Power Failure?

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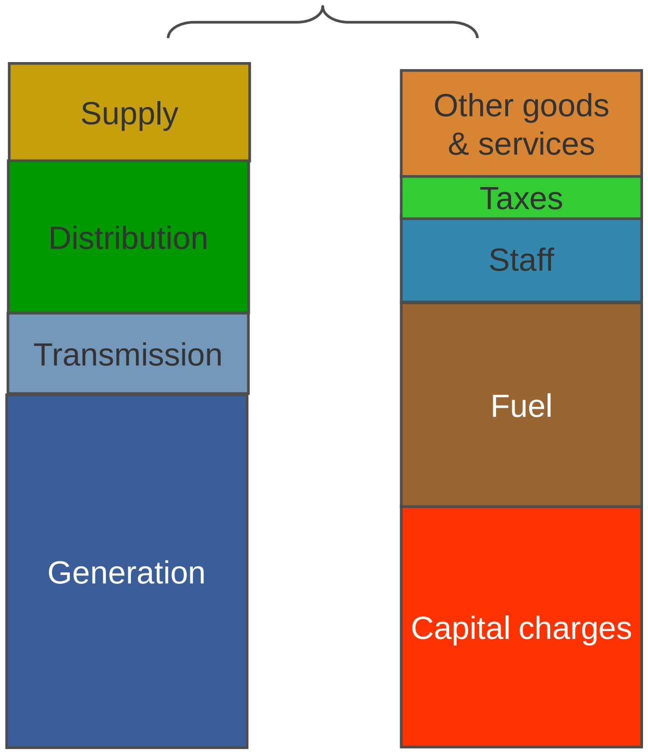
Agenda

Nationalised Monopolies' Trading Arrangements

