



Drax Intelligence

Flexibility Focus

A quarterly update on demand-side revenue streams

A review of Q2 2026 and
look ahead at Q3 2026

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Welcome to the fifth edition of our quarterly newsletter focusing on the key market, policy and regulatory developments affecting consumer-led flexibility (CLF).

The second quarter of 2026 has seen a range of unseasonal weather events that shaped demand and generation, impactful geopolitical events, as well as ongoing policy and regulatory evolution. We've also seen some substantial changes to the Demand Flexibility Service (DFS) this quarter, including a very high value event and the addition of demand turn-up

As with every quarterly report, we look at the biggest developments in this edition. If there are topics that we've missed that you think we should cover in future, or any other ways we can improve the content, please send your feedback to insights@drax.com.



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Q2 developments

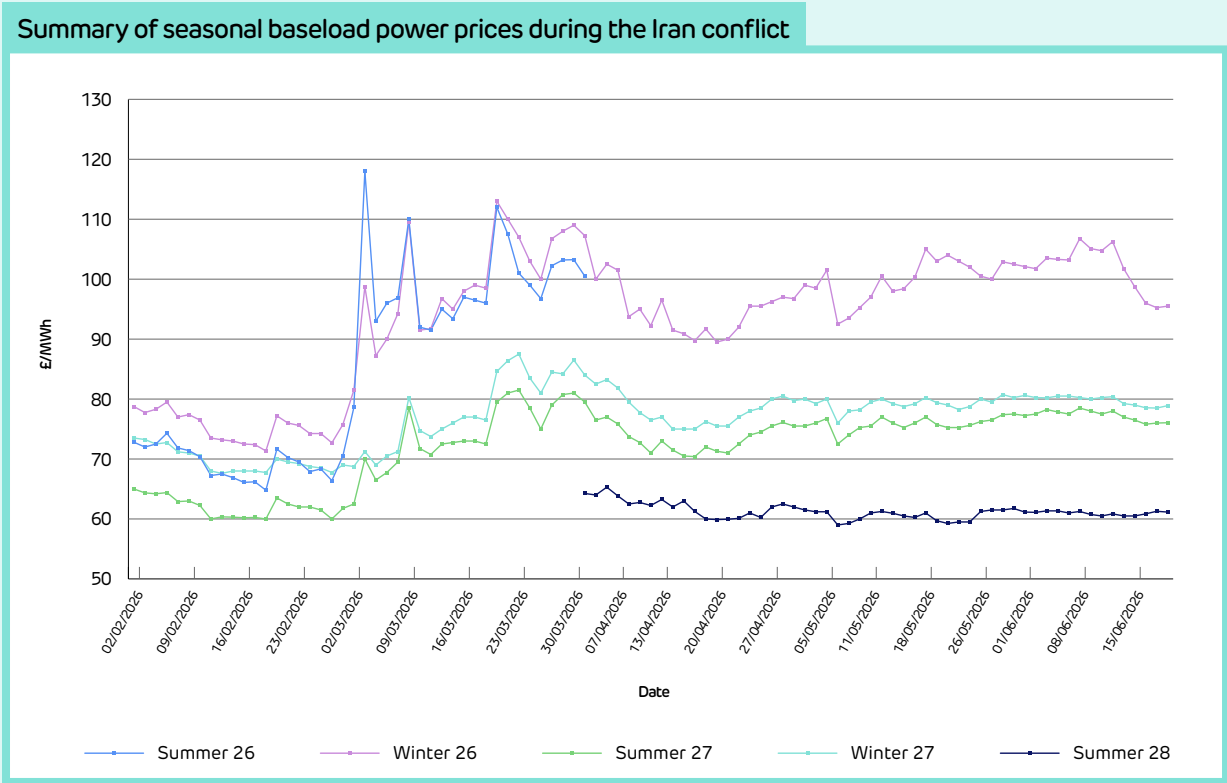
Market updates

Heatwaves and peace deal talk hesitation caused market volatility

Developments in the conflict in the Middle East, as well as the short-term impacts of extreme heat have dominated power prices in the second quarter of 2026. On-off peace negotiations in the Middle East intermittently increased transit of energy cargoes via the Strait of Hormuz. Meanwhile, a Europe-wide heatwave during the week commencing 22 June led to power market volatility on several days.

