noble clean fuels

FAO:

Phil Slarks
Wholesale Markets
Ofgem
9 Millbank
London
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Dear Mr Slarks,

**Wholesale power market liquidity:**
**Final Proposals on a "Secure and Promote" licence condition**

NCFL is a 100% subsidiary of the Noble Group Limited. NCFL has approximately 250 energy trading and commodities professionals in London trading wholesale gas, oil and oil products, electricity, coal, carbon and metals. It is a private limited company under the laws of England and Wales with Company Number 6810620.

NCFL has gas licenses in the UK, Germany, Netherlands, Belgium and Austria and power licenses in the UK, Germany, France and Nordic regions. The company has been actively trading, transporting and taking delivery of the commodities in all these countries. NCFL trades OTC and also on several commodity exchanges in Europe including ICE, EEX, Endex, APX, Nordpool and EPEX.

NCFL is currently trying to develop new power projects in the UK and is working with a number of developers on some well advanced opportunities.

NCFL's business would therefore see significant benefit from the creation of a robust, liquid power market where we can judge the value of future investments as well as expanding our trading activities. As noted above, we do continue to assess physical assets and would like to take some developments forward. Again this would be helped by the existence a robust forward power price curve. As we trade in related markets such as gas and carbon, we would also be better able to efficiently hedge our position if there is a market with easy entry and exit, where parties do not to fear ending up with stranded positions.

## Introduction

NCFL welcomes Ofgem's proposals to improve liquidity in the GB power market and believe that timely action is required if many other energy policy goals are to be met. Like many parties, NCFL is concerned that the fundamental issue is the underlying market structure and Ofgem's proposals may not be able to overcome the inherent problems created by the internal trading of the integrated utilities. Ofgem must therefore keep the market under careful review and if necessary push for structural remedies, possibly via a sectoral referral.

NCFL also believes that Ofgem should keep under consideration the use of a self supply restriction. This could enhance the proposals that Ofgem has set out and could provide a further stimulus if these proposals prove too limited in their impact.

## Market Impacts

NCFL believes that Ofgem has correctly identified the key benefits that will arise as a result of increasing liquidity in the market. While many benefits will be difficult to measure against a background of rising prices (for a wider variety of reasons), NCFL believes that liquid markets are significantly more efficient in informing both short and longer term decisions.

The market will be able to make more efficient investment decisions and new entrants should find it easier to enter the market if there is a liquid market. There have been numerous examples of new entrants finding it difficult to get reasonable contractual terms, or secure the types of products that they need to enter the market and manage their risks in an economic manner. NCFL has also found market entry difficult, despite our size and wide experience in traded markets across the world. Ofgem's two pronged approach to helping smaller parties should at least prompt some improvement in the trading environment.

It has been to the detriment of customers that the market has remained illiquid for so long. As well as deterring investment and market entry, it has allowed the big 6 to consolidate their positions and pass rising costs to customers unchallenged by the rigours of a competitive market. Suppliers have been unable to develop more innovative products, and seem to have ignored the opportunities offered by load management and demand-side services, as their market positions have generally allowed them to continue to maintain the status quo. Ofgem must push ahead with reform to the benefit of customers.

**Market Making Obligations**

NCFL welcomes Ofgem's proposal for mandatory market making (MMM). We think that the design is well thought out and the ability of the big 6 to contract out their obligations, to post bids and offers for specific power products on platforms that licenced parties can access, should ensure none have a problem in compliance. NCFL believes that there are a number of parties who would be able to take on the MMM obligations and we would be happy to discuss with obligated parties any contracting out they wish to do. While the parties concerned may have to pay for a commercial service, we do believe that there are parties in the market who can and will offer such a service to them.

NCFL suspects that the big 6 will have concerns over the design of the MMM obligation. We believe that in liquid markets traders are generally placing bids and offers on screens all day every day, and well functioning markets, with propoer trading controls, shouldn't represent a risk to businesses, but an opportunity to manage risk efficiently. However, as the market is relatively immature Noble would suggest that there may be a case for some form of "soft landing". To this end we have made some suggestions below on some areas of the design.

*Products* – Ofgem's proposed products represent a good spread of products that offer suppliers, and other market participants, the tools they need to risk manage and meet the needs of customers in the most efficient manner. That said, the products will need to be kept under review, with; market coupling, a change in the gas day, the change in the power calendar, etc., all posing as market changes that could see new products develop.
In light of the EMR proposals, Ofgem should consider a longer dated baseload product, to reference the baseload power receiving FITs with CfDs, as well as potentially smaller clip sizes in prompt peaks. These products would help new entrants and smaller suppliers, but also smaller peaks should allow all parties to manage the risks around marginal cash-out prices.

