Virtual Trading Hubs not needed – we already have spreads

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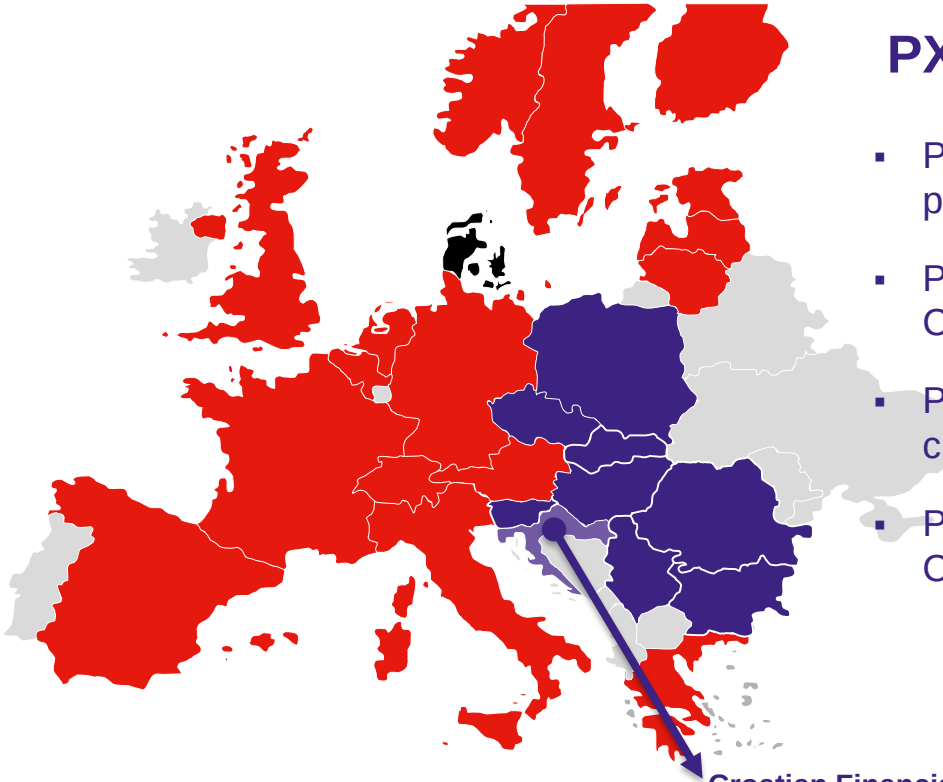
Vision

Develop pan-European energy trading platform

- One membership
- Easy access
- Attract new players
- Develop new areas
- New products