"Cost plus – take it or leave it"

Costs £m

Divide by Sales (TWh)



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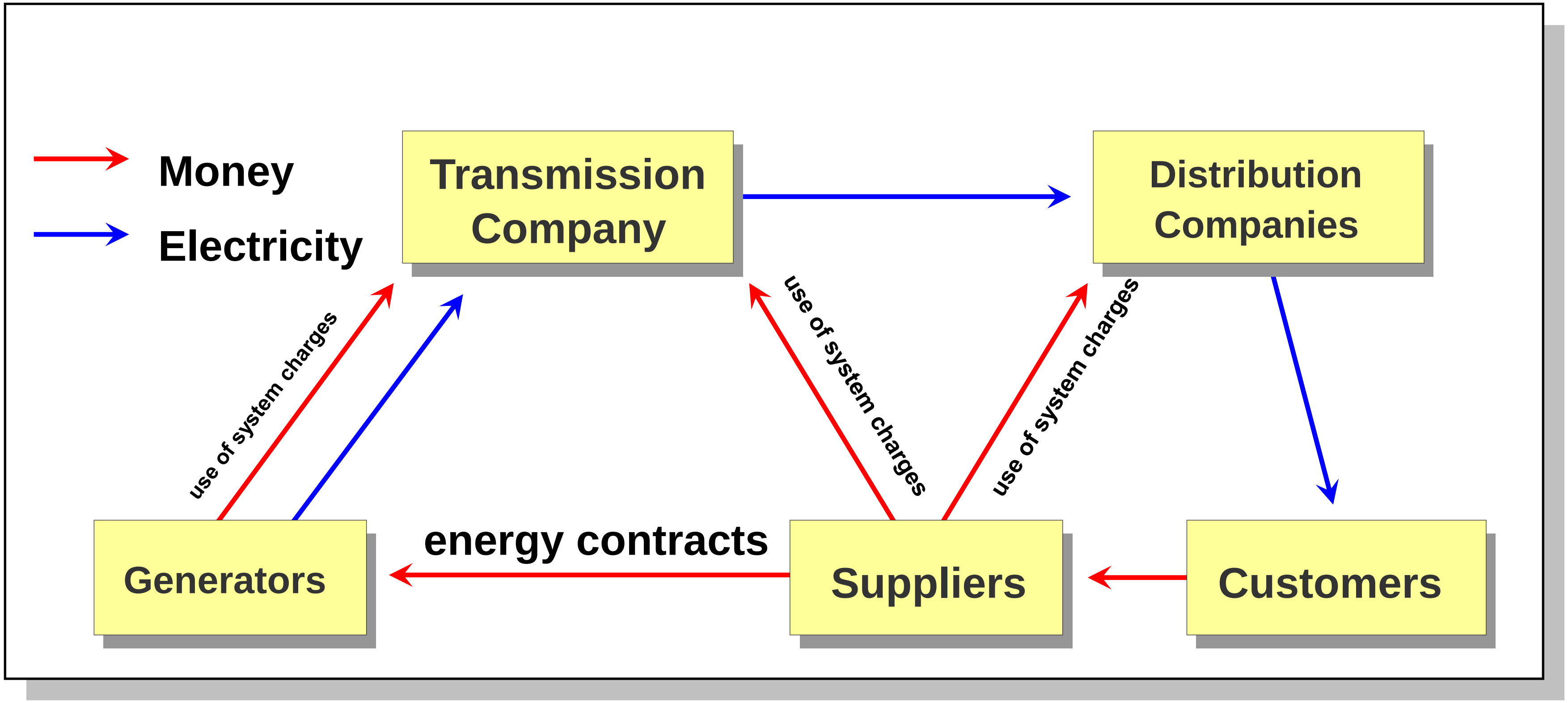
£80/MWh

