

# How should the European forward markets look and what should be the next steps?



European Federation of Energy Traders

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# How should the European forward markets look like?

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- ➔ Energy shall be possible to trade forward OTC and at exchanges
- ➔ All TSOs shall auction transmission rights between all bidding zones

## Benefits of transmission rights

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- ➔ Enabling competition across bidding zones also in retail markets
- ➔ Delivering welfare gains for European consumers through more efficient markets
- ➔ Providing the right price signals and aiding liquidity
- ➔ Enabling proper incentives based regulation of TSOs and reduce risk for TSOs

# Transmission rights: TSOs are natural sellers

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- ⇒ Transmission shall be auctioned by TSOs for longer maturity for the timeframes supply contracts are typically concluded, 1-3 years
- ⇒ Coordinated allocation method (FB only if it shows increase of cross-border capacity to the market)
- ⇒ Transmission rights shall be auctioned in a coordinated way by a centralised auction office with the same rules for all borders between bidding zones
- ⇒ Secondary markets shall be facilitated by TSOs and regulators and it shall be possible to slice the transmission rights

# Transmission rights: maximise capacity

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- ➔ TSOs shall allocate maximum available capacity and there shall be no discrimination against cross-border transactions.
- ➔ Regulators shall ensure this. Incentives based regulation could be an efficient tool. However, as incentive regulation is difficult to apply, regulators will have to take up the challenge and dive into it
- ➔ For example: there are numerous examples of TSOs shifting bottlenecks to the border. Did regulators question this practice?

# Transmission rights: transparency and firmness

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- ➔ Transparency is needed for capacity calculation method/process and determination of long-term capacity
- ➔ Transmission capacity shall be firm. In case of financial firmness: compensation at initial price in case of force majeure, otherwise compensation according to market spread
- ➔ TSOs shall be able to buy back capacity in case of reductions in available capacity.

# Transmission rights: PTRs and FTRs

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- ➔ Transmission rights shall be auctioned as options either as Physical Transmission Rights (PTRs) or as Financial Transmission Rights (FTRs)
- ➔ PTRs shall be based on Use-It-Or-Get-Paid-For-It and automatically given to market coupling or day-ahead auction if not physically nominated. This ensures that there is no hoarding of capacity
- ➔ FTRs will always be automatically settled by the hourly day-ahead market price difference

# Contracts for difference

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## as e.g. applied in Nordic

- Not issued by the TSO but by the market participants, which engage with each other via a central clearing house
- Pay out the difference in energy price between a price area and the system regional price (which is virtual)
- No link to the underlying physical transmission of capacity (i.e. CfD does not reflect the transmission path) thus it is difficult to hedge with the OTC market
- It is a purely financial market
- CfDs are needed to enable hedging the local price in case of a virtual system price



# Example – Cross-border supply



## Hedging with transmission rights

- Supplier A buys a transmission right from bidding zone 1 to bidding zone 2 in the auction or in the secondary market
- Supplier A contracts a delivery to customer B

## Hedging with CfDs including fundamental actors

- Supplier A sells a CfD contract in bidding zone 1 to customer D
- Supplier A buys a CfD in bidding zone 2 from Supplier C (competitor)
- Supplier A contracts a delivery to customer B

