

Response to the Danish Regulator survey options for hedging electricity price risk in DK1 and DK2

Brussels, 15 October

Detailed comments

A. The company's role and exposure in the electricity market

1. Which of the following descriptions fits the company's activities and exposure in the electricity market? Select all that apply. *

- ☐ Electricity producer with direct exposure to electricity price risk
- ☐ Large electricity consumer with direct exposure to electricity price risk
- ☐ Electricity supplier to end customers with direct exposure to electricity price risk
- ☐ Electricity trader
- ☐ Aggregator or portfolio manager
- ☐ The company trades financial electricity products for its own account.
- ☐ Broker/intermediary of products for hedging electricity price risk
- ☐ Financial company
- ☐ Provider of risk hedging or risk management for other companies
- ☒ Other

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Other, please specify what:

We are the organisation representing energy traders on gas, electricity and carbon markets across Europe. While we, as an organisation, don't engage in trading, we represent aggregate views of market participants, active across European energy markets.

*2. Does the company have direct exposure to electricity price risk in DK1 and/or DK2?
Select all that apply **

☒DK1

☒DK2

☒No direct exposure to electricity price risk

*3. What is the approximate annual volume of the company's activities in the Danish electricity market that give rise to electricity price risk? Please indicate the approximate total volume in DK1 and DK2. Select one answer. **

☐Under 100 GWh

☐100 GWh–1 TWh

☐1–5 TWh

☐Over 5 TWh

☒Not applicable

☐Do not wish to disclose

B. Use of hedging

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*4. Which instruments are used to hedge electricity price risk related to DK1 and/or DK2?
Select all that apply. **

☒ System price futures/forwards

☒ EPAD DK1

☒ EPAD DK2

☒ Direct DK1 area price futures/forwards

☒ Direct DK2 area price futures/forwards

☒ Long-term transmission rights (LTTR)

☒ Other OTC products

☒ PPAs

☒ Other bilateral agreements

☒ Financial products linked to other bidding zones

☒ Other instruments

☒ Hedging of electricity price risk related to DK1 or DK2 is not used.

*Please specify other instruments and/or any **comments or clarifications**:*

On a general note, we encourage having different market instruments available to market participants so they may best construct their hedge and find the most efficient path to trade across bidding zones. We also support having long-term instruments working

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together, such as EPADs and Long-Term Transmission Rights (in the form of Financial Transmission Rights).

We support exploring the possibility for auctions across bidding zone borders for FTRs and EPADs. For an EPAD auction, one suggestion would be to explore between DK2 and SE4.

C. Proxy Hedging and Time Horizon

*5. Are products linked to prices in other bidding zones or the Nordic system price used to hedge electricity price risk in DK1 and/or DK2? Select all that apply. **

☐ Nordic System Award

☒ DK1 – used to hedge exposure in DK2

☒ DK2 – used to hedge exposure in DK1

☒ Germany (DE/LU)

☒ Sweden (SE3)

☒ Sweden (SE4)

☒ Norway (NO2)

☒ Netherlands (NL)

☒ United Kingdom (GB)

☐ Other prices

☐ Products linked to other prices are not used to hedge electricity price risk in DK1 or DK2.

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☐ Don't know/cannot assess

Proxy hedging means that electricity price risk in DK1 or DK2 is hedged using a product that is linked to a price other than the price in the bidding zone where the price exposure is located.

*Other prices, please specify which ones, and/or any **comments or clarifications**.*

Proxy hedging is an important part of hedging used by market participants. Germany is particularly important for proxy hedging, as it is the most liquid electricity market in Europe. For example, proxy hedging with Germany helps cover the longer-term horizon.

Market participants also observe that less hedging products and opportunities are used in DK2 as the bidding zone tends to be less liquid.

*6. Is there a need or desire to further hedge the price risk that results from the product used being linked to a price other than the price exposure that is desired to be hedged? **

☒ Yes

☐ No

☐ Don't know/cannot assess

☐ Not applicable – proxy hedging is not used

Any comments or clarifications

Cross-border hedging opportunities are essential to hedge risks, including price risks and basis risks. Germany holds an important role in proxy hedging as a natural and liquid hub.

