Survey and interviews with South Australian electricity and gas retailers

Prepared for Australian Energy Market Commission

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1 Introduction

The Australian Energy Market Commission (AEMC) is reviewing the effectiveness of retail competition in the supply of electricity and gas in South Australia. The Australian Energy Market Agreement (AEMA) requires the AEMC to review the effectiveness of competition in the retail supply of electricity and gas in each jurisdiction participating in the National Electricity Market (NEM), and publicly report the results. The South Australian review follows a review of competition in the State of Victoria undertaken in 2007.

As an input to its review of competition in South Australia, the Commission:

- Asked each retailer participating in the South Australian energy markets and potential retailers that had considered entering the market but had not done so, to complete a written survey; and

- Conducted confidential face-to-face interviews with each existing and potential retailer.

The interviews were facilitated by the market research company, McGregor Tan, and were attended by LECG and AEMC representatives.

This report summarises the findings from the surveys and the interviews.

The remainder of this report is structured as follows:

Chapter 2: Key themes

Chapter 3: Methodology

Chapter 4: Background and company profiles

Chapter 5: Retailer rivalry

Chapter 6: Customer participation and experience

Chapter 7: Conditions for entry, expansion and exit

Appendix 1: Retailers invited to participate

Appendix 2: Electricity retailer survey

Appendix 3: Gas retailer survey

2 Key themes

This chapter provides a summary of key themes which emerged from the survey responses and during interviews with energy retailers. Themes are organised under the following headings:

- Retailer participation and customer shares;
- Conditions for entry and expansion;
- Customer participation and retailer rivalry; and
- Emerging industry structure.

In responding to questions, many retailers chose to draw comparisons between South Australia and Victoria. There appear to be several reasons why comparisons were made with Victoria; the AEMC has recently completed a review of competition in gas and electricity retailing in Victoria; elements of the regulatory environment and gas market rules were viewed as more advanced in Victoria; and Victoria is adjacent to South Australia and inter-connected.

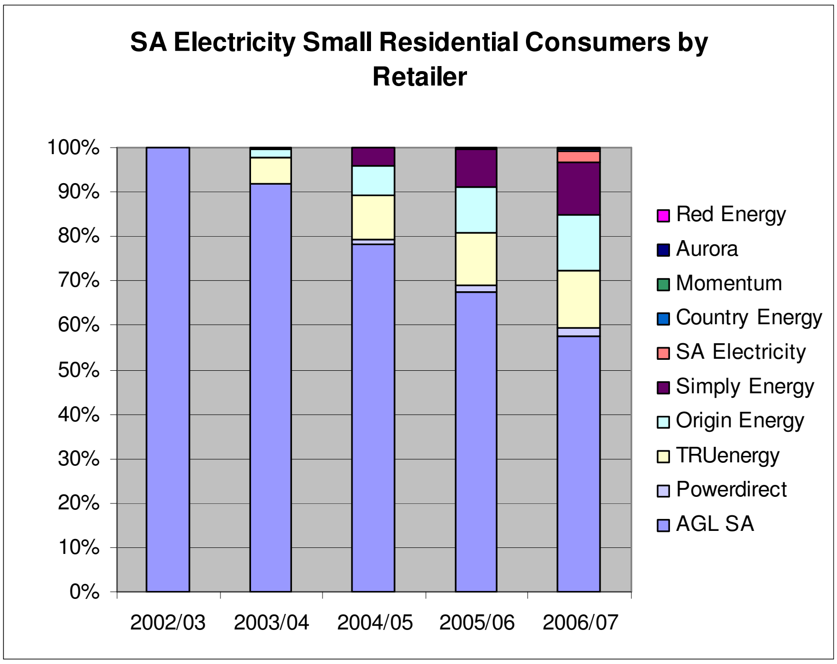
2.1 Retailer participation and customer shares

Fourteen firms are currently licensed to retail electricity in South Australia (with the intent of supplying small customers) and ten firms are licensed to retail gas. If this survey had been undertaken 18 months ago, nine electricity retailers and four gas retailers would have been actively marketing to new customers. Currently, five electricity firms and three gas firms responded saying they were actively marketing for new customers in South Australia. Retailers (particularly those who are not vertically integrated) pointed to high wholesale spot prices, and an inability to recover these costs in the face of standing offer prices as their main reason for suspending active marketing.

