



POWER MARKETS HOPES & CONCERNS

OPCOM



**Emerging Europe
Energy Summit**

Austria, Vienna Marriott Hotel, 3-4 November 2005



Session B: Power

10 items, 10 minutes
Many challenges
How to deal with?

Let's keep from the agenda:
developing markets, energy trading, realistic (option for) vision about "after unbundling", security of supply without distortion of the (integrated) market, price reductions, power markets across the borders in the region

But also to discuss about us.

How to navigate in this power world?

Not worldwide.

Not "internal".

Still regional.

Who are we?

From where are we coming?

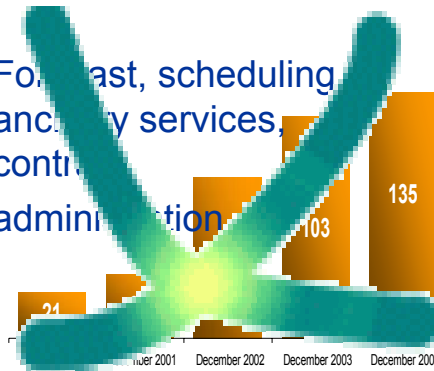




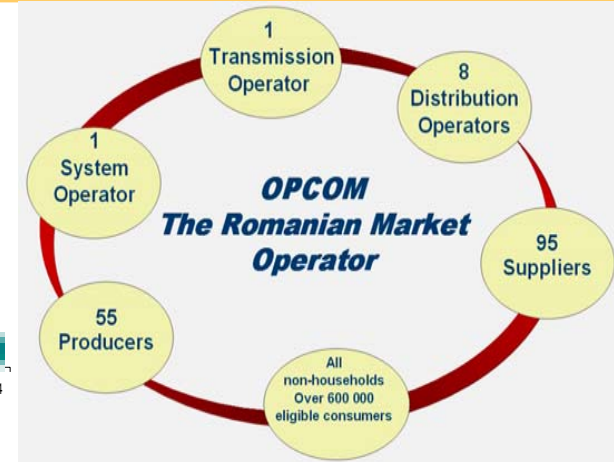
developing markets

This was OPCOM
till now:

Forecast, scheduling
and ancillary services,
contract administration



Participants number



Main Roles of a Power Exchange:

- To provide a reliable price for other physical and financial markets;
- To support the reliable generation schedule making.

For a marketplace to face the challenges of the liberalization process is a “never ending story”: Each stage is rising different problems.

The Marketplace has to prospect these challenges, correctly appraise the impact, cooperate with and ask for support of the regulator.



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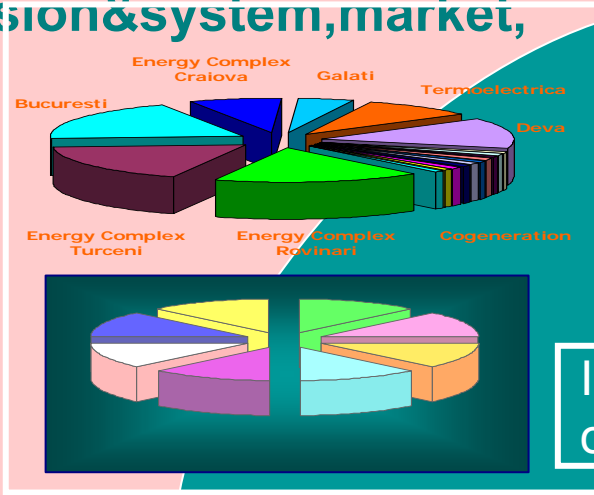
Stages of the liberalization process:

- Unbundling, big generation companies splitted or forced to divest; distribution splitting
- Privatization;
- Consolidation, vertical integration through mergers and acquisitions;



Unbundling: generation, transmission, distribution, retailers, operators: transmission&system,market,

Spot Market launch before privatization



Increasing opening degree

After 1990, the consumption declined in Romania: excess of capacity was encouraging the competition

