INOGATE/ERRA Training Programme:
Introduction to the Regulation of Electricity Markets
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The Role of Electricity Traders and Exchanges

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Introduction

- Terminology
- About traders
  - Review of the basic types of traders
  - What should you expect from players?
  - What players expect from you?
- About exchanges
  - Why exchanges are important?
  - Current exchanges in Central Europe
- Ideas for the future
Terminology

Exchanges

Traders

- A very simple definition
  - Buy/sell [electricity] with the intention to make profit

- Terminology
  - Liberalisation – competition
  - Traders – optimizers – brokers
  - Whole sale – retail

- Comments:
  - Traders and physical players (generators, DisCos) have different profitability cycles;
  - Liberalisation does not necessarily reduce prices

- A very simple definition
  - Organised market to buy/sell electricity

- Terminology
  - Pool – exchange
  - Clearing prices – index trading

- Comment:
  - Exchanges do not create markets – it is the other way around
Typical Players and Games

- Eric Berne: Games People Play (1964)
- The CCC
  - Classic – cigar – cognac
  - Buy cheap, sell expensive
  - **Game**: Back – to – back (only)
- The Scottish
  - Everything is done at minimum (financial) level, even though there is usually a serious mamma company somewhere in the back-ground
  - **Game**: The Malenkij – small – petit trades
Who are the most typical traders?

- **The Visitor**
  - Active trader outside the energy sector and would like to try its luck in energy;
  - Good general understanding of trading, but energy is (and likely to remain) a fringe activity
  - **Game**: The I-am-happy-to-try

- **The Mamma’s baby**
  - Trading house of one of the big investors/incumbents
  - Very experienced, with excellent credit, BUT strict internal controls that might not be able to accommodate CE and SSE requirements
  - **Game**: All-you-want-to-know-about-trading, but...
A Day in the Life of a Typical Trader

➢ Get into the office before 7am
➢ Check P&L account and positions from yesterday
➢ Update analysis and spreadsheets with latest data
➢ Decide how to manage open trading positions and implement any new ones
➢ Enter the day’s bids into the power exchange(s) and buy cross border capacity
➢ Keep an eye on the coal, emissions and gas markets
➢ Watch political, weather news
➢ Get some lunch by the desk while watching the markets
➢ A plant has tripped, need to re-cover positions from market
➢ Mark all the books to market, check the end of day P&L
➢ Finish around 6pm
A practical example

- How different traders will react to the same tender invitation?

- HEP tender
  (http://www.hep.hr/hep/oglasi/upload/997.pdf)

- Cal11, base-load electricity, with HEP’s option to interrupt on 13 named-days, plus on an extra 35 days (up to ten days maximum, in any calendar month);

- Offers to be submitted on 13 May, with validity until 28 May 2010
<table>
<thead>
<tr>
<th>Will not participate</th>
<th>Will participate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Visitor</td>
<td>CCC</td>
</tr>
<tr>
<td>Mama’s baby</td>
<td>Scottish</td>
</tr>
</tbody>
</table>
. . . And the winner is?

[to be discussed after a vote]
What should you expect from players?

- General good standing
  - Test of the reasonable business (wo)man
  - No under the table deals
- Selfishness
  - Intention to maximize profit
  - See the positive side of this selfishness: traders help to discover regulatory faults
- Limited (time) commitment
  - If markets work, fine; if not, do not waste time and move on
- Respect
  - Regulator – regulated relationship in Anglo – Saxon versus Ottoman/Habsburg empires
  - Work in partnership approach (“same boat”)
    - Consultation, regulator – trader meetings, etc
What players expect from you?

- Level playing field for all
  - ‘Preferential trader’ status in Serbia
  - SWEPOL cable between Poland and Sweden
- User-friendly, pro-market regulation
  - Allow as many players as possible to join the game
    - Remove barriers to entry (local offices, translation, etc.)
    - Listen to traders: VAT treatment at OpCom, Romania
  - Do not change ground rules without giving proper advance warning
    - Introduction of ‘export penalty’ in Slovakia after the SE auction
- Try to resist political pressure
  - Short term fix versus long term damage
    - ‘Week-end legislation’
Exchanges

Why exchanges are important?
- No counterparty risk;
- Sign of market maturity;
- Price discovery
## Leading CE exchanges

<table>
<thead>
<tr>
<th>Name</th>
<th>Location</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>EEX</td>
<td>Germany</td>
<td>Contradiction: not a CE – based exchange, but THE most important one for CE trading</td>
</tr>
<tr>
<td>PXE</td>
<td>Prague</td>
<td>Very successful exchange, with non-Czech products and regional plans</td>
</tr>
<tr>
<td>OpCom</td>
<td>Bucharest</td>
<td>THE most liquid day-ahead exchange in the region; but serious issues with VAT</td>
</tr>
<tr>
<td>PolPX</td>
<td>Warsaw</td>
<td>Challenging registration process, but the exchange has great potential</td>
</tr>
<tr>
<td>HUPX</td>
<td>Budapest</td>
<td>An exchange that had been in the making for years; still not running . . . <a href="http://www.hupx.hu/doc/sajtokozlemeny_20091217_eng.pdf">http://www.hupx.hu/doc/sajtokozlemeny_20091217_eng.pdf</a></td>
</tr>
</tbody>
</table>
Live-access to EEX, OpCom and PoIPX

[Live internet access to above exchanges to check latest prices]
Ideas for the future

• Future is relative:
  ✦ We can start discussions here and now

• Some introductory (provocative) points:
  ✦ Competition or regulation or well-regulated competition will produce the best prices for customers?
  ✦ Do traders create extra value or just capture ‘bits and pieces’ others leave on the table?
  ✦ How to reduce (limit) political interference in energy regulation?
  ✦ Do mandatory pools slow down the natural development of power markets?
  ✦ And finally, was this presentation useful?