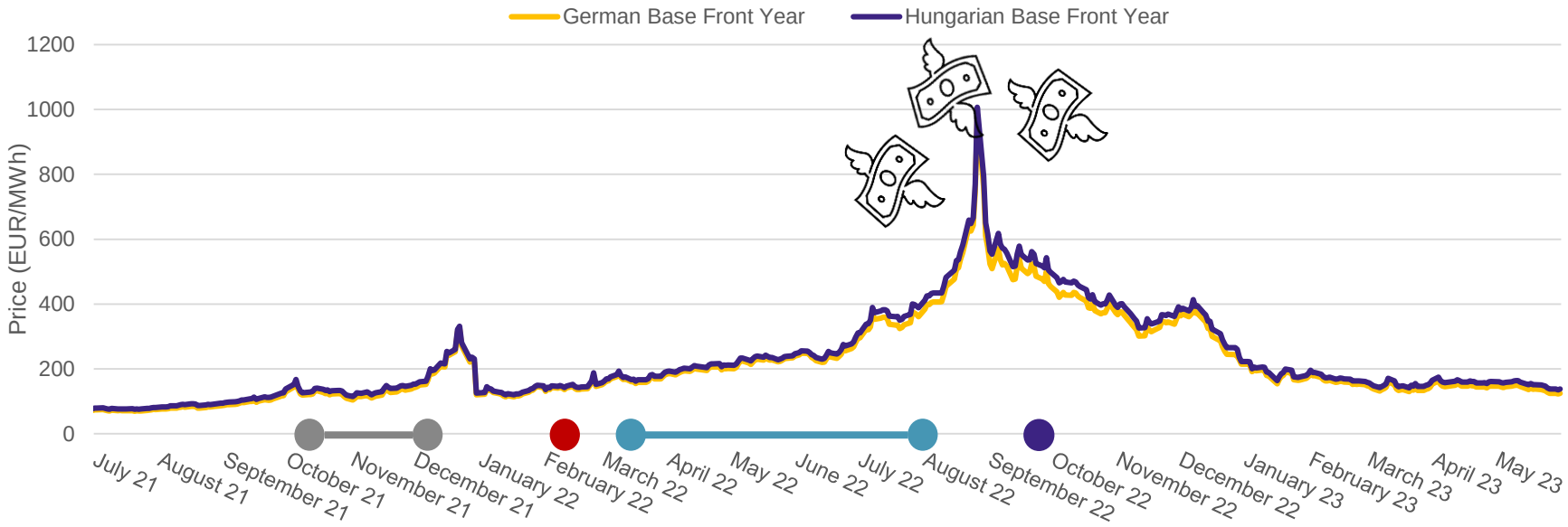


PXE Role

- PXE became an integral part of EEX
- PXE is responsible for CEE/SEE markets
- PXE acts as a local help to clients in the region
- PXE is responsible for CEE/SEE products

Croatian Financial Futures coming on June 21, 2023

Look back on price development



RU gas supply cut by 25%

24/2/2022 RU invades Ukraine

RU cuts gas supply to 5 EU member states and later cuts sNS1 by 60% .. Oil leek, maintenance etc

Suspected sabotage on NS1 and NS2

Focusing on improving EU electricity forward market liquidity

Unchanged elements	Long-term markets	Short-term markets	Retail markets
	Goal: **securing prices** & competitiveness	Goal: **less gas-dependent** market design	Goal: **consumer protection** and empowerment
• **Maintaining marginal cost-based pricing** (merit order) • **No split of the electricity market** into non-fossil and fossil • **No perpetuation of crisis-related temporary revenue skimming**	• Establishment of **Regional Virtual Trading Hubs** • Strengthening long-term contracts (**PPAs**) by introducing **guarantees** • Renewable support via **Contracts for Difference (CfD)**	• Optimization of spot - closer to real-time, **order book sharing** • Launch of "**peak shaving products**" to reduce demand • Introduction of **flexibility products** and frameworks for storage • **New entity** taking over today's **key responsibilities of market coupling operators**	• **Extension of contract rights** (right to fixed contract, multiple contracts, fixed plus variable) • Introduction of **supplier of last resort** in all states • Right to "**energy sharing**" for prosumers • Transfer of **crisis measures, potential for regulated prices**

Focus topic of EEX

Regional virtual trading hubs

What is proposed?

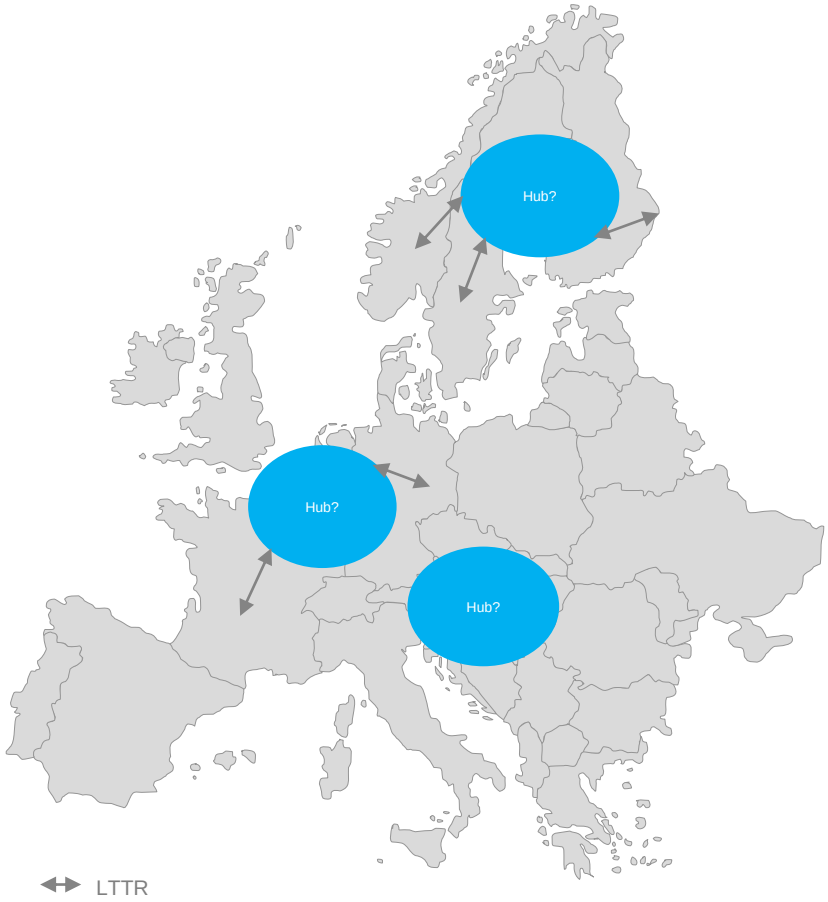
regional virtual trading hubs combined with zone-to-hub long term transmission rights (LTTRs). Such hubs would contain several of today's bidding zones.

