

European Gas Target Model

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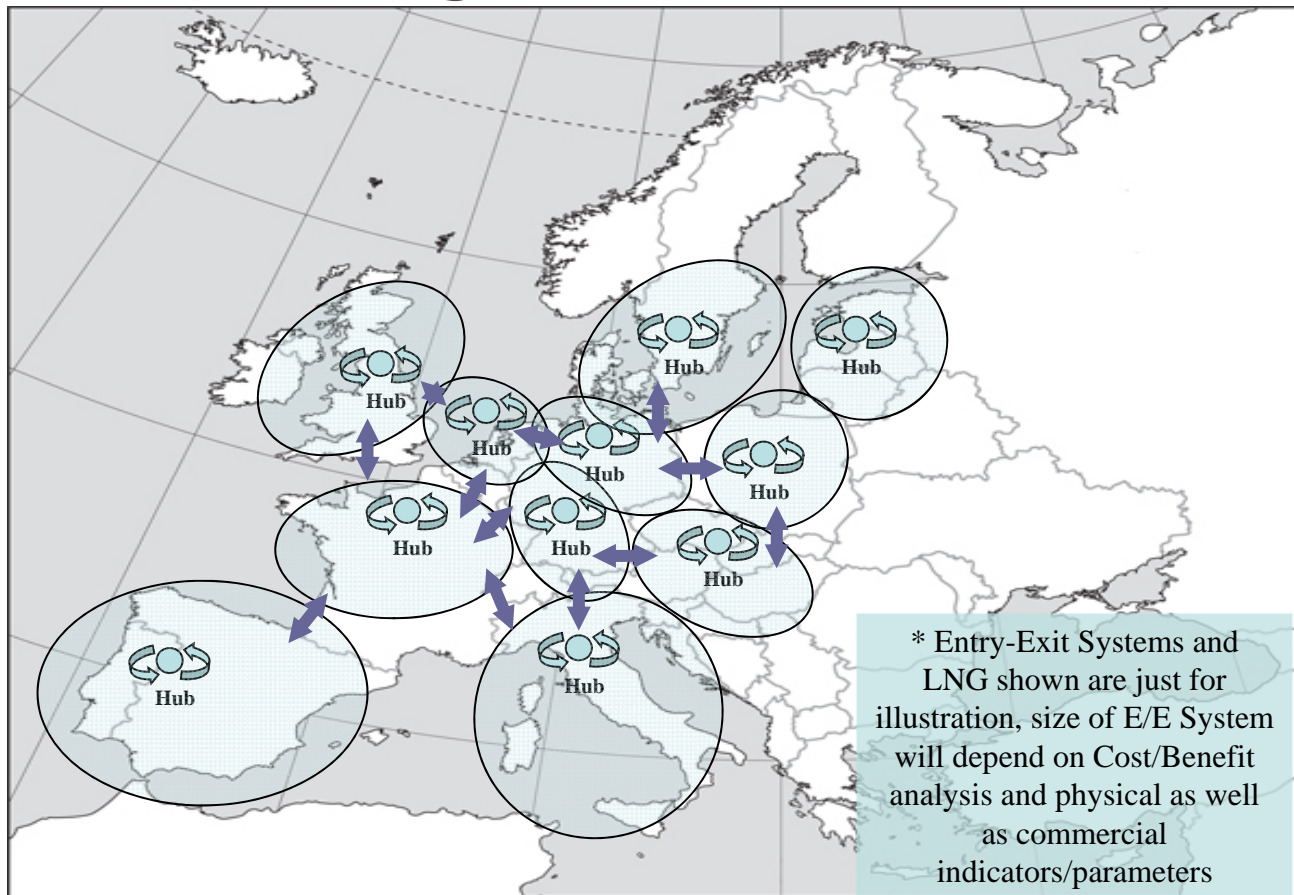
Agenda

- Drivers for a Gas Target Model
- Gas Target Model- the vision
- Network Codes- a step towards the target model?
- How efficient are GB interconnector flows?
- What is needed to promote cross-border investment?