8p/kWh

Led to

- Gold Plating – engineers' playground
- Inefficiency
- Corruption?

1989 Act - Competition wherever possible

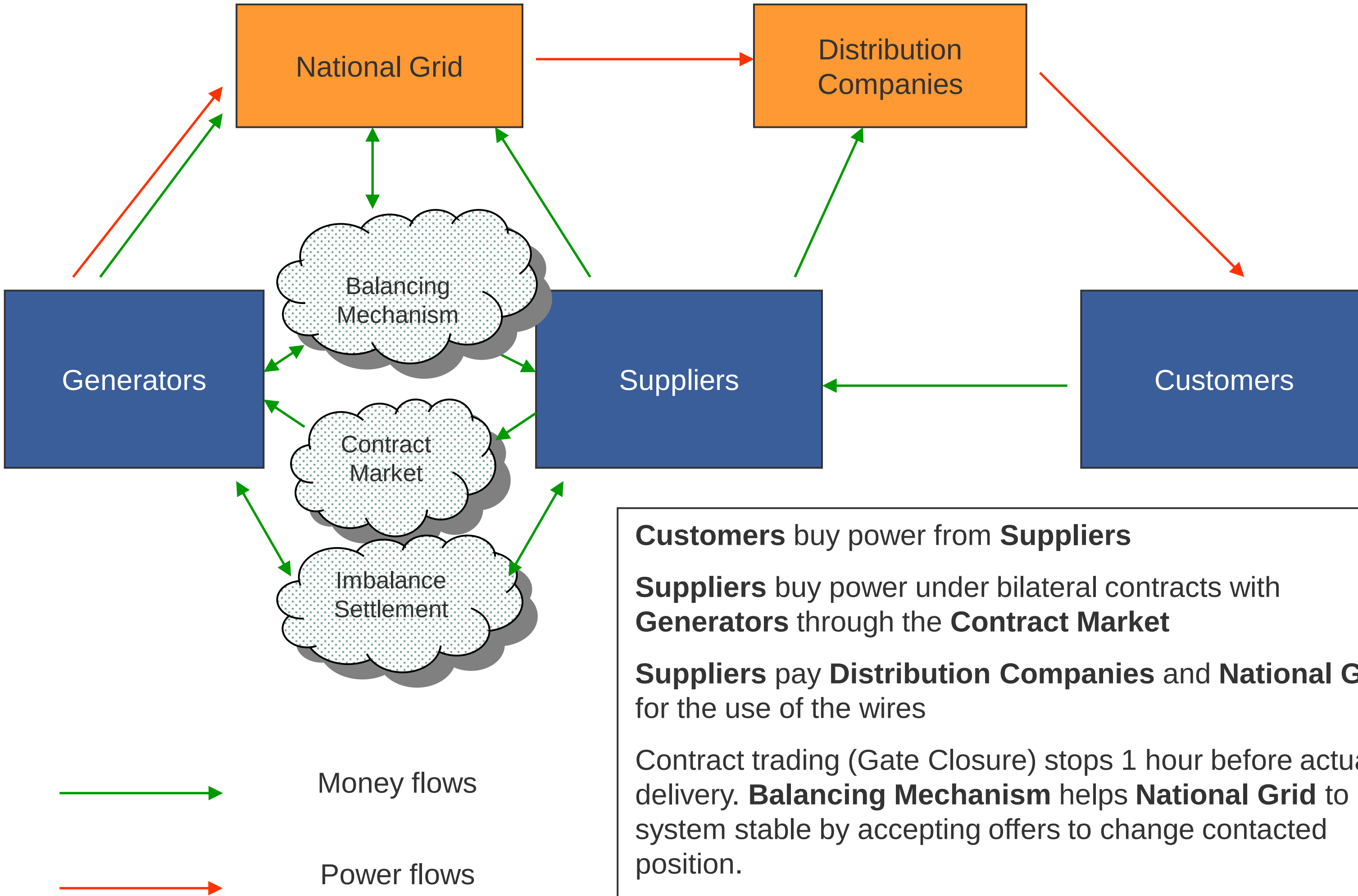


"The market should decide what, when and where new generation is built "

How to trade power?

- “Impossible” – Lord Marshall - 1988
- “No problem” – Prof Caramanlis MIT - 1985

British power market structure:



Customers buy power from **Suppliers**

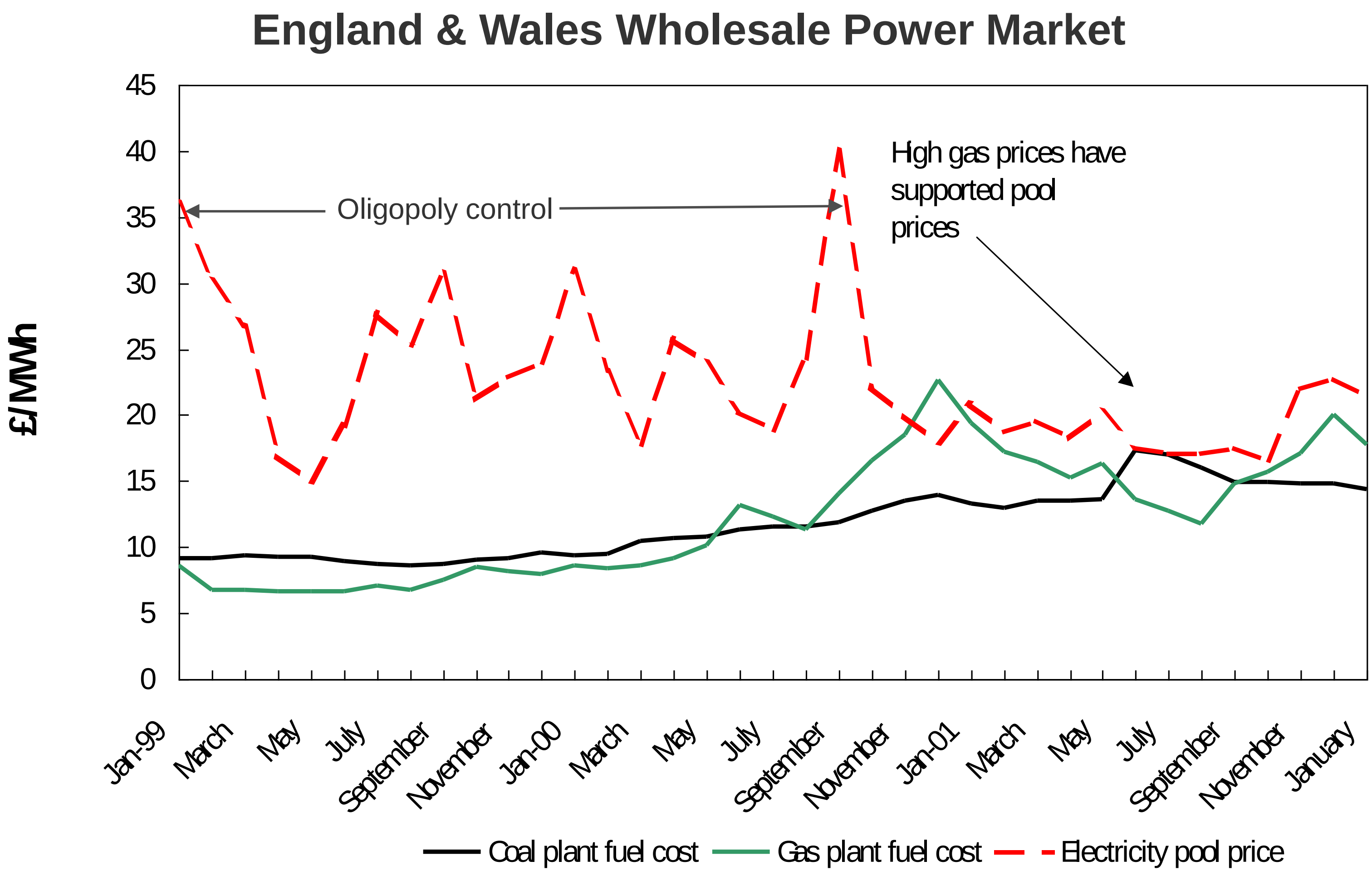
Suppliers buy power under bilateral contracts with **Generators** through the **Contract Market**

Suppliers pay **Distribution Companies** and **National Grid** for the use of the wires

