

To: Cathryn Scott, Wholesale Markets and Commercial, Ofgem
Via: Supplier@ofgem.gov.uk

20th September 2018

Dear Cathryn,

Response to Open letter: Secure and Promote Update

Thank you for the opportunity to respond to your Open Letter on Secure and Promote detailing your minded-to view to suspend the Market Making Obligation (MMO) license condition.

Our view is that Secure and Promote has been positive in opening competition and ensuring that independent suppliers are able to access wholesale gas and power at reasonable prices. The MMO license condition has been important in achieving this. We recognise that the UK generation and supply mix is rapidly changing and are fully supportive of the proposed review in 2019. However, we worry that a temporary suspension, without running through an Impact Assessment, could have a number of unknown and unintended effects.

Bid-Offer Spreads

During the market making window there has been significant reduction in the bid-offer spread. This has provided participants with the ability to execute wholesale power trades at a fair market price. This is important as it means that lack of vertical integration does not present a competitive disadvantage.

Fair pricing

It is difficult for smaller suppliers to participate through the existing broker platforms for a number of reasons, primarily including

- The clip sizes that small suppliers look to purchase to efficiently hedge are frequently much smaller than those available through the broker platform
- Efficient access requires underlying trading and credit agreements with a large number of parties. These agreements take time and significant cost to execute.

Without the ability to effectively post offers on a broker screen, smaller suppliers often trade through direct bilateral with larger participants in the wholesale market. The MMO obligation is important to provide sight to the fair value of these contracts and ensure that the smaller suppliers can access a fair wholesale price.

Market Visibility

Outside of the market making window very little trading activity takes place. There are frequently very wide spreads, missing bids/offers or no visibility to either side. During these periods it is difficult to ascertain an accurate view of the forward curve. This accurate view is vital as it provides us with the ability to continuously review our tariffs and ensure they remain set at an accurate, cost-reflective level.

Churn

There has been a clear increase in wholesale churn since the license obligation was introduced. This represents a healthier, more liquid market.

Summary

The MMO has had a clear, demonstrably positive effect on wholesale market access. Generation and supply markets have evolved significantly since the introduction of Secure & Promote in 2014 and, without running a detailed impact assessment process, it is hard to know what impact these proposals would have on market liquidity, visibility and bid-offer spreads. There are imminent significant hedging pressures on small suppliers with price cap hedging and the introduction of PAR1 and this would provide even greater uncertainty over the ability to effectively hedge our costs.

Yours sincerely,

Matt Bunney
Head of Procurement
Octopus Energy