What is the goal?

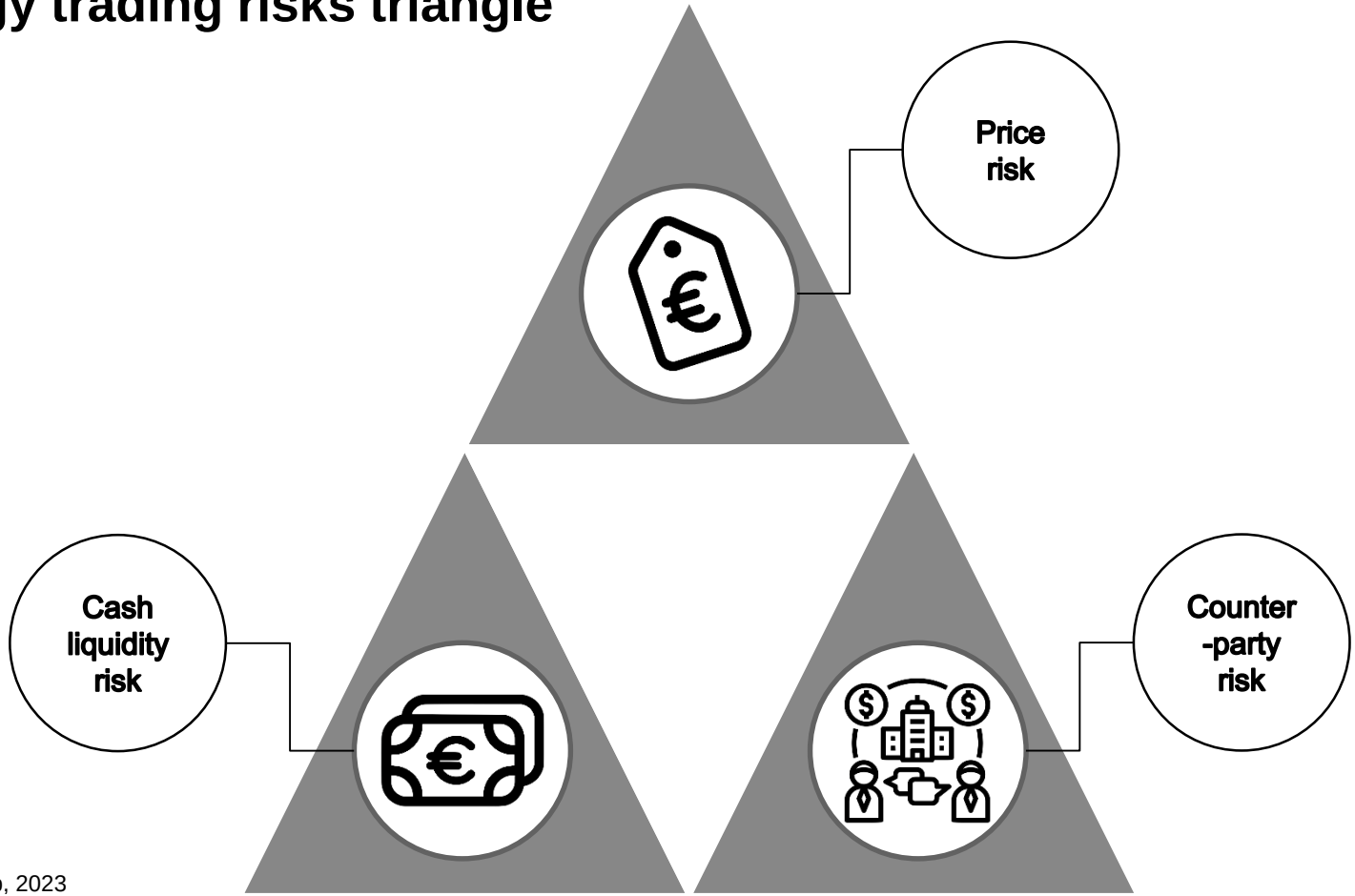
is to stimulate forward market liquidity, especially in illiquid bidding zones.

