

**BOC GASES'S (BOC) RESPONSE TO OFGEM'S NON-DOMESTIC SUPPLY
MARKET REVIEW CONSULTATION, OFGEM LETTER DATED 11 NOVEMBER
2005**

BOC welcomes the opportunity to respond to Ofgem's letter concerning the appropriateness of a market review of the non-domestic supplier market.

BOC is a large and intensive energy user. BOC regards access to an efficient and competitive supply market is seen as a necessity if it is to supply its customers' at the lowest cost. Many of the customers compete in global markets and require competitive prices to survive and prosper. Current market conditions mean that many customers are not doing so.

BOC would welcome Ofgem conducting a market review of the non-domestic supplier market.

BOC's specific response to the questions in the letter dated 11 November 2005 is set out below;-

Q1: Do you consider that there is sufficient justification for Ofgem to conduct a review of the non-domestic gas and electricity supply markets? Please provide specific evidence or data.

A1: Yes, BOC's experience is when seeking supply offers for electricity and natural gas requirements that very few suppliers are prepared to make an offer for supply.

In addition all offers are almost identical in respect of the level of price offered. All prices are all derived from the reported wholesale market prices. BOC believes these traded markets are thin and illiquid and have been becoming more so (see chart below for electricity) BOC believes that it is possible for the market to be moved by market players.

BOC believes in particular with respect to electricity that as many of the large suppliers are vertically integrated, having both production capacity and a supply business, they are able to self-hedge. These companies therefore do not have sufficient incentive to trade in the wholesale market requiring it only for marginal amounts of product to balance their short-term positions. BOC believes that the wholesale markets can be used for market signalling between players.

BOC believes that it is in the interests of the vertically integrated players for the wholesale prices to move up as the increases their profit margin.

BOC believes that there are insufficient product types available from suppliers.

Q2: against the indicators above (or any additional indicators you consider relevant) to support your position.

- **Parallel movements in the prices offered by suppliers or other evidence of collusion.**

Offers to BOC in response to invitation to quotation are almost identical.

- **Sustained increases in retail margins;**

Retail margins may be low but Ofgem should look at the rise in the operating margin between production costs and wholesale selling prices. That is for electricity between generating cost (especially coal and nuclear sets) and the wholesale price. And for natural gas, between production cost and wholesale selling price.

- **Barriers to entry, or barriers to expansion, for supply companies;**

The lack of deep and liquid wholesale markets is a barrier to entry. As is the complexity and credit required of new entrants.

- **Impediments to customers' switching supplier**

Some standard supplier's terms and condition of contract such as high and uncertain Default Charges in case of supply contract overrun and the complexity of data issues are barriers of this kind.

- **Low degree of product differentiation (compared to previous performance and/or performance in other geographic or sector markets)**

All products tied to wholesale market prices and forward curve.

If you do consider a review is necessary, please answer the following questions:

- **which indicators of competitiveness should be the focus of this review (for example, market dominance of particular company(ies), quality of service, barriers to entry for suppliers), and why?;**

For the reasons set out above Ofgem should focus on market dominance of the large and integrated suppliers and on barriers to entry for suppliers.

- **should the review cover all market segments (for example SMEs, medium and large gas and electricity supply markets) or focus upon a particular sub-set of these, and why.?**

BOC believes that market dominance and barriers to entry for new suppliers effects all areas of the gas and electricity supply markets. So all market segments should be reviewed.

Hugh Mortimer, 12 January 2006

UK power market traded volumes drop by a third in 2005

December saw the lowest average daily reported volume in the UK power market for over three years, according to Heren Energy data. However, January has so far seen a near doubling in daily average volumes compared to the previous month.

December '05 daily average volume (1,323 GWh) was 20% lower compared with December '04 (1,659 GWh).

Overall daily average volumes, based on reported trades, for 2005 were 2,317 GWh. This was down 31% from 2004 average volumes, which stood at 3,340 GWh. The 2004 volume itself was just over half the average daily volume reported for 2003 (6,099 GWh).

The downturn in volumes traded on the UK power market has been a consistent trend for the last four years, since the collapse of Enron and later TXU Europe. But while the long-term downward trend has been largely a consequence of the (either forced or voluntary) withdrawal of players from

the market, the recent drop in liquidity reflects other factors too.

One is the smaller contract sizes now being traded. Whereas 20 MW clips were once the norm for curve trades, 10 MW is now standard. The increasing interest in spark-based deals has also seen a growth in 15 MW clips (employed to balance against a standard 25,000 therm gas trade), with 5 MW transactions often 'tacked on' to 10 MW deals in order to make up the volume.

Credit issues, market volatility and the generally risk averse nature of the UK power market have also impacted liquidity further along the curve, particularly in the recent climate of rising prices. In particular, sellers have been few and far between, as the recent price spikes have weakened any appetite to go short along the curve, especially for the Winters. Dwindling activity in the UK gas market has also contributed to the slide. GR ●