Drivers for a gas target model

- Third package
 - Provides for legally-binding network codes to create single gas market
- Madrid Forum (Sept 2010)
 - Initiate the process to establish a gas target model to explore the interaction and interdependence of all Network codes
- European Commission (February 2011)
 - The EU needs an fully functioning, interconnected and integrated internal energy market.
 - The internal market should be completed by 2014 as to allow gas and electricity to flow freely

Gas Target Model- the vision



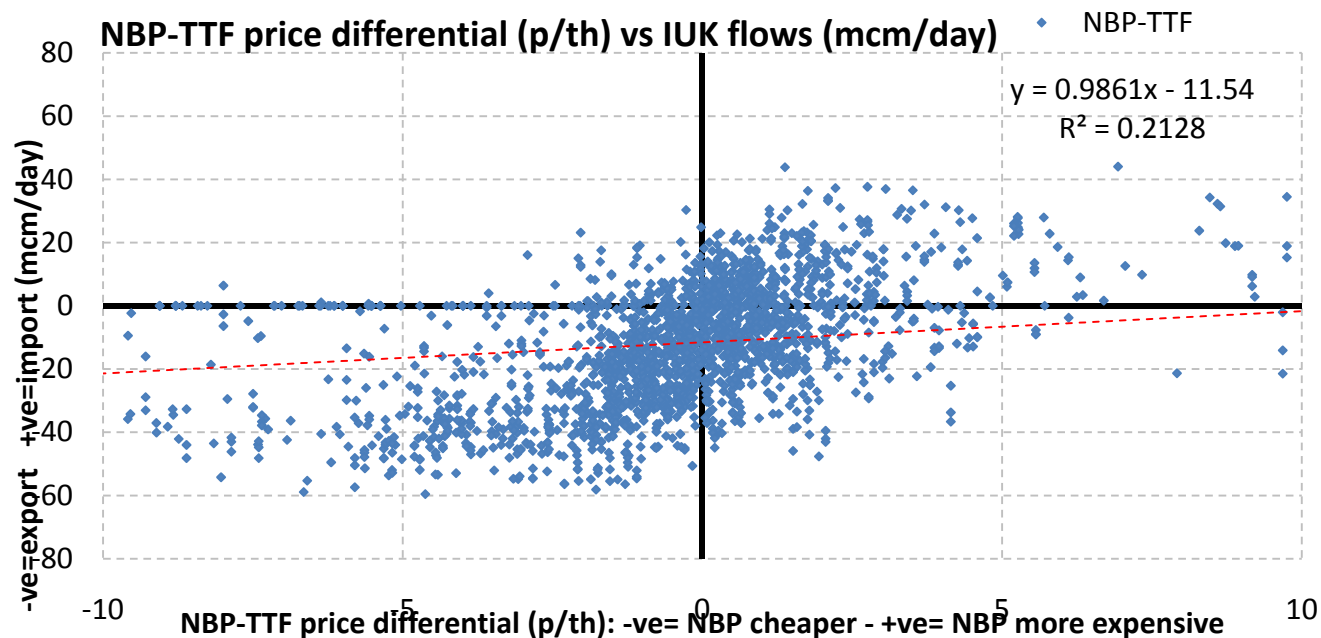
Liquid hubs with sufficient and efficiently used infrastructure

Network codes- a step towards the target model?

Framework Guidelines	Problem	Proposed solution
Balancing FG	Non-market based balancing regimes are bad for liquidity	<ul style="list-style-type: none"> • Market-based TSO procurement- • Daily balancing- intra-day constraints possible,
Capacity Allocation Mechanisms FG	Lack of harmonisation and lack of cross-border cooperation may create barriers to trade	<ul style="list-style-type: none"> • Bundled product • Explicit auctions as standard allocation method • Reserve price outstanding- Tariff Network Code
Congestion Management Provisions (CMP)	Capacity hoarding	<ul style="list-style-type: none"> • Creation of firm day-ahead capacity market by restricting re-nominations rights • Overbooking and buy back incentive scheme approved by NRA

Focus on efficient use of existing capacity but is this enough ?

How efficient are GB interconnector flows?