Is there are a need or demand for new istruments?

NO, well functioning hedging possibilities independent of transmission capacity are already present – the location spread offered by EEX

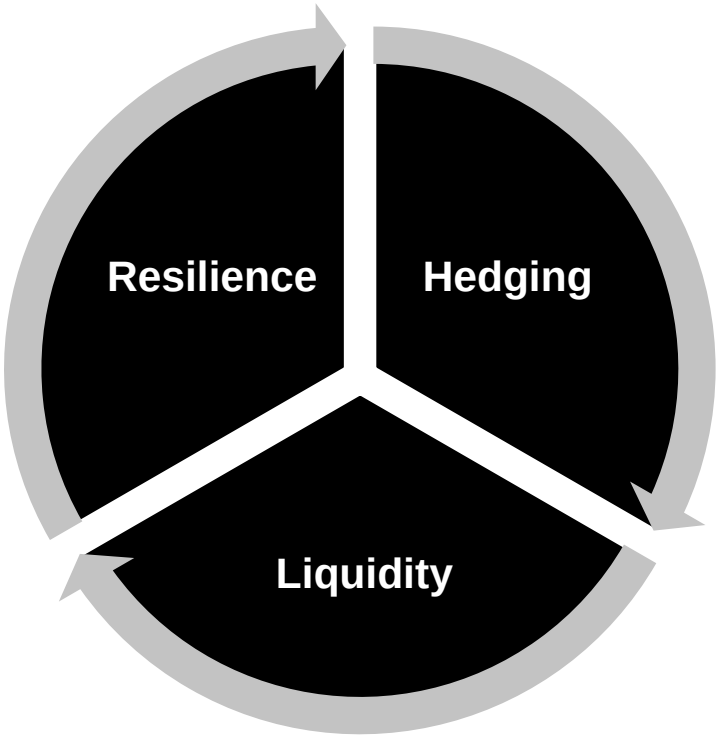


Energy trading risks triangle



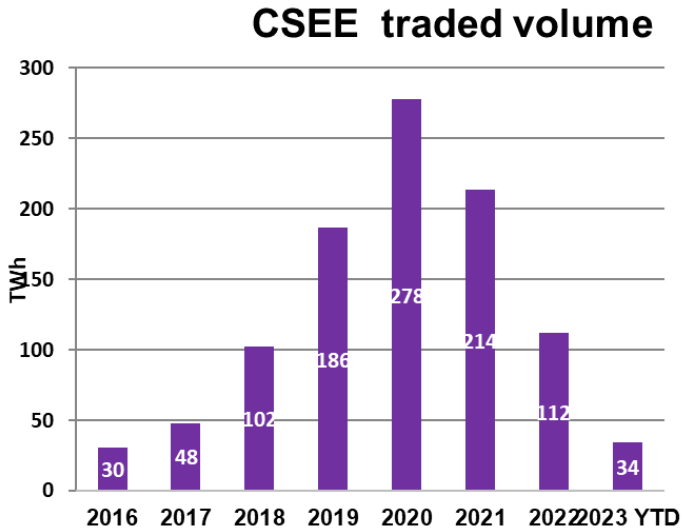
Role of the Exchange – not only in the Crisis