We mention this change in circumstances to illustrate that surveys of this nature inevitably report events and views at a particular point in time; we have where practical tried to provide some context by asking how circumstances might have differed in the past and retailers expectations as to future events. However, the answers are necessarily coloured by the retailers' current experience.

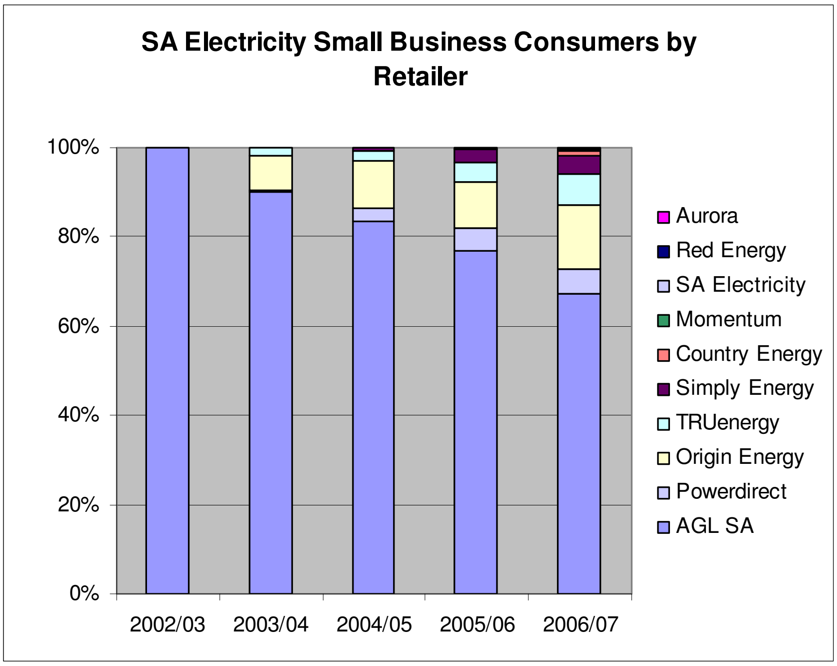
Changes in the customer shares of South Australian electricity retailers, when measured in terms of customer numbers, since the introduction of full retail competition are shown in the figures below. Customer shares for residential and small business customers are shown separately. (Source: ESCOSA Annual Performance Report 2006/2007)[1]

Figure 1. Electricity: Share of residential customers



[1] AGL acquired Powerdirect in March 2007. Their market shares may now be considered together.

Figure 2. Electricity: Share of small business customers



The following figures show changes in customer share for gas retailers since the introduction of full retail competition. As with the electricity figures presented above, customer share is based on customer numbers. (Source: ESCOSA Annual Performance Report 2006/2007)