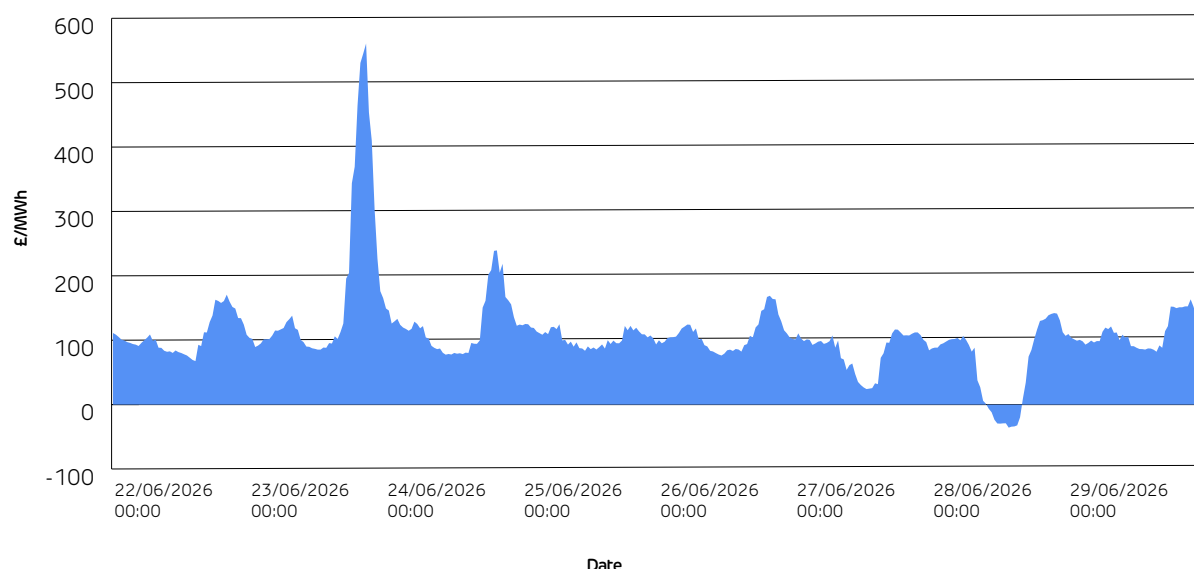
After starting in February, the US-Iran conflict escalated in March when Iran attacked Qatar's Las Raffan refinery and caused long-term damage to its export capabilities. Iran also functionally closed the Strait of Hormuz, preventing around 20% of the world's LNG supply from reaching the market driving high gas and power prices.

April began with the news of peace talks resulting in a two-week ceasefire which lowered prices again, though they rose steadily once again into the start of May. The signing of the Memorandum of Understanding on 14 June opened the Strait of Hormuz, easing supply concerns and causing a sharp drop in prices. You can see these developments in the graph below.



Prompt prices then spiked during the heatwave which began on 22 June. High temperatures increased demand for cooling while impacting the thermal efficiency of generation assets. Alongside low wind levels, this caused extreme pressures on the grid in the late evening as solar output dropped off. This resulted in the National Energy System Operator (NESO) issuing its first ever summer Electricity Margin Notices, while within-day prices reached £560/MWh on 23 June shown in the graph below. The heatwave also affected generation in Europe, with multiple French nuclear reactors shutting down due to high river temperatures. While the heat impacted power flows across Europe, NESO relied heavily on interconnectors to balance supply and demand through the worst of the heatwave, shown in the graph below.

Half-hourly wholesale electricity market index prices for 22 to 29 June 2026



At the time of writing in early July, hostilities between the US and Iran have resumed with the US calling the Memorandum of Understanding 'over' causing prices to rise again as Iran closed the Strait of Hormuz to shipping once more.

NESO published draft Winter Outlook

NESO published its Early View of Winter Outlook 2026/27 Report on 23 June. This annual report assesses the security of electricity supply from November '26 to March '27, providing an overview of the potential system tightness over the period.

NESO forecasts that the de-rated margin (the excess supply during average cold spell peak demand accounting for reserve requirements) will be 5.5 GW. NESO describes this as 'adequate'; it's slightly lower than the last winter period but in line with the recent average. NESO predicts that the Loss of Load Expectation (LOLE) is below 0.1 hours per year. It expects the tightest days in mid and late January but forecasts adequate operational margin.

NESO is due to publish the full report in October this year, which will incorporate its latest demand and asset availability forecasts.



Policy and regulation updates

Reformed National Pricing (RNP) Delivery Plan

In April, the Government published the RNP Delivery Plan. This is the next stage of the overarching electricity market policy review, following the Review of the Electricity Market Arrangements (REMA) decision to maintain a single (rather than zonal) GB wholesale market. In the plan, it highlighted a current misalignment between generation and network build.

The RNP programme has three desired outcomes: reforming siting and investment levers to support delivering of a Strategic Spatial Energy Plan (SSEP), bearing down on network constraint costs, and improving system operability and efficiency.

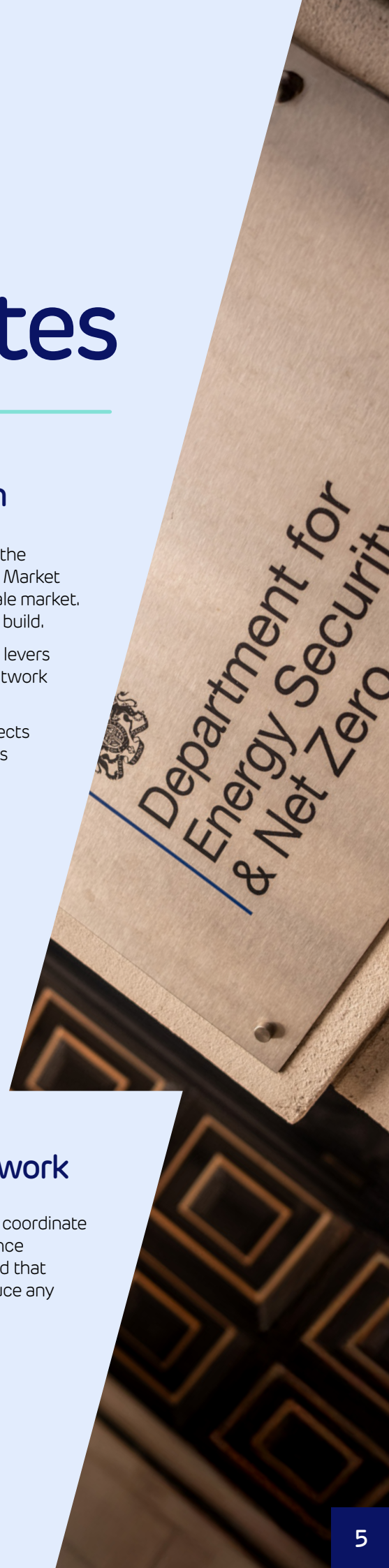
The first could influence where and how large-scale generation and demand connects and operates. The Government has outlined five options to progress placing various levels of emphasis on connections reform and the role of locational charges. It has preferred options within these and consulted on its proposals.

