MARKET BRIEF

30 August 2011

ELECTRICITY AUTHORITY
TE MANA HIKO

Contents

Request for Proposals: FTR manager

The Authority will release a request for proposals (RFP) for the role of FTR manager this week. Suitably qualified parties are encouraged to tender for this role, which is to establish and operate an FTR (financial transmission right) market in New Zealand. Proposals from single parties and consortia will be welcome.

The skills required for the role include:

- knowledge of and experience in running financial markets;
- ability to work with parties in the industry and the Authority to further develop FTRs; and
- ability to develop and operate a mathematical model of the electricity grid.

The RFP will be posted on the Government Electronic Tenders Service (GETS) website, www.gets.govt.nz.

Security and Reliability Council

Meeting papers for the meeting of the Security and Reliability Council (SRC) held on 18 August are available at:

- http://www.ea.govt.nz/our-work/advisory-working-groups/src/18Aug11/

Transmission Pricing Advisory Group: 22 August 2011

Meeting papers for the 22 August meeting of the Transmission Pricing Advisory Group (TPAG) are available at:

- http://www.ea.govt.nz/our-work/advisory-working-groups/tpag/22Aug11/

Updated consultation calendar

The Authority has published an updated consultation calendar for major projects currently underway. The purpose of the calendar is to provide notice of likely upcoming consultations in order to assist interested parties to better allocate resources if they wish to make submissions.

All dates in the calendar are indicative but the Authority will be endeavouring to meet the indicated timetables. The calendar is available at:

- http://www.ea.govt.nz/about-us/documents-publications/work-programme/

Dispatchable demand: Submissions published

Submissions on the Dispatchable demand consultation paper have been published and are available at:

- http://www.ea.govt.nz/our-work/consultations/priority-projects/dispatchable-demand/submissions/

Scarcity pricing proposed Code amendments: Submissions published

Consultation on the proposed Code amendments for the scarcity pricing arrangements closed last Friday and the submissions received have been published and are available at:

- http://www.ea.govt.nz/our-work/consultations/priority-projects/scarcity-pricing-proposed-code-amendments/submissions/

More Standardisation of distribution arrangements: Further papers published

Two papers associated with more standardisation of distribution arrangements have been published.

Appendix B of the Summary of Submissions paper is available at:

- http://www.ea.govt.nz/our-work/consultations/priority-projects/more-standardisation-proposed-code-amendments/submissions/

A companion paper to the consultation paper is available at:

- http://www.ea.govt.nz/our-work/consultations/priority-projects/standardisation-muosa-and-proposed-code/

Note that this companion paper is not part of the formal consultation on more standardisation.

Current consultations

- Standardisation: Model use-of-system agreements and proposed Code amendments
  The deadline for the MUoSA components of this consultation has been extended by four weeks to 5pm on 6 October 2011, however, responses to questions 5 to 23 are still required by 5pm on 8 September 2011.
  The paper is available at:
  http://www.ea.govt.nz/our-work/consultations/priority-projects/standardisation-muosa-and-proposed-code/

Hedge disclosure

The 16th August 2011 Information on the Market provided contour plots of hedge market activity, in particular contract duration and price. Hedge markets provide a rich source of information about market expectations of future prices, both in the contract and wholesale market.