Figure 3. Gas: Share of residential customers

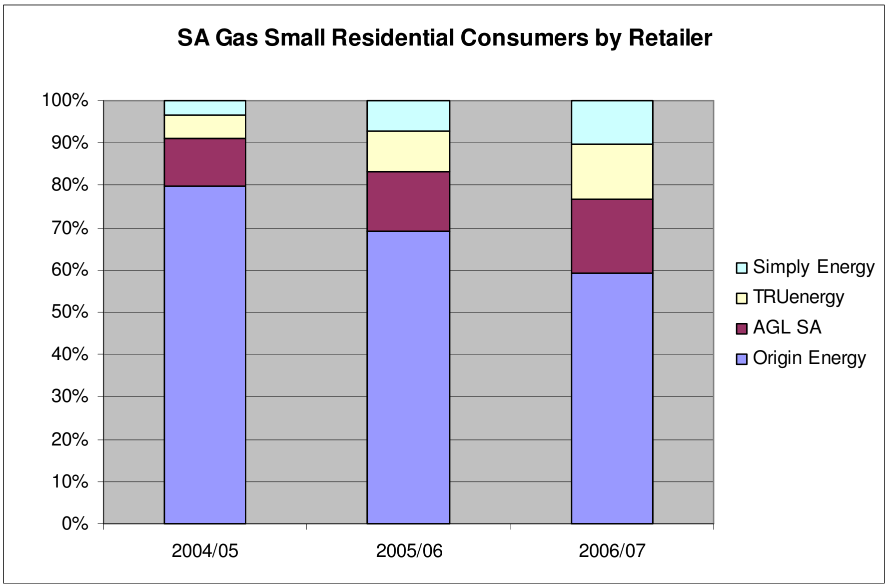
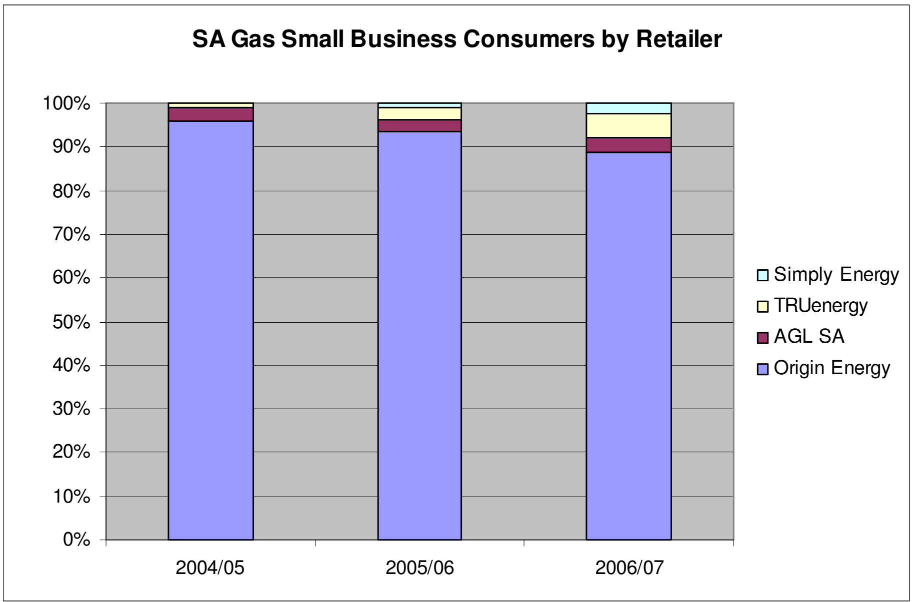


Figure 4. Gas: Share of small business customers



Most retailers drew our attention to these changes in customer share as illustrating the competitive nature of the retailing electricity and gas in South Australia. Electricity retailers, in particular, emphasised the number of retailers that had entered South Australia and the decline in the share of customers served by the host retailer as evidence of strong competition.

2.2 Conditions for entry and expansion

2.2.1 Market conditions – electricity

Retailer price offers in South Australia are predominantly, though not exclusively, expressed with reference to the standing offer; for example, an offer might be made at a set discount to the standing offer price. All retailers surveyed consider the standing offer price when preparing their own price offers, and eight out of 10 responded that the standing offer price was either an important or a very important factor in influencing their offer price.

All respondents noted that over the past 18 months or so, wholesale electricity prices in South Australia have risen significantly and spot price volatility has increased. Retailers generally perceived these wholesale price increases as having reduced substantially or eliminated the margin previously available between the wholesale price and the standing offer retail price. Smaller retailers pointed to the lack of liquidity in forwards markets in South Australia (relative to say Victoria), and cited the lack of trading through the Sydney Futures Exchange. Most retailers said that the drought and constraints on the interconnector meant the supply of forward contracts reduced markedly and were priced at levels at which it would be unprofitable to take on new customers. Most retailers commented that the recent sale and purchase of the Torrens Island Power Station had removed both demand and supply from the forward markets, reducing liquidity.

With one exception, retailers said that hedge and other risk management contracts were available. However, the smaller retailers said that the prices offered for those contracts had been too high over the past 12 months or so to allow them to hedge their risks and take on new customers profitably. Vertically integrated retailers maintained that internal transfer prices meant that they paid the same price for hedges as standalone retailers; if the trading teams could achieve a better price by selling to a third party they would do so. Some larger retailers maintained that periods of volatility are inherent in electricity markets and that poor risk management by some retailers should not be blamed on the market.

A number of retailers stated that the structure of the South Australian electricity sector meant that one vertically integrated retailer could periodically exercise market power.