The Government is also considering how to alleviate constraint costs, which will likely interplay with the above options. Currently constraint costs are very high and without mitigation could continue to rise to between £6-8bn based on the NESO's current forecasts. One solution to high constraints mentioned in the delivery plan is better use of flexible demand. The Department for Energy Security and Net Zero (DESNZ) expects ongoing workstreams to deliver this, including the NESO's Demand Side Flexibility Routes to Market Review (discussed further below) and the Demand for Constraints Project.

Finally, a range of changes are in various stages of development and implementation to support system operability and efficiency. We covered many of these in our last quarterly update, as they were the first proposals DESNZ consulted on.

DESNZ opted against CLF engagement framework

Last year, DESNZ consulted on whether the market needed a formal framework to coordinate and improve consumer engagement in CLF. It concluded there's not enough evidence showing a need for a formal CLF consumer engagement framework at this time and that CLF activity should remain market-led. DESNZ has therefore decided not to introduce any additional engagement standards.



Demand-Side Flexibility (DSF) Routes to NESO Markets Review

As part of the Clean Flexibility Roadmap, NESO committed to providing quarterly updates on its DSF Routes to Market Review. It published its Q2 2026 update on 29 June highlighting its progress against the workstreams aimed at increasing DSF participation across GB markets.

The key points to takeaway are:

- NESO is investigating DSF Balancing Mechanism (BM) skip rates - how often it bypasses assets during operational decisions - which remain higher than other technologies.
- It launched an innovation project exploring 'synthetic' metering, which uses an adjusted meter feed for Balancing Mechanism (BM) participation.

- NESO is continuing to progress detailed design of its Demand for Constraints (DfC) market. This is a long-term contract to incentivise new, additional, flexible final demand capacity in certain Scottish regions to alleviate thermal constraints.
- DESNZ will be launching a £20m trial run by UK Research and Innovation (UKRI) to remove Final Consumption Levies (FCLs) which include policy costs, from demand turn-up. NESO is supporting both the trial scoping as well as any enduring policy implementation process. DESNZ will use data from the UKRI trial to consider if and how permanent change would operate. It's seeking powers, subject to Parliamentary approval, that could allow their permanent removal from demand turn-up.

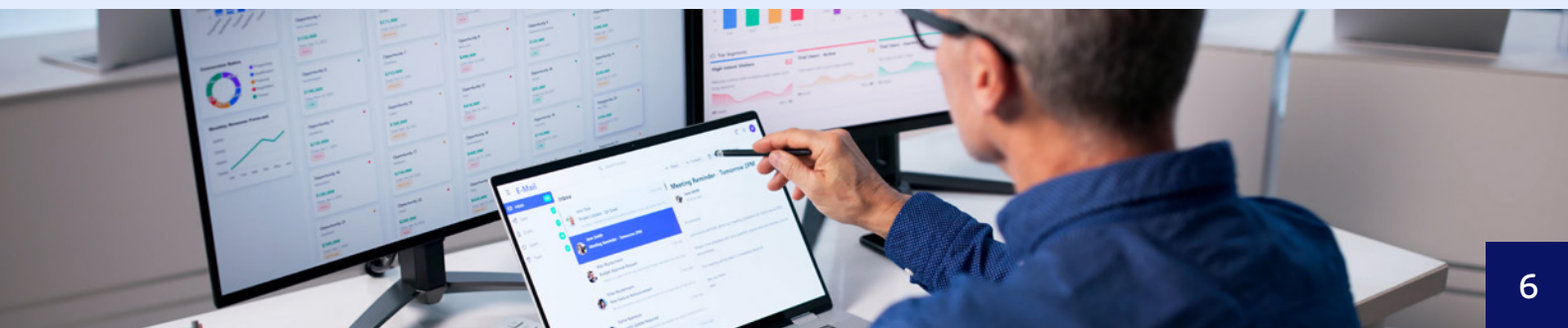
Capacity Market: Consultation Response on changes for Prequalification 2026

On 14 May, the Government released its full response to the consultation on proposed changes for the 2026 Capacity Market (CM). Back in February, it announced that for now it wouldn't proceed with a Multiple Price Capacity Market (MPCM). Following this, the Government announced changes for the upcoming CM prequalification that will likely streamline application processes as well as measures to remove opportunities for strategic bidding in the auctions.

