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Institute of Energy for Southeast Europe

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Session IV: “The Energy Crisis and the New Electricity Market”

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Let me first thank you for inviting the European Federation of Energy Traders to this significant and topical conference. My name is Mariana Liakopoulou and I serve as Markets and Policy Associate working in the EU liaison office of EFET.

For those of you who may not be familiar with us, we represent about 130 companies from across all corners of Europe – advocating for competitive and well-functioning energy markets at European and national level. As well as making the case for markets, we also work to make those markets work better, through our standard contracts, PPAs and data exchange standards. We also maintain a strong focus on the power and gas markets of Central and Eastern and Southeast Europe through our dedicated task force, alongside a particular focus on the Greek market through our WG Greece.

So, let me begin by briefly commenting on the title of our session:

The recent price rises have certainly caused significant problems for customers in many parts of Europe. We should ask whether they're driven by a design issue or by fundamentals – and I'll start there.

We should then consider how to respond to those rises in a way which doesn't interfere with the market.

And before we talk of a 'new electricity market' we really need to ensure there is both a problem with the market and a better alternative available that we can afford to go for in times of crisis.

So, let's start by approaching this in an energy system integration context. The power price surge over the last month or two is the result of the European wholesale power market's appropriate reaction to changing fundamentals indicating scarcity in the market.

A demand-side recovery from the pandemic has coincided with tight supply in electricity production, owing to poor conditions for RES-E production since early autumn and low hydro reservoir capacity.

At the same time, we've witnessed tight supply in commodities used for electricity production. Low storage levels, strong global demand for LNG, and reduced Russian flows via Belarus and Ukraine (or simply the market sentiment around the mere prospect of them) have put upward pressure on wholesale gas prices. Higher gas demand in the power sector (and thus higher prices) is the result of the inherent intermittency of renewables, so there's this circular effect that we must consider here. Although gas pricing and market design is not the topic of this session, it is important to keep note of the value of hub-based competition, as opposed to oil-indexed LTCs, in supporting inter-M-S price convergence over the past decade, as recently highlighted in ACER's preliminary assessment of high energy prices.



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And of course, higher demand for fossil generation by power or heat plants covered under the EU ETS boosts demand for EUAs, leading to a surge in EU carbon prices.

So, electricity prices are rising, and households and certain businesses cannot cope with it. Which begs the question of what's the right reaction?

Disproportionately affected domestic and industrial customers need to be protected by national governments and NRAs, without distorting price signals for all.

Of key importance here is to balance short term intervention with minimisation of long-term cost to the operation of the EU internal energy market.

Markets are compatible with consumer protection, and the EC's Communication on Energy Prices is a good start in outlining pertinent measures, such as temporary deferrals of bill payments etc. Well-informed consumers can react if directly exposed to high prices.

However, we have also witnessed some examples of national interventions changing the rules of the game by affecting wholesale price formation, like the clawback measures on low-carbon generation enacted in Spain and Romania, to which EFET recently reacted.

Cost increases hurt customers, but their drivers are demand and supply, not the market design. Continued integration of our EU internal energy market is the way forward. Our market is delivering. It reacts to fundamentals and it's already helping manage volatility from short-term price changes.

Consumers accounting for an appreciable part of the total market are not directly exposed to price volatility of the spot market. Certain categories of electricity buyers, notably industrial, large commercial and public consumers and retail supply companies, have the chance to buy power forward at fixed prices and/or use other types of contract, such as futures and options, to hedge their exposure to volatile wholesale spot prices. Hedging techniques allow certain retail suppliers to offer fixed-price contracts to households (or else to change prices less often.)

However, national responses to the affordability challenge that modify market fundamentals and are not proportionate and tailored to those consumer categories directly exposed to volatility threaten the accuracy of and the case for hedging. This comes with risks of weakening EU energy market integration in a time when it's needed the most due to our decarbonisation pledges for 2030 and 2050.

Price signals sent by energy and carbon markets need to deliver incentives to innovate, invest, become more energy efficient and switch away from carbon intensive fuels. If allowed to do so, the probability that Europe will find a least cost decarbonisation pathway increases.

However, national price interventions that risk increasing wholesale prices in the short term may damage the investment climate in the medium term – making any investment (e.g., in RES, new flexibilities etc.) more expensive (or potentially too risky.) And this, of course, undermines the ability of individual countries to reach their decarbonization targets in a cost-efficient manner.

In this sense, a move back to national markets would be a backward step at this stage. At the same time, there is lack of clarity on a Plan B, as market design changes can take years,



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jeopardize new green investment and spur regulatory uncertainty creating costs for the entire system.

As our EU wholesale market based on marginal pricing is delivering and reacting to global drivers, incl. demand, committing to improving the IEM is the way forward, via for example, further improving forward markets – or else the ability of market participants to protect consumers from short-term volatility via hedging.

So, to wrap up: distortive interventions, for well-intentioned reasons, will raise costs in the long run. There are ways to protect the vulnerable and national governments and regulators must act based on EU-level guidance without hindering free formation of prices. Building on competitive EU-wide markets in energy commodities and related contracts, the liberalization story of which dates back twenty-five years, is the way forward. EFET will keep working to make these markets work, as these markets are best placed to provide solutions for each aspect of the so-called energy trilemma: Affordability, Security of Supply, Decarbonisation.