



2 November 2018

Ms. Jessica Robinson
Director, Pricing
Energy Retail Market Monitoring
Independent Pricing and Regulatory Tribunal
PO Box K35
Haymarket Post Shop
NSW 1240

Submitted online to www.ipart.nsw.gov.au/Home/Consumer_Information/Lodge_a_submission

Dear Ms. Robinson,

RE: Review of the performance and competitiveness of the retail energy market in NSW

Origin Energy Limited (Origin) welcomes the opportunity to respond to the Independent Pricing and Regulatory Tribunal's (IPART) draft Retail energy market report.

Origin supports IPART's finding that competition has continued to develop for residential and small business customers in both the electricity and gas retail markets in 2017-18.

Origin concurs with IPART's finding that competition in the energy market in NSW has objectively increased since pricing deregulation. Customers now have a range of retailers who are actively competing for their business. This drives better products, offers, service and outcomes for customers. Origin also supports the recommendations made by IPART to allow energy retailers to respond to the problems identified with the market rather than for Governments to intervene. Origin supports IPART's recognition that the AEMC rule change requiring retailers to write to standing offer customers annually to advise that better offers exist, coupled with specific actions retailers have committed to with the aim of assisting NSW customers, should result in greater market transparency and consumer confidence in the energy market.

We strongly support IPART's finding that a regulated default tariff is not warranted. This is further supported by the finding that retail prices reflect the underlying costs of supply. We believe the re-introduction of regulated retail tariffs is likely to lead to adverse market outcomes including a reduction in competition, stifling of innovation and increase the risk of regulatory error. We note the measures currently being implemented in response to both the Prime Minister and NSW Government. We recognize the need to improve price transparency for customers and could support a default reference

price from which all retailers can discount, with sufficient headroom incorporated to enable true competition among retailers for the benefit of consumers. However, we remain opposed to a default price cap, which would be a return to price regulation and stifle and potentially lessen competition.

Origin's response to specific issues identified in the draft rule report are set out below.

Key Indicators of Competition

IPART has identified a continued trend of engagement in the energy market in NSW. IPART found that NSW remains the second most competitive electricity market in the NEM, supporting the AEMC's report, which indicates this has been the case since 2011¹. IPART also found that switching rates in NSW were relatively high, and relies on this data as an indicator of customer engagement. This approach is consistent with that taken by the AEMC and reflected the AEMC's finding that customer engagement across NSW remained stable in the past year. The AEMC reports that switching rates are relatively high, with 19% of customers switching their electricity retailer in 2017, and 14% switching gas retailers.² IPART reports similar findings regarding consumers engagement, reflecting strong price competition in the market.

IPART expressed concern that incumbent retailers appear to prevent small retailers rapidly gaining market share by undercutting pricing in retention marketing activities. Origin is committed to making energy more affordable and offers both new and existing customers products which we think will work best for them. Organizations have a natural motivation to retain customers, and retention activities are one mechanism to achieve this which support strong price competition in the market. Customers who engage with a retailer are likely responding to price competition by switching or demanding lower prices from existing providers, or sometimes both. Further, new entrants into the market put firm pressure on pricing as they offer new products and service differential. New entrants put pressure on existing retailers to provide innovative responses to their product offerings.

Energy Prices

IPART's report highlighted that energy costs have reduced in real terms, although the percentage of reduction provided to a specific customer depended largely on which distribution network supplied them. Origin supports this finding, and we have taken steps to shield customers from market volatility where we have been able to. For instance, in NSW we voluntarily absorbed some of the cost for our vulnerable customer base in 2017, and in 2018 made the decision to absorb what would have been a 3% price increase for all customers.

IPART's report was also consistent with the recent ACCC report, which confirmed the rise in power prices was primarily a result of over-investment in the networks that transport electricity, rising wholesale prices following sudden plant closures and the cost of government green schemes. The ACCC's recommendations will require network reforms to be implemented, and until such time retailers are only able to manage increasing costs to consumers to a limited extent. In real terms residential customer

¹ AEMC 2018 Retail Energy Competition Review p.268

² Ibid.

electricity bills are lower than before price deregulation,³ and we are pleased to see that IPART has presented evidence of the competitive retail market working in the interest of consumers, even when constrained in its ability to truly do so by external factors. We recognize that energy affordability remains a key issue for many Australians and we too want to bring prices down.

The sustainable way of achieving lower prices is to take a whole of industry approach that addresses network, wholesale and green costs. Retailers are already working to make it easier for consumers to engage with the energy market confidently, through developing new products and services, such as Origins 'Savernator' dollar-value comparison tool, designed with customer needs in mind. Origin have also presented offers in dollars-per-month terms on our website for some time. Origin notes that this work will need to continue so that more customers can experience the benefits a competitive market can deliver, but retailers cannot provide lower pricing alone. We support sensible and well considered energy market reform that delivers good outcomes for consumers and the market.

IPART's Bill Estimation Methodology

IPART's bill estimation methodology appears to take a fair and reasonable approach to making a representation of the spread of offers in the market, and associated cost to consumers. Origin does not consider that it represents our NSW customer base, as our most common offer is also one of our cheaper offers. As such we consider that IPART's allocation of 25% of consumers to the mid-point between lowest and standing offer pricing may result in an over-estimation of our customers costs. Origin does not consider this problematic so long as IPART recognizes that this estimation practice is imperfect. If a consistent methodology is applied in undertaking future market assessments, the mechanism is appropriate to provide a representative picture of the overall market.