Specific outcomes that will impact demand-side response (DSR) include:

- Streamlined reporting obligations for low-capacity DSR components by only requiring Capacity Providers (CPs) to list components that are 30kW or greater on CM Registers. The Government has done this to accommodate significant numbers of small components such as commercial EV chargers which would fall outside of the current threshold.
- DSR capacity will need to demonstrate 50% of its Capacity Obligation during DSR tests, a change from the current 1MW capacity demonstration.

- New measures will require DSR applicants to report technology type and customer type.
- DSR de-rating methodology won't change for now, although the Government recognises concerns that it should improve the methodology and plans to consult on this further.
- There were also specific changes to evidence required for multi-year DSR agreements that meet specific thresholds.
- Proven DSR CPs will have to declare any Permitted On-Site Generation Units (POSGUs) at the application stage. For Unproven DSR CMUs, CPs will need to declare POSGUs at the point of notifying DSR CMU Components.
- For all technology types, there'll be a 30% increase in Termination Fees in future CM agreements (awarded from 2027 onwards) to account for inflation since the scheme began.



Ofgem Capacity Market Rules: change proposals 2026

On 26 June, Ofgem published its decision on its Statutory Consultation on Capacity Market Rules change proposals, which ran from 10 April to 24 May 2026. It has decided to implement all 13 rule changes for 2026 prequalification. Some of the key changes are as follows:

- Ofgem has changed how it calculates load following Capacity Obligation (LFCO).
- It has also addressed deadline misalignment for Metering Assessment in the CM Rules. Rules now specify when CPs must complete a Metering Assessment, providing more clarity.
- New rules clarify existing controls around how CPs declare Connection Capacity, including the need to declare Connection Agreements and declare Connection Capacity.
- A new rule will reduce the complexity of metering to avoid an operational bottleneck for testing that would arise as domestic and small DSR participation increases. It'll also enable the use of Code of Practice (CoP) 11 compliant asset-level metering systems as another metering solution in the CM. The Delivery Body won't require a Metering Test as Balancing and Settlement Code qualified agents independently assure meter readings are by. CoP 11 metering will reduce reliance on a manual bespoke metering configuration, reducing burden on all participants.
- It's now allowing an authorised meter operator agent, rather than solely Settlement Body metering agents, to complete and verify metering statements. This'll avoid issues where there haven't been enough available assessors to complete the metering statements.
- Ofgem will review and simplify the Exhibit templates submitted as part of applications for the 2026 prequalification, except for exhibit ZA.

P462 The removal of subsidies from Bid Prices in the Balancing Mechanism

As part of its RNP Delivery Plan, DESNZ said it would continue to support the code modification process which analyses the potential impacts of P462 and develops its design.

P462 is a proposed code modification to the Balancing and Settlement Code (BSC). Currently, when subsidised renewable generators bid to turn down in the Balancing Mechanism (BM), they include the cost of the subsidy they would lose if bid down, within their bid prices. This is because subsidy payments and their generation output directly link. By including foregone subsidy revenue within bid prices, this results in negative bid prices whereby NESO pays them to turn down.

P462 proposes to introduce a separate "make whole" payment covering the cost of lost subsidy revenue in the event a renewable generator is bid down, this would then remove the lost subsidy element from bid prices. P462 would impact bid pricing behaviors and the bid stack more generally, likely resulting in less negative bid prices from subsidised generators; however, the full impact of P462 is unclear at this time. CEPA are currently doing additional analysis on behalf of the code modification workgroup, to try and better understand the potential impacts of P462. Ultimately, the modification will be subject to a final decision from Ofgem.