- essential price transparency
- long-term investment signal
- eliminating counterparty risk by clearing
- long – term hedging possibilities: not only for conventional power production but is increasingly used by RES developers



Counterparty risk

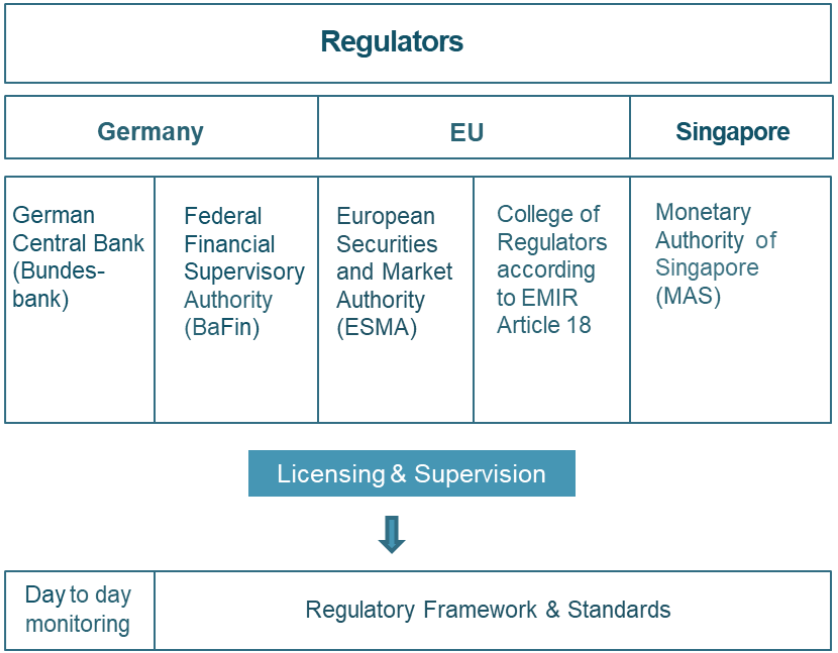
- The crisis increased counterparty default risk => the OTC market dried up and trading shifted to exchange/clearing.
- clearing requires collateral ("margins"), which led to increased financial liquidity needs.



Governmental support effective in WE countries, very bad in CSEE countries

A bit about margins

- ECC assumes the counterparty risk for all transactions concluded at its partner markets. In the event of a default of a Clearing Member ECC ensures payments to non-defaulting Clearing Members.
- ECC complies with the risk standards stipulated in the European Market Infrastructure Regulation (EMIR) and the Principles for Financial Market Infrastuctures (PFMI)
- ECC Pays Interest on EUR margin assets – second highest amout paid back to the market in Sept 2022

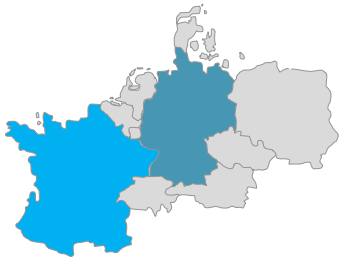


Financial Risk / Price Risk

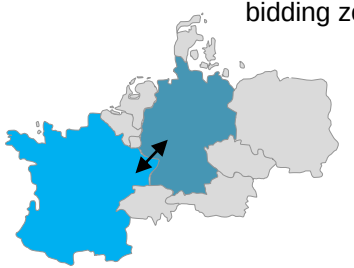
- Market participants use the forward market to manage financial risk
- Market participants do not need to be part of the same bidding zone => contracts are financially settled
- To be properly hedged there is no need of to ensure transmission capacity
- Market participants typically enter into long-term hedges at an earlier stage before actual delivery
- Allocating cross-border capacity sooner then necessary only leads to troubles.
- The physical transmission capacity is made available in the spot market as part of WELL functioning market coupling in Europe – without the market participant being actively involved

Direct, proxy and combined hedge

Direct hedges (trading the own bidding zone)



Proxy hedges (trading another bidding zone)

