

OPINION on position limits on EEX French Power Base contracts

I. Introduction and legal basis

1. On 2 February 2021, the European Securities and Markets Authority (ESMA) considered that sufficient information was received to assess a notification from the Federal Financial Supervisory Authority (“BaFin”) under Article 57(5) of Directive 2014/65/EU on markets in financial instruments¹ (“MiFID II”). The notification is regarding the exact position limits BaFin intends to set for the French Power Base Futures and Options commodity contracts in accordance with the methodology for calculation established in Commission Delegated Regulation (EU) 2017/591 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the application of position limits in commodity derivatives² (“RTS 21”) and taking into account the factors referred to in Article 57(3) of MiFID II.
2. ESMA’s competence to deliver an opinion is based on Article 57(5) of MiFID II. In accordance with Article 44(1) of Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority)³ (“ESMA Regulation”), the Board of Supervisors has adopted this opinion.
3. On 23 May 2019, ESMA issued a first opinion regarding the exact position limits BaFin intended to set for the French Power Base Futures and Options commodity contracts. The position limits considered by BaFin in October 2017 were 25,222,306 MWh for the spot month limit and 119,518,652 MWh for the other months’ limit. In this opinion, ESMA concluded that the position limits considered by BaFin complied with the methodology established in RTS 21 and were consistent with the objectives of Article 57 of MiFID II.
4. According to Article 57(4) of MiFID II, a competent authority shall review position limits where there is a significant change in deliverable supply or open interest, or any other significant change on the market, and reset the position limits. Whereas the open interest underpinning the position limits set out in BaFin’s initial submission had been calculated based on the information provided by the trading venue, BaFin has now calculated again the open interest based on position reporting data. Consequently, BaFin considered that since there had been a significant decrease in the open interest compared to its initial submission, the position limit

¹ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

² Commission Delegated Regulation (EU) 2017/591 of 1.12.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the application of position limits commodity derivatives (OJ L 87, 31.3.2017, p. 479).

³ Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15. 12.2010, p. 84).

had to be reset for both the spot month limit and the other months' limit. ESMA understands that the new position limits will apply after the date of the issuance of ESMA opinion on those revised position limits. The new limits are replacing the previous position limits as determined by BaFin from the date of their application.

5. In the opinion herewith, ESMA is assessing whether the new position limits BaFin has set for the French Power Base Futures and Options commodity contracts comply with the methodology established in RTS 21 and are consistent with the objectives of Article 57 of MiFID II.

II. Contract classification

Commodity base product: energy (NRGY)

Commodity sub product: electricity (ELEC)

Commodity further sub product: base load (BSLD)

Name of trading venue: European Energy Exchange

MIC: XEEE

Venue product codes: F7B, O7B

III. Market description

6. The French Power Base Future is a derivative contract referring to the average power spot market price of future delivery periods of the French market area. The contract can be either physically delivered or cash settled.
7. Electricity is a grid-bound commodity, where delivery takes place through meshed transmission system grids. This means that market participants have no control over the actual destination of the generated power. Electricity can only be stored to a minimal extent, i.e. by means of battery storage. In fact, electricity is still widely considered as a non-storable commodity. There are also some seasonal effects in the electricity market. Due to heating demand in winter or higher demand in summer due to air-conditioning, electricity generation tends to be higher in times of climatic extremes. However, such seasonal effects are rather small.
8. The French electricity market is relatively concentrated and characterised by the dominant position of Électricité de France (EDF) which is the country's main electricity generation company with a market share of 82%⁴. EDF is substantially owned by the French Government, with around 85% shares in government hands. The wholesale market in France has limited liquidity with the majority of trading taking place OTC.

