

## FESE statement on the role of exchanges in energy markets

15<sup>th</sup> November 2022, Brussels

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Financial markets are critical infrastructure for the European economy. They serve the needs of participants to raise capital, handle investments, access cash, and manage risks that affect both retail and institutional investors. Derivatives markets demonstrate every day that they are able to manage the extraordinary volatility and stress under which they are operating due to the ongoing energy crisis.

As pointed out by Commission President Ursula von der Leyen in her State of the Union speech, Europe faces first and foremost an energy supply crisis triggered by the Russian invasion of Ukraine. This explains price fluctuations in commodity exchange-traded derivatives (ETDs), rather than anomalous market behaviour. It is precisely during periods of heightened uncertainty and volatility when these risk transfer mechanisms (e.g. hedging) are most needed. That's why exchanges should remain fully functional and open to market participants during times of increased stress.

Exchanges are instrumental in the discovery of prices of financial instruments, including derivative contracts, through the free interaction of the forces of supply and demand. Subject to their overarching duty to run an orderly market according to the EU MiFID II/R<sup>1</sup> as well as the Market Abuse Regulation<sup>2</sup>, exchanges will allow the market to determine prices at any given time. In particular, for derivatives, exchanges organise an open and transparent mechanism that helps market participants transfer risks. The role of exchanges is to be the neutral operator of this market mechanism. This means that they do not have a preconceived notion of the intrinsic value of a financial instrument admitted to trading. Indeed, exchanges ensure that market participants using their facilities can obtain the best price for the size and type of trade at a given time, without any intervention.

Exchanges have a suite of dynamic and configurable systems to manage periods of increased price volatility. These so-called circuit breakers and similar mechanisms ensure that new information and rapidly changing events are reflected in an orderly manner in market demand and supply conditions. Circuit breaker functionalities diminish the likelihood and extent of short-term price spikes or aberrant market moves. However, these are not price manipulation procedures but essential safeguards to protect an orderly price discovery mechanism. Large price fluctuations over a trading day can still happen if an orderly balance of supply and demand forces drive them.

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<sup>1</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments.

Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments.

<sup>2</sup> Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse.

Generally, these safeguards are working as intended. Consequently, it would be redundant to bring in new types of trading halt mechanisms to alleviate the consequences of the energy supply scarcity. Given that the current energy crisis is primarily driven by an energy supply scarcity, imposing additional artificial price control mechanisms (such as price collars or corridors) will not tackle the fundamental forces that drive prices. Furthermore, if exchanges cannot provide a fair and transparent market price, there is a risk that certain commodity derivative contracts will move to the significantly less transparent OTC space, thereby potentially creating financial stability risks. Prices should reflect fundamental economic realities.

For further information about the functioning of circuit breakers for energy markets, please refer to the Europex FAQ on the subject ([here](#)).