Romanian Way

realistic vision about "after unbundling"

Impact on participants' number, liquidity, competition, price



security of supply without distortions

Normally, the market development needs:
market players, sufficient as number,
their daily reliability supporting the system,
their daily interest supporting market,
their financial health guaranteeing cash-
all above items supporting the functioning mechanism

How can the market players deal with different challenges:

- **lack of reliability, efficiency**
- **lack of creditworthiness**
as first stage threats;

- **incentives for investment possibly distorted**
as second stage threat and

- **the menace upon liquidity caused by**
vertical integration
as final threat.

The needed refurbishment is asking investment.
The renewable also is looking for investment.
Privatization, a solution to attract funds.
Privatization, also a driving force bringing health

The mechanisms providing incentives for investment are:
-guaranteeing priority in operation (long term contracts), having impact on competition,
or
-payments for reserve, having impact on final price

After acquisitions, the aim of owners is to consolidate the business, going to vertical integration (fuel, generation, distribution, supply).
Possible mergers or additional strategic acquisitions can withdraw volumes from wholesale market, decreasing liquidity.



Main Roles of Liquidity:

energy tra

To facilitate efficient decisions by market players

- adapt supply and demand to the changing circumstances
- the prices are reflecting supply and demand opportunities
- to decrease the market power, making the prices less volatile.

Liquidity Preconditions:

To have liquidity is supposing sufficient players needing trade

- natural partners: suppliers without their own adequate generating capacity and producers without their own end-user customers
- if a generator is merging another generator the number of players will decrease and the concentration will increase
- if a generator is merging a supply business the market liquidity can be damaged.



