Vanja Munerati
Ofgem
9 Millbank
London
SW1P 3GE

10th September 2010

Dear Ms Munerati,

GB wholesale electricity market liquidity: Summer 2010 assessment

InterGen welcomes this opportunity to comment on Ofgem's consultation document '*GB wholesale electricity market liquidity: Summer 2010 assessment*. Our detailed response is attached below.

We would be happy to discuss with you any of the issues raised in our response.

Yours sincerely,

Chris Ridgway

InterGen’s response to Ofgem’s consultation paper “GB wholesale electricity market liquidity: Summer 2010 assessment”

Executive summary

InterGen is the UK's largest and most successful new entrant independent generator, having invested £1.4 billion in the UK since 1995. InterGen owns and operates three highly efficient gas fired power stations in the UK totalling 2,490MW and actively trades in the prompt and forward wholesale power and gas markets. InterGen is currently pursuing a number of development opportunities in the UK including the construction of two further 900MW CCGTs, representing a further £1 billion investment.

InterGen continues to share Ofgem’s concerns about the low level of liquidity in the GB wholesale electricity market. However, as stated in our responses to Ofgem’s July 2009 and February 2010 consultation documents, InterGen believes that low liquidity is just one of the symptoms of GB’s largely vertically integrated market structure. Vertical integration is not compatible with a truly competitive, liquid, rational and transparent wholesale electricity market, which can only be achieved with meaningful separation of the activities of generation and retail supply. InterGen continues to support the implementation of a self-supply restriction to address liquidity issues, increase competition and reduce the barriers to entry into the market for smaller, independent suppliers and generators.

InterGen remains supportive of Ofgem’s continuing investigation into market liquidity, though urges Ofgem to develop the potential regulatory interventions that were set out in the February 2010 document. It is necessary for such corrective actions to be compatible with the proposals for energy market reform due to be announced later this year. Accordingly, InterGen believes that a detailed implementation programme for each of these interventions should be developed with greater urgency to help inform the market reform process and to allow Ofgem to move without further delay if it decides that action is appropriate.

Our responses to the specific questions asked in the latest consultation paper are below.

<u>CHAPTER: Two – Proposed metrics</u>

Question 2.1: Do you agree that the proposed framework provides an adequate range of evidence for assessing market liquidity?

Yes. InterGen is supportive of Ofgem's approach of assessing liquidity by monitoring a broad range of both quantitative and qualitative metrics and believes the proposed metrics are both adequate and appropriate.

<u>CHAPTER: Three – Preliminary assessment</u>

Question 3.1: Do you agree with the assessment of the metrics in this chapter?

Broadly yes, with a number of qualifications described below.

Aggregate churn (metric 1)

The forecast outturn for aggregate churn for 2010 in Figure 1 is based on a linear extrapolation of trading in the first five months of 2010. This is likely to overstate the actual outturn as, historically, market liquidity tends to reduce over the Summer holiday months and again towards the end of December.

Regarding Ofgem's comments in paragraph 3.12, it may be possible for Ofgem to obtain data from the main electricity market brokers which would allow an assessment of the degree to which the churn rate has been affected historically by the Big-6 vertically integrated companies trading amongst themselves.

Bid-offer spreads (metric 2)

Although not stated explicitly in the consultation paper, it is suspected that the Heren data used for the analysis of this metric are the reported closing prices. These are frequently a notional spread (for example, £0.2/MWh) around the last traded price and may not reflect the spread between bid and offer prices throughout the day, particularly for illiquid products.

A better measure would be the amount of time the bid-offer spread for each standard product (e.g. for each of the next 6 seasons, say) was within a number of defined ranges (e.g. £0.0/MWh to £0.2/MWh, £0.2/MWh to £0.4/MWh, …, £1.8/MWh to £2.0/MWh, greater than £2.0/MWh, no spread available). This can be monitored by aggregating the real-time price information across the 4 main broker screens. There are software products available that allow market participants to collect and analyse such data.

