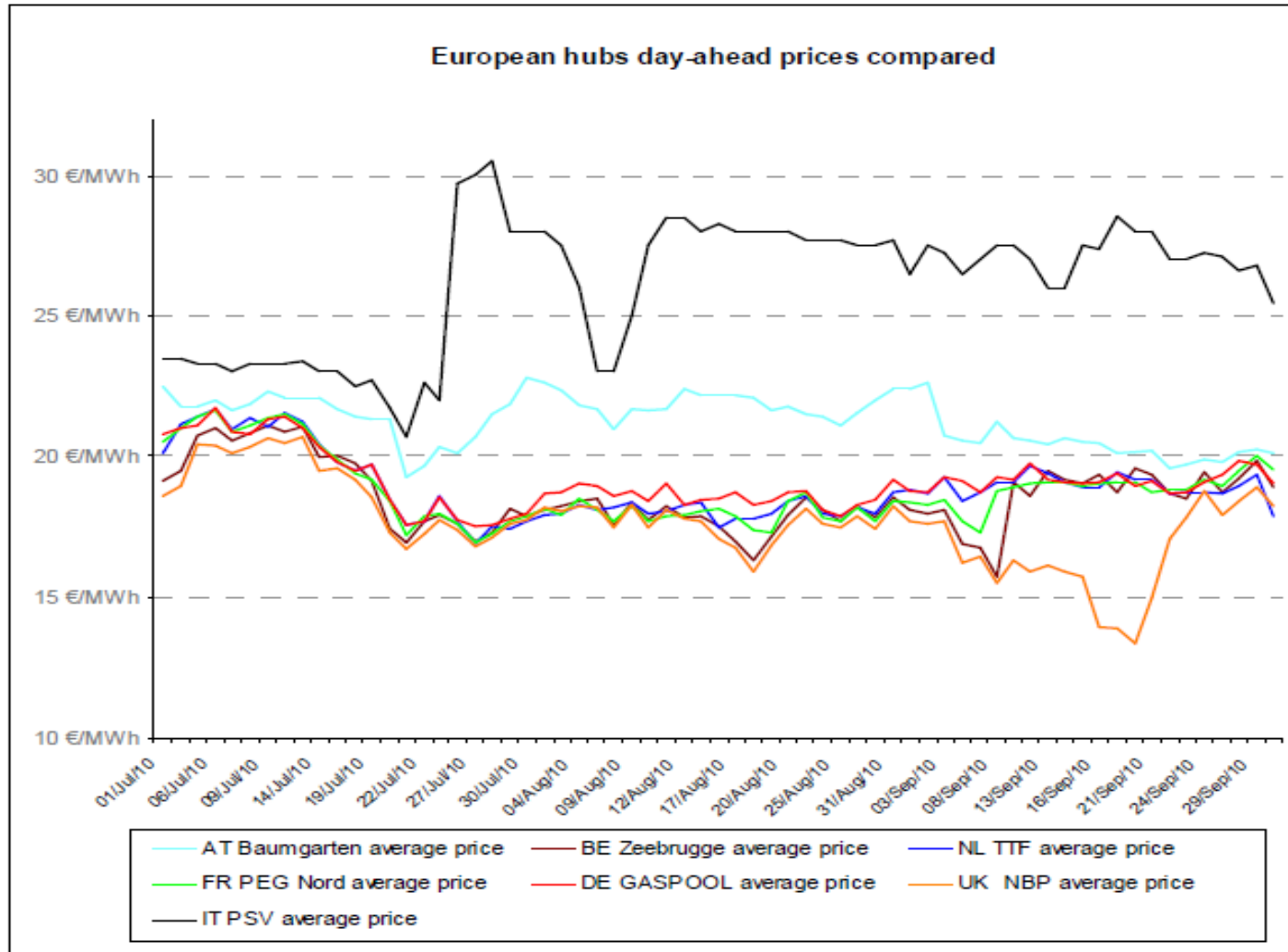
Key indicators on European gas markets Average traded volume