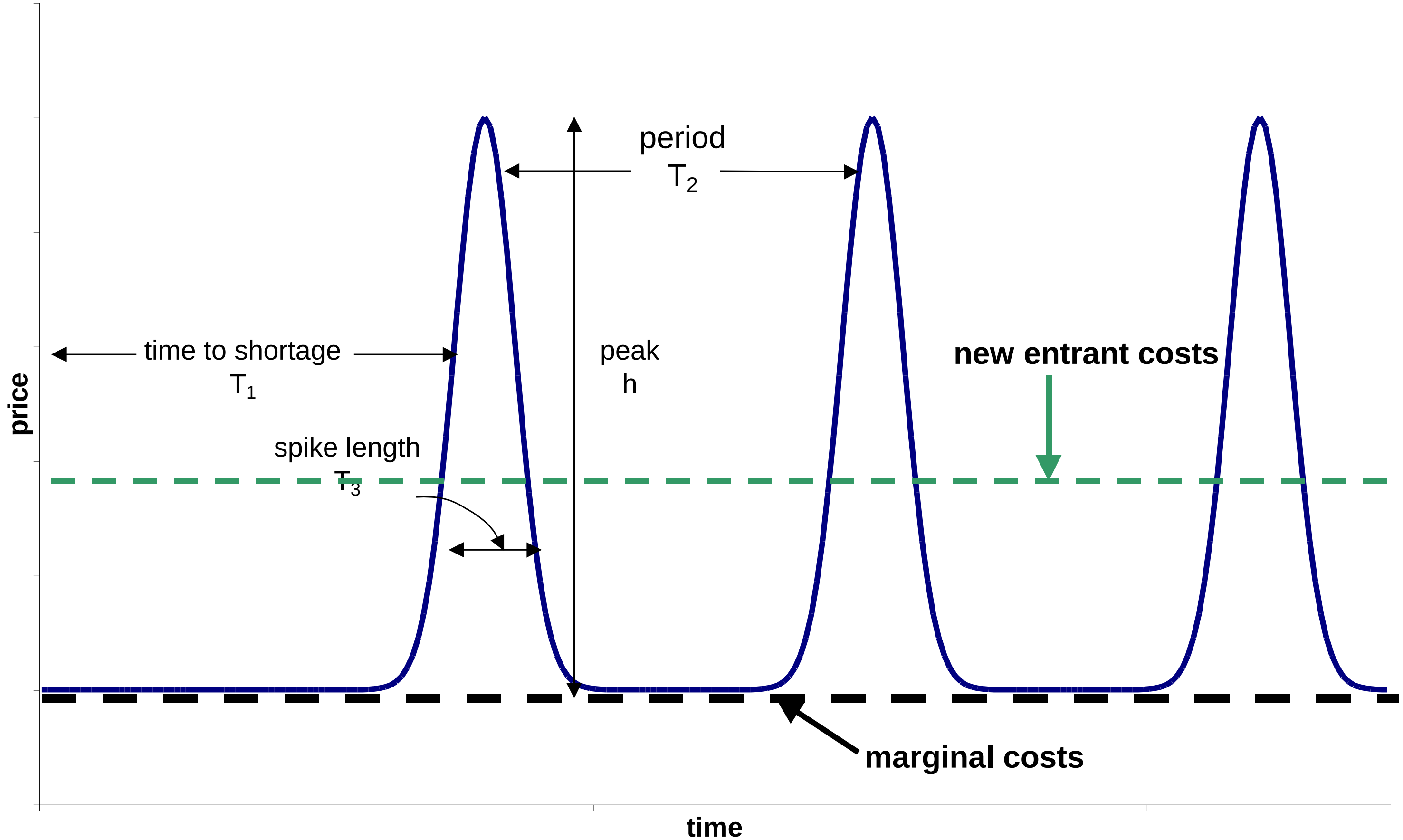
Contract trading (Gate Closure) stops 1 hour before actual delivery. **Balancing Mechanism** helps **National Grid** to keep system stable by accepting offers to change contacted position.

Ex post surpluses and deficits from the contract positions are sorted out through the **Imbalance Settlement**

Transition of “ordered” to competitive market



Price behaviour in competitive markets?



Prices in competitive markets

- Oligolpoly
  - Likely to be stable at or just below new entrant costs
  - …but probably unstable.
- Volatile
  - When demand<< supply (most of the time), at marginal costs of production
  - Soaring when demand ~ supply, then collapsing when plant built
- Who, in their right mind, would invest?
- Since 2010, all new plant first secured a long- term contract.
  - Storr, Capacity, CFDs
- So much for the market making investment decisions

Risks of generation:

- Construction
- Operation

Leave to "market"

- Timing
- Fuel technology

Socialise?

Currently delivered through the LCCC and ESC

Two issues remain

- Governance
  - Who oversees the investment decisions?
- Efficiency
  - Is the reliance on Contract for Differences sensible?
    - Will generators be confident of matching the reference price?

Back to the future?

- Central Agency
  - Purchases all power under long term competitive contracts
  - Capacity commissioning and retirement decisions independent of Government, consistent with Law
  - Sells power to unregulated Suppliers by a published tariff & purchases from large embedded generation
  - Would enjoy a very low cost of capital
- Generators
  - Rewarded for providing capacity and efficiency. Market fuel prices are “passed through”
  - NOT rewarded for trading
- Suppliers
  - Rewarded for efficient & accurate billing, customer management – but NOT trading

Questions?