

Prof. R. Vaidyanathan

Professor of Finance. IIM Bangalore[Retired]

25th September 2023

To:

The Chairperson

Central Electricity Regulatory Commission (CERC)

3rd Floor, Chanderlok Building,

36, Janpath, New Delhi- 110001

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Dear Shri Jishnu Barua

Subject: Comments on Staff Paper on Market Coupling - Reg

I am former professor of Finance at IIM Bangalore and a Fellow of ICSSR-Visiting Faculty at various universities in USA/UK. I had privilege of being in various committees of regulators like SEBI/RBI/IRDA/PFRDA. I am also on the board of many corporates and ID on IGX Board. I have been also attending economic advisory committee meeting of the Prime Minister. Energy Market is my interest area. The views expressed here are my personal views and does not represent that of any organisation I am associated with.

I have gone through the staff paper issued by the Hon'ble Commission to introduce market coupling of power exchanges. In my view, in the current context and market structure, such proposal will not yield any gains. In the staff papers honourable commission has elaborated example of market coupling done among the European countries where markets operating in different countries were coupled to take advantage of diversity demand and supply and also for optimum utilisation of inter country transmission network. Whereas, in the staff paper commission has proposed coupling of different exchanges operating with same Indian geography.

It is a common practise to have multiple stock exchange/commodity exchanges/power exchanges in same geography and with skewed market share among the exchanges, but I have not come across any case of market coupling among them. We have NSE with more than 90% market share operating with BSE, but SEBI has not considered any market coupling among them. Similarly, is the case between MCX and NCDX. There are many more examples in other countries. In case of electricity also there are two exchanges operating in UK without market coupling. The proposal of market coupling of Indian power exchange is counterproductive and not being supported by any economic theory.

The market coupler, as it is currently envisaged, will take over the price discovery function from the exchanges. There is no precedence to believe that this will lead to better price discovery. On the contrary, such a move will remove the agency of the PX's and reduce it to a mere trading desk since bids would be forwarded to the market coupler who would then establish the market-clearing price.

The market coupler in its current proposal threatens redundancy of investment done in products and algorithms by the PXs. The incentive that is required for investors to invest in a PX may be curtailed, leading to lack of product and innovation. If this price-discovery is curtailed, PX will not show interest in developing the market which will ultimately affect the liquidity in the market and the prices discovered will be out of sync with real demand-supply equation on the ground, leading to social-welfare losses, hurting affordability. This will negatively affect the development of market which only constitutes around 7% of the overall transactions and is still in an early stage of evolution.

There is little evidence to back the role of the market coupler in enhancing competitiveness in this market. Rather if GRID India become the market coupler it may lead to conflict of interest with both grid operations & market operations vested in one single entity. Besides, the GRID India will have no incentives to assume any business risks or become customer responsive or develop the power market. The need of the hour is therefore to identify structural factors impeding the market and work towards removal of the same rather than disrupting the existing market which is working efficiently during last 15 years. It is important that the regulatory framework should enable further competition amongst the private power exchanges to extract the best out of which will eventually benefit both market and consumers. On the contrary the proposed market coupling will reduce the effective competition amongst

the power exchanges. Instead of competition and innovation in the market, market coupling will promote free rider problem that may lead to emergence of many non-serious fly by night operators at the cost of incumbent power exchanges.

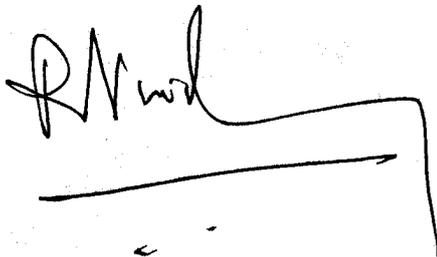
To ensure robust markets, there is a need to consider a phased, calibrated approach focusing on institution- building. A strong market is in the interests of everyone. The power exchanges through their standardized products and efficient price discovery have contributed to whatever growth has been achieved in the power market. There is a need to further strengthen & nurture the existing market mechanism rather than disrupting it through market coupling. Market coupling will take away the price discovery function of power exchanges and make them meagre bid collecting agencies. This may also create regulatory uncertainty for the sector and affect the investor sentiments in the long run. Equally important to consider all transactions through exchanges as in the case of other markets like shares etc. This will increase the role of exchanges and also make markets more efficient

While the above submission revolves around the need to have competing power exchanges instead of a market coupling operator, I request the Commission to bring out comprehensive study on the market issues for a complete view on the market design aspects and take concrete measures to increase the liquidity in market, which in turn can provide definite benefits to the market participants.

With Warm regards

Yours sincerely

Prof.R. Vaidyanathan

A handwritten signature in black ink, appearing to read 'R. Vaidyanathan', is written above a horizontal line that ends in a right-angle turn.

Copy To:

The Secretary,
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