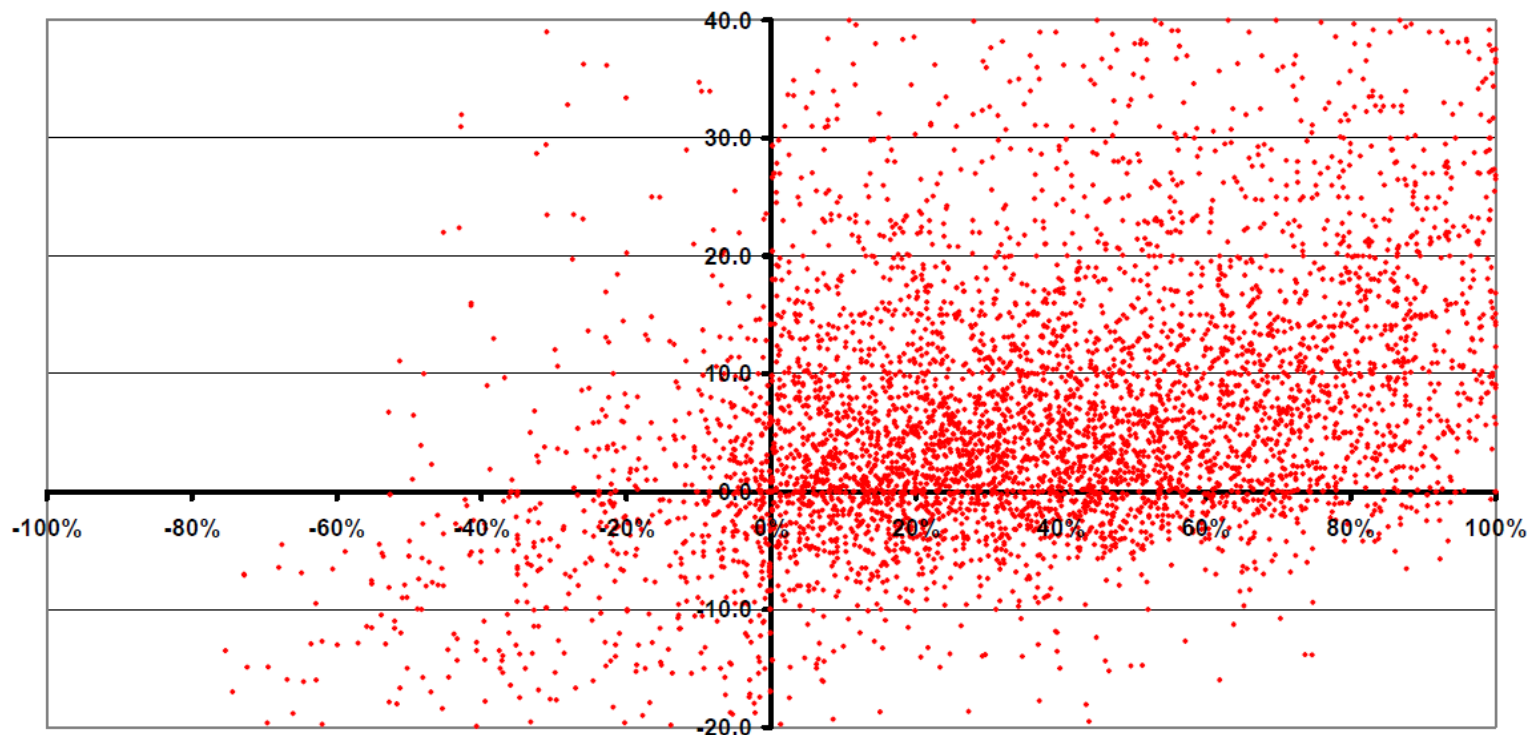


	NBP-ZEE	NBP-TTF
Correlation		
IUK Imports mcm/d	0.33	0.57
IUK Exports mcm/d	0.13	0.29

IUK flows not always in the direction of price differences ?

Explicit auctions..

