

Level 17, Casselden
2 Lonsdale Street
Melbourne Vic 3000
GPO Box 520
Melbourne Vic 3001
tel: (03) 9290 1800
www.aer.gov.au

Contact Officer: Kevin Fincham
Contact Phone: 07 3835 4677

Mr John Pierce
Chair - Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

Rule change—Market making arrangements in the NEM

The Australian Energy Regulator (AER) welcomes the opportunity to comment on the rule change process underway regarding market making arrangements in the NEM.

As highlighted in our 2018 wholesale electricity markets report, we have observed a general decline in the volume of contract trading across the NEM and most acutely in South Australia. It is difficult to quantify how liquidity (the ease of buying and selling) in the contract markets has changed over time. Contract markets are complex and participants' trading positions are commercially sensitive. As part of our report, we examined the liquidity of contracts traded on the ASX using publicly available data and found that:

- Forward contract markets are liquid only to about two and a half years
- The contract market is not liquid in South Australia compared with other regions.

In the first instance, our view is that the market liquidity obligation (MLO) as part of the retailer reliability obligation (RRO) should be the primary mechanism for market making requirements in the NEM. Any additional mechanisms should be complementary and not substitutes for the MLO in circumstances where it is triggered.

In general, we consider a voluntary scheme would be unlikely to materially increase the incentive for large, vertically integrated businesses to offer contracts. Forward contracts are important for standalone participants and insufficient contract liquidity is a potentially material barrier to entry for new participants.

While the proposed model would enable the AER to monitor and enforce compliance with the mechanism, it would remain voluntary and as such we would not be confident of its effectiveness. Further, we expect that operation of a centralised tender process and related compliance and enforcement would impose onerous requirements that are not justified by the incremental benefits of the proposed mechanism above that being developed by the ASX.

If you have any questions in relation to this submission, please contact Kevin Fincham on 07 3835 4677.

Yours sincerely

A handwritten signature in blue ink, consisting of a stylized 'P' followed by a cursive 'C' and a long horizontal stroke.

Paula Conboy
Chair
Australian Energy Regulator

28 February 2019