

Market Surveillance by organised market places

EMIT Forum – 7 September 2018

Cosimo Campidoglio

Head of Market Monitoring Analysis & Statistics (GME)

1. GME

- *GME as an OMP*
- *Institutional role*
- *Remit compliance*

2. Principle issues in Market Monitoring

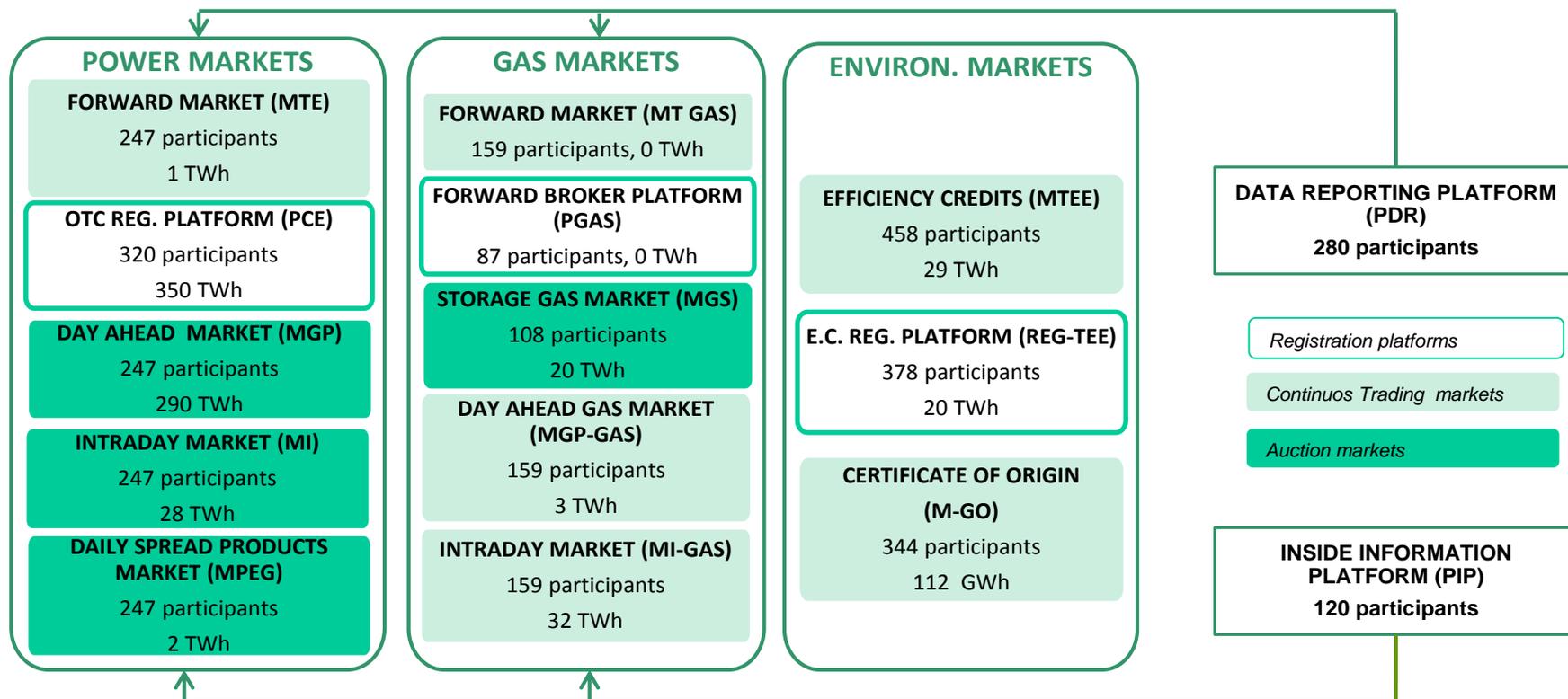
- *From theory to practice*
- *Limited insight*
- *How to monitor*
- *What to monitor*

3. Technical issues in Market Monitoring

- *Screening process*
- *Validation process*
- *Validation principles*
- *Market design*