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We would also welcome the establishment of auctions for LTTRs and EPADs, including looking towards further long-term horizons. For LTTRs, we recommend using FTRs options. For EPADs, bi-weekly auctions can be set up.

*7. Which time horizons are relevant for hedging electricity price risk related to DK1 and/or DK2? Select all that apply. **

☒ Up to 3 months

☒ 3–12 months

☒ 1–2 years

☒ 2–5 years

☒ More than 5 years

☐ Not applicable

☐ Don't know/cannot assess

D. Assessment of hedging options in DK1 and DK2

*8. Does the company consider that, under current market conditions, there are sufficient opportunities to hedge electricity price risk in DK1? **

☐ Yes

☒ Partially

☐ No

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☐ Don't know/cannot assess

☐ Not applicable

*9. Does the company consider that, under current market conditions, there are sufficient opportunities to hedge electricity price risk in DK2? **

☐ Yes

☐ Partially

☒ No

☐ Don't know/cannot assess

☐ Not applicable

*10. If the possibilities for hedging electricity price risk in DK1 and/or DK2 are assessed as only partially sufficient or not sufficient, which factors are most important? Select a maximum of 3. **

☒ Insufficient liquidity

☐ Large bid-ask spreads

☒ Products are not available in the requested time frames.

☐ Available products do not adequately follow actual price exposure

☒ The profile of available products does not match the hedging needs

☐ Collateral/margin requirements

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- ☐ Counterparty or credit relationship
- ☐ Transaction costs
- ☐ Other conditions
- ☐ Don't know/cannot assess
- ☐ Not relevant – the options are considered sufficient

*Other matters, please specify which and/or **any comments or clarifications***

In addition to the selected three options, we also underline a large bid-ask spread, which we see as linked to and similar to insufficient liquidity. Available products do not adequately follow price exposure is another component we flag as part of the factors for insufficient hedging opportunities.

E. Hedging of price differences between bidding zones

*11. For which of the following bidding zone boundaries is it relevant to hedge price risk associated with the price difference between the bidding zones? Select all that apply. **

- ☒ DK1–DK2
- ☒ DK1–Germany (DE/LU)
- ☒ DK1–Netherlands (NL)
- ☒ DK1–Norway (NO2)
- ☒ DK1–Sweden (SE3)

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☒ Dk1-Great Britain(GB)

☒ DK2-Germany (DE/LU)

☒ DK2-Sweden (SE4)

☐ Other bidding zone limits

☐ None of the above

☐ Don't know/cannot assess

Other bidding zone limits, please specify which ones

We reiterate the importance of Germany in proxy hedging. We also recommend the measures of setting up auctions for LTTRs and EPADs to increase coordination and price discovery.

*12. Are there considered to be sufficient opportunities to hedge price risk associated with price differences between the relevant bidding zones? **

☐ Yes

☒ Partially

☐ No

☐ Don't know/cannot assess

☐ Not applicable

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*Any **comments or clarifications**, including if the assessment differs between bidding zones*

We highlight the importance of combining German futures with FTRs to help hedge price risks.

13. If long-term transmission rights (LTTR) are used as part of the hedging, please describe how they are used. (Please indicate which bid zone limits LTTR are applied to, which price risk they are used to hedge, and whether they are combined with other products or positions.)

Market participants often hedge their position in the more liquid bidding zones, where spreads are narrower, and they can lock the prices years in advance, which is called proxy hedging. In Europe, the most liquid natural hub is Germany. As it neighbours DK1 and DK2 and the prices often correlate, it is a rational choice for market participants.

LTTRs complete the proxy hedge. A participant fixes the price level with German baseload futures. It then holds FTR options on the border between Germany and its Danish zone to cover the basis risk.

The direction depends on the exposure. A supplier or consumer in DK1 buys German futures and an FTR option from DE to DK1. A producer in DK1 sells German futures and buys an FTR option from DK1 to DE.

