Mercury

Via email: WholesaleConsultation@ea.govt.nz

28 March 2022

Hedge Market Enhancements: Commercial market-making scheme

Mercury welcomes the opportunity to provide feedback on the Electricity Authority's (Authority's) consultation paper *Hedge Market Enhancements: Commercial market-making scheme*, 15 February 2022 (Consultation Paper).

The Authority is seeking stakeholder views on amending the current market-making service levels in the Code to align the requirements of the current four regulated market makers with a new commercial market marker. The proposed Code amendments include allocating the total market-making volume of 12MW equally over the five market makers; changing to a rolling twenty trading days exemption scheme; and introducing a refresh obligation. The Consultation Report also notes that the Authority is not proposing to change the current total market-making volume of 12MW per contract, nor the spread between bid and offer prices.[1]

Mercury supports these proposed amendments in general. Our comments are limited to a proposal that the refresh obligation is more targeted with the aim of enhancing efficiency. We also request that the Authority clarify the consistency between the proposed change to a rolling twenty trading days exemption scheme and the drafting of subclauses 13.236N(1)(b) and 13.236N(2) of the proposed Code amendment in Appendix C of the Consultation Paper. Furthermore, we request that the Authority clarify its proposed process for engaging with the ASX and regulated market makers when making any relevant changes to the agreements between the ASX and market makers.

Mercury expands on this proposal and these requests along with providing additional comments on the Consultation Paper in our response to the Authority's consultation questions in the Attachment.

Mercury looks forward to engaging constructively with Authority and industry stakeholders on the implementation of these code amendments and the introduction of the commercial market maker.

Yours sincerely

Tim Thompson
Head of Wholesale Markets

[1] Consultation Paper, page ii.

The Mercury Building, 33 Broadway, Newmarket 1023
PO Box 90399, Auckland 1142 New Zealand
PHONE: + 64 9 308 8200
FAX: + 64 9 308 8209
mercury.co.nz

Attachment: Mercury response to consultation questions

Consultation Questions	Mercury Response
Q1. Do you have any feedback on the Authority's proposal to align regulated market-making obligations with commercial market-making obligations?	Mercury agrees with the Authority that the regulated market-making obligations and commercial market-making obligations should be aligned with each other, and for completeness with the mandatory backstop arrangements in the Code. Inconsistent obligations would lessen economic efficiency because the resulting different risk profiles faced by market makers would reduce the level of competition in the hedge market among market makers.
Q2. Do you agree that the total volume should remain at 12 MW per contract, if not why?	Mercury considers that the current total volume of 12 MW per contract is adequate and should remain.
Q3. Do you agree that the spread between bid and offer prices should remain at a maximum of 3% if not why?	Mercury considers that the current spread between bid and offer prices should remain at a maximum of 3%. We note that the Authority may revisit bid-offer spread following receipt of cost information from RFP respondents regarding cost/service level trade-offs. Should the Authority choose to revisit the bid-offer spread, we request the Authority to consult with the regulated market makers.
Q4. Do you agree that changing to a rolling 20 trading days exemption scheme will benefit the New Zealand electricity futures market if not why?	Mercury supports changing the exemption scheme so that each market maker has five discretionary exemptions from providing services over a rolling twenty trading days. We expect this change would reduce the hedge market volatility and market-maker financial risk compared with the current scheme, as a result providing a more robust forward price curve. The Authority also notes " … *the proposed Code amendment does not explicitly reference the exemption regime"* as it is currently covered by the agreement between the regulated market makers and the ASX.[2] Accordingly, following the consultation, should the Authority confirm its position on introducing the change, it indicates that it would work with the ASX to have the change reflected in the agreements between the ASX and each regulated market maker. We request, therefore, that the Authority clarify its proposed process for engaging with the ASX and the regulated market makers on making any relevant changes to the agreements between the ASX and the market makers. Furthermore, as expanded in our response to question 9 below, Mercury seeks a clarification of the consistency between the proposed change to a rolling 20 trading days exemption scheme and drafting of subclause 13.236N(1)(b) and 13.236N(2).
Q5. Do you propose an alternative solution to maintaining market-making services through a calendar month?	Mercury does not propose an alternative solution to maintaining market-making services through the month.
Q6. Do you agree that introducing a refresh obligation will benefit the New Zealand electricity futures market if not why?	Mercury supports the introduction of a refresh obligation, but we consider that more targeted refresh obligation would enhance efficiency compared with the one proposed by the Authority. That is, Mercury considers that the refresh obligation should only be required for the front 4 quarterly contracts and the 6 monthly contracts - i.e. 12 lots to open and the refresh. The refresh obligation should not be required for the remaining contracts. Focusing the refresh in this way would enhance the efficiency trade-off between the cost of introducing the obligation and the benefits from improving

[2] Ibid. para. 4.9

The Mercury Building, 33 Broadway, Newmarket 1023
PO Box 90399, Auckland 1142 New Zealand
PHONE: + 64 9 308 8200
FAX: + 64 9 308 8209
mercury.co.nz

	liquidity. We expect the introduction of the proposed obligation would help spread trades over the duration of the session as well as reduce the potential to inadvertent trading at market opening. As a result, we anticipate that it would increase market liquidity,enhance confidence in the forward price curve and reduce market-maker financial risk.
Q7. Do you have any feedback on the Authority's cost-benefit analysis set out in Appendix A?	Mercury does not have any comments regarding the cost-benefit analysis set out in Appendix A.
Q8. Do you have any feedback on the Regulatory statement in Appendix B?	Mercury does not have any comments regarding the Regulatory Statement in Appendix B.
Q9. Do you have any feedback on the Code amendment set out in Appendix C?	Mercury seeks a clarification of the consistency between the proposed change to a rolling twenty trading days exemption scheme and drafting of subclause 13.236N(1)(b) and 13.236N(2). As noted above, Mercury supports the Authority's proposal to change exemption scheme so that each market maker has five discretionary exemptions from providing services over a rolling 20 trading days rather than 2 exemptions per month. However, subclause 13.236N(1)(b) and 13.236N(2) of the proposed Code amendment states (underline added for emphasis): *(1) (b) in addition to the exemptions in paragraph (a), for up to two NZEF market-making periods <u>each month</u> at the participant's discretion*. *(2) To avoid doubt, if the participant meets the criteria for exemption in subclause (1)(a)(i) or (1)(a)(ii) in relation to a NZEF market-making period, that NZEF market-making period will not count towards the participant's two exemptions in subclause (1)(b).* Mercury requests the Authority to clarify whether the drafting of the cited subclauses should be consistent with the rolling 20 trading day proposal.