GME as an OMP

- **State-owned company:** regulated monopoly, following directives given by Government and Energy Regulator
- **Multicommodity OMP:** power, gas and environmental markets
- **Single NEMO** for the Italian power market
- **RRM and IIP Provider** for the REMIT compliance
- **Institutional role:** it supports market monitoring function of NRA pursuant to applicable law provisions

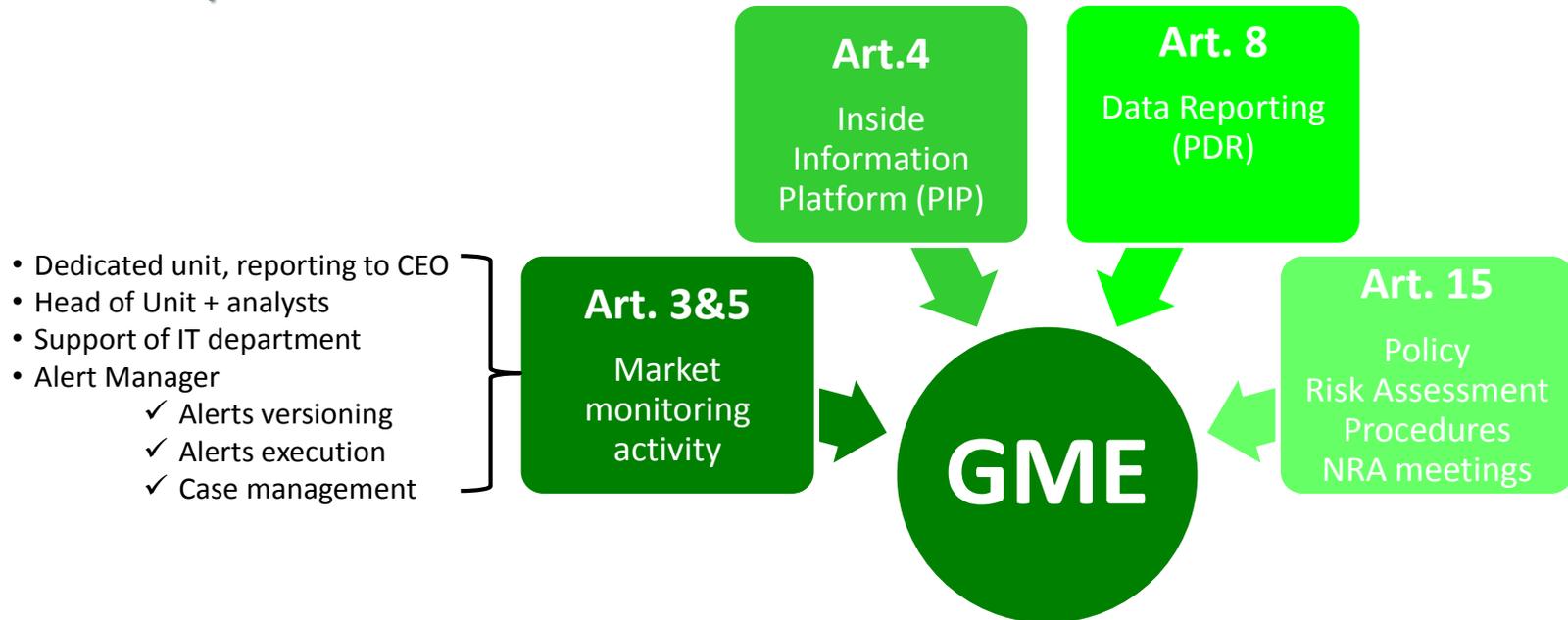


Institutional role

The monitoring activity is carried out by GME in accordance to specific legal obligations and mandates provided for European Regulations, National laws endorsed by ministerial decrees and company's internal procedures. Furthermore, GME supports the NRA in its monitoring activity, by providing data, reporting, analysis and simulations.

