



Time for retailers to rebuild consumer trust and confidence

Australian Energy Market Commission (AEMC) Retail energy competition review 2018

This year's report found competition in the retail energy market continues to evolve. However it is not delivering expected benefits for people who don't understand their energy deal, don't think they are getting value for money, and can't access opportunities to control their bills. Whilst some consumers are benefitting, they need to shop around for cheaper prices or innovative deals.

What is the review of retail energy competition?

The Australian Energy Market Commission (AEMC) monitors the state of retail competition in electricity and gas markets every year. It looks at whether competition is working to deliver benefits to customers.

Key finding

Many retailers continue to offer complex tariff structures and conditional discounts leaving consumers confused and dissatisfied. Consumer trust in energy retailers has fallen from 50 per cent to 39 per cent and many are responding by taking matters into their own hands, by investing in solar PV or batteries.

Overview of the state of competition

The AEMC retail energy competition reviews are conducted at the request of the Council of Australian Governments (COAG) Energy Council. The 2018 review is the fifth review of retail energy markets in national electricity market. It covers residential and small business consumers in retail electricity and gas markets in Queensland, New South Wales, Australian Capital Territory, Victoria, South Australia and Tasmania.

This year's review shows improvements in the structural indicators of competition, with new entrants in electricity and gas markets, reductions in market concentration and increases in the market share of second tier retailers. Although limited, emerging benefits include some innovative pricing offers such as fixed pricing and fixed billing options and bundled deals with other services. Solar PV systems, batteries and energy management applications, are providing consumers with options to manage their energy usage and bills.

Recent retailer announcements point to flatter or falling energy prices. It is positive that the big retailers are passing through falling wholesale prices but it's just the beginning of what retailers need to do to regain the trust and confidence of their customers.

In the year under review the closure of Northern and Hazelwood generators and higher gas commodity costs drove rises in wholesale energy prices. Many retailers were slow to respond to these changes and continue to offer complex tariff structures and conditional discounts. Retailers are not helping consumers understand the reasons for change, or offering deals that customers understand, value, or that provide opportunities to respond. Consumer satisfaction has decreased and consumers are not confident that the retail energy market is working in their long-term interests.

As a result of limited retailer-led innovation, and decreasing technology costs, some consumers are taking matters into their own hands, investing in solar PV systems or batteries to reduce their energy bills. Not all consumers are able to take advantage of such developments however, which highlights the need for appropriate consumer protections.

Tier 2 retailers have strengthened their competitive position and the market share of the big three retailers, Origin Energy, AGL and EnergyAustralia, continue to fall.

Structural signs that competition is continuing to develop

- There are 16 gas retail brands and 33 electricity retail brands across the NEM-based jurisdictions.
- *Vertical integration and stand-alone retailers:* In all jurisdictions with price deregulation, the market share of the big 3 retailers continues to fall, although they still retain dominant positions in each jurisdiction

Tier 2 retailers have strengthened their competitive position, especially those with generation assets. In contrast, smaller electricity retailers without generation assets have found it more difficult to compete. A number indicated reductions in wholesale contract market liquidity exposed them to higher wholesale costs over the past year, affecting their ability to provide competitively priced offers.

- *Wholesale contract market transparency:* Some stand-alone electricity retailers questioned whether higher wholesale costs were similar to those experienced by vertically integrated retailers. Currently there is neither visibility of over-the-counter contract costs, nor information publicly available on the internal transfer costs of retailers with access to their own generation.
- *Innovation:* The consumer-led growth in solar PV systems and the emerging interest in batteries represent a structural shift in the retail market and a departure from the traditional retailer electricity supply model.

Competitive energy market yet to deliver desired outcomes for consumers

- The pricing and product offerings of energy retailers are confusing for consumers. Common characteristics of energy market pricing include:
 - complex tariff structures
 - discount claims that are hard to compare
 - most discounts are conditional
 - increasing price dispersion, which is driven by discounting not effective customer segmentation.
- In the past year, there has been an increase in the number of retailers offering 'no discount', fixed price and fixed bill plans that make it easier for consumers to understand what they will pay for their energy. At this stage, the number and take up of these alternative offers is limited.

