

13 June 2016

## WHOLESALE ENERGY PRICES: MARCH 2016 – MAY 2016: PART II: ELECTRICITY

*In this new series of articles, Dominic Whittome covers wholesale energy prices between March and May 2016, discussing issues such as fluctuations in the price of Brent crude, falling shale production and decreasing prices across Europe's gas and electricity exchanges, as well as the possibility of these rising again in the future.*

Baseload power prices, like gas prices, fell, by 5% to just under £35/MWh with the spark spreads unchanged. The carbon market was also soft, with the EU Allowance trading fractionally, if stubbornly, below €5/tCO<sub>2</sub> as initial excitement after the Paris Convention gave way to falling prices across Europe's gas and electricity exchanges and OTC platforms.

However, while there is no obvious shortage of baseload power or surplus (if sporadic) renewable projects, UK and European grids are facing potentially significant shortages of flexible, peaking electricity to keep their networks stable. It is this market which will be weighing on Industrial & Commercial market prices and electricity bills in the domestic sector too.

The prospect of extreme electricity balancing market prices (now uncapped up to £3,000/MWh) may feed back into gas prices, especially if gas becomes the dominant marginal price setter and CCGT/gas's share of the generation mix rises further. In response to the network balancing & generation margin problem, the government has said it will amend the Capacity Market, changes which will hopefully be clarified very soon.

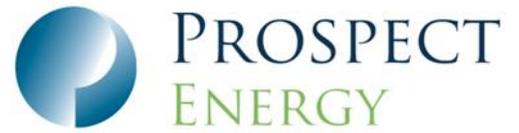
With gas and coal plants closing in recent months, even preferring to pay a release penalty to get out of stand-by generation contracts, it is clear that the sub-£20/GW capacity prices payable under the existing STOR program have not galvanised this new flexibility/storage supply 'sector' in the way policy makers had hoped. Perhaps the most probable outcome to the latest government consultation will be a series of short-term, piecemeal measures.

These changes are anticipated to include higher, longer-term payments for spinning reserve generation under the Capacity Market and possible regulatory incentives (e.g. grid access) and financial incentives (e.g. reduced transmission & distribution tariffs) for private wire interconnector, smart grid/micro-generation, large scale batteries and other storage/modulation projects which help local networks to keep their grids in balance.

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