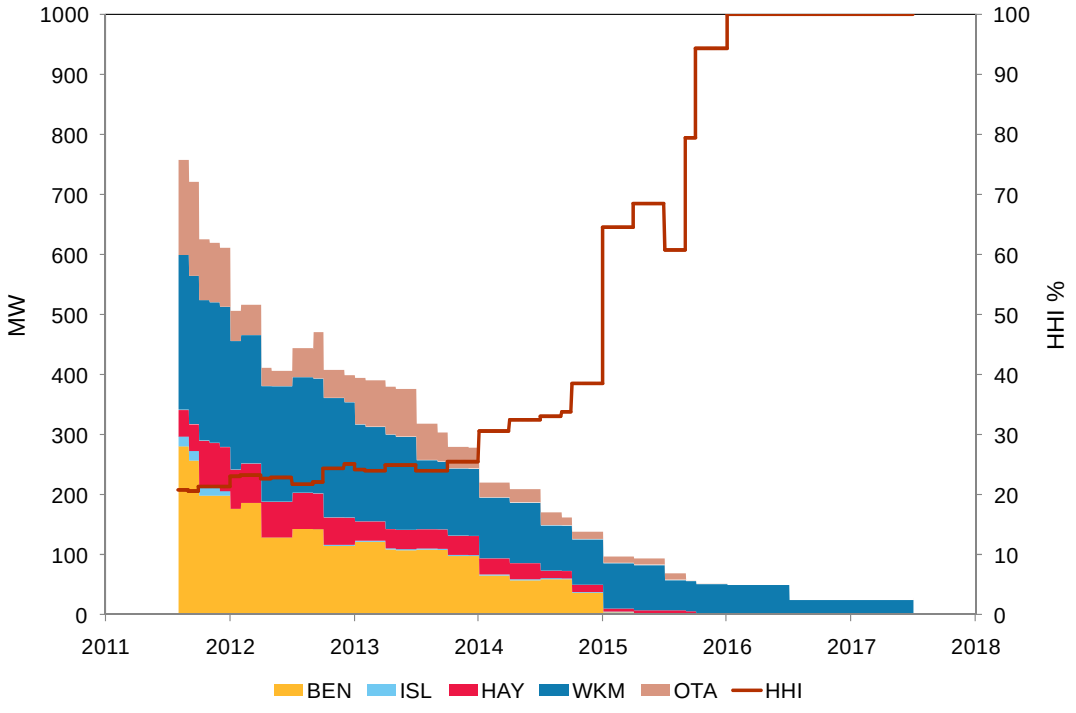
This view of future prices should be tempered by the volume and concentration of the market for contracts. If the volume is low, or only one or two companies are involved, the spread and mean of contract prices for a future interval may shift to a different value as time goes by. This is because the volume traded and number of companies involved will increase, and with greater liquidity and visibility, prices will represent the risk/price tradeoff of the market as a whole, instead of only a few participants.

The hedge disclosure website does not reveal the identity of parties to contracts, and so participants can only be guided by the volume of contracts. Nevertheless, the Authority is able to make available measures of concentration that protect the confidentiality of participants.

A common measure of concentration is the Herfindahl–Hirschman Index (HHI). This is a single number that combines together the market shares of all participants. It is calculated as the sum of the squares of the market share of all participants. The market share is expressed as a fraction, and the HHI as a percentage. For example, a market with two equal suppliers would have a supplier HHI of 50%, and a market with three suppliers of 0.5, 0.25 and 0.25, would have a supplier HHI of 37.5%.

An HHI of greater than 20%-30% is considered to be quite concentrated, such that there may be competition issues. However the relationship between HHI and the level of competition is probably best considered an intuitive relationship, and not predictive.

Figure 1: Mean quantity of hedge contracts across various locations as a measure of market concentration



In the above figure, we see the volume and HHI of suppliers in the New Zealand contracts markets, as recorded in the hedge disclosures database. This is for the supply side of all Contract for Differences contracts, on all three platforms - over the counter, ASX, and Energy Hedge. Volume data has been broken down by location and colour coded from South to North as the graph is ascended (Benmore - orange, Islington - light blue, Haywards - red, Whakamaru - blue, Otahuhu - brown). In this graph the HHI is measured over the supply side of confirmed contracts, totalled over all locations.

Volume drops rapidly, from a near term peak at nearly 800MW, with most volume at Benmore and Whakamaru. As short term contracts expire, the volume decreases rapidly and concentration increases quickly. Beyond an HHI of say 40%, contract prices may not be a reliable indicator of wholesale price. This point occurs in early 2015, after which there is a dominant party with greater than 50% market share.

Subscription

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