As margins were squeezed, the majority of the smaller retailers ceased actively marketing for new customers. Most retailers indicated they would still accept 'walk-ins'; that is, the retailer would accept customers that approached them, but they had ceased activities such as door-to-door campaigns and outbound telemarketing. The smaller retailers said that at current margins it was not profitable for them to pay the cost of commissions from active marketing.

The larger retailers maintained that they were still actively seeking new customers, though less emphasis was placed on these marketing activities currently relative to other state jurisdictions and relative to the level of marketing in South Australia 12 months ago.

Several retailers contrasted the situation in Victoria, where the price of hedge contracts has fallen and standing offer prices have risen in 2008, allowing a margin for competition, with the situation in South Australia, where margins remain very tight.

Those retailers that had ceased actively marketing (and those that have not yet entered the market) were for the most part keeping a watching brief on the market and indicated they would return to active marketing (or actively consider entering the market) should they perceive improved margins either from a reduction in wholesale prices or through lifting of the standing offer rates. A number of retailers, however, noted that even a temporary withdrawal may potentially have a longer term impact on competition through its effects on profits and confidence, and hence investment, in the market.

2.2.2 Market conditions – gas

Gas retailers reported similar market conditions to electricity. Wholesale prices for gas were viewed as high relative to the regulated retail prices. The gas retailers said that there had been little if any margin available between the wholesale gas prices and the regulated standing offer price for gas. Most retailers noted that the Essential Services Commission of South Australia (ESCOSA) was currently reviewing the regulated retail gas price. Retailers emphasised their concern that this review should result in an adequate margin; one retailer commented that it would consider exiting South Australia if sufficient margins were not available following the review.

In addition to the perceived lack of margin, retailers observed that the retail gas business in South Australia was a low volume business – households consumed less gas than say households in Victoria and a lower proportion of households are connected to gas.

Almost all retailers said that they would only consider marketing gas as a dual fuel – that is, to customers that also took electricity. None of the new entrants, or prospective entrant retailers, considered retailing gas as a standalone business.

The retailers that had temporarily ceased actively marketing gas said they were unlikely to re-engage in the market in the medium term (whereas electricity retailers were maintaining a watching brief and would re-enter if conditions allowed).

Those retailers continuing to market for new customers suggested that they were not doing so as aggressively as 12 months ago or were placing comparatively greater emphasis on marketing in other states.

2.2.3 Other barriers to entry and expansion - electricity

Retailers generally viewed the South Australian market as having low barriers to entry, provided they could access hedge and risk management contracts at acceptable prices. All retailers with customers in South Australia mentioned the number of new entrants since full retail competition as evidence of low barriers to entry. They also mentioned the fall in the host retailer's customer numbers as evidence of the ability for new entrants to establish a market presence. One retailer suggested that barriers to entry may have been too low in electricity; that it was too easy for a retailer to gain a licence and enter South Australia, with the retailer of last resort bearing the risk if a new entrant retailer was not able to sustain its business after not taking sufficient hedge cover.

Retailers did not face problems accessing distribution infrastructure for electricity. However, concerns were expressed by smaller retailers about prudential requirements, both for access to the local distribution network and to the National Electricity Market Management Company (NEMMCO).[2] Their concern was that as small retailers they had to provide cash backed guarantees, whereas large established retailers had investment grade credit ratings and hence were not required to provide cash backed guarantees. A number of the smaller retailers felt that prudential policies were inflexible

[2] The concern in relation to NEMMCO's prudential requirements related to the ability and willingness of generators to 'reallocate'. Reallocation would allow a retailer to 'offset' its settlement obligations to NEMMCO with payments due to it from a generator under a forward contract (that is, NEMMCO can reduce one party's debit to NEMMCO and reduce the other party's credit position correspondingly).

and did not allow for instruments such as receivables insurance, or recognise payment history.

No retailer raised economies of scale as an issue for initial entry and expansion; retailers were able to make use of infrastructure and expertise developed in other states and outsources various tasks. Views were mixed on whether a retailer expanding to a larger scale would encounter issues of investment scale. Some retailers maintained that the models adopted by new entrants were feasible only for relatively small scale operations; others took the view that recent entrants were advantaged by not having legacy systems that were difficult and costly to change.

Customer attitudes, brand loyalty, advertising and marketing requirements were not generally regarded as significant barriers to entry by retailers.