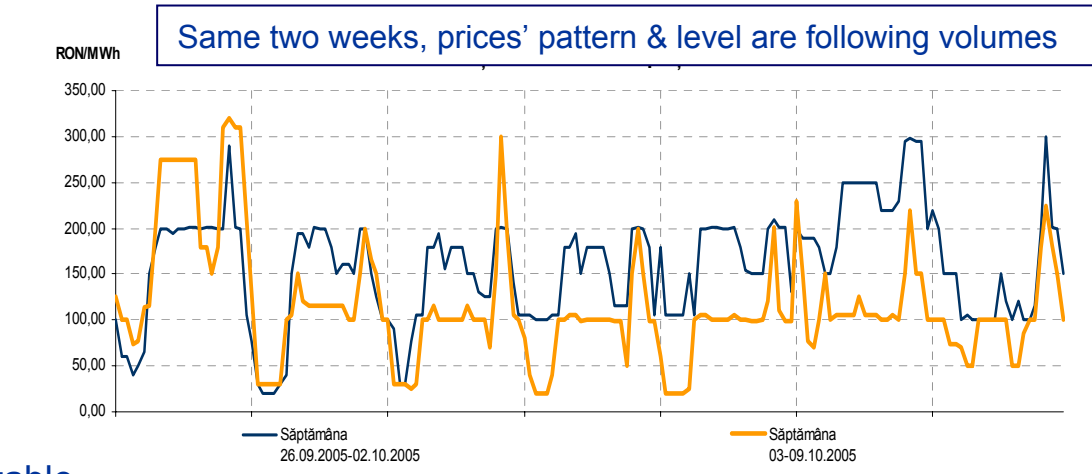
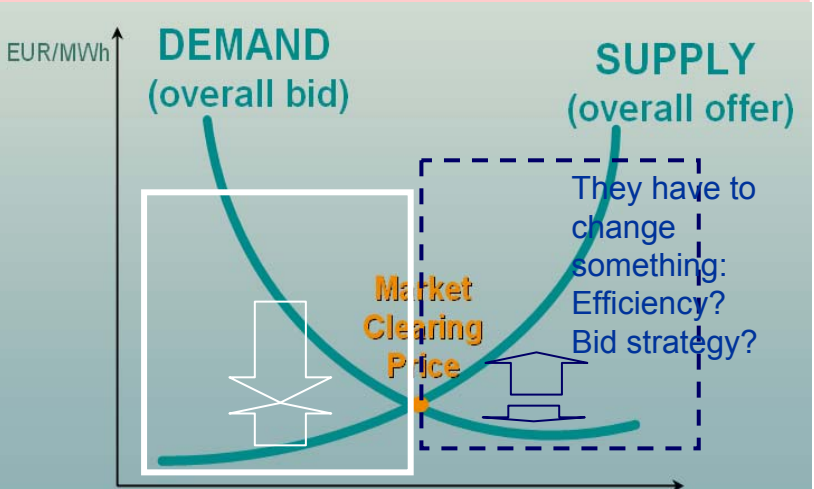
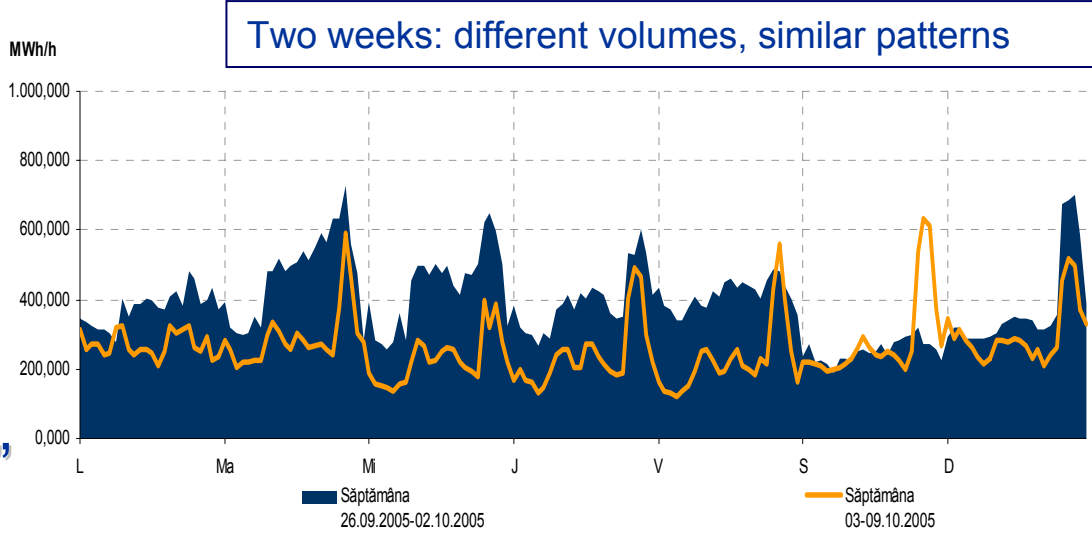
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Price reduction: an illusion

How much **real** before liberalization?
Price: is matching opposite interest
 is joining diversified opportunities,
 is reflecting variable costs

This means : "price discovery"



They are happy: market price better than acceptable



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Price

What are the preconditions?

- Lack of regulatory intervention:
 - no caps, no floors, no other mechanisms,
 - no competition with balancing market