The borders used are mainly DK1–DE/LU and DK2–DE/LU. DK1–NL can be used in the same way against the Dutch market. No LTTRs are issued on DK1–DK2 or on the borders with Norway and Sweden, so participants with positions there rely on EPADs.

The main limit is maturity. German futures can be traded several years ahead, although liquidity thins out beyond three years. Danish FTR options are only auctioned for the year

ahead and the month ahead. Maturities of three to five years and larger volumes would close that gap.

Moreover, PPAs are market-efficient tools to foster investment in new low-carbon energy sources and provide long-term price certainty. Long-term PPAs can expose participants to bidding zone price differentials, for which LTTRs could provide an additional hedging instrument. The introduction of LTTRs would provide increased hedging opportunities and facilitate the development of cross-border PPAs.

Additionally, we see a complementarity of LTTRs with EPADs that can be set up in the wider Nordic region. The combination of EPADs and LTTRs in Nordic forward power markets can provide further hedging opportunities to cover cross-border risks. Their co-existence and complementarity can be seen in two ways:

- EPADs can complement forward transmission rights to hedge non-standard volumes (MW) that are not fully covered by available transmission rights;
- EPADs can give market participants flexibility concerning when and for which period hedging takes place when forward transmission rights are auctioned at fixed dates for fixed delivery periods. Secondary markets for forward transmission rights largely mitigate this lack of flexibility, but they take time to develop, especially given the absence of LTTR auctions in the Nordic area. Secondary markets for EPADs would also be possible with EPAD auctions, as the products acquired are fungible.

F. Possible improvements

*14. Which of the following changes are considered to have the greatest positive impact on the possibilities of hedging electricity price risk in DK1 and/or DK2? Select a maximum of 3. **

☐ Increased market making in existing hedging products for DK1 and DK2

☐ Longer maturities available

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- ☒ Access to products with other product profiles
- ☐ Increased access to products to hedge price differences between bidding zones
- ☒ Long-term transmission rights (LTTR) on additional relevant bidding zone borders
- ☒ Other changes
- ☐ None of the above
- ☐ Don't know/cannot assess

Other changes, please specify which ones, as well as any comments or suggestions for other changes

We support LTTRs and EPADs on additional relevant borders, as the two are complementary. For LTTRs, we recommend FTR options with longer maturities, issued at maximum capacity in both directions. For EPADs, TSO auctions could follow the examples of Statnett and Svenska kraftnät, and the SE4–Lithuania arrangement starting in 2026.

We also support increased market making in existing hedging products for DK1 and DK2, as we already expressed in our response to Energinet consultation from last year (<https://www.energytraderseurope.org/documents/response-to-energinets-consultation-on-market-maker-model/>). We would like to use this opportunity to ask about the current status of the scheme and when it will be implemented.

G. Closing remarks and contact

15. Does the company have any other comments about the possibilities for hedging electricity price risk in DK1 and DK2 that are not covered by the questions above?

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Insufficient long-term transmission rights increase hedging costs and reduce the ability of suppliers to offer long-term fixed-price products to Danish consumers and industrial customers.

Additionally, we would like to flag our joint study

(link: <https://www.energytraderseurope.org/documents/assessment-of-potential-impacts-of-regional-virtual-hubs-on-the-forward-markets/>) with Eurelectric and Europex on the impacts of introducing Virtual Trading Hubs in Continental Europe on forward markets. Notably, there would be a significant effect on the German market and impact its liquidity, which is key for proxy hedging purposes.

The study reveals that regional VTHs are far from providing a more efficient basis for (proxy) hedging than existing physical hubs. Furthermore, the study considers that the introduction of VTHs in continental Europe is likely to have negative effects on the liquidity of forward markets, splitting the liquidity and discriminating against areas not covered in Virtual Hub calculation.

*16. May the Danish Utilities Authority contact the company with a view to clarifying or elaborating on the answer? **

☒ Yes

☐ No

Any comments

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