1. Market dialogue

Since October 2011, Germany's natural gas market has been divided into two dual-quality market areas or balancing zones. The number of gas market areas in Germany has thus fallen from 19 in 2006 to the current two.

In January 2015, ACER published the updated Gas Target Model (GTM II), which sets out criteria to assess the liquidity of wholesale natural gas markets and a process for regulators to review whether their market areas meet these criteria. Should market areas not meet the criteria, and should compliance not be foreseeable in the medium term, regulators should consider the proposed options for market integration.

In connection with the review process proposed in GTM II, the Bundesnetzagentur commissioned management advisors Wagner, Elbling & Company (WECOM) to draw up a report presenting the potential and impact of further national or cross-border gas market integration, alternative national measures to improve liquidity in the market areas, and criteria as a basis for a detailed evaluation of market area integration options.

Building on this report, the Bundesnetzagentur launched a market dialogue with a focus on the following issues:

- liquidity and competition in the wholesale markets in the two German market areas NetConnect Germany (NCG) and GASPOOL,
- advantages and disadvantages of national and cross-border market integration, and
- benefits of national measures to improve the situation within the NCG and GASPOOL market areas ("internal measures").

On 3 November 2016, the Bundesnetzagentur held an accompanying open workshop in Bonn attended by numerous market players. The following companies and associations responded to the subsequent invitation for written comments: 8KU, ARGEnegie, BDEW, EnBW, Engie, EFET, E.ON, FNB-Gas, GEODE, INES, Open Grid Europe, OMV, PEGAS, RWE Supply & Trading, SW Heidenheim, Statoil, ÒhuGa, Uniper, VICI/VIK and VKU.

The respondents generally consider the development of the two German market areas to be good, especially in relation to short-term trading. In respect of the medium and long-term trading...
horizon, however, they generally see further potential for development as regards liquidity. Many market players consider L-gas trading liquidity to be insufficient.

According to the WECOM report and to the majority of the market players, the requirements set out in GTM II can generally only be met through integration with the market area in the Netherlands (TTF), since this is currently the only market area in Europe that fulfils the GTM II requirements. Many respondents, in particular larger gas traders, consider it sufficient to be able to hedge open positions via the neighbouring liquid trading point TTF.

The respondents voiced widely varying expectations regarding the economic benefit of integrating the two German market areas with the TTF. VKU, VCI/VIK, EnBW and Open Grid Europe expect the benefits to outweigh the disadvantages, while FNB-Gas, Uniper, 8KU and PEGAS expect the disadvantages to outweigh the benefits. The remaining respondents had no clearly expressed expectations but showed a more critical tendency. Many pointed out that there should be no deterioration in particular in the capacity situation for DSOs. All the respondents agree that a detailed cost-benefit analysis is required before any market integration measures are taken.

The market players also had widely varying answers to the question of what action was needed to respond to the lack of L-gas trading liquidity. EnBW stated that the Bundesnetzagentur had abandoned the best instrument to increase L-gas trading liquidity, namely abolishing the conversion charge in favour of a levy or contribution. Such a levy had, it said, been a major contributing factor in the development of the market area in the Netherlands. GEODE and BDEW generally see the need for discussion as regards L-gas liquidity. VKU and Thüga are in favour of separating the L-gas areas from the rest of the market areas and attaching them to the TTF. By contrast, Uniper, RWE Supply & Trading and FNB-Gas, together with GASPOOL and NCG, expressly object to the proposed model. EFET and PEGAS are also more critical than not of the proposal.

The respondents also differed in their assessment of the internal measures proposed in the WECOM report to improve the situation in the German wholesale market. None of the proposed measures is, however, expected to have a decisive impact on liquidity in the medium and long-term markets as required in GTM II. The responses to the proposals to restrict the linking of balancing groups and introduce obligations for market makers and for conducting gas auctions were largely negative. The responses to the proposals to create within-day gas transport capacity products and improve transparency in respect of overall transport costs and aggregated gas consumption and system status in the market areas were largely positive.
2. The Bundesnetzagentur’s conclusions

The Bundesnetzagentur finds that the market areas in Germany have developed well in recent years. It agrees that trading in medium and long-term products in the two German market areas does not correspond to the requirements for a liquid trading point set out in GTM II and that there is generally further potential for development. The Bundesnetzagentur also believes, however, that currently only the TTF meets the GTM II criteria. The reason for this, in the Bundesnetzagentur’s view, is that the TTF market area served as the benchmark for the model. The Bundesnetzagentur therefore does not believe that market integration is necessarily the only conclusion to be drawn, but generally considers bottleneck-free access to the TTF (a trading point with long-term liquidity), as is currently available, to be sufficient. Various hedging options are available to the market players, especially on account of the liquid spot markets in the NCG and GASPOOL market areas, where prices strongly converge with those at the TTF.¹

Looking ahead, the Bundesnetzagentur expects full implementation of the European network code to lead to a further improvement in the linking and liquidity of the European gas markets and in turn to a further reduction in the price risks. The Bundesnetzagentur also shares the assumption of a large number of market players that at the present time the costs of market integration could exceed the benefits, especially in light of the need to adjust the regulatory framework to accommodate the different balancing systems in Germany and the Netherlands and in light of the past consolidation of market areas in Germany. Here, it has not yet been possible to completely eliminate the related capacity restrictions within the NCG and GASPOOL market areas. In this context, the WECOM report concluded that the highest theoretical capacity restriction rate would be expected if only the two German market areas were integrated. The need for measures to prevent capacity restrictions could, however, not be ruled out even if the two German market areas were integrated with the TTF.

