Mandating Shared Order Books without Cross-Border Capacity sets a Grave Precedent – Would we require the same of other types of marketplaces?

In its proposal of Electricity Market Design reform of March 2023 , the EU Commission has introduced an article forcing spot Power Exchanges (NEMOs) to share Order Books at all times, even when no cross-border transmission capacities are available (new art. 7, 2019/943 EU Regulation). This would set a perilous precedent for all type of marketplaces and platforms across the whole European economy. To understand why this proposal is nonsense, let's start with an analogy with Streaming Platforms.

What would this mean for Streaming Platforms and viewers?

Let's consider for example Netflix and Amazon Prime. Both offer to their subscribing customers a dedicated platform with some differentiated content: size of the library (number of TV shows and movies), the quality of movies, subtitles, targeted content per country/region etc.). Online comparison[1] shows for instance that compared to Netflix, Amazon Prime has a smaller library but may offer more recent movies and TV shows. Netflix, on the other hand, generally offers TV shows and movies that are over a year old, but has a much larger library of shows and movies than Amazon, including TV shows they produce on their own. Clients currently have the choice between two differentiated services at various prices.

Now let’s imagine that EU authorities force Streaming Platforms to merge their content: Netflix and Amazon would both have to offer each other’s content on their own platform.
At first this new EU regulation would be welcomed by all customers. Indeed, for the same price, Netflix users would get a few additional movies, and the users of Amazon would get many more movies! So, the day after the EU regulation enters into force, all customers are pretty happy and spend a nice evening…

Then, a few weeks or months later, Netflix users start to notice that their favorite TV-shows that used to be produced by Netflix are cancelled one after the others and that no new content makes its way onto the platform. Also, their platform navigation is becoming less fluid.

Why?

- ⇒ The free access of competitors to Netflix content has allowed those to offer access to Netflix library and services at a lower price.
- ⇒ Consequently, Netflix’ users have found it a good idea to cancel their Netflix subscription while continuing to benefit from the access to Netflix contents via other platforms.
- ⇒ Netflix has been forced to react by decreasing the price of their subscription.
- ⇒ The reduced revenues of Netflix have forced them to make strategic investment choices and they had to reduce investing in the production of new TV shows, the purchase of new movies and their IT systems.

Streaming Platforms would have no incentives anymore to innovate and invest to improve the quality of their platforms, the range of their content catalogues, the attractiveness of their subscription prices etc.

Such lack of innovation incentive for Streaming Platforms will adversely impact not only competition between platforms – via loss of rivalry and of dynamic competition – but also users.

Indeed, after having dreamed to have access to the full range of movies and TV shows at low cost, time for disenchantment would come for users extremely fast and, bored by frozen content catalogues, they would start regretting the old times when new content was added on a regular basis.

Most probably, the convergence of the rival platforms’ contents would lead to their merger, as there would be no rationale anymore for competition. The users would be left out with one platform and no choice anymore. No competition anymore but one streaming monopoly, which would have little incentives to innovate, to invest, to offer competitive prices, all this to the detriment of the users.

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[1] https://www.diffen.com/difference/Netflix_vs_Prime_Video

What would this mean for the power trading sector?

Spot Power Exchanges invest and compete offering various products, building customer base and liquidity over years, like Netflix and Amazon do. If spot Power Exchanges are forced to share the assets they have built on the merits - in that case not TV shows and movies but liquidity of orders for trading electricity, as reflected in their Order Book - they will be constrained to stop investing to enrich their services and offer. Liquidity is the result of dynamic competition between exchanges, in particular through investments, innovations, and differentiation strategies. The suggested Electricity Market Design reform would deny power exchanges any protection and incentive for entrepreneurship, instead inciting them to sit back and rely on competitors' investments and innovations. Indeed, such investments will ultimately only benefit their competitors. As in the Streaming Platforms example, such a mandatory sharing of asset could be understandably welcomed by some users in the short term, but detrimental to all of them in the long term.

Currently, spot Power Exchanges are mandated by the CACM Regulation to share their Order Books when there is cross-border capacity[2] at the expense of dynamic competition between power exchanges: this is a unique exception in the exchange industry worldwide, be it for commodities, stocks, bonds (or any other exchange traded product) and an exception that is only justified by the fact that cross-border transmission capacity can be considered a natural monopoly and therefore access to it needs to be regulated to optimize its usage and facilitate cross border trade. This exception has always been fully acknowledged by EPEX SPOT. That being said, this exception should not let policymakers and stakeholders lose sight of what normal competition looks like, i.e. with no market interference such as the sharing of assets.

The EU Commission, ACER, NRAs, energy stakeholders, and now the EU legislator seized by the Commission's proposal for an Electricity Market Design reform, should think twice about the deep implications that a mandatory sharing of spot Power Exchanges liquidity assets outside the periods of available cross-border transmission capacity (therefore without any economic justification) could have on the energy and other industries, be it digital platforms, commodities marketplaces, or stocks exchanges. This would constitute a change of market paradigm and would set a serious precedent that will ultimately be detrimental to consumers.

For the power market specifically, in the midst of the worst energy crisis Europe has gone through, mandating to share Order Books without cross-border capacity would hamper innovations in new short & long term products crucially needed for the energy transition and the integration of significant renewable capacity. Such innovations and investments include capacity markets for the security of supply, hedging products in the short-term markets to address volatility and the associated flexibility needs in the day-ahead & intraday markets for the balancing of the power grid but also local markets to alleviate congestions with localized flexibility sources at different voltage levels. If the innovative trading solutions and products developed by a spot Power Exchange to address the energy transition are simply passed on to its competitors, both that first innovator and follow-on competitors will be discouraged from investing in future developments, to the ultimate detriment of electricity consumers.

Paris, 8 May 2023

[2] Between the intraday cross-zonal gate opening time ("IDCZGOT") and the intraday cross-zonal gate closure time ("IDCZGCT") as defined in the ACER decision No 04/2018 on the Intraday Cross-Zonal Gate Opening and Gate Closure Times.