Revenue opportunities

Wholesale arbitrage

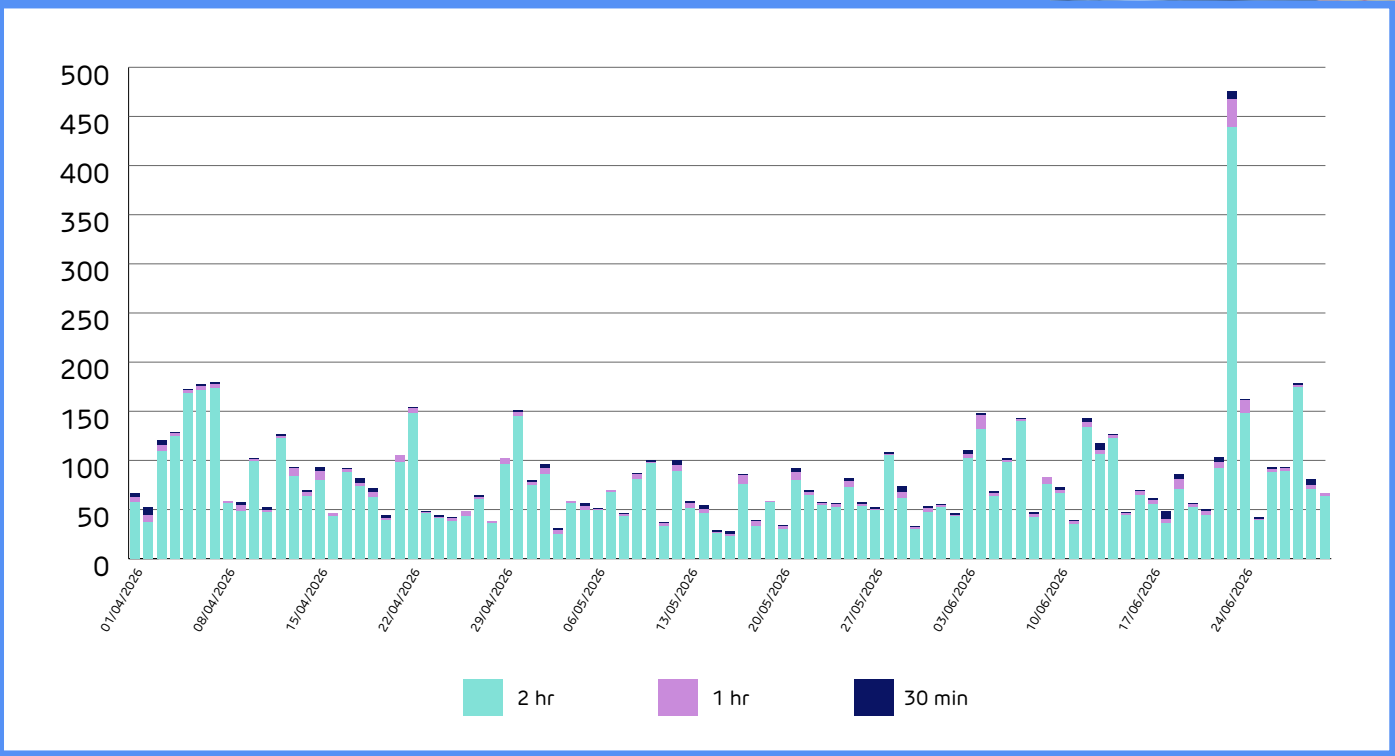
In Q1 2026, we saw similar levels of volatility in wholesale prices compared to Q1 2026. The greatest daily volatility occurred on 23 and 24 June, due to high temperatures that cause high levels of demand for cooling across the day and into the evening. As solar generation decreased from around 6pm onwards and wind generation sat lower than forecast, this caused a spike in prices from 6-10pm on 23 June. The highest daily maximum price across the quarter was £560.81/MWh on 23 June, £269.92/MWh greater than Q1's. The second highest was £239.51 on 24 June, which was lower than Q1's £273/MWh on 6 January.

The greatest spread (the difference between the highest and lowest prices on the same day) also occurred on 23 June, at £475.43/MWh. The lowest spread was £27.55/MWh on 16 May.

However, it wasn't just the weather that caused market volatility. Due to on and off peace discussions between the US and Iran, we saw periods of fluctuating prices over the quarter. There were periods of high prices, with daily maximum prices exceeding £150/MWh on 21 days. The average spread across the three months was £84.10/MWh and higher than Q1 26. This highlights unusual levels of volatility for the time of year. In spring, electricity prices have previously been less volatile than in the winter, however, ongoing geo-political tension and the hottest June on record, have created the backdrop for volatility.



Daily maximum £/MWh value for a single load shift of varying durations (wholesale only)

