



Webinar Trading in the Japanese market - FAQ

Question 1: Is it possible to sell out in the spot market overseas even though there is no power outage? In other words, I think the problem is that the price is determined by the purchase price.?

Answer: The day-ahead spot markets in Europe use similar auction mechanisms as the JEPX in Japan. To our knowledge, it has never happened that the market did not clear. So, there has always been a match between supply and demand. In a situation with a tight supply-demand balance, capacity with (very) high marginal costs will also be offered in the market. This can come for example from old or very inefficient power plants that do not produce power under normal conditions. At the same time, in such situations demand appears to be more responsive. Especially large industrial companies with flexible power demand find ways to reduce their demand and financially benefit from the high power prices. They either trade in the market themselves and sell power to the market that they previously bought in the forward market. Or they have an arrangement with their supplier, which is permitted to reduce their demand in specific circumstances. Finally, there is more and more flexibility from smaller consumers and producers who can steer their electricity consumption or production profile.

Question 2: Could you please explain bit more about the EEX Japan power trading. Is it physical spot trading? Or forward trading? How does it really work?

Answer: EEX is offering a clearing service to trade Japanese power futures. This is forward trading, not spot trading. The futures are financially settled against the spot price (JEPX). A somewhat special part of the EEX futures trading is that the trade itself is not done on the EEX platform, but directly with a counterparty (bilaterally), for example via a broker. EEX essentially takes care that a registered contract is correctly financially settled. It also takes over the credit risk via its clearing house¹. If you would like to know more about the trading of forwards, futures, swaps or other contracts in power markets, and how they are used for risk management, we can provide further explanation or training.

Question 3: In Europe, regarding the electric trading, has option trade started or not?

Answer: Yes, power options can be traded in the European market. Compared to the market in forwards and futures, the option market is relatively small, though the total size is still significant. As an example, last year 80 TWh of options were traded across Europe at the EEX, one of the main exchanges in Europe². Options are also traded bilaterally, i.e. directly between counterparties, often via brokers. Apart from power options, it is also possible to trade spark or dark spread options. The underlying of these options is the spread (difference) between the power price and the underlying fuel (the fuel is gas in a spark spread and the fuel is coal in a dark spread). Dark and spark spread options are used to hedge exposures of power plants. For an option market to develop it is required to have an active and liquid forward/future market. The reason is that options are typically hedged with the underlying, which is a forward/future contract.

If you would like to know more about options and the hedging or valuation of power stations, we can provide further information or training – info@kyos.com

¹ <https://www.eex.com/en/markets/power-derivatives-market/japanese-power-futures>

² https://www.eex.com/fileadmin/Global/News/EEX/EEX_Press_Release/20210119_EEX_Group_Annual_Volume_Report.pdf