⁴ https://ec.europa.eu/eurostat/statistics-explained/index.php/Electricity_market_indicators

9. The underlying of the French Power Base Contract is the delivery or acceptance of delivery of French electricity with a constant output of 1 MW during the delivery time (00:00 until 24:00) on every day of the week during the delivery period. The possible delivery periods for this contract are: day, weekend, week, month, quarter and year.
10. With respect to French Power Base futures contracts, at maximum, the following maturities can be traded: for “Day Futures” the respective next 34 days; for “Weekend Futures” the respective next 5 weekends; for “Week Futures” the current and the next 4 weeks; for “Month Futures” the current and the next 6 months; for “Quarter Futures” the respective next 7 full quarters; and for “Year Futures” the respective next 6 full years.
11. EEX offers trading in options on the French Base Future (Month, Quarter, Year). Regardless of the different maturities, the corresponding futures position of the underlying asset is booked upon exercising of the option.
12. With respect to options on the French Power Base Future, at maximum, the following maturities can be traded: the next 5 delivery months, the next 2 delivery quarters, the next 2 delivery years.

IV. Proposed limit and rationale

Spot month position limit

Deliverable supply

13. Deliverable supply amounts to 101,759,993 MWh.
14. The deliverable supply has been calculated based on statistics provided by ENTSO-E (European Network of Transmission System Operators for Electricity). It is composed of the domestic Net Generating Capacity (NGC) of France as displayed on the Website of ENTSO-E for the year 2020 and the average yearly import capacities for 2020. These values of ENTSO-E have been converted from yearly MW to MWh. The overall value was then divided by the factor of 12 in order to align the deliverable supply to the time frame of one calendar month for the spot month period.

Spot month position limit

15. The spot month limit has been set at 20,351,999 MWh, which represents 20% of the deliverable supply. The spot month limit applies to the French Power Base Futures and Options. It includes daily contracts, weekend contracts, weekly contracts and one monthly contract.

Spot month position limit rationale

16. The baseline figure for the spot month limit amounts to 25% of the deliverable supply, i.e. 25,439,998 MWh, as required by Article 9(1) of RTS 21. There are no financial counterparties acting as a market maker. Thus, the limit is to be set within a range of 5% - 50%.
17. The following factors were considered relevant for adjusting the limit downwards:
 - deliverable supply under Article 17 of RTS 21: underlying power for France is also used as the deliverable supply for other commodity derivatives in the EU, for instance at ICE Endex;
 - characteristic of market of the underlying: with EDF there is one vertically integrated key market player that dominates parts of the underlying power spot market which is to be taken into account under Article 20(2)(d) and (e) of RTS 21.
18. In considering the volatility in the contract, as required by Article 21 of RTS 21, there has been some variation in the price of the commodity derivative but the BaFin has not found evidence that this is excessive or that lower position limits would reduce volatility.
19. Based on the above, BaFin considered that setting the spot month limit at 20% of the deliverable supply was adequate, which translates into a spot month limit of 20,351,999 MWh.

Other months' position limit

Open interest

20. Open interest amounts to 63,220,951 MWh. Whereas the open interest of the previous position limit was calculated on basis of information from the trading venue, the open interest for the position limit at hand has been calculated on basis of the reports of daily net positions submitted to BaFin pursuant to Article 58 MiFID II.
21. The daily net positions have been added up and divided by the factor 2 ("net approach"). The number provided is the average size of daily open interest calculated on basis of daily reports from December 2019 till end of November 2020. Option positions have already been reported to BaFin delta adjusted.

Other months' position limit

22. The other months' limit has been set at 15,805,238 MWh, which constitutes 25% of the reference amount. The other months' limit applies to the French Power Base Futures and Options. It includes monthly, quarterly and yearly contracts.

Other months' position limit rationale

23. The baseline figure for the other months limit amounts to 25% of open interest, i.e. 15,805,238 MWh. The following factor was considered relevant for adjusting the baseline upwards:

- maturity, under Article 16(2) of RTS 21: upward adjustment due to large number of separate expiries (seven monthly contracts, seven quarterly contracts and six yearly contracts; in contrast to daily and weekly contracts, monthly, quarterly and yearly contracts are traded in significant volumes).