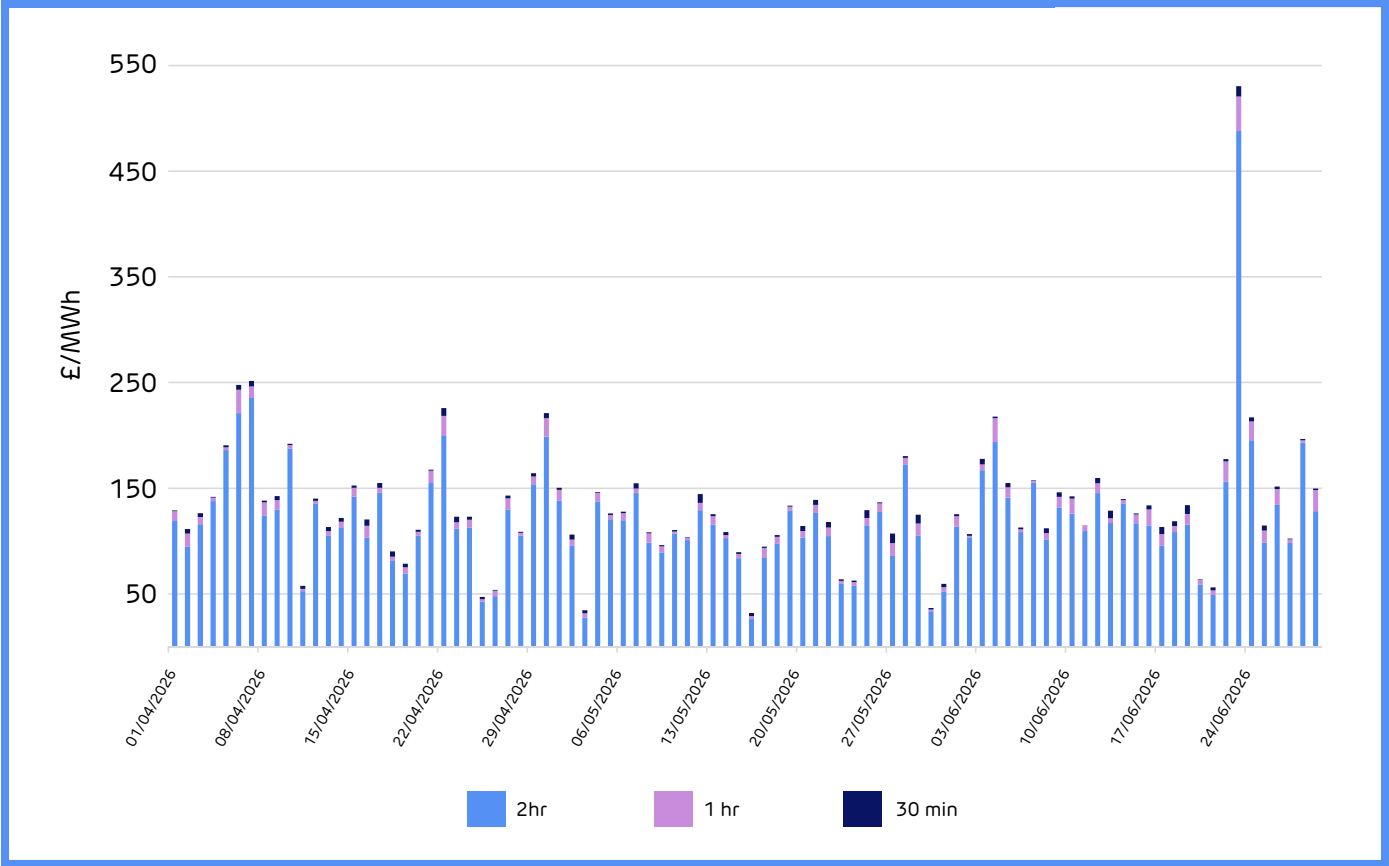


Delivered cost arbitrage (example customer)

The delivered cost arbitrage is usually less in summer compared to winter (from February onwards), as the winter seasonal time-of-use charges (e.g. triad charges and Capacity Market Supplier Charge) come to an end. Costs in the summer are more reflective of wholesale prices rather than third party charges. However, due to volatile wholesale markets, there have been greater opportunities than average for the time of year.

By shaving peak demand consumption, customers on a tariff that fully passes costs through could have saved up to £530.50/MWh on 23 June, during the period of high electricity demand, due to high temperatures, and low wind. This was £86/MWh more than the highest potential savings in Q1 26. The average amount that flexible participants could save over the three months was 48% lower, however, at £132.68/MWh for 30 minutes of peak demand shaving. The average for two hours of demand shaving dropped to £121.71/MWh which was 53% lower than Q1 26.

Daily maximum £/MWh value for a single load shift of varying durations (delivered price)



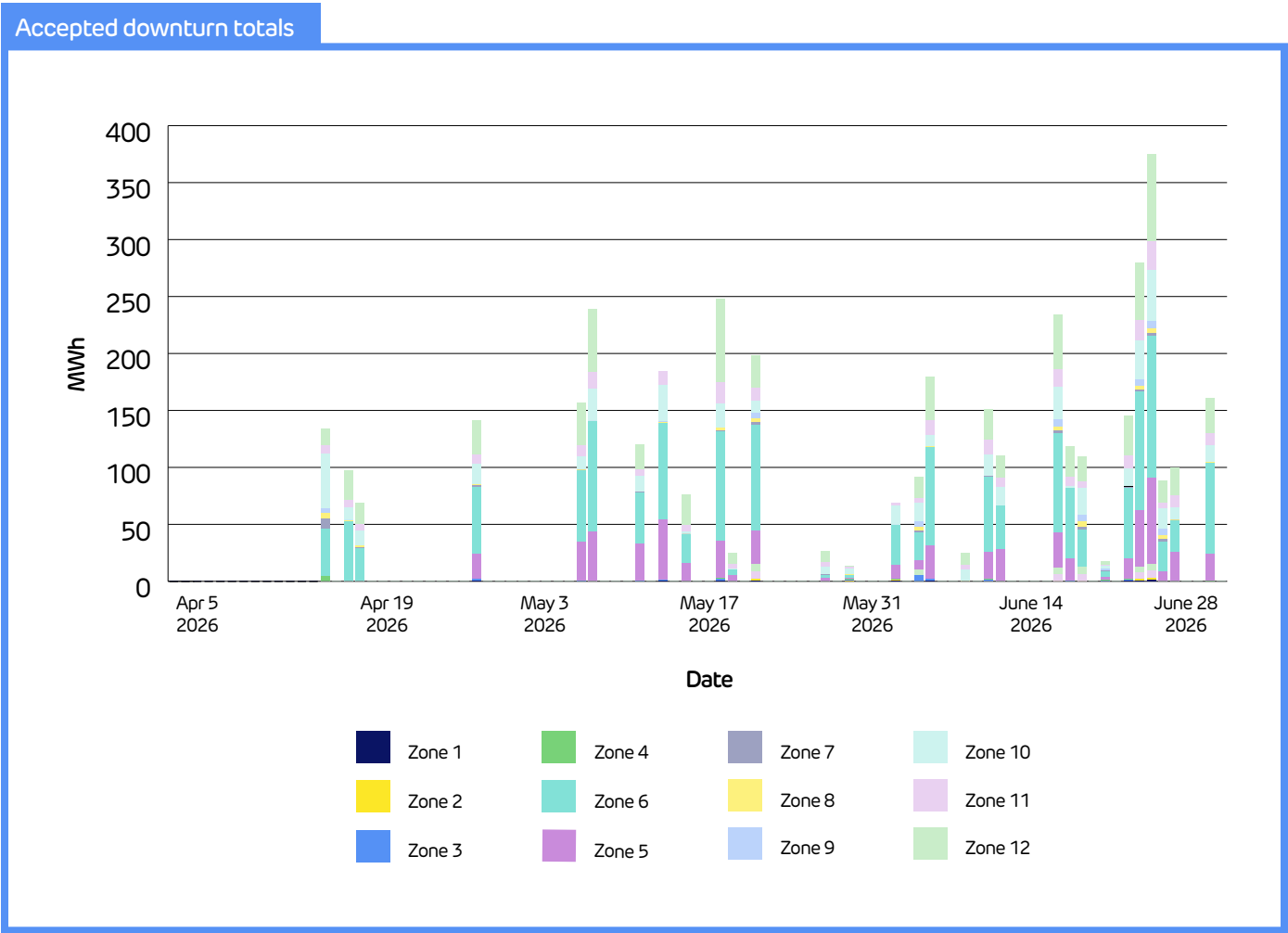
Demand Flexibility Service (DFS)