Use of F - NL "Capacity" (% of av capacity) versus Price difference (€)
Before MC



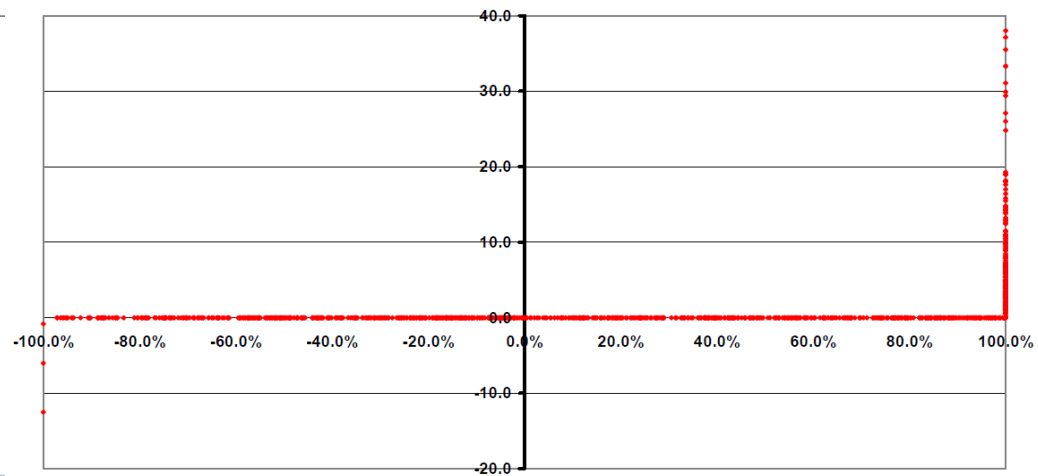
...deemed inefficient for cross-border electricity flows

Impact of Market Coupling at NL, Bel, Fr borders

Use of F - B capacity (% of av capacity) versus Price difference (€) during MC



Use of B - NL capacity (% of av capacity) versus Price difference (€) during MC



More investment in gas infrastructure?

Security of
supply
considerations

New demand patterns
(e.g. to accommodate
electricity generation)

Unconventional
sources of gas

Increasing
import
dependency

ENTSOG's 10 Year Network Development Plan:

- "Difficult to draw clear conclusions"
- "Many investments are still needed to address security, sustainability and competition in a satisfactory manner"

(February 2011)

Options for a cross-border investment regime

Option 1: Merchant approach

- Exempt (“unregulated”) investments

Option 2: Regulated model

- TSO makes business case, NRA adjusts revenue allowance

Option 3: Tendering model

- NRA to identify investment and to trigger competitive tender

Option 4: Market-led model

- Market to signal demand for capacity in Open Season

NRAs to investigate a market-led approach

- Regular auctions at each IP (consistent with CAM FG), based on:
 - Information on available capacity
 - Information on reserve price
 - Incremental price steps for additional capacity
 - Estimated project cost for additional capacity
- Each network user to signal how much capacity at what price
 - **Protects consumers** from asset stranding
 - **Avoids underinvestment** as network users signal value
- Enables **SoS considerations** to feed into decision making (when setting economic test)
- Proposed by some **network users**
- Does not require harmonisation of price controls

Successful at GB entry points but untested cross-border

Key issues

- **Coordination between NRAs:**
 - What level of user commitment is required to trigger investment? (risk of asset stranding versus risk of underinvestment)
 - How to take into account externalities, such as Security of Supply benefits?
 - How to allocate the cost between markets (where some socialisation occurs)?
 - Overlap with Open Seasons and CAM process?
- **Coordination between auctions:**
 - Coordinate timing across Europe
 - Several rounds of auctions (for additional capacity) to allow network users to correct their positions depending on auction outcome
- **Frequency:**
 - quarterly, annual, or bi-annual?

Conclusions

- Gas Target Model will call for liquid functioning gas hubs linked by:
 - Sufficient interconnector- climate that promotes investment
 - Efficient use of gas infrastructure
- How does GB fair against such a vision?
 - NBP the most liquid hub in Europe
 - Efficiency of interconnector flows?
 - Investment climate for cross-border infrastructure, LNG, storage?
 - Other barriers- gas quality?

What does this means for GB market?

The background of the slide is a composite image. On the left, there are rows of solar panels under a bright sun. On the right, a hand is shown holding a white document. In the foreground, there is a close-up of a blue gas flame from a burner. The overall theme is energy and customer service.

ofgem

Promoting choice and value
for all gas and electricity customers