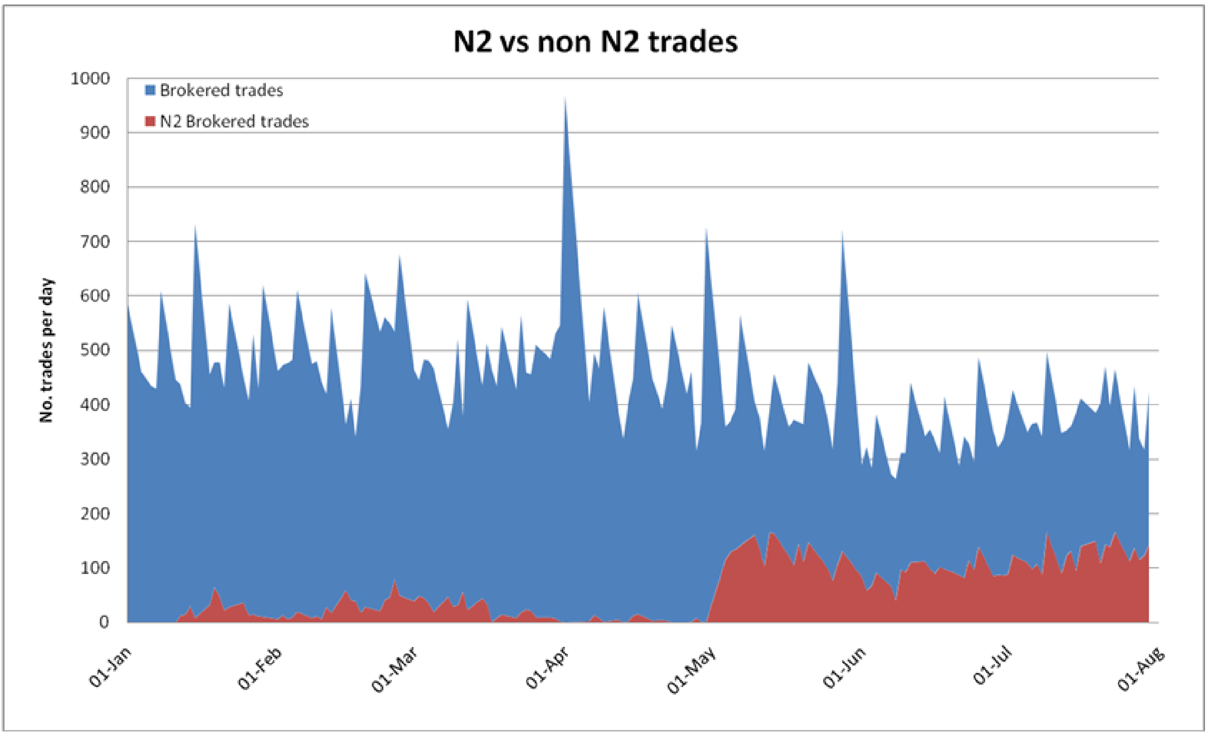
Use of platforms which promote price transparency (metric 3)

As stated in previous consultation responses, InterGen does not believe an increase in exchange-based trading for longer-term products would be of benefit to smaller independent market participants who have limited capacity to provide collateral for margining. Accordingly it is suggested that it is most appropriate to monitor this metric for prompt trading only.

Regarding Ofgem's comments on price discovery and transparency in paragraph 3.21, there are software products available that allow market participants to aggregate, store and display real-time price and volume data and actual trade data from the 4 main broker screens.

To the extent data can be obtained, it could be informative to examine the degree to which smaller market participants engage in both shorter and longer-term exchange-based trading in those markets listed in Table 5 of the consultation document.

InterGen does not agree with the statement in paragraph 3.32 that N2EX has generated significant day-ahead prompt volumes from the start of May 2010. Rather than generate additional volumes, the overall volume of prompt trades (N2EX plus brokered) has actually fallen, as shown in the figure below. Thus N2EX has fragmented the existing prompt market. Further, we have identified a number of occasions when there have been price discrepancies for products between the two markets.



Volume of trading along the forward curve (metric 4)

InterGen notes that there has recently been an increase in the frequency for which bid and offer prices are quoted for longer dated products (specifically the seasons out to Summer 2015), albeit with wide bid-offer spreads. However, the number of transactions that have taken place for longer-term products remains very low and comparable to that seen in previous years. It is possible that the recent change in bid and offer behaviour is limited to a very small number of players attempting to demonstrate the existence of a longer dated market.

Diversity of products (metric 7)

As well as monitoring the products stated in Table 9, InterGen would suggest a more frequent availability of "overnight" products (covering the period 23:00 to 07:00 seven days a week) in the forward markets would be of benefit to smaller suppliers in shaping their position more closely to the needs of their customers. A Market Maker, proposed as one possible solution in the February 2010 consultation document, could be particularly useful in delivering an improvement in this metric and metrics 8 to 10.

Question 3.2: Do you have any comment on the level of improvement in the metrics that would make a significant difference for market participants?

As a first step, a suitable target for each of the proposed metrics would be a figure comparable with the corresponding metric for the UK gas market, which is generally agreed to be sufficiently liquid.

InterGen agrees that the proposed metrics should be monitored over time to determine the rate of progress towards improving liquidity. However, it seems unlikely that any of the metrics will change substantively in the period of time until Ofgem's next assessment of market liquidity in Q1 2011. Were they to do so, it is doubtful that this could be interpreted as demonstrating a long-term, sustainable improvement in market liquidity.