Active market surveillance preventing gaming

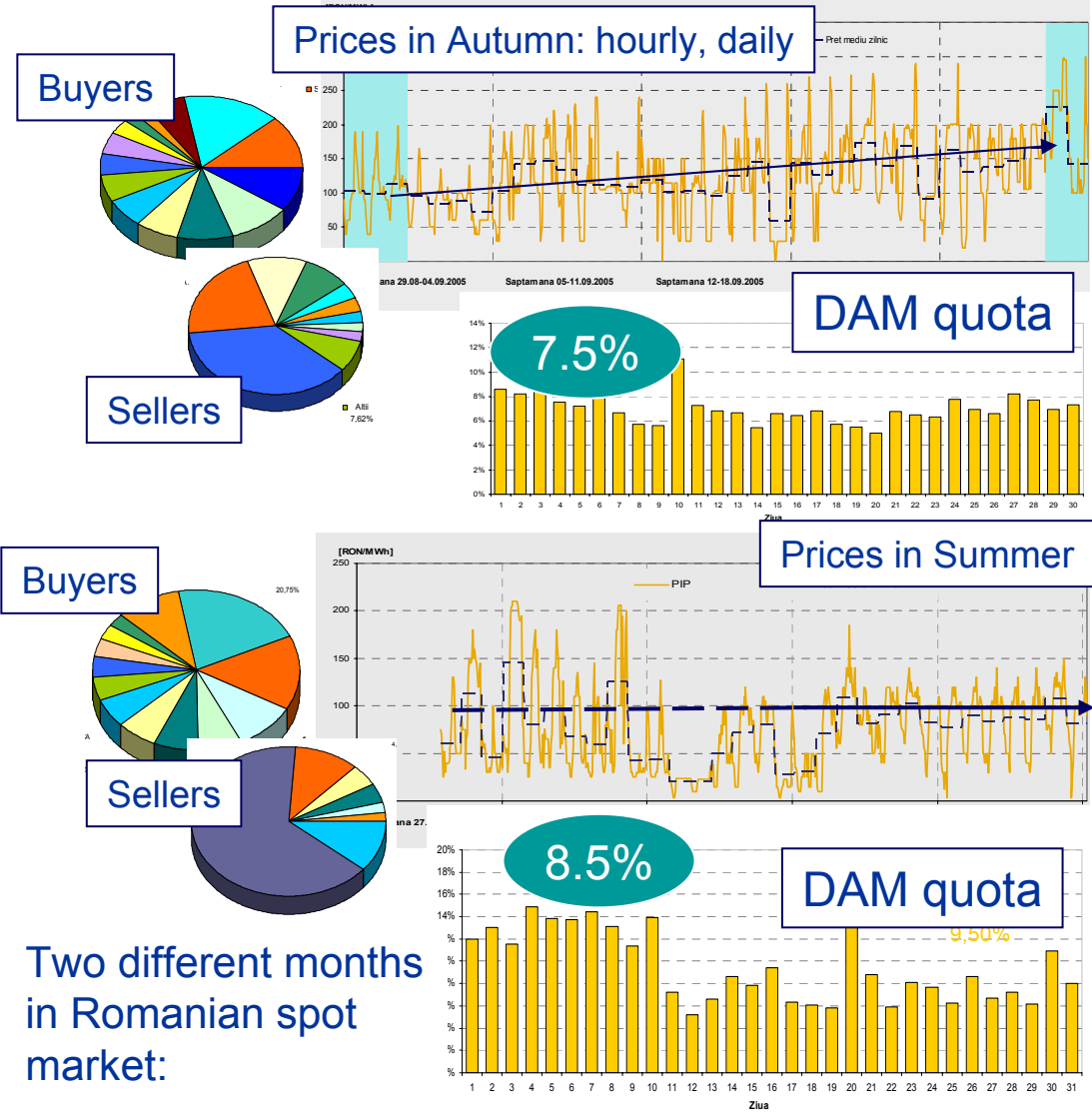
Transparency, avoiding insider trading, reducing potential collusion effects

What are the menaces?

To much volatility: not so good

-Gas and water based technologies are possible inputs for volatility: global or regional/seasonal acting

- How to manage these challenges?