Average traded volumes (TWh/month), OTC+Exchanges, Spot+Futures, Oct09-Sept10

Source: Brokers and Exchanges. Analysis: Powernext

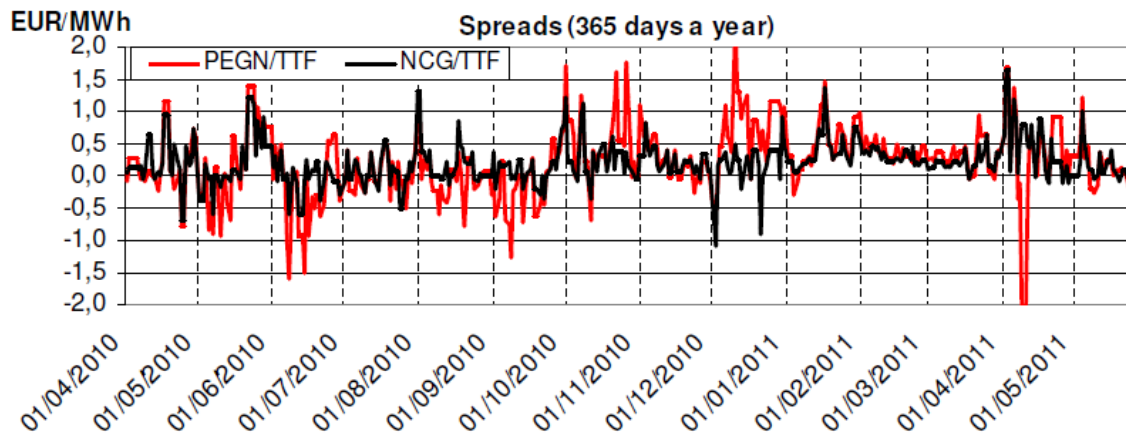
Wholesale markets in Europe?



Source: Platts.

Price alignment in NW Europe?

Focus on TTF, NCG and PEGN markets Spreads and correlation

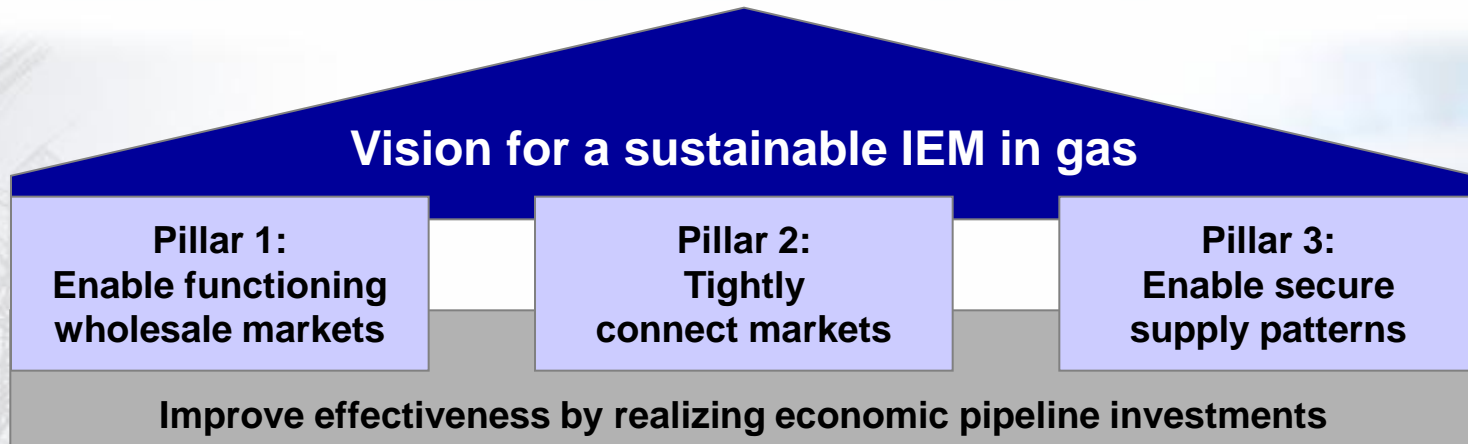


30d correl	PEGN - TTF	NCG - TTF
365d a year		
Average	84%	92%
Max	100%	100%
Min	11%	63%
DA product only		
Average	88%	94%
Max	100%	100%
Min	48%	76%

What can we conclude?

