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**Hub development and regional balancing markets
Focus on the SSE region**

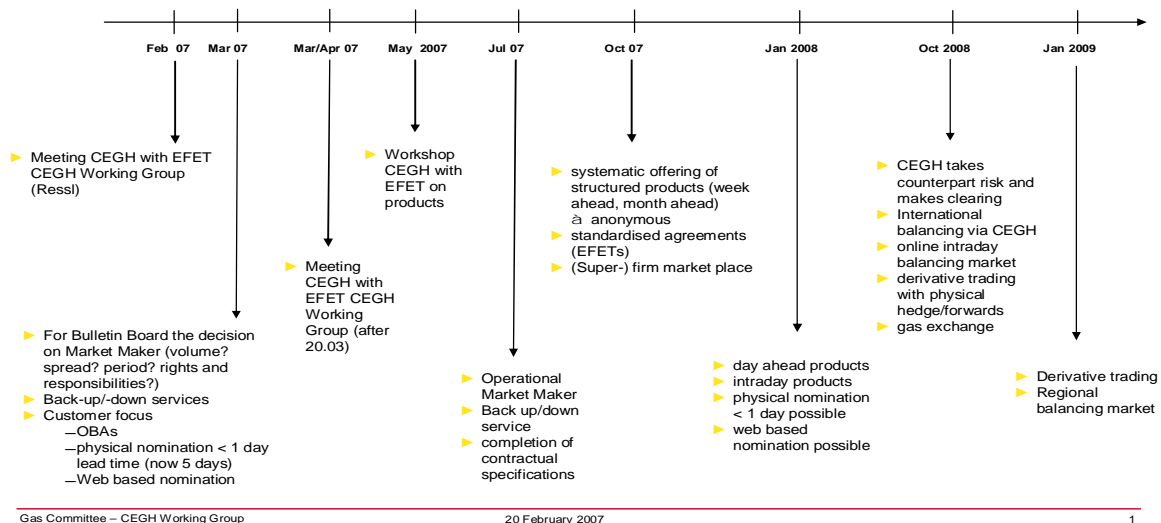
Hubs play a crucial role as platforms for physical and/or financial transactions of natural gas and are vital for the functioning of natural gas markets. The efficient evolution of physical trading at hubs located between different transit routes implies convenient transportation to and from hub locations to create a foundation for liquid trading. EFET welcome the readiness of regulators to support Hub development within the SSE region.

Nevertheless it is worth pointing out that by creating regional markets the operational and physical issues have to be taken into account rather than follow regional borders as defined in the gas regional initiative (the whole SSE region). We believe that in the SSE region it is too early to define the optimum geographical extent of gas hubs, but as a first step we should encourage the development and expansion of existing trading points that have the potential to develop into major gas hubs.

Therefore we propose to focus on the development of a national hub – PSV - for the Italian gas market and a regional hub – CEGH – covering Austrian, Hungarian, Czech, Slovakian, and maybe Slovenian gas market. For the different interconnected networks (balancing zones) standardised agreements and procedures should be put in place between the TSOs in order to facilitate gas trade.

At the last meeting in Milan a timeline was presented for CEGH development. This ambitious plan had been prepared by the EFET CEGH ad hoc development group in accordance with CEGH (see below). There is a slight delay due to the postponed workshop on products and services which should be offered by CEGH; this came about because of the sudden and important agreement of Gazprom to join the efforts to create CEGH. The workshop will now take place near the end of July.

Timeline – CEGH Development



EFET recapitulated requirements and preconditions which have to be in place in order to facilitate liquid trading. These are:

- Access to transportation capacity in and out of the hub is ensured.
- Capacity availability and utilization rates should be published in accordance with the Gas Transmission Regulation 1775/2005/EC.
- Capacity availability should be maximized through secondary trading of capacity, use-it-or-lose-it, and sales of interruptible capacity.
- Backup / back down services to ensure hub firmness and transparent cash out price for settlement of shortfall or over delivered quantities.
- Harmonisation of OBAs between different TSOs whose networks link to Baumgarten is essential for enhancement of offered services.
- Harmonisation of standardised products (day/week/month ahead) and gas sales agreements throughout the regional market (GRI) is of utmost importance.
- Transparency on prices.
- Stable regulatory framework that takes reality into account. A non-discriminatory access to system use and flexibility services as well as a market based balancing system on a regional level is furthermore necessary.

Overall, for the development of a fully liquid hub, the ability to access and exit s virtual trading point via any of the pipelines in the area needs to be fully incorporated in to the hub design (e.g. as in an entry/exit system).

It seems to us that most preconditions are still lacking in the case of CEGH. Therefore we call on the relevant parties (TSOs, hub, regulators) to support this initiative and to solve the outstanding problems so that further delay to the timeline does not occur.

EFET recognises that the Madrid Forum has set a goal of market-based balancing throughout the EU. This requires trading hubs to develop in local markets, and that the markets must be of sufficient size to support liquidity at the hub. We therefore call on the authorities and TSOs to take practical steps to help advance the creation of two principal hubs in the SSE region offering balancing services based on the expansion and consolidation of CEGH and PSV.¹

Since the last meeting in Milan a meeting of a Task Force on development of PSV took place. The Task Force was established with some interested parties in order to foster development of PSV to become a more effective trading hub and balancing market.

The next meeting of the Task Force on PSV should concentrate on users' priorities for further development of PSV as a balancing point and setting up of a timeline for particular steps for achieving these priorities.

¹ Access to physical interconnection between hubs (and balancing markets) remains a critical issue that should continue to be dealt with in parallel by the GRI

Appendix

Some practical features of a balancing market

- Improves liquidity at the hub by adding a major counterparty in the form of the TSO
- It requires flexibility to be made available - usually this requires some form of commitment from the historical player who holds most of the flexibility required to balance the market
- Costs of balancing the system should be reduced when the market is liquid - the TSO can acquire flexibility as and when it needs it, rather than contract for an unknown amount on a yearly basis, which then reduces the available supply of flexibility throughout the year.
- Increasing the number of transparent transactions leads to the development of a more reliable price for imbalance cash out and/or settlement of contractual shortfall
- It can start as a mechanism where the TSO is the only buyer/seller of gas then evolve into a commodity market where all shippers can participate.