REPORT FROM THE COMMISSION (5.1.2005)
Annual Report on the Implementation of the Gas and Electricity Internal Market

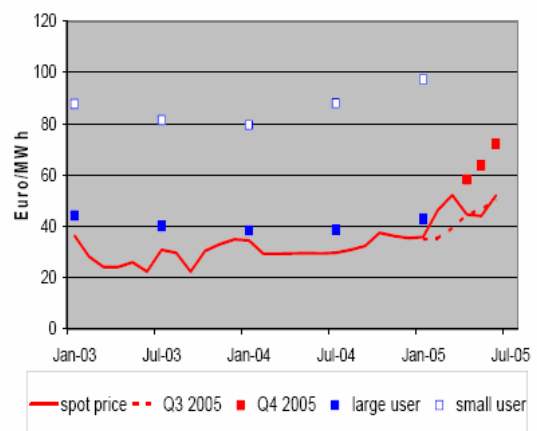
price reduc

“although electricity prices are lower than 1995 in real terms, they have increased in the last 18 month, partly due to increased prices for primary energy sources”

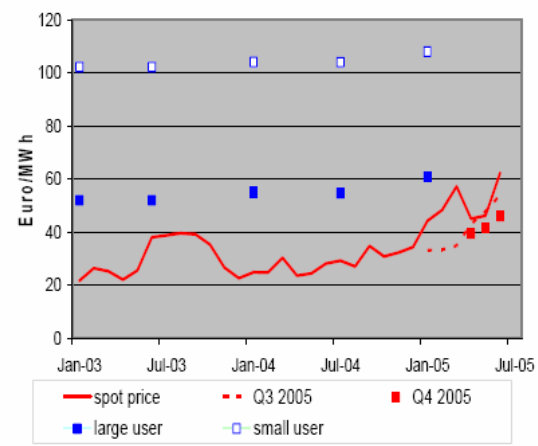
“2004 saw a convergence of wholesale prices at around the level of E30/MWh in both bilateral markets and standardized power exchanges”

What is happening now in Europe?

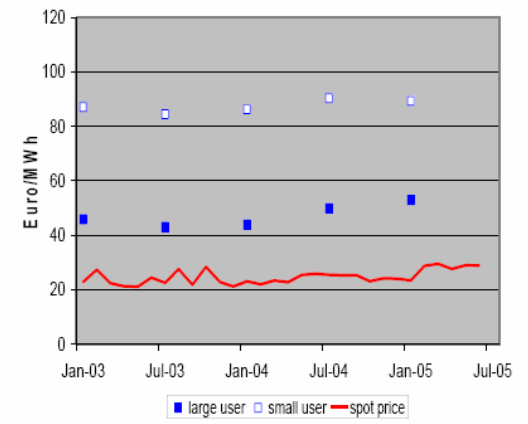
Graph 3 Summary of average wholesale and retail prices 2003-2005: UK



Graph 4 Summary of average wholesale and retail prices 2002-2005: Iberian region

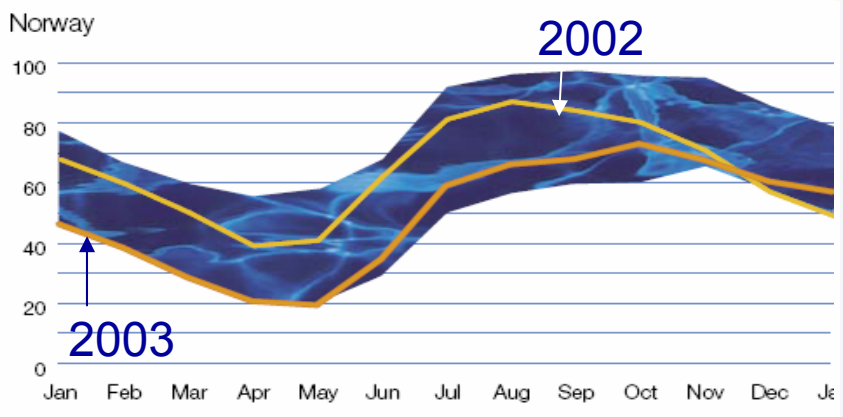


Graph 6 Summary of average wholesale (PolPX) and retail prices 2003-2005: Central (PL, CZ, SL, HU)