- No apparent trend in price convergence over the last 12 months
- PEGN can live a life of its own, sometimes
- BUT: these numbers are based on ICIS Heren price close (marginal trade at 4.30pm UK time)
 - Can send different signals than the vast majority of the trades executed during the day, especially when there is little liquidity at the close

Objectives of the IEM



Pillar 1: Structuring network access to the European gas grid in a way that enables functioning wholesale markets so that every European final customer is easily accessible from such a market.

Pillar 2: Fostering short- and mid-term price convergence between the functioning wholesale markets by tightly connecting the markets through facilitating cross-market supply and trading and potentially implementing market coupling as far as the (at any time) given infrastructure allows.

Pillar 3: Enabling the establishment of secure supply patterns to the functioning wholesale markets.

Foundation: Improving the effectiveness of pillars 1 to 3 by making sure that economic investments in pipelines are realized, as well as, the integration of renewable resources.

Overview of high level options

MECO-S & LECG

Enabling Markets:

- **Market areas (sub-) national or cross-border**
 - Full vertical integration
 - Merge of market areas

LECG + MECO-S

- **Trading region**
 - Merger of energy systems
 - Separate user zones with national balancing system

only MECO-S

Connecting markets:

- Bundling of capacity
- Harmonisation of contracts, Gas-day
- Explicit Auctions
- Make capacity available via UIOLI and/or Overbooking

LECG + MECO-S

- **Market coupling**
- Day-ahead in auctions/allocation as possible

LECG + MECO-S

GTM in context of the EU Regulatory framework

- **Step 1:**

FG and Codes on CAM, Balancing, etc. and CMP guidelines have the aim that capacity between those functioning markets will be used as effective as possible leading to improved price alignment between the markets.

- This will maximize efficiency and thereby public welfare in / from supply & trading on a European scale by making sure that all gas assets (procurement contracts, storage, ...) are used in the most economic manner.

- **Step 2:**

GTM proposes several models on cross border level to realize liquid wholesale markets: All European final customers will be served from a functioning wholesale market.

- These functioning wholesales markets will act as enablers and fertilizers for retail competition because they provide easy access to competitively priced gas and are the basis for proper risk management.

Draft vision for the GTM - 1

- Functioning wholesale markets in Europe
 - If a country is able to create a functioning market within the country itself
 - Market area
 - If a country is not able to create a functioning market within the country itself
 - Cross-border market area
 - Trading region
- Connected functioning wholesale markets in Europe
 - Explicit versus implicit auctions
 - How to value short term capacities? (discussion in the Tariff FG work stream)