24. The following factor was considered relevant for adjusting the limit downwards:

- characteristic of market of the underlying: with EDF there is one vertically integrated key market player that dominates parts of the underlying power market which is to be taken into account under Article 20(2)(d) and (e) of RTS 21.

25. In considering the volatility in the contract, as required by Article 21 of RTS 21, there has been some variation in the price of the commodity derivative but the BaFin has not found evidence that this is excessive or that lower position limits would reduce volatility.

26. Based on the above, BaFin considered appropriate to set the other months' limit at 25% of open interest, i.e. to 15,805,238 MWh, as different factors outweigh each other.

V. ESMA's Assessment

27. This Opinion concerns positions held in French Power Base contracts.

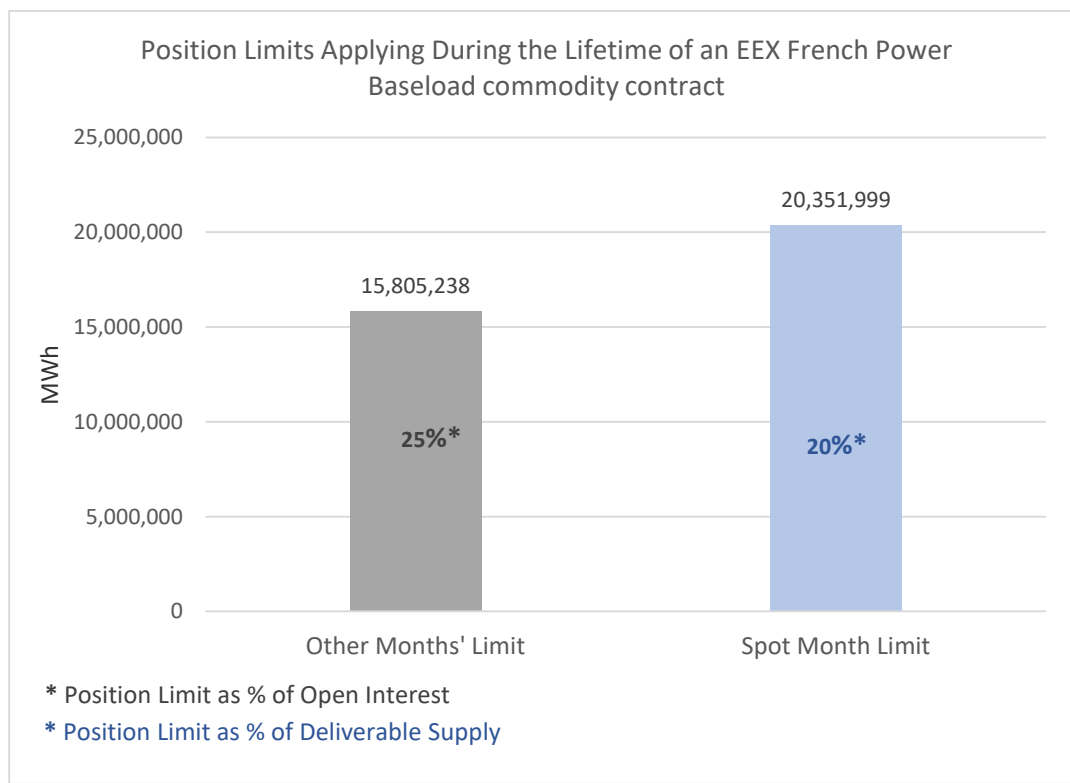
28. ESMA has performed the assessment based on the information provided by BaFin.

29. For the purposes of this Opinion, ESMA has assessed the compatibility of the intended position limits with the objectives of Article 57(1) of MiFID II and with the methodology for calculation of position limits established in RTS 21, in accordance with Article 57(3) of MiFID II.

30. The overall open interest for the contract amounts to 63,220,951 MWh, which translates into 87,807 lots. Since the number of investment firms acting as market makers in this contract is less than three, the range for the limit is from 5% to 50% of the reference amount, according to Article 19(2) of RTS 21.

