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Dutch fret about prized TTF as price cap looms

The Netherlands is fiercely opposed to the EU's TTF price cap proposal, saying it could harm security of supply and financial stability, as it also worries about the measure destroying liquidity on the benchmark European gas index.

By Karolin Schaps

At the ministry of energy in the Netherlands, there are concerns that EU-wide efforts to fix one crisis may create another – particularly for the country's TTF trading hub that emerged 20 years ago to become the benchmark for pricing gas in Europe.

The European Commission last month proposed to temporarily cap the Dutch front-month TTF gas contract at EUR 275/MWh. The measure, designed to rein in excessively high energy prices for end consumers, will be triggered when the front-month TTF contract trades above the cap level for two weeks and when the European Gas Spot Index (Egsi) is at least EUR 58/MWh higher than a reference LNG price for 10 consecutive trading days. European energy ministers are set to decide on whether to implement the cap in mid-December.

Traditionally defenders of the liberal market economy, the Dutch are fiercely opposed to the measure they fear will result in unintended and severe consequences. "The adoption of this measure, even if it is never triggered, poses serious risks for energy and financial markets, potentially harming security of supply and financial stability," a Dutch energy ministry spokesman tells Montel. Parts of the gas trading market will lose liquidity or could even stop functioning, he warns. "If we are not careful, we will replace the current crisis with an even bigger one."

Intercontinental Exchange (ICE), which facilitates the bulk of exchange-based trading for TTF contracts, warns that an additional USD 33bn in margin requirements will be needed if the cap is implemented – quantifying the potential threat to financial stability at a time when the energy market is already under severe capital strain.

The potential consequences for financial stability have also caught the attention of the European Central Bank, which has said it is assessing the implications of the price cap measure for financial stability. Beyond this, the bank is also concerned about gas traders moving more of their business from exchanges to the less transparent over-the-counter (OTC) market, which is not targeted by the price cap. Lower margin requirements ➤

in the bilaterally-traded market have already given reason for moving more trading to the OTC market. However, the ECB warns that more non-centrally cleared trading will increase risks for counterparties and ultimately for the financial system.

Others have expressed similar concerns. "There are significant unintended negative consequences and large risks for financial stability and security of supply as a consequence of price interventions in TTF, possibly with long-lasting damage," says Bert den Ouden, founder and former CEO of Dutch exchange APX and founder of Europex, an association of European energy exchanges.

Next to capping the TTF front-month contract, the European Commission has also proposed to develop a new LNG benchmark. It argues that TTF indexation used to determine long-term LNG supply pricing no longer accurately reflects the price of LNG transactions in Europe. This is a blow to the Dutch TTF hub. The huge growth of the LNG market in recent years has been one of the main factors driving liquidity on the Dutch TTF hub as traders from across the globe use it as a benchmark for pricing LNG exports to Europe.

But the recent gas price volatility and the threat of market intervention has already affected the TTF's standing as an LNG pricing benchmark. "We see some indication that because of the turmoil, people outside of Europe are starting to think it's better to look at Henry Hub [in the US] or oil indexation," says Erik Rakhou, associate director at Boston Consulting Group and gas and hydrogen expert.

The EU's energy regulatory agency Acer is working on introducing the new LNG benchmark by 31 March, based on daily price assessments which traders can use to inform their LNG pricing. The new benchmark's success will very much depend on whether market participants will apply it. One option is to make the new benchmark a requirement in LNG procured through the newly established European gas purchasing consortium. The joint initiative aims to pool European gas buying to allow all EU member states equal access to gas supply deals and to enhance transparency in concluding long-term gas purchase agreements.

"Over the years we have observed that emerging benchmarks have only reinforced the importance of an anchor price indicator such as TTF. That may also be valid for the present developments in the LNG market and its indirect connections to TTF," says Paul van Son, honorary president of the European Federation of Energy Traders, which he co-founded in 1999.

Dutch gas traders have brushed off the impact of the price cap on day-to-day activities, with some saying a ceiling of EUR 275/MWh is no more than just a far-fetched cap and others calling it ineffective due to the conditions attached. Others see the mechanism as faulty and as not addressing the underlying issue of gas supply shortages which have been supporting prices over the past year. Even prior to Russia's invasion of Ukraine in February, which exacerbated the TTF price rally, the gas market was tight and reacting nervously to supply limitations. "The real problem is not the market; it is scarcity which pushed up prices. Therefore, these measures of a price cap and a new benchmark are fighting the wrong problem," says Hans van Cleef, senior energy economist at ABN Amro.

Ultimately, the EU executive wants to act to reduce energy prices for Europe's end consumers and to help stem inflationary pressures on the bloc's economy. Its proposal to intervene in the wholesale gas market has split opinions among member states and ministers are yet to decide a way forward. "Price caps and subsidies distract from the fact that we are at war economically with Putin, who uses gas and food as weapons," says Rob de Wijk, professor of international relations and security at Leiden University and founder of The Hague Center for Strategic Studies. ■