

23 May 2019

Australian Energy Market Commission
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Sydney South NSW 1235

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Short Term Forward Market Consultation paper

Snowy Hydro Limited welcomes the opportunity to comment on matters raised in the Consultation Paper from the Australian Energy Market Commission (the Commission) on the Short Term Forward Market.

Snowy Hydro Limited is a producer, supplier, trader and retailer of energy in the National Electricity Market ('NEM') and a leading provider of risk management financial hedge contracts. We are an integrated energy company with more than 5,500 megawatts (MW) of generating capacity. We are one of Australia's largest renewable generators, the third largest generator by capacity and the fourth largest retailer in the NEM through our award-winning retail energy companies - Red Energy and Lumo Energy.

Snowy Hydro questions the need for a voluntary Short Term Forward Market (STFM). There are already effective OTC market which allows participants to contract with maximum flexibility at short notice. There is little evidence participants have not been able to obtain short-term hedges through OTC arrangements and the Australian Securities Exchange (ASX) has not been inundated for new exchanged traded products of shorter duration. Further to this, Snowy Hydro argue that:

- There is nothing preventing a counterparty contacting any major generator business and securing short dated contracts
- A facilitated solution crowds out innovation in this financial product space
- It is anticipated that short dated contracts are normally sought when there has been inadequate hedging and the Retailer/Counter-party is potentially exposed to large spot market losses. Hence the price or size of the bid/offer spread would be high to reflect the risk.
- Financial products should continue to be developed from market facing participants. The ASX and Financial and Energy Exchange (FEX) Group could provide the most efficient markets at the lowest cost if there was a demand for a STFM.

Current market conditions are sufficient

Benefits of a STFM are already addressed by the forward contract market that supports the NEM's real-time market. Market Participants can already hedge pricing risk using financial derivatives under the current frameworks. In addition, generators can structure their bids in the real-time market based on their costs, plant characteristics and contract position to ensure dispatch of their generation fleet to cover their contract positions.

The current market conditions provide some certainty over which plant will be running and for how long. If the expectation is that the proportion of fast-start plant in the NEM is going to increase to manage real-time volatility then market signals for slower-start generation may not likely be needed.

The NEM's real-time market also delivers benefits similar to those of a STFM. For instance, the information in pre-dispatch means any scheduling improvement through the implementation of a short term forward market may be limited.

Potential Benefits

The rule change proponent suggests the introduction of the voluntary STFM is expected to encourage intermittent generators to sell short-term products swap or option products, since they currently have limited options to manage their risk in the short term, allows gas powered generators to have greater short term price visibility and that the benefit of increased price certainty may facilitate more demand response in the wholesale market. Snowy Hydro believes across the three benefits mentioned a strong case has not been made to introduce the voluntary STFM. The ASX has not been requested to develop new exchanged traded products of shorter duration.

The NEM currently has an effective OTC market which allows participants to contract with maximum flexibility at short notice. There is no evidence participants have not been able to obtain short-term hedges through OTC arrangements. If generation and load become more responsive over time to the Spot market then it would become increasingly important that both non-schedule generation and load informs the market of their intent. Transparency is key to allowing providers of risk management products to make available contract volumes which are efficiently priced.

The industry has continued to work hard to improve transparency through the recent Australian Financial Markets Report (AFMR) which continues to be enhanced. The AFMR survey provides clear evidence that our markets are performing well and contributing solidly to the growth of the Australian economy which clears up misconceptions around the lack of transparency in the market.

Snowy Hydro notes that there are numerous rule changes which are expected to assist demand response without the need for a further rule change. The Commission firstly needs to properly undertake a comprehensive understanding of the interactions between the current rule changes before proposing changes to the market that could become costly on market participants. The uncertainty of cost recovery for demand response will be improved due to the five minute settlement rule change. Five minute settlement was partly implemented to allow for the price signals for demand response and align the timing of such response with the physical needs of the power system. In addition the Commission is reviewing the wholesale demand response market which is proposing to further assist demand response.

