

OMF
PO Box 5830
Wellesley Street
Auckland 1141

9 May 2017

**Submission - Financial Transmission Rights development:
issues and options paper**

Dear Sir/Madam,

Thank you for the opportunity to make a submission around the development of Financial Transmission Rights.

If you have any questions please contact:

Karl Arns
Dealer, Carbon & Energy
OMF
PO Box 5830
Wellesley Street
Auckland 1141
Karl.arns@omf.co.nz
09 521 7802

Appendix A

Submitter: OMF

Q1. Do you agree that further enhancing the FTR market could support the issues identified by the Authority, and provide benefits to the wider hedge market?

Yes. Further development of the FTR market is crucial to increasing the efficiency of the wider hedge market.

Q2. Are there other issues with the current arrangements for FTRs that we have not identified?

In our view one of the biggest barriers to increasing competition is the ability to hedge retail load at smaller hubs at the edges of the grid.

We note participants recently had the opportunity to vote on the development of new FTR hubs and we are pleased to see RDF2201 & KIK2201 reaching the CBA stage. Additional regional hubs would be welcomed to help independent retailers hedge regional price risk.

We acknowledge the opportunity for the independent retailers to be heard on this matter has already come and gone, however a lack of education and resources inevitably skewed the results in favour of the vertically integrated incumbents. The inclusion of two 'Non Hub' results in the top 5 shortlist gives support to our view the voting process was dominated by the incumbents. Difficulty in hedging retail load centres is a barrier to growing market share if not an outright barrier to entry and so we don't think 'Non Hub' is the best outcome for increasing competition or developing the hedge market.

Q3. Are there any other ways to develop the FTR market that we have not identified? If so, please describe them.

OMF has no further recommendation at this point in time.

Q4. What are your views on the relative merits or priority of these twelve potential developments? Could some of them complement or substitute for others?

Listing an FTR like derivative on the ASX is an option well worth pursuing. This resolves four out of the five issues highlighted by the EA by:

- Reducing barriers to participation
- Improving the ability to purchase or resell FTRs as and when desired.
- Reducing volatility in the daily assessment of an FTRs value
- Improving the ability to mesh FTRs with other commonly used risk management products

And removes the need to:

- Change the electricity code
- Allow short selling
- Open the market to overseas participants
- Create a bulletin board

Additionally, more frequent auctioning and additional hubs can only be positive developments for the FTR and wider hedge market.

Incumbent participants have put up some resistance to the provisioning of additional hubs and more frequent auctioning, citing resourcing constraints and internal transaction costs. The incumbents are arguably in the best position to manage and implement these proposed changes so ultimately we don't think the resistance is justified.

We stress the need for only simple, pragmatic developments to be pursued. The following proposals are highly involved and we question whether the underlying demand and benefits of these initiatives are commensurate to the work and time required:

- short selling
- overseas participation
- bulletin board
- preferential pay out FTRs

Q5. Do you agree the Authority should provide policy direction on the four developments in Group 1, but that service providers can lead further assessment of the developments in Group 2?

Yes.

Q6. What are your views on the merits of extending direct participation in the FTR market to parties based in Australia?

We question the basis under which the Authority makes the statement 6.3 (b):

Overseas parties trading primarily on a proprietary basis are likely to be interested in selling FTRs, increasing supply, noting that they would only be able to sell obligation FTRs, absent other developments.

ASX futures can be easily package to create a product that is equivalent to an obligation FTR. Overseas parties can easily access the ASX and therefore we don't believe access to obligation FTRs is the underlying driver of this discussion.

In our view the Authority needs to focus its attention on the developments most likely to provide the greatest benefit to the wider hedge market. Extension to Australian based parties will not provide the desired benefits outlined by the authority and there are other developments that should take priority.

Q7. What are your views on the merits and practicality of allowing parties other than the FTR manager to originate FTRs?

If such a party exists then we are all for this development, however we would want to see some indication there are parties interested in short selling material volumes before any further work is done pursuing this.

Q8. What are your views on the merits and practicality of developing an FTR derivative product?

There is a number of benefits to implementing such a product.

An FTR derivative resolves four out of the five issues highlighted by the EA and removes the need to:

- change the electricity code
- allow short selling
- open the market to overseas participants
- create a bulletin board

Q9. What are your views on the merits of developing a bulletin board?

OMF quotes FTRs in the secondary market on a semi-regular basis. The number of responses we get to secondary market offers is typically quite disappointing. As highlighted by the Authority – secondary transactions are rare. The relative infrequency of secondary trades is a function of lacklustre underlying user demand for secondary trading, and is not due to the absence of a platform to facilitate such dealing.

Q10. Of the two approaches to overcoming the inherent limitations in the supply of FTRs that have been discussed (allowing parties to originate or develop a derivative product), which do you consider preferable and why?

The FTR derivative is more attractive.

- Price discovery and settlement pricing occurs on a daily basis and not just when the FTR period is auctioned. This is the primary appeal.
- Short sellers can participate in the FTR derivative if they wish – without the complexity inherent in changing the code and opening the FTR auction and clearing manager channels to accommodate short positions.
- ASX futures positions can offset against the FTR derivatives, reducing margin requirements.

Q11. Are there other approaches to overcoming the inherent limitations in the supply of FTRs that the Authority has not identified?

We are pleased to see the FTR manager constantly reviewing and tweaking the offer methodology to strike the right balance between offer volumes and the frequency of revenue inadequacy.

Q12. What are your views on how these developments would complement each other? To what extent might they be dependent on each other?

The FTR derivative is our clear preference for the reasons listed above, in part because it solves a number of the issues identified by the Authority and removes the need for multiple changes.