

Statkraft on: Proposal for Amendment of Pricing Methodology

First amendment of Methodology for pricing balancing energy and cross-zonal capacity used for the exchange of balancing energy or operating the imbalance netting process - 02 June 2021

Statkraft welcomes the harmonization of the balancing energy markets at European level. The envisaged price cap based on the so-called Value-of-Lost-Load (VoLL) is assessed positively. Statkraft has repeatedly called for this in recent years.

In principle, a price cap is a "second-best" solution.

However, the balancing market in Germany without a price cap has shown what can happen: the occurrence of extremely high balancing energy prices. With the introduction of MARI and PICASSO without a price cap, similarly high prices can appear again.

In order to avoid situations with extreme prices, it would be desirable that sufficient competition would prevail on the balancing energy market and that extreme prices could only arise in real scarcity situations. However, competition in the balancing energy market is apparently not sufficient at the moment, as extreme prices have also occurred in situations that were not characterized by real scarcity.

The balancing energy market has high barriers to entry, which discourages many potential balancing energy providers:

- Investment and maintenance of systems
- Uncertain revenues, not at least due to frequent regulatory changes (also at European level)
- High requirements in terms of availability and redundancy

For direct marketers (but in principle for all balancing group managers), balancing energy prices must also be manageable in the long term, because prices that are too extreme make balancing group management a matter of luck: An actually "good" direct marketer (with low average forecast errors) can get into financial difficulties due to individual quarter hours with extreme balancing energy prices. Extreme price risks for balancing group managers lead to additional risk premiums, which ultimately make the integration of renewable energies unnecessarily expensive.

The balancing energy market is also not a "normal" market, as demand is fixed in the short term. The TSOs are forced to purchase balancing energy and cannot react to extreme prices by reducing demand.

In principle, according to Article 30 EBGL, balancing energy prices should correspond to the real-time value of the energy. In an extreme shortage situation, which is also characterized by a lack of offer, competitive pricing can only take place to a limited extent, if at all. In this respect, a price cap in the VoLL area is appropriate for this reason as well.

Therefore, we consider a start with a price cap to be justified.

However, a maximum price around 5,000€/MWh higher than in the intraday market does not seem reasonable. Providers of balancing energy must have the opportunity to offer their capacity at the same price on the intraday market beforehand and, if necessary, to achieve reliable marketing there. Otherwise, they may withhold power in the intraday market in the hope of obtaining higher prices in the balancing energy market. Different maximum prices can thus lead to incorrect pricing in both markets.

Both the existing technical cap for the intraday market at the level of €9,999/MWh and the cap at the level of €99,999 for the energy price offer of the balancing reserve provider are arbitrary, as they are not oriented to the VoLL.

In any case, there is no real "technical cap", as any auction mechanism could technically deal with other limits as well. If, for whatever reason, the intra-day trading platforms were to increase their price cap substantially and change it, for example, to €99,999/MWh, then in the logic consulted, the price cap on the balancing energy market would have to be increased to over €100,000/MWh.

Based on the experience with the German balancing power market, it can then be expected that suppliers would test this price limit. On the intraday market, five-digit bids would immediately be squeezed out by lower bids. But on the balancing market, there is an incentive to speculate on a briefly reduced offer in order to be subsequently executed - albeit with a very low probability - at an extremely high price.

The introduction of "marginal pricing" in the determination of balancing energy prices may further increase the incentive for such behaviour. In any case, it would lead to incalculable risks for balancing group managers and to distorting windfall profits on the side of the balancing energy providers.

- ➔ Therefore, we propose to set the price cap for balancing energy at the value of €9,999/MWh, which seems appropriate as an estimate for the VoLL. This would also ensure that the same price ceilings exist in the intraday market and the balancing market.
- ➔ In addition, we propose regular monitoring to make appropriate adjustments. If there is sufficient offer and at the same time indications that the VoLL should be significantly higher, the price cap can be adjusted step by step.

Statkraft is a leading company in hydropower internationally and Europe's largest generator of renewable energy. The Group produces hydropower, wind power, solar power, gas-fired power and supplies district heating. Statkraft is a global company in energy market operations. Statkraft has 4,500 employees in 17 countries.

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