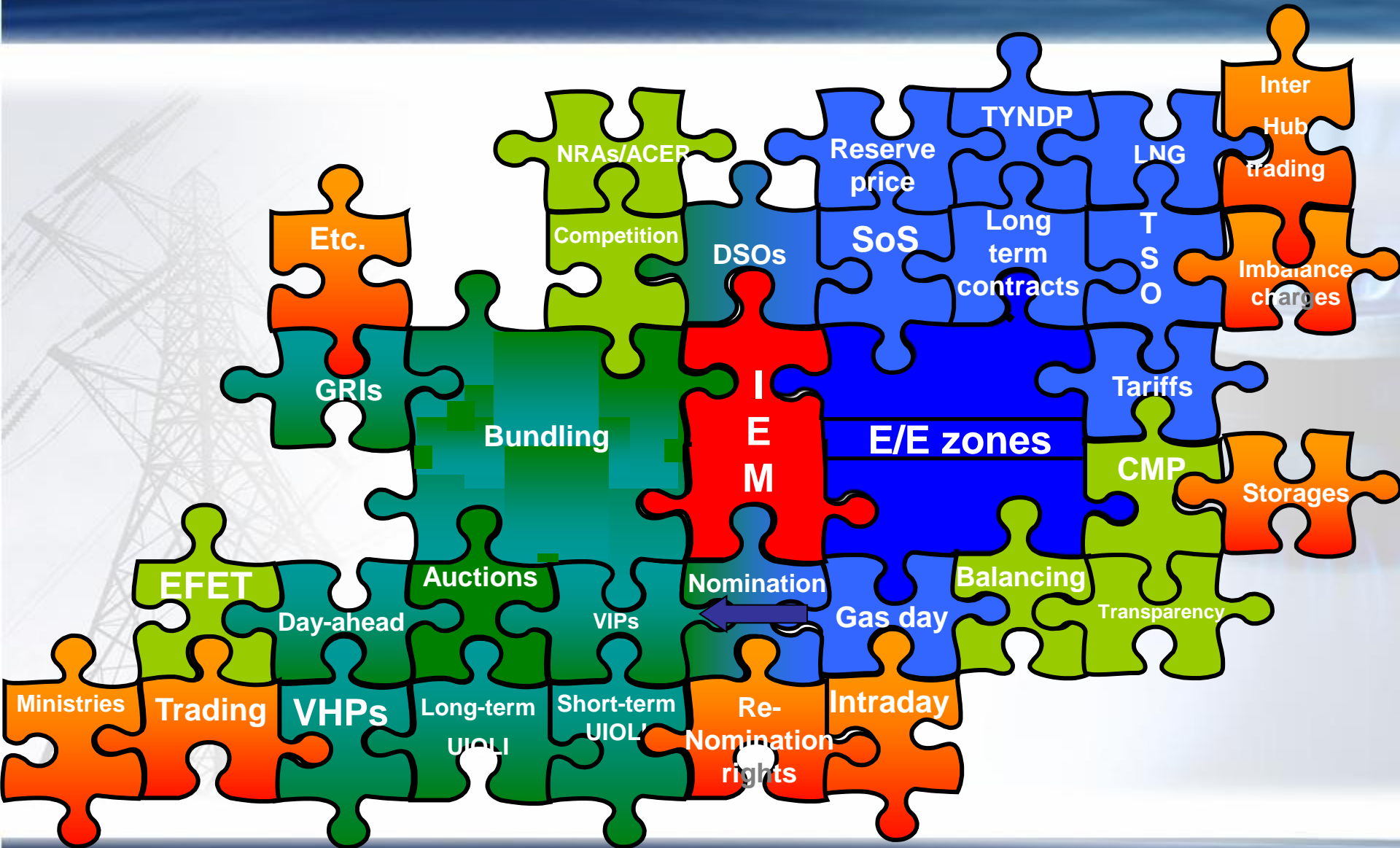


Draft vision for the GTM - 2

- Secure supply patterns
 - Short-term trading will allow to respond to the growing need for flexible gas demand
 - Ensure that gas comes to Europe
- Ensure that economic investments take place
 - Regular 'bidding' process



EER vision: core elements



Draft vision for the GTM in a nutshell

- Efficient use of existing infrastructures
- Functioning wholesale markets in all of Europe
- Connected functioning wholesale markets in all of Europe
- Secure supply patterns that ensure gas flowing to Europe
- Economic investments need to take place



Next steps

- Public consultation paper based on discussions with stakeholders to be published soon
- Public Consultation over summer
- Presentation of stakeholder feedback in next Madrid Forum in September

The background of the slide is a light blue gradient with a faint, semi-transparent image of a high-voltage electricity pylon on the left and a gas burner with blue flames on the right.

Thank you for your attention!

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