Underlying costs of supply

The Minister for Energy and Utilities requested IPART to undertake a review of whether the changes in electricity and gas retail prices into 2018-19 reflect efficient costs in a competitive retail market. IPART estimates that costs have decreased by around 9% for 2018-19 using a point in time estimate of wholesale market prices,⁴ however observed that retail prices did not decrease in line with this overall decrease. Origin notes that when IPART made the same assessment but effectively assumed that retailers purchased hedge contracts over a two-year period (rather than 30 days in June) then it found that retail prices for 2018-19 would not be expected to decline. IPART has demonstrated that costs are reflective over this more extended period, and customers benefit from the smoothing of costs as they do not experience unnecessary cost spikes.

We note that Origin held its prices flat in NSW for 2018-19 and in doing so absorbed \$80 million in cost from what should otherwise have been a 3% electricity price increase.

IPART's report recognized that in a deregulated and competitive market, retailers have the capacity to manage their risks. To manage risk and consumer confidence retailers seek to achieve stability in year on

³ IPART *Review of the retail energy market in NSW 2017-18* 1.1, page 1.

⁴ IPART *Review of the retail energy market in NSW 2017-18* 1.3.1, page 4.

year prices. The retail price is only one component of the overall cost stack. Origin endorses that IPART found no strong evidence that retailer margins were higher than appropriate in NSW. Additionally, the specific review of the mid-year price change was found consistent with a competitive market, as it was in line with the underlying cost of supply in the wholesale market. Considering this finding, Origin supports IPART's position that there is no need for pricing intervention. IPART's report indicates that retailers are passing through efficient costs and are doing so whilst shielding consumers from market volatility where possible. IPART understands the complexity involved in ensuring that costs were passed through efficiently, in a manner that provided certainty and predictability to consumers, as evidenced in the approach taken to making this assessment. Origin would question the purpose of price intervention where the existing market is performing appropriately and supports IPART's recommendation to avoid price regulation.

Default price is not a preferred option

Pricing intervention undermines certainty and creates additional risk, which will only serve to exacerbate supply and price issues. In such an environment we are unlikely to see the investment in new energy generation needed to deliver truly sustainable lower prices. Origin does not support pricing intervention, as it has the potential to lead to long-term adverse outcomes; reducing investment in generation, slowing innovation in new energy services and reducing choice in both products and providers. The investment and innovation possible when there is policy certainty forms the basis of reduced costs to customers in the future.

Origin does support reform that makes it easier for customers to understand and compare offers. Origin has progressed work to assist customers confidently engage with the market without the need for pricing intervention, already having launched products that make it easier for customers to understand and manage their bills. Origin believes that competition is enhanced by customers being able to understand their options and that ease of engagement will help change customer behaviors, leading to more intense competition and pushing lower pricing. Introducing a regulated price will not change customer behaviors, will increase price risk and result in the narrowing portfolio of products and services. A regulated price will undermine any effectiveness in the market and have the inverse effect of increasing energy costs. Many reforms suggested by the ACCC will in combination lead to pricing reductions and market stability without the need for a default price. Re-introducing price regulation or a 'default tariff' is likely to lead to lower levels of competition and higher prices, as it imposes risk on the market.

Need for Stable Frameworks

Origin supports IPART's view that the most effective way governments can ensure sustainable prices in the future is to provide conditions that encourage new investment in the wholesale market to increase supply, and replace existing generation as it reaches the end of its asset life. Actions on network costs and government green scheme costs, should be equal priorities. Origin sees positive and consistent long-term energy policy as fundamental, if the industry is to continue to deliver the investment required to meet growing demand at the least cost to consumers. IPART has raised concerns that the lower pricing that could have been found for consumers as network costs reduced over the review period was negated by

rising wholesale energy costs as the impacts of the reduction of wholesale capacity played out across the NEM. Origin absorbed and smoothed out much of this volatility to provide stability for consumers.

Origin shares IPART's concerns that the imposition of a regulated price tariff would lead to poor consumer outcomes. This pricing imposition is unnecessary where the market has produced evidence of working to the benefit of consumers, and does not deliver a framework in which investment is likely. Further, we are concerned about the lasting impact of regulatory error; setting a default price that is either too low or too high will result in market instability, lower consumer engagement rates, and higher prices as innovation and investment are stifled.

Closing

Origin supports IPART's analysis that competition continues to develop in NSW. We strongly support IPART's finding that a regulated default tariff is not warranted, as energy prices are reflective of the underlying costs to supply customers. Origin continues to address the non-price concerns raised by IPART and other monitoring bodies, such as retention and discounting practices. IPART's report highlights the need for policy makers to create the right conditions to provide market participants the incentive to make positive investments which will start to bring long term pricing results.

Should you have any questions about our submission or wish to discuss further, please contact Courtney Markham on (03) 9821 8086 in the first instance.

Yours sincerely



Keith Robertson

Manager, Wholesale and Retail Regulatory Policy