Residential consumer interaction with the retail energy market varies

- Consumer attitudes towards the retail energy market in April 2018, compared to April 2017, showed that:
 - 25 per cent of consumers were confident that it was working in their long-term interests (down 10 per cent)
 - 50 per cent of consumers felt they had access to easily understood market information (down seven per cent)
 - 58 per cent were confident they could make good decisions (down 11 per cent).

Consumer trust in the sector dropped from 50 per cent to 39 per cent in the past year. The decline in consumer metrics is correlated with the large price rises.

- Consumers have responded differently to the challenges faced:
 - some have disengaged
 - some have become more motivated to shop around
 - others have invested in solar PV or batteries to gain greater control over their energy consumption and bills
- *Consumer disengagement:* Only around 20 to 40 per cent of customers that have been with Big 3 retailers for more than three-to-four years, are on discount levels similar to those customers that have just joined.

Retailer inertia and a lack of transparency have emerged as significant barriers which are preventing consumers from gaining the maximum benefits possible in terms of prices and services.

- *Consumer benefits from engagement with the market:* Switching rates increased with the recent price increases, as over the past year:
 - more than a quarter of customers in South East Queensland and Victoria changed electricity retailer
 - 19 per cent of consumers in Victoria and 14 per cent in New South Wales changed gas retailer.

A residential customer moving from a median standing offer to the cheapest market offer can save:

- on electricity, \$832 in South Australia, \$574 in Victoria, \$504 in South East Queensland, \$365 in New South Wales, and \$273 in the Australian Capital Territory.
- on gas, \$716 in Victoria, \$192 in the Australian Capital Territory, \$185 in New South Wales, \$161 in South Australia and \$31 in South East Queensland.

These savings have generally increased from last year across jurisdictions.

The review identified 19 commercial comparison websites. These simplify the choice for consumers, and assist in changing plan or retailers. However, the commercial sites lack transparency about how many retailers and offers they compare. The Government comparison websites, *Energy Made Easy* and *Victorian Energy Compare*, have much broader coverage, but do not have a switching function and, historically, awareness has been low.

- *Consumer options to use solar PV systems, batteries, and energy management products and services:* Consumers have demonstrated their willingness to invest in their own energy generation and management capabilities. There were:
 - 154,877 residential solar PV installations in 2017, an increase of 25 per cent from 2016, which added 938MW of solar capacity to the NEM.
 - Battery installations increased by around 275 per cent in 2017 from a low base, and interest in household batteries increased considerably.

An assessment of the financial benefits of an investment in solar PV or a combined solar PV and battery system (e.g. excluding the non-market values people attribute to being off grid) indicate that, accounting for the small-scale renewable energy scheme:

- Solar PV systems are attractive in a broad range of consumer circumstances. They deliver a short-term payback and longer-term benefits.
- Batteries require considerable cost reductions or improvements to battery life to be as financially attractive as solar PV systems, and larger batteries are less financially viable.

Differences in the consumer protections available to solar customers may not be well understood. For example:

- If an electricity retailer supplied the solar system, the customer will likely be covered by a jurisdictional ombudsman scheme.
- If the system is supplied by another provider, then the protections in the National Energy Customer Framework will generally not apply and the consumer will have to rely on Australian Consumer Law and jurisdictional fair trading offices.

Vulnerable customers need protection

- Vulnerable consumers were particularly affected by increases in energy prices that occurred in 2017.
- While the overall number of customers in retailer hardship programs has remained relatively stable, the number of customers being excluded from these programs has increased considerably, often for non-payment. Consultation is underway on a rule change proposal to strengthen retailer obligations so hardship customers are given improved support.

Consumer empowerment is important for a well-functioning energy market and vulnerable consumers need protection.

