AFMA

11 June 2020

Prabpreet Calais
Australian Energy Markets Commission
(lodged online at www.aemc.gov.au)

Dear Prabpreet,

Delayed Implementation of Five Minute and Global Settlement

The Australian Financial Markets Association (AFMA) welcomes the opportunity to provide comment on the Consultation Paper – NATIONAL ELECTRICITY AMENDMENT (DELAYED IMPLEMENTATION OF FIVE MINUTE AND GLOBAL SETTLEMENT) RULE 2020. ("consultation paper").

AFMA represents the common interests of its members in dealing with issues relevant to the good reputation and efficiency and competitiveness of wholesale banking and financial markets in Australia. Our members include Australia's major energy companies and other users of over-the-counter electricity derivatives.

Whilst acknowledging the overall purpose of the rule change request and the consultation, AFMA's focus is on the efficiency and competitiveness of electricity financial markets. Accordingly, our comments are limited to those areas that relate to this focus.

The stakeholder feedback template in Attachment 1 provides AFMA's views on the relevant questions. Please feel free to contact me via mchadwick@afma.com.au if you have any questions.

Yours sincerely

M. Chadwick

Mike Chadwick
Head of Education and Director - Markets

ATTACHMENT 1
STAKEHOLDER FEEDBACK TEMPLATE

CHAPTER 4 – SECTION 4.1 – TIME PERIOD FOR DELAY

Question 1 – Time period for delay	
a) If a delay to the start date of 5MS is necessary, is a 12-month delay appropriate? Alternatively, please explain why another time period is preferable and, if applicable, the implications on cash flow and capacity? Would the rules need to commence at the start of a quarter to align with the contract market, or could 5ms commence mid-quarter? What would be the impact of a mid-quarter commencement?	The majority of AFMA's energy market members consulted by AFMA support a delay to the start date of 5MS, although views differ regarding the appropriate length of delay. Almost all members consulted supported a delay of between 12 months and 24 months. One member suggested a delay of 6 months, although noted that this may cause issues for FY2022 contracts. Most others noted however that a 6-month delay to 1 Jan 2022 would not be ideal given that this would be during the peak summer demand and the Christmas/New Year holiday period, where information technology system freezes are often in place. Some also questioned whether a 6-month delay would provide any material benefits for industry or consumers. Members that supported a delay period of 12 months or more noted that this would allow for AEMO to ensure system readiness. Some noted that the window for user acceptance system testing was already narrow prior to the onset of COVID. A 12-month delay would allow market participants to reduce the level of overlap in their respective work programs and provide for more sequential development and implementation of system changes. The delay also provides the industry with an opportunity to deprioritise program activities and defer capital costs from FY2021 to FY2022. One also noted that a delay may mitigate additional risks for smaller retailers who will have to absorb material IT costs due to the duress associated with an economic downturn. All members agree that the rules should commence at the start of a quarter to align with the start date of financial contracts. A mid-quarter commencement could give rise to some additional costs or complexity for participants to adapt their wholesale trading systems. One noted that starting on 1 July 2022 (ie; 12 month delay) would have the benefit of aligning with financial year contracts.

Question 4 – Electricity contract market	
a) To what extent have you purchased 5-minute cap products for FY 2021-22? What would the impact of a delay be to the value of those 5-minute cap products as risk management products for your business?	There has been very little activity in 5-minute cap products for FY21-22 to date. With respect to futures contracts, the ASX had not yet listed the new cap products on the exchange prior to the onset of COVID-19, and hence there has been zero turnover, despite market participant interest. However, the ASX should be in a position to list either 5-minute or 30-minute cap contracts when a decision regarding the delay is made in early July, so a timely decision is welcomed by market participants. In the Over-the-Counter (OTC) markets, it is understood there have only been a few transactions. It is likely that those contracts would have included an allowance to maintain existing 30-minute pricing in the event of a delay to 5 minute settlement, which would suggest renegotiation impacts would be limited.
b) Would a delay to commencement of 5MS impact swap, captions or any other financial hedging products trading for FY2021-22 and beyond? If so, how?	Our members generally expect limited negative impact on financial hedging product trading as a result of a delay to five-minute settlement implementation. The uncertainty associated with the current consultation is probably affecting liquidity somewhat whilst the decision is pending, but as noted above, market participants welcome a timely decision to alleviate this. With respect to swaps, any impact on trading should be limited, given contract settlement outcomes do not materially change under five or thirty-minute settlement. With respect to caps, if anything, trading and liquidity would most likely improve once a delay is announced relative to a no-delay scenario. More market participants are comfortable with selling 30-minute caps, whilst the implementation of five-minute settlement will likely reduce the number of participants who are able to sell five-minute caps. One member has noted that the value of settlement residue units may be impacted.