

IESO SENIOR MANAGEMENT UPDATE

To: Stakeholder Advisory Committee

Date: March 26, 2014

Subject: **Market Operations Update**

Information Item - Recent Market Pricing

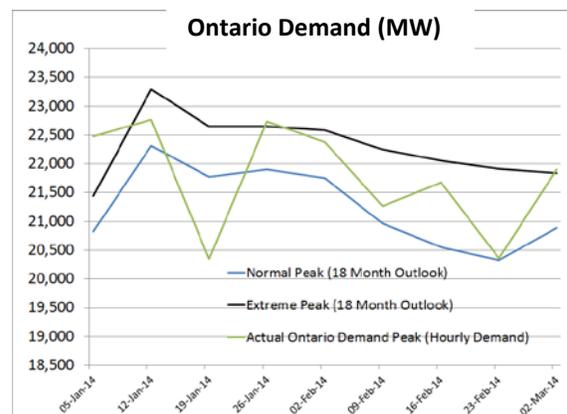
Ontarians have seen one of the coldest winters of the past few decades in 2013/2014, and neighbouring states and provinces have been impacted by these very cold temperatures as well.

With the cold temperatures, demand for electricity and natural gas have been unusually high and sustained over this period. This high demand for electricity combined with rising costs for natural gas – a critical input for the production of electricity – have led to high market prices for electricity. These conditions are not unique to Ontario and are similar to what neighbouring jurisdictions are facing.

High electricity demands in Ontario are in-line with our 'extreme weather' planning scenario. These conditions have not impacted the reliability of the Ontario electricity system. While electricity demand has been very high, there have not been any reliability issues associated with meeting that demand.

Earlier this winter, Ontario had been a net exporter, and over the past several weeks Ontario has been a net importer as the electricity markets respond to changes in price across jurisdictions. Imports have competed with domestic generation allowing the least expensive resources to be scheduled to supply electricity to the system.

Higher natural gas prices are a product of higher demand for natural gas as a fuel for both heating and electricity generation. Higher demand for natural gas has led to lower storage levels and significant competition on the real-time natural gas spot market. The experience of this winter could linger through the summer as gas storage inventories were drawn down sharply. Storage inventories in the U.S., which stood at record highs two years ago, have now been drawn down to well below historical averages.

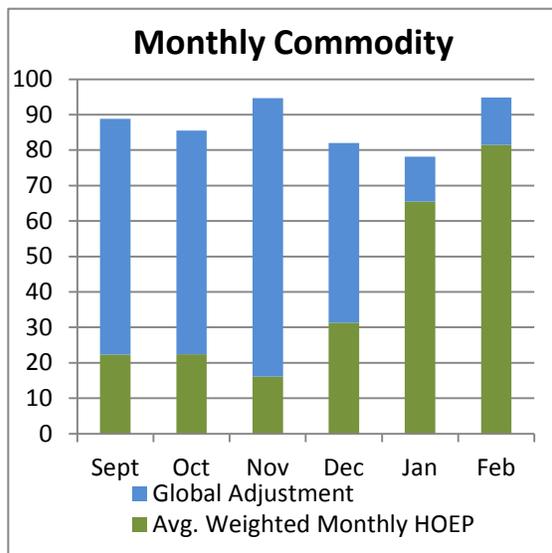


Residential customers in Ontario pay Time-Of-Use rates, which are set every six months to avoid exposing this class of customers to daily and monthly price fluctuations. Despite the fixed Time-Of-Use rates for this class of consumers, cold temperatures lead to higher consumption and higher monthly bills.

Customers who are exposed to the hourly price have seen average Hourly Ontario Energy Prices (HOEP) that have been significantly higher than in previous years as a result of these conditions, with the average weighted HOEP at \$65.43/MWh for January and \$81.83/MWh in February. At \$964.28, the fourth highest HOEP since market opening was set during the evening of February 27 and the value of the market demand on March 4 was \$135,158,028 – the highest since market opening.

The HOEP and the Global Adjustment (GA) have a partially correlated and inverse relationship – lower HOEP prices lead to higher GA costs, just as higher HOEP prices will lead to lower GA costs. That’s because when generators recover more of their fixed costs through the market price they do not need to receive those payments through their contracts, thereby lowering GA. However the GA does not offset variable costs like fuel. Ontario Power Generation (OPG) returned \$66 million to the GA in January, and \$138

million in February. This is reflective of the average market prices that exceeded the regulated rates paid to OPG’s nuclear and baseload hydro assets. Similarly, payments to contracts with fixed rates such as Bruce Power, NUGs and renewables were less with the higher market prices.



While customers have recently seen increases in the hourly costs, it is important to note that the monthly average electricity commodity costs (which combines the impacts of the HOEP and the GA) have not seen these swings over the past several months.