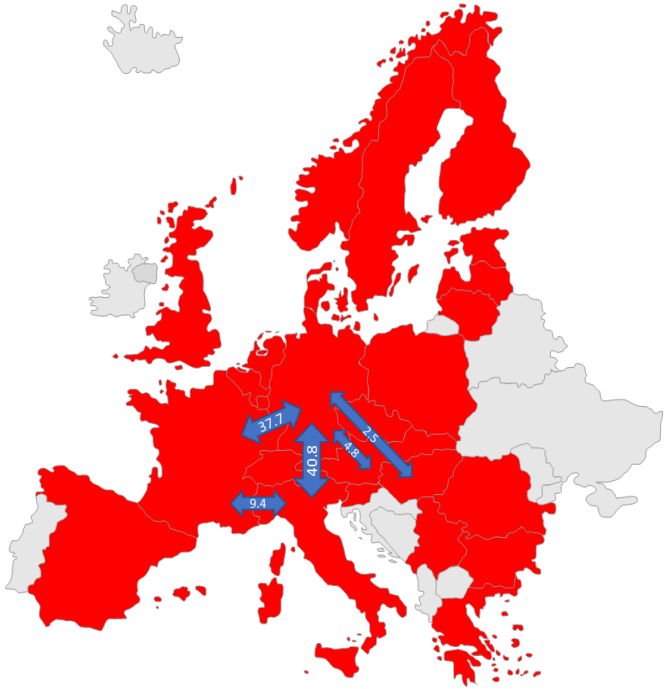


Combined hedges (trading another bidding zone + spread product

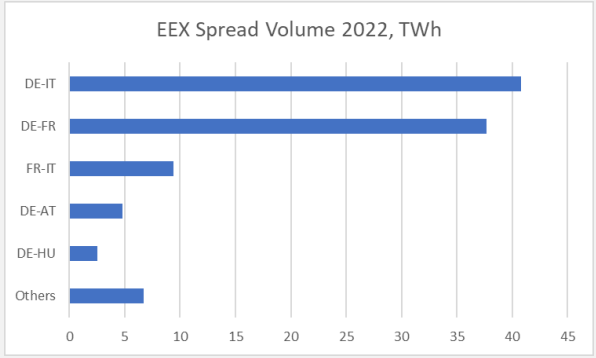
Due to the financial character of power futures contracts, **market participants can trade with anyone to hedge their price risk**. Determining the **value of the hedge** are the price of the forward contract and its underlying. Three possible ways of hedging:

- **Direct hedge**: E.g. German power producer hedges price risk by trading German power future.
- **Proxy hedge**. E.g. Czech power producer trades German power future to hedge its production. This is possible due to the high price correlation on the day-ahead market.
- **Combined hedge**: To mitigate the remaining risk that Czech and German day ahead prices show certain degree of divergence at the time the power future contract will expire (i.e. cross-border risk), the Czech power producer may in addition buy a Czech – German spread product to mitigate the remaining financial risk

Combined hedge in practice: EEX Spread contracts



- Since 2014, EEX offers locational spread contracts. In 2022 volumes exceeded **100 TWh**
- **+38 locations spread contracts**, +20 of which traded actively, ½ of which are with German power.
- Also **Hungary, Italy and France are transforming into trading hubs**.
- As the contracts are not outright futures but a trading technique that results in two different positions in the two different markets, thereby **supporting the individual market's liquidity**.