The small business experience of the retail energy market

- Small businesses were significantly affected by increases in energy prices that occurred in 2017, as they pay more per-unit of energy and consume higher levels than residential consumers, but do not have the same hardship or payment plan protections.
- Over the past year, 36 per cent of small business customers expressed surprise by the increase in their energy bill, and of those:
 - approximately half absorbed the price rise
 - approximately half made efforts to reduce their consumption
 - 17 per cent looked to change retailers.
- Differences in size, turnover and energy use materially affects engagement.
 - Businesses with above 100 employees are generally more aware of energy management options, and more confident in finding the right information to choose plans.
 - Smaller businesses are less confident in finding the right information, have lower levels of trust and are less likely to invest in new technology.
- Retailers have been more active in approaching businesses, with a 30 per cent increase in approaches from the previous year, and 90 per cent of small businesses were approached by a call from a retailer, an increase of 33 per cent.
- Small business owners from a cultural or linguistically diverse background saw greater value in renewable energy and new technologies that increased energy management.

Consumer empowerment is important for a well-functioning energy market

- Consumer empowerment can be advanced through:
 - improved quality and ease of access to consumption data
 - improved access to enabling technology that provide consumers more control over their energy consumption and bills
 - further education of consumers.

A coordinated and considered approach to energy markets is required

- The Commission considers that while competition in the retail energy market continues to evolve, it is currently not delivering the expected benefits to consumers.
- If further government intervention in the sector is being contemplated, it must be done against the possible impact it may have on the key consumer outcome areas of: price, choice, level of service, and innovation.
- A focus on enabling consumers to have greater control over their energy usage and bills, and targeted interventions where necessary is preferable to re-regulation.

Discounting remains the predominant way of competing. This high level of discounts is an issue because they are not from a standard base across retailers, and penalties can be significant if conditions are not met.

Recommendations

The review makes a number of recommendations that relate to enhancing competition in NEM retail energy markets and improving consumer outcomes.

Protecting consumers

Recommendation 1: Taking into account any voluntary codes that have been developed by industry and the ECA to protect consumers receiving services from new energy service providers, the AEMC will assess whether changes to the NECF are also required to protect these consumers. The work will commence in March 2019, unless otherwise advised by the COAG Energy Council.

Recommendation 2: The AEMC to assess how retailers support customers in financial difficulty, unless advised otherwise by the COAG Energy Council by January 2019. The review would look at the support options retailers provide commercially, and how these operate with required hardship provisions.

Enabling consumers

Recommendation 3: Retailers and comparison service providers establish an industry code of conduct for energy comparison sites and obtain ACCC authorisation for the code if necessary. The code development and any authorisation process should be funded by industry and involve representatives from consumers and other affected stakeholder groups. Failing the development of an effective code, regulatory measures may be considered.

Recommendation 4: All comparison websites should display, in a prominent location the number of retailers and plans represented on their site as a proportion of all retailers and plans available in the consumer's distribution area.

Improving market transparency

Recommendation 5: The AER to separately report on customer numbers, switching rates and contract type for both residential and small businesses.

Recommendation 6: The AEMC will work with industry to make data on over-the-counter electricity contracts available to the market in a form that enhances transparency of the wholesale cost of energy. This work will be done in conjunction with any proposed mechanism that would give visibility of over-the-counter contracts in the National Energy Guarantee work program.

Background

The AEMC retail competition reviews were initially undertaken to support the commitment made by jurisdictions in 2004 to deregulate retail energy prices where effective competition could be demonstrated. In the retail energy market, price deregulation of gas and electricity has been implemented in most jurisdictions. Given the extent of deregulation, this year's review focuses on how competition is evolving and the outcomes it is delivering for residential and small business consumers.

Consistent with the approach taken in 2017, to consider the overall effectiveness of competition in retail energy markets, the review examines a range of market measures and indicators within a structure-conduct-performance framework. The market measures and indicators are not considered in isolation, as no single measure or indicator captures all the information about the effectiveness of competition in the retail energy services market. Instead, the review assesses evidence provided by a range of indicators and measures and their trends over time. The analysis of measures and indicators uses market and retailer data, quantitative consumer research, a retailer survey and stakeholder feedback.

For information contact:

AEMC Executive General Manager, **Kris Funston** (02) 8296 7811

AEMC Director, **Michael Bradley** (02) 8296 7868

AEMC Adviser, **Prabpreet Calais** (02) 8296 0605

Media: Communication Director, Prudence Anderson 0404 821 935 or (02) 8296 7817

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