Tuesday 8 May 2012

# RenewableUK Response:

# Retail Market Review: Intervention to enhance liquidity in the GB power market consultation

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RenewableUK as the leading trade association in the renewable power industry, with 650 company members right across the value chain in the wind, wave and tidal stream sectors, thanks Ofgem for the opportunity to contribute to this important policy area. The industries we represent will be providing the majority of the renewable electricity that will be required to meet targets for 2020, and bring the best opportunities in the renewables sector to provide thousands of jobs in the UK and stabilise consumer prices.

RenewableUK is fully supportive of adding liquidity to the market and welcomes working with Ofgem and others in the future to make this a reality. However, further work is needed to determine the most effective methods necessary to increase liquidity in the GB power market. Short-term liquidity addressed in this consultation does little to solve many of the problems currently being faced by generators and small suppliers. More should be done to increase long-term liquidity, which would involve more focus on generators and Power Purchase Agreements (PPAs).

The views expressed in this consultation response reflect the consensus position of our diverse membership and therefore we urge Ofgem to also consider the views of our individual members in their own responses.

**Please find the below responses to the questions outlined in the appendix:**

**Question 1: Do you agree with the objectives we have identified?**

RenewableUK largely agrees with the three fundamental objectives including ensuring the availability of products which support hedging, robust reference prices being generated and an effective near-term market. We understand the ultimate goal is to increase competition within generation and supply markets and that a critical aspect of reaching that goal is to add liquidity as well as credit and collateral.

The three objectives identified are strongly interlinked. An effective near time market should serve as a foundation for setting a robust reference price. As soon as the market believes in an explicit reference price which is not easily manipulated by individual market players, it is likely that both market participants and trading platforms will drive the process of offering products which support hedging.

However, any interference within the market should be carefully considered because the consequences of getting it wrong can have harmful impacts to consumers. The industry is supportive of liquidity, competition and transparency but favours a less prescriptive approach to reach these end goals. Furthermore, any steps taken to address liquidity and competition should have the necessary flexibility with regards to the outcome of the Electricity Market Reform (EMR) process.

**Question 2: Do you think there are other objectives we should be considering?**

Added transparency could have positive impacts on the market and should be considered as an overall objective. For instance, the access to live generation data is currently cumbersome and costly, and should be improved. The existing service is of some use since it allows for particular historical data, however, it does not allow for an on-going monitoring of the market, in spite of the fact that all this information is already made available to National Grid.

As mentioned previously, more should be done to increase long-term liquidity including examining obstacles to market entry. Barriers preventing entry into the market have had a substantial impact on long-term liquidity.

**Question 3: Do you agree with our views on market developments since summer 2011?**

Progress toward objectives one and two such as signs of improved trading in financial products and the narrowing of bid-offer spreads seem to be understated, and volumes of exchange trading having increased seems to be only briefly acknowledged in the consultation document. Some action may be required, but before rushing to any premature conclusions robust analysis must be conducted. That said, the progress so far has been limited and recent, so it is not currently possible to draw definitive conclusions.

**Question 4: What specific further developments would be necessary to meet our objectives?**

No comment.

**Question 5: Do you agree that objectives one and two are current priorities given market developments?**

It appears from Ofgem's own analysis that given the impact of market developments that objective one focusing on hedging is more critical to address than objective two focused on reference prices.

**Question 6: Do you agree that the MA is the appropriate mechanism to meet our immediate objectives?**

Before a mandatory auction is implemented the need for it should be made abundantly clear. That is not yet the case. More work should be done to ensure there is not a more preferable option available such as re-examining the Market-Maker option for instance.

There is a danger that if an auction was scheduled to be held on a monthly basis, that any increase in trading would only be around the time of the auction, leaving little activity in the market at other times; evidence of this limited time window activity is apparent in the Virtual Power Plant (VPP) markets in the United States and France.

If a mandatory auction is determined to be necessary in the end it may be more appropriate to implement a gradual increase in the amount required to be auctioned. There is little downside to at first require a 10% mandatory auction, then 20% if needed and ultimately 25%. With clearly set benchmarks to be met intervention could be kept to what is minimally required to achieve improved liquidity. Just as there has been progress with other market developments it is possible a 10% mandatory auction could adequately meet the objectives set out by Ofgem. This proposed gradual levelling is more in line with what Ofgem originally proposed in 2011 and would prevent any more intervention than necessary.

**Question 7: Do you agree that, at the present time, the other mechanisms identified would not be appropriate for Ofgem to pursue?**

No comment.

**Question 8: Do you agree with the key features of the MA we set out?**

In section 4.23 Ofgem acknowledges that, "If the market were to develop to meet our objectives, we would be able to revise the obligated volume level downward accordingly". This begs the question why not start lower with a required amount of 10% and work upward toward 25% if necessary. The two examples cited on page 29 have mandatory auctions levels of 10% (France) and 15% (Texas) respectively.

The obligation on the Big Six requires that they sell the obligated volumes, as specified, in the market irrespective of whether they have the relevant shape in their portfolio. Those with large renewable portfolios will be disproportionately disadvantaged, as wind generation will be exposed to the volatility of the full power price, not just the spark spread. This creates a disincentive for further investment in the renewables required to meet 2020 targets. It will also deter the creation of aggregating services, required by independent renewable generators. RenewableUK suggests that variable sources of energy such, as wind, should be excluded from the mandatory auction requirement.

**Question 9: Do you consider it appropriate to have buy-side rules in place and do you have any comments on the detail of such rules?**

No comment.

**Question 10: Do you consider that there are benefits and risks to the approaches that we have not identified?**

Ofgem should consider the impact on renewable generators as a specific class of generator. We are concerned that as currently proposed vertically integrated companies will have obligations placed on them relating to last year's production. This will create a specific production risk for those companies with sizable renewable generation.

**Question 11: Which approach do you consider is best placed to deliver our objectives at least in terms of cost and risk?**

The second approach where obligated parties individually identify service providers seems to have fewer risks, which would make it the optimal option. It seems to be a simpler approach with less interference and the advantage of the first approach is not apparent.

The risks identified for the second approach on page 38 seem achievable when compared to the first approach. There does not appear to be any benefit to Ofgem identifying a single service provider and is better left to be decided by obligated parties themselves.

**Question 12: Do you consider that both approaches are able to meet our objectives?**

No comment.

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