

Third-Party Proposal: Publication of Near Real-Time Data at UK Sub-Terminals: Modification Reference Number UNC006

Impact Assessment Consultation Response from Barclays Capital

10 March 2006

Barclays Capital is pleased to submit these comments on Ofgem's Impact Assessment for proposed Modification UNC006 "Publication of Near Real-time Data at UK Sub-terminals". The Impact Assessment presents a thorough and insightful analysis of the benefits and costs associated with the modification. We conclude that the assessment clearly demonstrates that the proposal will deliver significant benefits and that there is therefore a clear and unambiguous case for Ofgem to approve this modification. Our comments below address some of the specific assessment issues raised in the document.

Benefits

Economy and Efficiency

It is clear from Ofgem's analysis and previous analysis of the benefits (including our own), that even relatively modest changes to the risk premiums associated with uncertainty over the supply function yield very large benefits to consumers which are an order of magnitude greater than the likely costs. While Ofgem note that there are inherent difficulties in accurately modelling the benefits stemming from the release of sub-terminal flow information, the analysis in the Impact Assessment presents a measured and reasonable attempt to quantify these benefits. In particular, the modelling analysis has sought to isolate the impact of beach flows from other explanatory factors and, within beach flows, to focus on the incidence of outages. We share Ofgem's view that this provides a conservative estimate of the likely benefits given that it does not account for the response of other parts of the system via changes to the gas price. Moreover, the analysis focuses solely on the reduction in risk premia surrounding outages. In our view, the impact of poor information transparency is likely to be more pervasive than this since uncertainty over flows has an impact on risk premia at times other than when specific outages have occurred.

Market Volatility and Liquidity

The release of more information will mean that prices respond more accurately to changes in the underlying fundamentals. This will reduce undue volatility associated with uncertainty over the supply function, but may increase "volatility" at times of significant supply changes as the market reacts more quickly to supply events. Although it is unclear whether this will result in a net increase or fall in volatility overall, the crucial aspect is that decisions and prices will reflect actual market data rather than rumour and speculation, ie, whether volatility increases or falls, it is likely to be the "right" level of volatility. This will significantly improve liquidity – and reduce risk management premiums - as market participants will have significantly more confidence over the evolution of prices and the risks associated with volatility in taking their trading decisions.

Costs

IT Costs Incurred by NGG NTS

In total, any costs likely to stem from this modification are an order of magnitude smaller than the benefits. Although we do not have any direct knowledge of the costs likely to be incurred by NGG NTS, we share Ofgem's opinion that they are likely to be on the high side given that the projected costs have more than

doubled since the initial high level estimate for the May IA and the apparent failure to provide the requested clarity on the underlying requirement for changes to its systems.

IT Costs Incurred by Market Participants

We share Ofgem's view that market participants can choose how to use the information stemming from this modification. Any costs incurred by participants in this regard will therefore reflect the value that they place on capturing and using the additional data (which includes the possibility of not using the information at all and, hence, not incurring any additional costs). Consequently, we do not believe that the IT costs incurred by market participants should feature in the Impact Assessment as a direct cost associated with this modification.

Commercial sensitivities

With better information release, prices following any outage will move more quickly to the efficient level reflecting the true supply-demand balance. The corollary of the claim that producers will pay more as a result of the modification, is that producers currently enjoy an undue advantage in buying to cover shortfalls at prices which do not reflect the true supply-demand balance following an outage (ie, they have bought from another participant who has sold at prices which are artificially depressed because the outage information has not been released). As a consequence, any increase in "costs" to producers resulting from this modification represents a pure transfer of value from producers to market participants more widely and should be disregarded in assessing the costs of the modification. However, providing all market participants with equal information reduces the risk of selling to a producer following an outage at prices which fail to reflect the true market fundamentals. The removal of this risk will increase market participants' confidence in entering trades, improve liquidity and reduce risk management premia.

As Ofgem notes, information is made available real-time in the UK electricity market (and then on a unit-specific basis). We are aware of no attempts to remove this information on the grounds that producers are being unduly exposed following outages. Moreover, in Nordpool, generators are explicitly prohibited from trading following an outage at one of their plants until the wider market has been informed to ensure that no participant is able to benefit unduly from privileged or prompt access to outage information.

Risks

We welcome Ofgem's assessment that it is highly unlikely that information will be withdrawn as a consequence of this modification (and consequently that the risk of needing to install duplicate metering is low). However, to the extent that any risk of withdrawal remains, Ofgem (and the DTI) should consider changing the regulatory framework to underwrite the provision of this data.