FRAMEWORK	GME MONITORING ACTIVITIES		
 <p>REMIT</p>	<p><i>Organization of monitoring activities in accordance to ACER Guidelines</i></p>	<p><i>Timely reporting to relevant NRAs of any reasonable suspicion of market abuse</i></p>	<p><i>Offer data reporting and inside information publication services to MPs</i></p>
 <ul style="list-style-type: none"> • National law • NRA monitoring Deliberations • Ministerial Decree 	<p><i>Provision to NRA of data, reports, support</i></p>	<p><i>Timely reporting to NRA of any anomalous situation on monitored markets</i></p>	<p><i>Collection of transaction data on bilateral contracts from MPs</i></p>
 <p>Market Rules</p>	<p><i>Disciplinary powers in case of violation of the «fairness & good faith» principles</i></p>		

Remit compliance



Document	Content
Policy	Description of main goals, principles and solutions adopted in carrying out the MM activity
Risk Assessment	Justification of the monitoring coverage granted to relevant market conducts on each GME's market, based on the evaluated "risk" of market abuse
Corporate Procedure	Operational procedure, describing all steps carried out for the MM activity with different roles and responsibilities inside GME
Unit Procedure	Operational procedure, describing all steps carried out for the MM activity with different roles and responsibilities inside the MMU

Principle issues in MM

From theory to practice

REMIT

- Sets clear requirements on what and how to report
- Builds on experience already gathered in financial markets

ENERGY MARKETS

- Are deeply “local” (fundamentals, mkt design, regulation)
- Poorly fit the harmonized financial mkts approach

ACER's GUIDANCE

- To prompt EU harmonization in NRAs/OMPs/MPs approach to REMIT
- To bridge the gap between theory and practice



Great need of further work to include in ACER's guidance «principles» to:

- *design the process (up)*
- *identify STRs (down)*



Limited insights

Limited market overview

- Multiple arrangements on negotiation (bilateral vs OMPs)
- Cross-market / cross-commodities interactions (forward vs spot / gas vs power)
- “Mkt Coupling issues” (Cross Venue, cross border, XBID)

What

Limited strategies understanding

- Cross mkt
- Real time operation
- Net positions
- Regulatory constraints
- Information gathering

Why

GME in the Italian institutional framework

- Single NEMO
- Multicommodity OMP
- Institutional role and support from NRA
- REMIT Services provider on Inside information



Benefits

Better supervision and understanding of the markets

- Supervision of 100% of national market
- Centralization of market data and monitoring functions
- Standardization of monitoring approach
- Improvement of cross-market/commodities monitoring
- Access to third parties information

Principle issues in MM

How to monitor

REMIT Art.15 (obligations on PPATs)

- **Reasonable** suspect
- Notify NRA without **further delay**
- **Effective** arrangements & **procedures**

ACER's Guidance

- **Timeliness:** *four weeks from the anomalous event*
- **Procedures:** *Governance, HR, MM Strategy, procedures*

Problem

Solution

Implications

Dealing with constraints:

- HR
- Markets' features
- Governance
- Timeliness

A "sustainable" market monitoring activity:

- Risk Assessment defines which conducts to screen on which mkts
 - ✓ Chance to properly identify conducts (ex: with-holding in a small market).
 - ✓ Availability of relevant info to validate (ex: insider trading, illiquid mkts)
 - ✓ Available HRs (ex: prioritization)
- MM Strategy & procedures define a consistent and sustainable approach to MM
 - ✓ Which approach to conduct
 - ✓ Which alerts
 - ✓ Which validation process

MM as an interpretative & evolutionary activity:

- Completeness vs timeliness
- Diversified approaches between OMPs and within each OMP along the time
- KPIs useful to measure individual OMPs evolution, not to benchmark OMPs against each other

Principle issues in MM

What to monitor

REMIT Art.2 (conducts definition)

- **Insider trading** (precise info, not public, price sensitive)
- **Mkt manipulation** (false/misleading transactions, price positioning, fictitious devices, false and misleading information)



Problem

What is a conduct?