Compatibility with the methodology for calculation of position limits established in RTS 21 in accordance with Article 57(3) of MiFID II

31. BaFin has set one position limit for the spot month and another position limit for the other months.



Spot month position limit

32. The calculation of the deliverable supply is based on the domestic Net Generating Capacity (NGC) of France for the year 2020 and the average import capacity in relation to neighbouring countries in 2020. The source of data used to calculate deliverable supply (ENTSO-e statistics) ensures publicly available figures that are consistent at the European level.
33. ESMA considers that this methodology to calculate deliverable supply is consistent with Article 10(1) of RTS 21 that sets out that deliverable supply shall be calculated “by identifying the quantity of the underlying commodity that can be used to fulfil the delivery requirements of the commodity derivative.”
34. The monthly deliverable supply figure has been calculated by converting the capacity (expressed in MW) to MWh per month.
35. This approach is consistent with Article 10(2) of RTS 21, which sets out that “Competent authorities shall determine the deliverable supply [...] by reference to the average monthly amount of the underlying commodity available for delivery over the one-year period immediately preceding the determination”.
36. ESMA agrees with the downwards adjustment factors under Article 17, due to deliverable supply being used as well for other contracts, and under Article 20(2)(d) and (e) given the

characteristic of the market with a dominant position of the main market player. Overall, setting the limit at the level of 20% of the baseline seems adequate.

Other months' position limit

37. The open interest has been calculated by BaFin based on position reporting data where the daily net positions have been added up and divided by the factor 2 ("net approach"). The number provided is the average size of daily open interest from December 2019 till end of November 2020.

38. ESMA considers that such calculation of open interest by the competent authority provides the most accurate and reliable figure and promotes convergence in the setting of position limits by competent authorities. ESMA is also of the view that taking the period from December 2019 to November 2020 as a reference is sensible in this case as an average for a longer period of time gives a more stable measure of open interest and considers such approach consistent with Article 12 of RTS 21.

39. The other months' limit has been set at the level of 25% of the baseline, due to the fact that the upwards and downwards adjustment factors balance each other. ESMA agrees with the upwards adjustment factors under Article 16(2) due to large number of separate expiries, and with the adjustment under Article 20(2)(d) and (e) given the dominant position of one market player. Overall, setting the limit at the level of 25% of the baseline seems adequate.

40. Consequently, these position limits have been set following the methodology established by RTS 21.

Compatibility with the objectives of Article 57(1) of MiFID II

41. ESMA has found no evidence indicating that the proposed position limits are not consistent with the objectives of preventing market abuse and supporting orderly pricing and settlement conditions established in Article 57(1) of MiFID II.

42. Overall, the position limit set for the spot month and the other months appear to achieve a reasonable balance between the need to prevent market abuse and to ensure orderly pricing and orderly settlement, while also ensuring that the development of commercial activities in the underlying market and the liquidity of the French Power Base contract are not hampered.

43. However, ESMA notes that the spot month limit is more than two times the total spot month open interest for this contract (9,118,644 MWh for the period December 2019 – November 2020). ESMA is of the view that the application of the methodology set in RTS 21 needs to fulfil the objectives set in Article 57(1) MiFID II. ESMA is therefore of the opinion that the maximum level of open interest in the spot month needs to be taken into consideration when setting the spot month position limit, in addition to the amount of deliverable supply. ESMA therefore recommends the competent authority to monitor the effect of this limit on the market and to revise it if necessary.



VI. Conclusion

44. Based on all the considerations and analysis presented above, it is ESMA's opinion that the spot month position limit does comply with the methodology established in RTS 21 and is consistent with the objectives of Article 57 of MiFID II. The other months' position limit does comply with the methodology established in RTS 21 and is consistent with the objectives of Article 57 of MiFID II.

Done at Paris,

Steven Maijoor

Chair

For the Board of Supervisors