Consideration needs to be given by the Commission on the ability of demand response participants will have the ability to participate in a STFM so as to utilise the trading platform. Further to this, the focus on short term contracts is not clear when industry recently worked on the Retailer Reliability Guarantee (RRO) which is expected to encourage C&I customers to enter into long term contracts.

Costs

The Commission correctly notes in the consultation paper that *"there is a risk that if a STFM had low levels of utilisation, the costs of establishing the market would be incurred, but without the benefits being realised, which would not be in the long term interest of consumers."*¹ The ASX has listed monthly contracts which have been barely traded leading to a significant concern that there is also likely to be low levels of utilisation in the STFM. As an indicator of the lack of interest in the monthly contracts listed on ASX, currently there are five months listed (May19 - Sep19) for each node.

¹ AEMC, Short Term Forward Market, Consultation paper, 11 April 2019, pp24

However, there are only 10 lots of open interest across all of the contracts (5 lots in May19 NSW & 5 lots in Jun19 NSW)².

The screenshot shows the ASX website interface with a table of Open Interest and Face Value. The table is organized into sections: Open Interest, Quarterly Equivalent Open Interest, MWh, and Face Value. Each section has columns for State, B Month Futures, B Qtr Futures, F Qtr Futures, Caps, I Futures, AuR Options, Cal Options, Fin Options, Peak Option, and I Options. The 'B Month Futures' column is highlighted with a red box in the Open Interest and Quarterly Equivalent Open Interest sections.

State	B Month Futures	B Qtr Futures	F Qtr Futures	Caps	I Futures	AuR Options	Cal Options	Fin Options	Peak Option	I Options	Total
NSW	10	8,575	838	3,855	13,078	1,688	774	400	0	2,839	16,517
QLD	0	8,524	816	3,388	12,717	2,028	1,955	2,460	0	6,473	19,187
SA	0	1,722	3	790	2,915	0	0	0	0	0	2,915
VIC	0	9,185	454	2,057	11,686	2,841	1,859	1,332	0	6,032	17,748
Total	10	27,966	2,110	9,910	39,956	6,551	4,618	4,392	0	11,471	55,467

Further to this, the total volume traded on the exchange over the last year highlights that the volumes for monthly contracts are very low. The proponent has yet to prove that there is a demand for short term contracts.

In the rule change proposal, AEMO notes it could run an STFM using the Trayport platform. The proposal assumes that the market could follow a similar model to that used in the Gas Supply Hubs (GSH), using the same platform and processes for clearing, settlement and prudential arrangements all being operated by AEMO. Snowy Hydro questions the efficiency of AEMO running their own trading platform for short term contracts. As noted in the consultation paper, the costs associated with implementing the STFM through Trayport include:

- Trayport platform costs for AEMO and licensing for participants
- AEMO update of systems and processes, which could be dependent on the level of integration with existing systems
- legal/consultant fees to design products for the exchange
- STFM participation fees to cover the operating costs of the exchange
- any education and training of participants that is required³

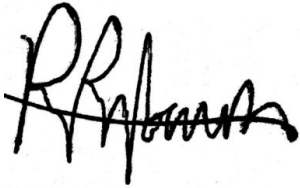
The majority of participants who the proponent notes as benefiting from a STFM which include smaller players are unlikely to be registered to Trayport. If there is a demand for short term contracts then the ASX has the systems and processes established to offer short term financial contracts. Additionally, Financial and Energy Exchange (FEX) Group has attained a licence from the Australian Securities and Investments Commission (ASIC) to start trading Australian financial derivatives. The ASX and FEX could provide the most efficient markets at the lowest cost.

² <https://www.asx.com.au/>

³ AEMC, Short Term Forward Market, Consultation paper, 11 April 2019, pp24

Snowy Hydro appreciates the opportunity to respond to the Consultation Paper and any questions about this submission should be addressed to me by e-mail to panos.priftakis@snowyhydro.com.au.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'P. Priftakis', with a horizontal line drawn through the middle of the signature.

Panos Priftakis
Regulation Manager
Snowy Hydro