- Is behaviour in itself a conduct ?
 - ✓ no need for intention / impact?
 - ✓ If so, great pressure on alerts!
- What is a conduct?
 - ✓ Strategic bidding vs mkt abuse (Trend setting vs trend following)
 - ✓ Liquidity manipulation
 - ✓ Excessive pricing
 - ✓ VAT frauds

ACER's Guidance

- **Examples / Conducts'** qualitative description



Solution

Conduct needs being assessed

- MM Strategy defines further conditions for conduct to be a mkt abuse.
 - ✓ conduct interpretation
 - ✓ design of alerts
 - ✓ principles for validation
- Market design matters:
 - ✓ auction vs continuous trading

Implications

Need to set common principles for local application

- Not all conducts trigger an STR
- Human interpretation
- Need for ACER to define high level principles:
 - ✓ to qualify conducts
 - ✓ to set thresholds
 - ✓ to validates incidents

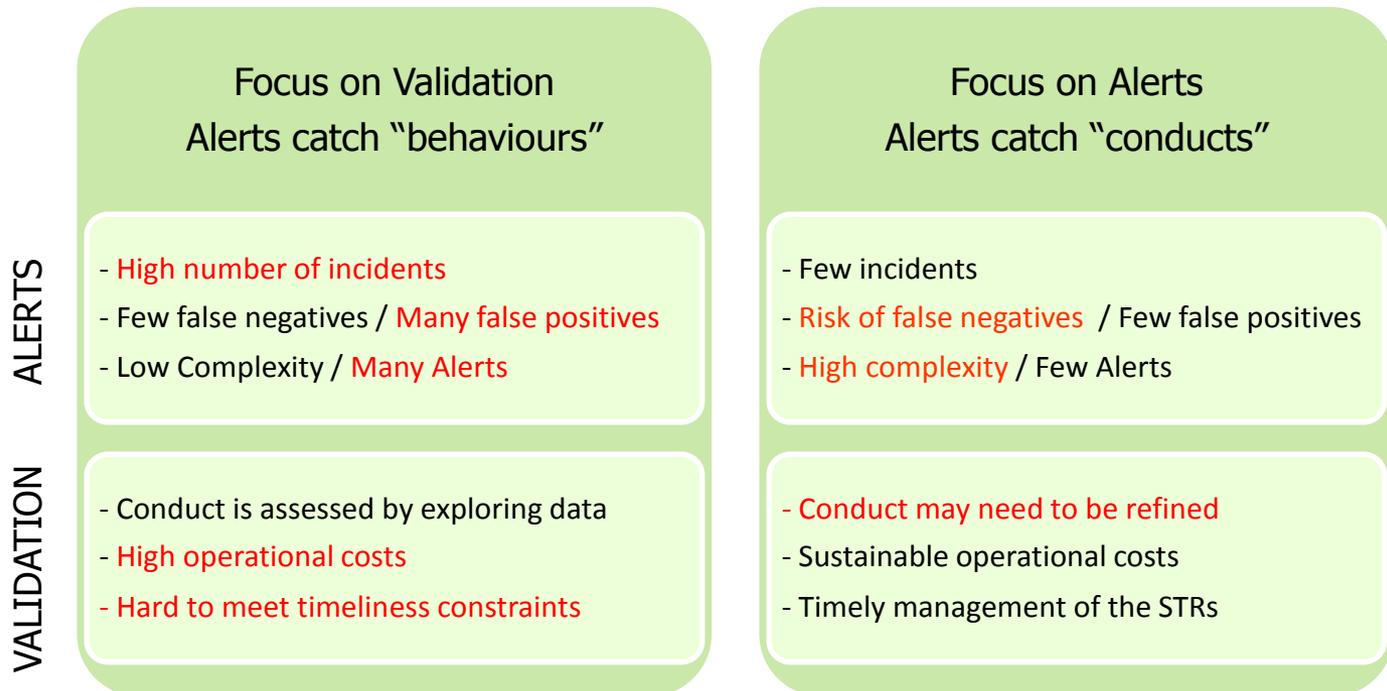
Technical issues in MM

Screening process

- Trade off between screening & validation, based on alerts' design
- No "best" solution: first approach suits in certain conditions (few markets, illiquid markets, low experience), second approach suits in other
- GME is progressively moving from first to second approach