The Bundesnetzagentur therefore at present considers the advantages of a stable regulatory framework to outweigh the possible advantages of further national or cross-border market integration. The Bundesnetzagentur does not rule out cross-border market integration, especially with the Netherlands, in the future. Precise statements about the expected advantages and disadvantages of a market integration project can, however, only be derived from a specific and detailed cost-benefit analysis based on the market integration criteria set out in the WECOM report. The Bundesnetzagentur does not, however, consider conducting such a specific cost-benefit analysis appropriate at the present time, since the European Commission’s current study – “Quo vadis EU gas market regulatory framework” – is looking at alternatives to the cross-border market integration options proposed in GTM II. The results of the “Quo vadis” study are expected at the end of 2017 and could lead to a legislative proposal from the European Commission.

The Bundesnetzagentur takes a critical view of the proposal to separate the L-gas areas from the rest of the market areas and attach them to the TTF. Although L-gas trading liquidity is lower than H-gas liquidity, in the Bundesnetzagentur’s view the proposal put forward to improve the

¹ One option is to book transport capacity and the corresponding transport of gas. Another option to hedge price risks is by trading in long-term products (e.g., futures) at the TTF: purchasing the products in advance and re-selling them at the TTF at the time of delivery and then acquiring the required gas directly in the NCG or GASPOOL spot market. There is also the possibility on the exchange of hedging market price risks between the German market areas and the TTF with a specially developed location spread product.
situation would undermine the market area conversion process. Moreover, current plans are to
end the supply of L-gas from the Netherlands to Germany as from 2030.

Finally, the Bundesnetzagentur agrees that national measures alone will not have a significant
stimulative impact on the long-term market, but anticipates a positive impact on the gas market
from the following measures:

*Option for within-day gas transport capacity booking at connection points to production, LNG
and storage facilities and end users*

The Bundesnetzagentur supports the plans of the Federal Ministry for Economic Affairs and
Energy to require gas TSOs to offer shippers within-day capacity at all entry and exit points in
their networks. In the Bundesnetzagentur's view, this measure will lead to an improvement in the
opportunities in the flexibility market for electricity and gas.

*Improved transparency concerning total cost of network access/transport*

The Bundesnetzagentur, in particular when implementing the network code on harmonised
transmission tariff structures, will work to enable shippers to understand and anticipate better
how the tariffs set for both transmission services and non-transmission services may change. As
of February 2017, gas shippers have access to the details of the revenue caps and various input
parameters and cost components to be published under section 31 of the German Incentive
Regulation Ordinance (Anreizregulierungsverordnung – ARegV). This information is available on
the Bundesnetzagentur's website at
https://www.bundesnetzagentur.de/DE/Sachgebiete/ElektrizitaetundGas/Unternehmen_Institutio
nen/Netzentgelte/Transparenz/Transparenz_node.html.

The Bundesnetzagentur can understand the market players' request for tariffs and levies to be
set well in advance to provide greater planning certainty. However, it should not be forgotten that
the more in advance tariffs and levies are set, the more difficult it is to take more recent
developments into account.

The Bundesnetzagentur will continue to ensure that gas shippers are increasingly better able to
adequately forecast developments in gas transport costs.

*Improved transparency concerning aggregated gas consumption and overall system status in
the market areas*

The Bundesnetzagentur supports measures that serve to increase the transparency of gas flows
within a market area. The Bundesnetzagentur will maintain a dialogue with TSOs, market area
managers and market participants when defining the detailed measures to ensure a balanced
consideration of the players' individual requirements.

3. Summary

Overall, the Bundesnetzagentur finds that the market areas in Germany have developed well in
recent years. Although there is generally further potential for development in respect of the
medium and long-term trading horizon, various hedging options are available to the market
players, especially on account of the liquid spot markets in the NCG and GASPOOL market
areas. At the present time, the Bundesnetzagentur therefore considers the advantages of a
stable regulatory framework to outweigh the possible advantages of further national or cross-
border market integration. The Bundesnetzagentur agrees with the market players that a specific cost-benefit analysis is essential before any market integration measures are taken. Looking forward, the Bundesnetzagentur anticipates a positive impact on the gas market in particular from the provision of within-day transport capacity and measures to strengthen transparency.