Location Spreads CSEE

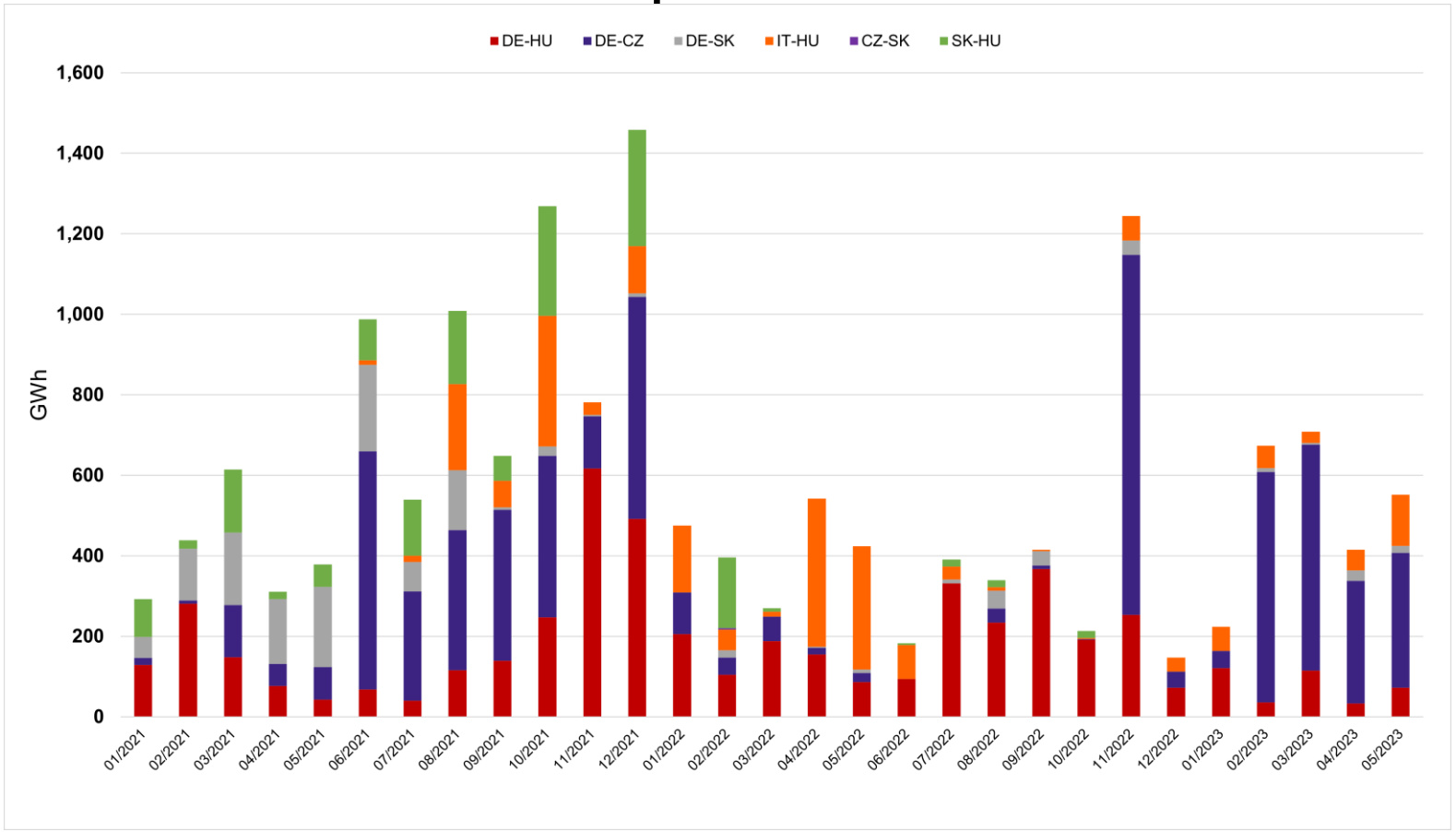
DE Power - PXE Polish
DE Power - PXE Czech
DE Power - PXE Slovak
DE Power - PXE Hungarian
DE Power - PXE Serbian

PXE Czech - PXE Polish
PXE Czech - PXE Slovak
PXE Slovak - PXE Polish
PXE Slovak - PXE HU

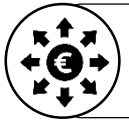
EEX Italian - PXE HU
EEX Italian – EEX Greek
EEX Italian – PXE Slovenian
EEX Italian – PXE Serbian

PXE HU - PXE Romanian
PXE HU - EEX Greek
PXE HU - PXE Serbian
PXE HU - PXE Slovenian
PXE HU - PXE Bulgarian

CSEE Volumes from Spreads



Key takeaways



Regional virtual trading hub could be offered by exchanges already today, hence there is **no need for regulatory intervention**.

While exchanges are free to develop futures on the hub, changing the current zone-to-zone LTTRs to zone-to-hub LTTRs could significantly **interfere with existing well-functioning trading hubs**.

Regional virtual trading hubs may pool liquidity, but are **prone to congestion** (e.g. Nordics), need additional **long term hedges** (10 years rather than 3) and **add complexity** to trading.

Forward market liquidity assessment should not only assess market design but also **external factors inhibiting liquidity,** e.g. non market-based support schemes, policy uncertainty and collateral requirements.

Thank you

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