Some policy differences between the States were perceived as having the potential to segment the operations in different jurisdictions. One example of such a policy difference raised in interviews related to smart meters; were Victoria to proceed with installing smart meters and South Australia to retain non-interval meters, retailers operating in each state would receive vastly different information flows and would begin to package retail products in Victoria and South Australia differently. Eventually the operations across different jurisdictions may become segmented.

A number of the smaller retailers commented that regulatory policy in South Australia had the potential to hinder efficiencies from operating in several jurisdictions. Retailers believed that some of the differences in regulatory requirements between States were not a function of different policy concerns, but a lack of sufficient care in standardising regulatory requirements. As an illustration, one retailer said that requirements to achieve the same outcome might be expressed differently, requiring billing software to be coded differently for each State.

Other potential regulatory policies were viewed as possibly altering the competitive field. For example, a number of retailers expressed a concern that the proposed Residential Energy Efficiency Scheme (REES) which would require retailers to assist consumers with energy efficiency schemes may favour host retailers with established infrastructure in South Australia. Many retailers expressed concern at ‘over regulation’ of service standards – the regulations in South Australia were perceived as being prescriptive in areas which should be left to competition (for example, how long it took to answer a telephone call and information required on billing statements).

Most retailers found ESCOSA professional and responsive; the regulator had welcomed entry and assisted retailers with information on regulatory requirements. Two retailers had the opposite experience with ESCOSA and had found it slow to respond, cumbersome and South Australian regulatory obligations requiring a disproportionate amount of management effort.

2.2.4 Other barriers to entry and expansion - gas

Retailers generally perceived higher barriers to entry to gas retailing in South Australia compared to electricity retailing and gas retailing in other states. These barriers included the difference in market design relative to Victoria and the investment required in building and retaining knowledge and skills specific to South Australia.

Some retailers had viewed future gas supplies as uncertain (the SEAGas pipeline is fully contracted, capacity on the MAPS is available but gas supply from the Cooper Basin is in decline). During interviews, the retailers that had expressed concern suggested that those concerns were easing and that the 'market' was becoming more confident of future gas supplies (coal seam gas supplied from Queensland via the MAPS was mentioned by most gas retailers). New entrant retailers, however, believed that it would be difficult to contract for small volumes of gas and the pipeline capacity needed for an entry strategy.

Small retailers also perceived that the arrangements for contract carriage and swing gas and related mechanics of the market were difficult to manage and could prove expensive relative to retail prices and volumes. For example, small retailers expressed concern that if they were not able to project gas volumes accurately they would be required to pay high prices (relative to the delivered retail price) for swing gas and additional carriage. These small retailers also expressed general concerns at relying on competitors for swing gas and other market arrangements.

Access to gas distribution network capacity was not generally considered a problem, except in some smaller rural areas. The cost of transport of gas to North Adelaide was perceived to be high, after taking into account various charges that might be incurred for variable volumes, especially in relation to the small volumes that could be anticipated by a new entrant retailer.

Identifying prospective customers was also considered more difficult for new entrant gas retailers than for new entrant electricity retailers; all households on any given street will purchase electricity although only a portion will purchase gas. Retailers commented that there were fewer customers connected, on average, to each segment of the gas network in South Australia than there would be for a comparable length of gas network in Victoria.

Marketing to small to medium-sized business users was considered particularly difficult. Not all small businesses used gas, and once the firm was identified as using gas, it was often difficult to gain the attention of the decision-maker. The decision-maker in a small business is often the owner or operator with many competing demands on his or her time. He or she may not have time to adequately consider any offers presented to them, especially as gas is likely to comprise only a small part of the cost structure of the firm. In addition, business owners can generally only be contacted during business hours, decreasing the window of opportunity.

Regulatory differences between South Australia and Victoria were generally not considered a major issue, because the design of South Australia gas arrangements were so different that any firm retailing gas in South Australia would need to build a dedicated team to transact in that State.

2.3 Customer participation and retailer rivalry

2.3.1 Customer participation

All retailers characterised electricity and gas as low involvement commodities; new and established retailers seeking to win customers from existing suppliers must actively market to those customers and provide offers which motivate them to switch to another retailer. Door-to-door sales were considered the most effective means of marketing, with outbound and inbound telesales the next most important.