Impact on MM KPI



Validation process

From INCIDENT to CASE

Classification of the incident

- Numerosity and type of Alerts involved
- Profile of the Market Participant
- Correlation with previous/other incidents

Market context analysis

- Market results (price, flows, zonal configuration...)
- Fundamental data (demand, supply, other data referred to the system)
- Dynamics observed in foreign markets

MP Behaviour analysis

- Periodicity
- Time/zone distribution of operations
- Historical behaviour
- Remit unavailabilities

From CASE to STR

Criteria

- **Impact** on Market Results
- **Frequency** of the behaviour
- **Intensity**: Offered quantity
- Number of MPs involved
- Trading Revenue

**Approach to validation
is progressively
more quantitative**

Validation principles

- Criteria needed to assess when a conduct is a suspicious market abuse.
- Trade off among three principles
- Criteria should be general, application should be specific (to OMP, market, etc...)

Intensity (volume/price involved of the conduct)

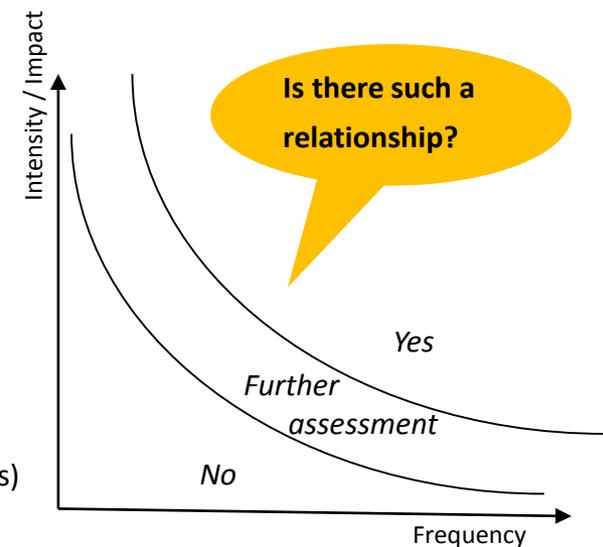
- ✓ Which volume is considerable relevant?
- ✓ Relevance with respect to himself or/and to the market?
- ✓ Which price is too high? What is an artificial level?
- ✓ Which is a reliable reference (internal vs external price reference)
- ✓ Absolute spike vs weighted average (fixed cost recovery)
- ✓ Spot vs Forward Market (same phenomenon, different thresholds)

Frequency (repetition of the conduct)

- ✓ When is it enough?
- ✓ Trade-off for timely reporting to the NRA (Art.15 REMIT and ACER Guidelines)

Impact (consequences of the conduct)

- ✓ Is the impact necessary at all and, if so, could be enough a single outlier?
- ✓ Price: only level or also volatility ?
- ✓ Volumes: What about VAT frauds and wash trades with no price impact?



Market design

- Remit has been designed based on experience from continuous trading market
- When applied to auction markets, it widely reduces to standard “market power abuse” policy

	Auctions	Continuous trading	Chances to manipulate in CT is higher
Time	Does not matter (whole session is affected)	Matters (window in a session)	Less time needed Higher frequency
Relevant market	Is the market zone at the end of the trading session?	Is the market zone during the trading session?	Relevant Market varies more frequently
MP size	Is needed (Pivotality)?	Can be relevant only to a specific moment & bidding behaviour can be sufficient to mislead the market ?	Smaller MPs able to
Abusive conducts	Reduce to price positioning	Involve also false & misleading transactions	More conducts feasible
Impact	Affects by definition the whole session	Can affect only part of a session	Narrower (shorter) impact

Thank you for the attention!

cosimo.campidoglio@mercatoelettrico.org