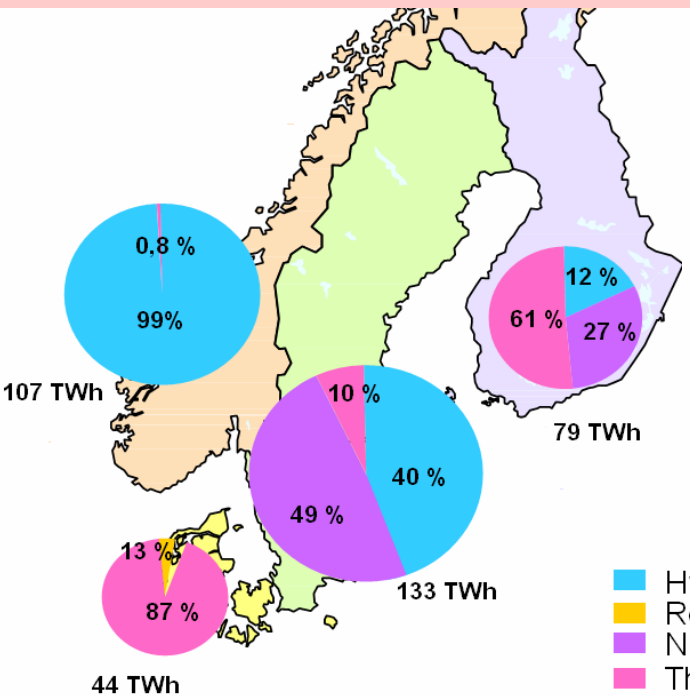




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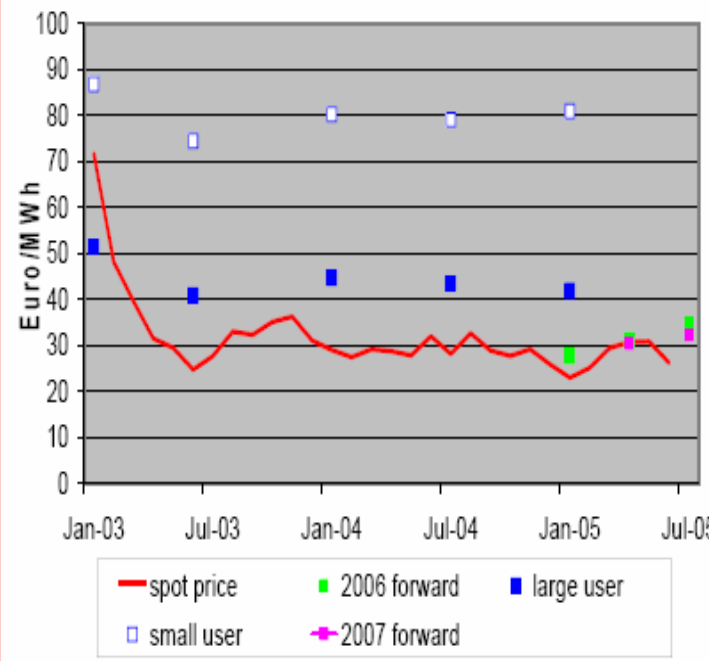
System price by day 1992-2003 (NOK/MWh)



Generation mix average last 5 years

- Hydro (55%)
- Nuclear (23%)
- Thermal (20%)
- Renewable (2%)

Hydro power
Renewables
Nuclear power
Thermal power



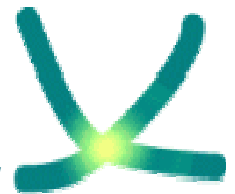
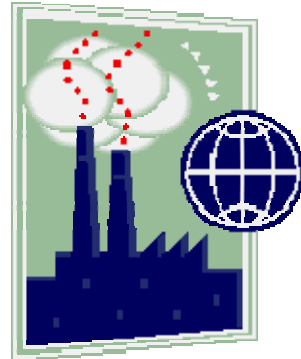


Regional issues:

power markets across

World Bank five key proposal:

- “ support a phased approach to market opening, starting with trading based on bilateral contracts and TPA, moving to a more sophisticated model only after the institutional framework is sufficiently developed;
- use regional benchmarking in its policy support work with individual countries and as a trigger for investment financing;
- use a special instrument for finance of investments for support development of the regional market;
- Support work to assess the economics of SEE gasification and costs of compliance with EU environmental standards;
- Complete a regional power GIS.”



