



Update on the BZ review and liquidity

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Bidding Zone Size vs Liquidity

- In general, the smaller the bidding zone, the lower the liquidity
- But there is no one-size-fits-all formula to quantify the effect of the bidding zone size on liquidity.
- If need be, we recommend to consider :
 - products at bidding zone level only (no proxy hedging, which does not cover the basis risk linked to the mismatch between the local price to be hedged and the hedging instrument)
 - continuous markets, e.g. different products on the forward market.DA auctions provide plenty of data, but have little meaning in terms of liquidity around the DA price, which is not known beforehand

If there exists no forward market at BZ level, then this means 0 liquidity and major challenges for the operators of generation, storage, or demand assets located in the BZ to hedge their positions.

- Liquidity can be related to the bid ask spread for a standard market depth (e.g. 200 MW)

Liquidity vs efficiency of the electricity system

Liquidity refers to the sufficiency of hedging opportunities for asset operators

- The lower the liquidity the higher the cost for a market participant to secure a market price for a given volume of energy during a specific period and in a specific bidding zone
- Low liquidity means a more risky framework for investors in price-exposed electricity generation, storage or demand assets. This can skew investment incentives and ultimately result in a sub-optimal, more expensive energy mix, with a detrimental effect on welfare.
- There is no obvious way to monetize the liquidity criteria
- This might remain a qualitative criterion of the BZ review (yet important)



Liquidity is a relevant indicator (but other ones should also be developed)

Other criteria should also be duly considered in the Bidding Zone Review

In addition to the criteria listed in CACM (incl. competition issues, short-term efficiency, investment signals,...) the BZR should carefully consider e.g. :

- Efficiency of the retail market: challenge for retailers to develop competitive commercial offers for small areas e.g. due to the volatility of balancing prices and the associated need for high mark-ups to cover volume risk.
- Citizen/political willingness to face the same conditions over a given territory
- Capability of the Single Day-Ahead Coupling and Single Intraday Coupling (auctions) mechanisms to address more interdependent variables/constraints

Some easily-monetizable criteria should also be added:

- Revenue redistribution and the associated stranded costs among : TSOs (individual congestion rents - RD&CT costs), consumers, generation and storage asset owners, levies' payers in each bidding zone
- There is no obvious way to weight the different criteria (monetized or not)