Supplier A has generation in bidding zone 1

Customer B has consumption in bidding zone 2

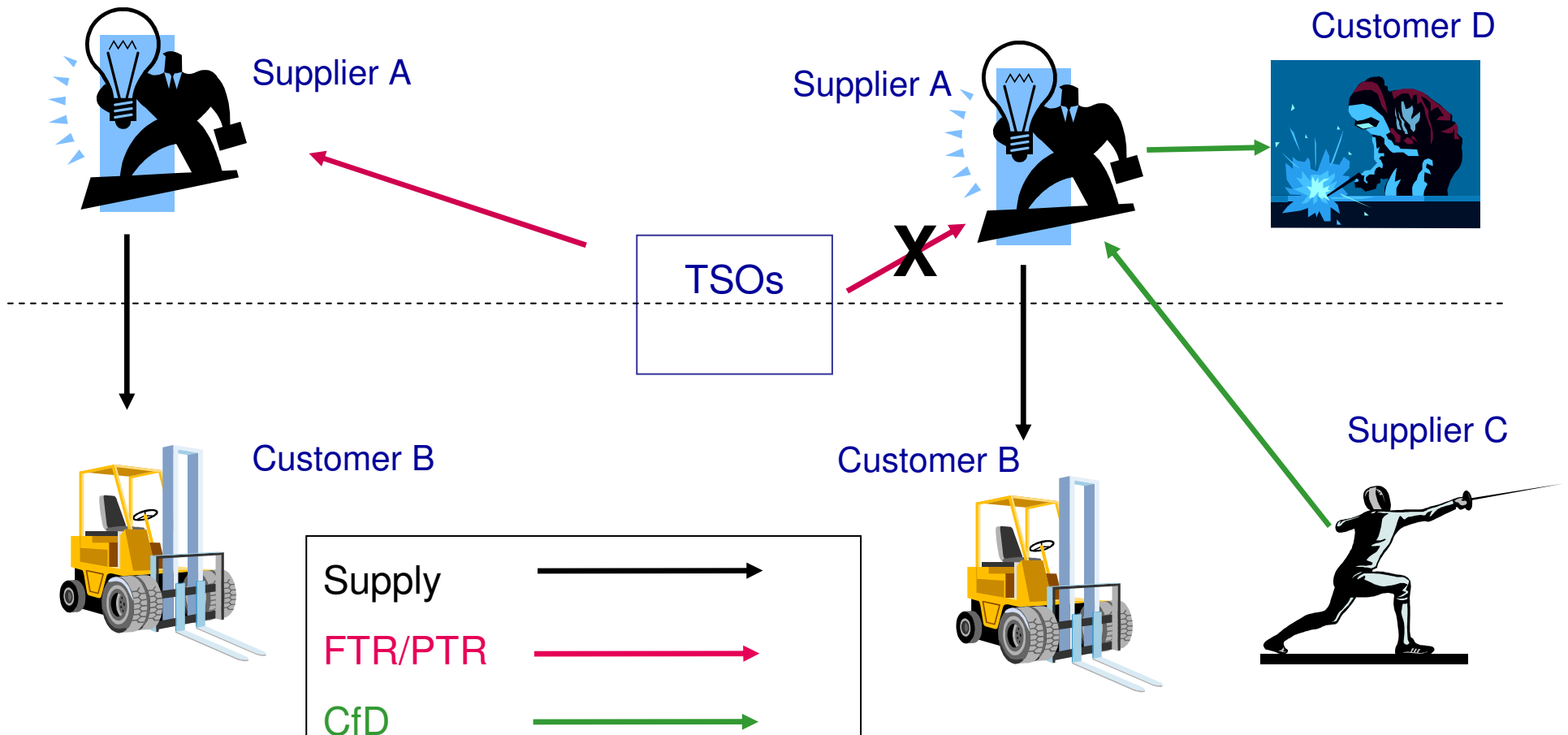
Supplier C has generation in bidding zone 2

Customer D has consumption in bidding zone 1

# Example – Cross-border supply

## Hedging with transmission rights

## Hedging with CfDs including fundamental actors



# Contracts for Difference

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- CfDs cannot replace transmission rights
- There is not a natural balance between supply and demand in all bidding zones and therefore no balance between natural buyers/sellers of CfDs
- TSOs are natural sellers of transmission capacity and shall sell transmission rights between all bidding zones

# Next steps

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- EFET would like all TSOs to allocate longer maturity transmission rights based on maximum available capacity
- Transmission rights shall be offered as Use-It-Or-Get-Paid-For-It
- Transmission rights shall be (at least) financially firm with compensation according to market spread in case of curtailment
- The draft framework guidelines on capacity allocation and congestion management for electricity have the possibility to improve cross-border competition

# Thanks for your attention

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