*Spot market:
a piece in a puzzle*

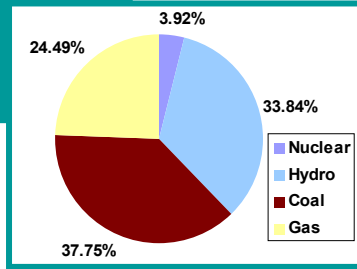
The bilateral contract market needs:

- Reliable interconnector capacity market-based allocated (long, medium term):
explicit auctions (SETSO TF dry run project)
- Transparent price signal and short term efficient allocation (spot markets providing implicit auctions: Borzen, OPCOM proposals).





The Romanian Power Market, since July 1th, 2005:
16.5 % Regulated
83.5 % Competitive



Who are we?

Current OPCOM voluntary markets:

zonal based spot trading system,
financial market system being implemented,
settlement services,
organization in place.

54 DAM participants, signatories of the Agreement, registered at OPCOM in October 20, 2005, with daily participation of almost 30 of them.

The DAM market first period (1 July – 21 October) results:
7.5% market share (av.405 MWh/h)
Average price: 30 Euro/MWh



- Supported by national stakeholders.
- Encouraged by existing and potential market participants.
- Sponsored by regional donors.
- Advised by experienced international consultants.
- Best suppliers IT trading platforms based.



Where are we intending to go?

Basis

- World Bank Athens process' approach: phased development
- Nord Pool historical evolution as extending trading area from pair of countries to all Scandinavian area
- ECSEE real framework: different stages of liberalization, PXs & TSOs ongoing projects as implicit and explicit capacity auction development
- Congestion management mechanisms as joint ETSO – EuroPEX development and documents issued by EuroPEX dedicated SEE
- European mini fora conclusions
- European PX's experience in making steps towards IEM
- Firm liquidity brought by large Romanian electricity market and important DAM share succeeded in present



Proposal

- Phased development from national PX to cluster (sub-regional), passing from neighboring countries approach stage. Market splitting in cluster as reliable congestion management method. Similar evolution of Borzen will support envisaged sub-regions market coupling.
- Borzen and OPCOM can equally but specifically focus on SEE market connection with the SEE neighboring countries' markets (Austria, Italy and Greece, Hungary, Moldova, Turkey or Ukraine).
- An open ownership structure intending to bring trust, neutrality and transparency;
- The incipient national market operators inside TSO's can play a further role within internal structure of a regional spot power exchange commonly owned, based on a decentralized organization;
- Regional stakeholders can participate in spot market design performance based on trading simulator;
- Started as bilateral market, the emerging SEE regional market will initially introduce the explicit auctions as bilateral trading support. The phased approach will enable a soft landing of implicit auctions, based on agreement with TSOs to share the cross-border capacity between explicit and implicit auctions increasing in time the implicit auctions dedicated one.



Conclusions

- - *There is enough room for two cooperating PXs in the region.*
- - *Successful, established spot marketplaces as Borzen and OPCOM: the most powerful driving force for markets development in SEE region, to provide transparently reference price for wholesale trade in the region.*
- - *Lack of evident benefits (discovery of trade opportunities and electricity prices) will not be replaced by political decisions.*
- - *Lack of political decision in ensuring the liberalization and market rules harmonization will jeopardize the process' pace.*
- - *Lack of cooperation and agreements of the power exchanges with the TSOs and between each country TSO and the Regulatory Authority will transform the projects into a "simple computer game".*

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