*Clip size* – The 5MW clip size will initially provide a balance between creating shape and limiting the administrative costs of the proposals, but as noted above there may be a case for smaller sizes in prompt peak products. Ofgem should review this in light of the timing of any cash-out changes. This is not just an issue around marginal cash-out, but would also allow smaller, intermittent generators to better manage their own imbalance risk in a market with increasing volumes of wind generation.

*Obligation periods* – NCFL has concerns that the obligation is framed in terms of making offers/bids available 50% of the market opening times as this could lead to periods of good liquidity and other periods with no market available. We are aware that there has been discussion about the use of windows to concentrate liquidity in certain periods. This proposal has some merits as it would concentrate activity and could build confidence, especially as the market develops. Whichever route Ofgem decides to go down, they need to couch the obligations in terms that ensure parties can reasonably access a liquid market every working day, or at least the majority of days.

NCFL believes that the big 6 should be replacing taken bids/offers very quickly if the market is to be truly liquid. This is an important design criteria and our traders would expect to keep altering their positions depending on the way the market is moving. There seems to have been some suggestion that if the market is moving fast, or against the party concerned, they should be able to suspend their trading. This does not seem sensible if the idea is to help parties manage risk which can arise at any time. There is no reason that the big 6's traders cannot respond to the market as other players do.

*Coverage* – Ofgem's proposal to place the obligation on the big 6 is proportionate as only the big 6 have the physical assets to help manage the obligation. While they have differing portfolios, they are all in a position to offer the products that Ofgem proposed to make them sell. EdF has been particularly vocal about its lack of peaking capacity, but it does have investment opportunities and also customers that it could sell DSR products to in order to create more physical peaking capability in future.

NCFL could see a case for extending the obligation to GdF, who has now grown its portfolio to a comparable size to Scottish Power. However, there is no point in extending the obligation to merchant plant all of which is obliged to bring all of their power to the market anyway.

*Third parties* – Ofgem's proposals to allow the big 6 to employ third parties to manage market making for them is a welcome addition to previous proposals and NCFL believes is a workable solution to overcome their concerns about regulatory creep. NCFL believes parties will be willing to offer these services to the big 6 if they do not wish to meet their obligations directly. It is a reasonable position for the big 6 to contract out obligations, as many companies do contract out services they do not feel able to meet themselves. It will be a commercial negotiation around the terms parties are willing to undertake the services for, but it will still offer greater liquidity if another party is taking on the obligations of one or more parties.

NCFL believes that third parties may also bring greater innovation to the market. They could be willing to consider different products, being available more of the time and even create new platforms. We recognise the concerns around financial regulations, but until directives such as MIFID are in place it is premature to suggest that the big 6 cannot undertake their own MM activities. Ofgem's proposal therefore offers them optionality, but does not impose a solution on them.

**Supply Market Obligations**
While NCFL would not expect to benefit directly from these proposals, Ofgem's suggested requirements represent a robust and proportionate response to the problems reported by smaller suppliers. The proposed obligations are not unduly onerous and represent the normal commercial behaviour that one would expect in a competitive market, where parties seek to do business with one another, rather than aiming to exclude potential deals.

The obligation will not be unduly onerous as there are few small suppliers. However, we could see merit in the obligation being extended to the big 6 suppliers to offer terms to smaller generators. This may help overcome some of the PPA issues that DECC is trying to address. Market access is an issue for parties on both sides of the market and any moves to make access easier would be welcomed.

**Wider Issues**
NCFL believes a licence condition that can be removed is more robust than a drop dead date. The new licence condition can refer directly to a rule book, in a similar manner to the way codes are reflected in licences. The rule book may also need some governance processes to offer the obligated parties some comfort over the process for any changes.

As noted above, Noble remains concerned over the fundamental problems surrounding vertical integration. We would urge Ofgem to continue to be clear that the market structure remains under review. Ofgem must not rule out a referral to the competition authorities if the issues surrounding lack of liquidity cannot be resolved via the proposed licence changes.

If you or your colleagues would like to discuss any of these issues further please do not hesitate to contact me.

Yours sincerely

Denis Bajolle

Head of non-Nordic Power Trading

Noble Clean Fuel Limited