First Quarter of the New DFS

On 14 April NESO delivered the new iteration of the Demand Flexibility Service. As we highlighted in our Q1 report, headline changes to the service included the addition of a demand turn-up component to the service, zonal procurement, allowing self-nominated baselines for I&C participants, and DNO-related participation constraints.

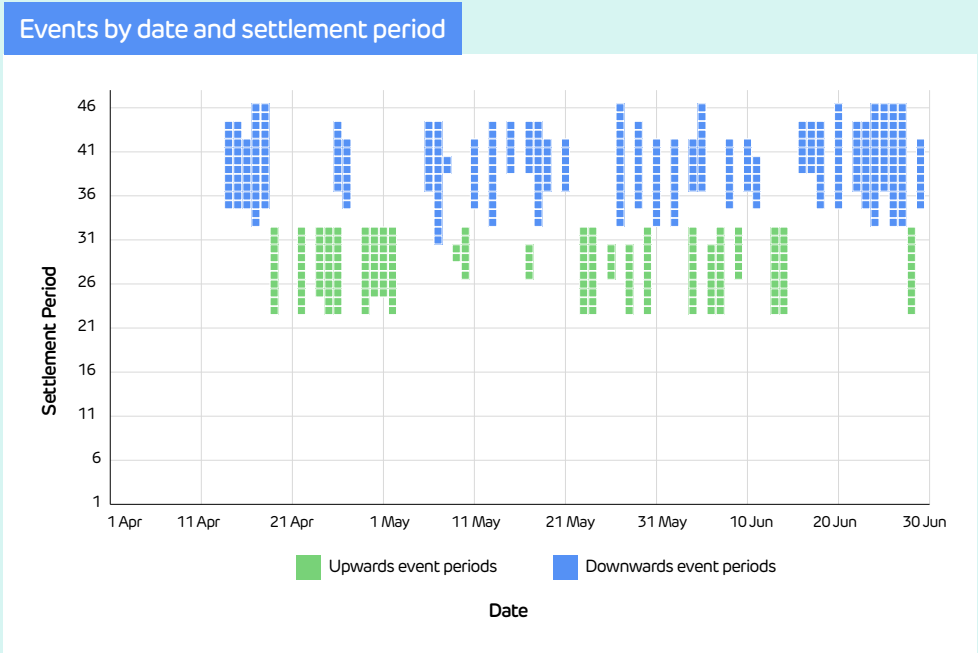
This quarter, NESO called 61 events between demand turndown (37) and demand turn-up (24). Demand turndown events occurred in a total of 344 settlement periods whilst turn-up occurred in 202. Whilst the turn down service saw just under 4GWh of bid volume accepted, with individual events peaking at around 350MWh, the service accepted only 0.5MWh for turn up. See the graph for more information.

The primary reason for the lack of uptake in demand turn-up is likely due to the application of third party charges to these additional volumes. This creates a cost threshold under which demand turn-up is not profitable. In March, DESNZ announced that they will be running a trial to offer discounts on the use of turn-up power from renewable sources to households and businesses in constrained areas – predominantly expected to be Scotland and the East of England. Since the announcement there have been no further developments, although the trial could occur this coming winter and result in more volume for this aspect of the service.



Increase in DFS Periods

In Q2 2026, NESO has called 50% more DFS events than Q2 2025, due to the addition of and increased need for demand turn-up events. Whilst the frequency of turndown events is nearly identical to last year, the average number of settlement periods for these events has increased from 5.35 periods per event to 9.24, with six downwards events spanning 14 settlement periods. This means these events are getting longer on average. It's worth noting that NESO may call both upwards and downwards events on the same day and they did so on three occasions this quarter.



