

20th October 2017

# Energy Saving Certificates Market Mechanism: How is it shaping up?

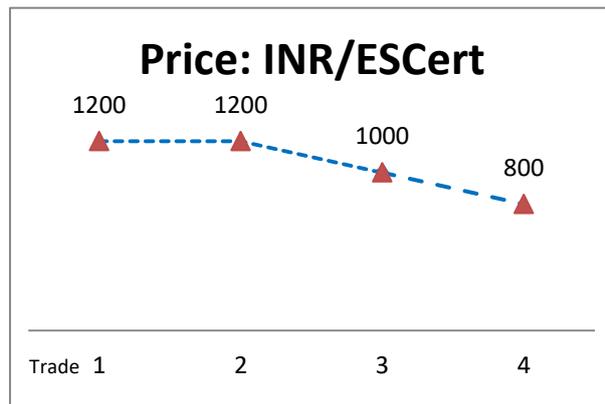
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The trading of Energy Saving Certificates (ESCerts) is progressing as scheduled in one of the power exchanges in India. The ESCerts, which have originated from the first PAT (Perform, Achieve and Trade) cycle out of energy interventions carried out by designated industrial units in eight energy intensive sectors of the Indian economy, are now up for trading.

To participate in trading of ESCerts in the power exchange, designated industrial units have to complete a two stage registration process. First an industrial unit needs to register with ESCerts registry as eligible entity and thereafter it needs to register with the power exchange. The trading rules allow those with issued ESCerts to participate as seller and those with verified shortfall (as compared to their assigned energy efficiency target in PAT cycle 1) to participate as buyer.

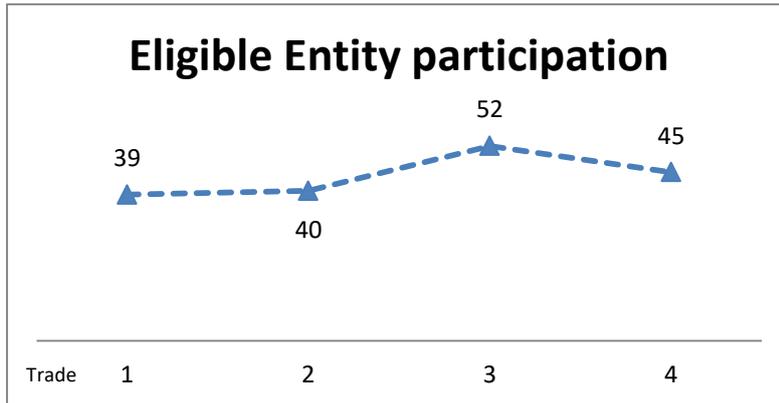
Trading sessions for ESCerts have been scheduled for every Tuesday. We have thus far witnessed



four such trading sessions starting with the first session on 26<sup>th</sup> September 2017. The first trading session discovered a clearing price of Rs1200 per ESCert. The clearing price held on to that level in the second session before dropping to Rs.1000 in the third session. In the most recent trading session (4<sup>th</sup> session) ESCerts price dropped further to Rs.800 per ESCert.

It is worth noting that, in the run up to PAT and through the M&V phase, many speculated (and reasoned) that the price of ESCerts would be upwards of Rs.10,000. This stemmed from the belief that the price of ESCerts will be higher than the penalty payable per TOE of shortfall, if that shortfall is not mitigated by purchase of ESCerts. This opportunity cost (penalty price to be precise) prompted many units to peg their ESCert price at Rs.10000 or thereabout. So the actual ESCert trade price, as we know now, is not good news for sellers. It is very encouraging though for buyers as they now see the possibility of complying at a cost much less than what they had budgeted for.

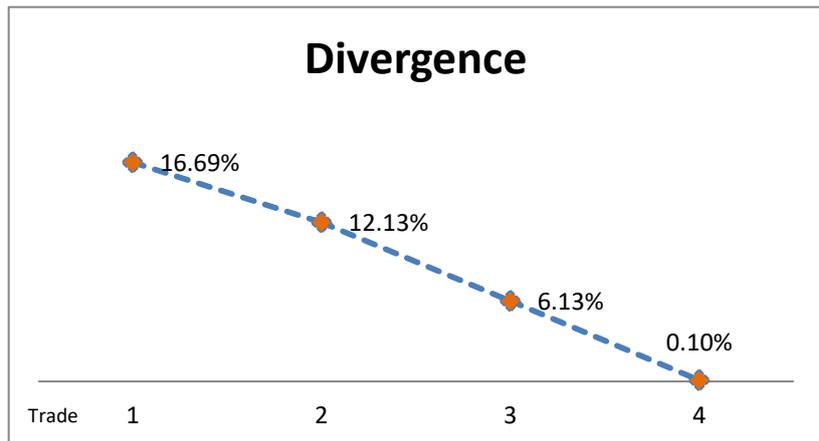
Of course, how long this price band holds is yet to be seen. While buyers should be rushing in to purchase their ESCerts at reigning price range, sellers should be really looking at their projected energy efficiency status at the end of second PAT cycle and deciding whether it would be prudent for them to bank their ESCerts rather than sell now. Sellers also need to take a hard look to see how much room they have to lower their asking price based on their individual circumstance in the face of supply glut and a very low price to start with.



Meanwhile, more and more industrial units are completing the first requirement for trading - registering for becoming eligible entity. There are about 200 designated consumers who have registered as eligible entity – so in the coming days many more should be participating in ESCert trade. Till now, the

participation in trading has been low. A very small fraction of the total number of designated consumers in PAT cycle 1 has participated thus far. This is perhaps partly because there were not too many units who had fulfilled the requirements of registering as eligible entities in time for participating in the first few trading sessions. To what extent, if at all, this is also due to subdued enthusiasm on account of firstly supply far outnumbering demand and secondly on account of lack of visible market upside is as yet unknown. For buyers the falling price trend till now may have also signalled the possibility of complying at an even lower price by postponing participation.

For a participant in ESCert trading session – successfully transacting would among other things imply that the aspirations of the participant and its insight into the market mood are aligned to the embedded market success requirement. Trading strategy embodies these. Perhaps one way to gauge how good was the trading strategy of participating units, is to look at



the success of the bids which emanated from trading strategy and how it is evolving. The trading started with a wide divergence (16.69%) between the maximum purchase bids which could have been theoretically cleared if there was perfect buyer and seller alignment. That divergence has been progressively reducing through the trading sessions. In the fourth trading session that divergence stood at only 0.10%. This is indicative of sellers reacting and quickly aligning their bids to catch the buyer in the face of the fact that supply of ESCerts was reported to be 2.7 times the ESCert demand.

We have with us now the outcome of only four trading sessions. Assuming no repeat participation a maximum of only 150 odd participants has so far participated in the market mechanism. Already 200+ eligible entities have registered with ESCerts registry out of 450+ designated consumers in PAT cycle 1 and many more are on course for registering. There is a significant quantum of ESCert demand yet to be fulfilled through exchange trade. So it will not be unreasonable to assume that many more will participate in the coming trading sessions. It will be interesting to see which way the ESCert market moves with increase in participants in trade against the backdrop of very low ESCert prices thus far.

Trading data source: ESCerts Market update by IEX published in <https://www.iexindia.com/#horizontalTab11>

Source of data on eligible entities: [https://beenet.gov.in/UI\\_Forms/General/Login.aspx](https://beenet.gov.in/UI_Forms/General/Login.aspx).

*The content of this article does not constitute any trading advice.*