Zonal Restrictions

NESO introduced zonal procurement in the updated service to better reflect locational constraints in its procurement approach. This is because response in constrained areas may, at times, exacerbate the challenges NESO faces. Northern zones have seen greater constraints on their participation than their Southern counterparts, in some cases up to 40% less requirement.



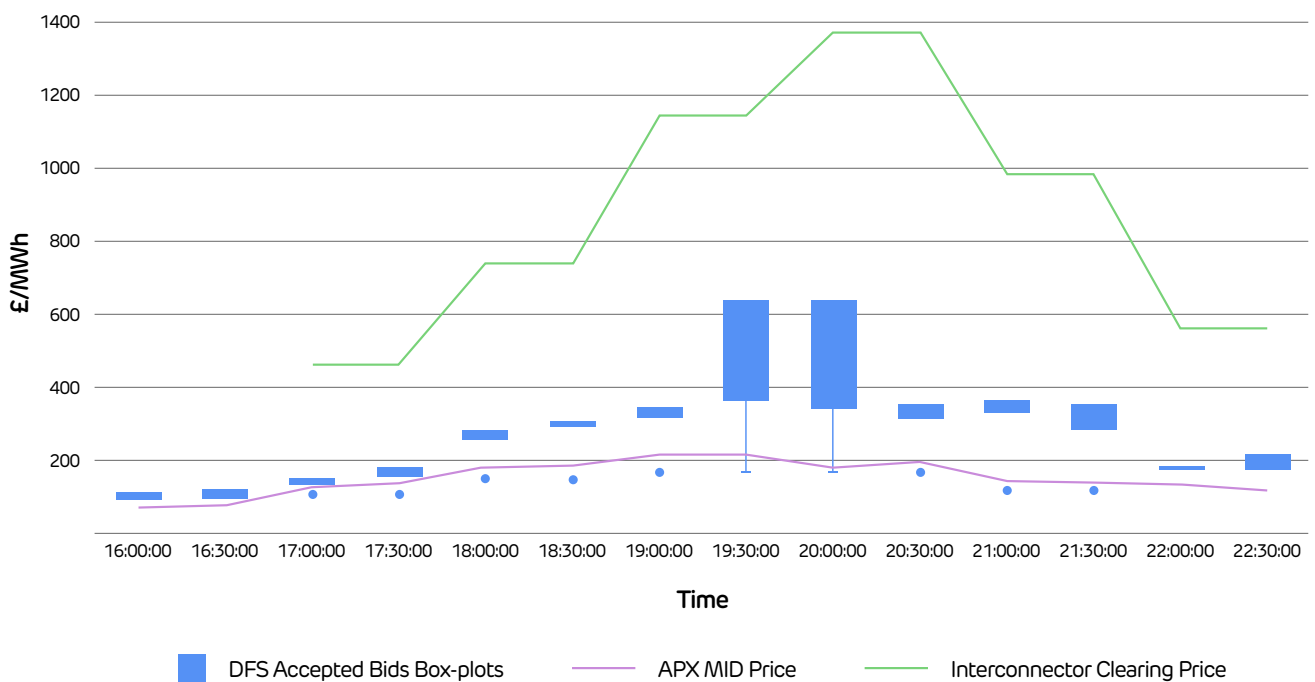
Looking at where turn down volume has been rejected; zonal constraints are unlikely to have stopped much participation, however. NESO has rejected minimal volumes in the Northern zones (1-4) whereas it rejected the most volume in zone 6, spanning an area crossing Wales, the Midlands and Yorkshire, which also contributed the most volume and almost twice the volume from the next highest zone, zone 12 – London.



European heatwave impacts

The European heatwave at the end of June had quite an effect on power grids across the continent. The UK imports a substantial amount of power from Europe, particularly France whose nuclear power stations couldn't operate at full capacity in the heat. This increased prices in Europe and NESO paid approximately £9.3m to procure 13.3GWh across the 5PM-11PM window with a weighted average price of just under £700/MWh and a peak of £1,155/MWh. DFS prices also spiked, with a max accepted bid of £649/MWh. As DFS essentially competes with the interconnector volume, DFS participants could have earned substantially higher revenues in aggregate. Only about 400MWh of DFS volume entered bidding, limiting NESO's ability to call upon volume.

DFS accepted bids on 24/06/26 with MID and interconnector prices





Looking ahead at Q3

What we're doing at Drax

We're continuing to develop products and services for our customers focused on supporting them achieve value from flexibility.

Look out for more information shortly.

Market and policy developments

Over the next quarter, DESNZ and NESO plan to make progress on the RNP workstreams, including some balancing and settlement reforms. As part of RNP, we expect to see further progress on how the connections regime and locational charging could combine, as well as which balancing and settlement reforms may be progressed.

The Capacity Market Prequalification Submission window for 2026 will run from 4 August for eight weeks until 29 September.

Changes to Static Firm Frequency Response will go-live on 31st July, including reducing the frequency trigger level from 49.7Hz to 49.65Hz, reducing the unit and bid order threshold to 0.1MW, and the introduction of tighter performance measures.

We're also still expecting a DESNZ consultation on Renewables Obligation Fixed Priced Certificates, which is now overdue.

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