Retailers admit that at times they have difficulty controlling the activities of door-to-door sales teams. Retailers were concerned about any improper approaches by door-to-door agents and had practices in place to address any problems quickly; retailers were conscious of the damage which could occur to their reputations and believed that all retailers acted responsibly and would address issues when notified of concerns.

A number of retailers found sponsorship of sporting clubs or associations an effective marketing tool, as well as advertising in local or community newsletters. Established retailers tended to use mass marketing, such as television, more than new entrant retailers to promote their brand. However, new entrants seeking to be identified with a new product offer used television to promote the product, but then switched to door-to-door or telesales to complete the sale. Established retailers tend to use bill insertions for promotion and marketing more than new entrant retailers.

Retailers commented that South Australian consumers were at least as well informed as Victorian consumers.

All retailers would accept all customers that clear credit checks. However, most retailers have demographic targets for their marketing campaigns. These demographics are primarily aimed at identifying higher volume and good credit risk customers. Retailers used quite sophisticated techniques to identify target neighbourhoods. Some retailers try to target niche markets, such as customers who are more likely to favour green products or customer groups likely to be less attractive to other retailers, such as rural customers. Customers in smaller communities were perceived as more loyal than customers in Adelaide.

Small business customers were more costly to acquire than residential customers, but more valuable once obtained.

2.3.2 Retailer product offerings

Retailers reported that price remains the overwhelming factor in a consumer's decision to switch retailers. Price offers are usually, but not exclusively, in the form of a discount to the standing offer. Many retailers attribute a lack of innovation in price offers to the regulated standing offer, saying that in the absence of the standing offer they would align terms more with customer demands. However, retailers provided only a few specific examples of the changes they would make to contract terms if price regulation were removed. A number of retailers commented that offering ‘a percentage off’ the standing offer was a simple and effective method of communicating their offer to customers; in the absence of the standing offer they would look for some other, easily understood, bench mark. These retailers questioned whether there was a demand by customers for more complex pricing arrangements.

Green energy or renewable energy is becoming an increasingly important element of product offerings to many customers. Retailers used green energy to differentiate their product to try move away from price based competition. However, retailers have generally found that customers were not yet willing to pay much of a premium for green energy, though they were willing to forego a small discount or accept other contract terms that produce value for the retailer.

Most retailers offer some form of cash and non-cash incentive to new customers switching to them, and to existing customers, as a way of retaining them. These non-cash incentives generally amount to less than 5% of the customer’s energy bill.

Customer service is viewed by many retailers as an important element of their competitive strategy to retain customers. Several retailers commented that customers joined them because of price discounts but remained with them because of better service.

Dual fuel is an important element of the marketing strategies for most retailers that operate in other States, at least as a general proposition. Dual fuel is viewed as important by retailers because it allows the retailer to gain from cost synergies – the retailer gains a second customer at little additional cost in terms of servicing or acquiring that customer. However, for the reasons outlined in sections 2.2.2 and 2.2.4, a number of retailers who have gained gas licences in South Australia do not now expect to enter the retail gas market.

Retailers reported quite different views in relation to whether dual fuel customers were more or less likely switch to another retailer. Some retailers maintained that there was no difference between dual fuel and single fuel customers in terms of their propensity to switch; other retailers maintained that dual fuel customers were much less likely to switch.

Retailers that provide services in addition to electricity and gas, such as re-selling broadband services, do so as add-on services which are marketed to customers at a later date. Having persuaded the customer to switch, the retailer avoids the ‘Do Not Call’ register and forms a relationship with those customers to introduce additional services. These services are not typically presented with the initial offer as retailers and customers generally find it difficult to jointly market and consider ‘essential’ services with ‘discretionary’ services.

Most electricity retailers made market offers in all regions in South Australia; the primary exception is where the service offered requires a change to the meters and the network distribution company does not have trained staff in that region (the network distribution company has a statutory monopoly for non-interval metering for residential customers). Two of the three gas retailers currently active in seeking new customers, offer market contracts in all regions, except for small rural communities which do not have reticulated gas networks.

2.4 Emerging industry structure

Retailers in South Australia generally perceive a national trend towards a relatively small number of large, vertically integrated, dual fuel (electricity and gas) companies. Within this emerging market structure, retailers expect there would continue to be room for new standalone entrants as well as small, and niche market retailers.

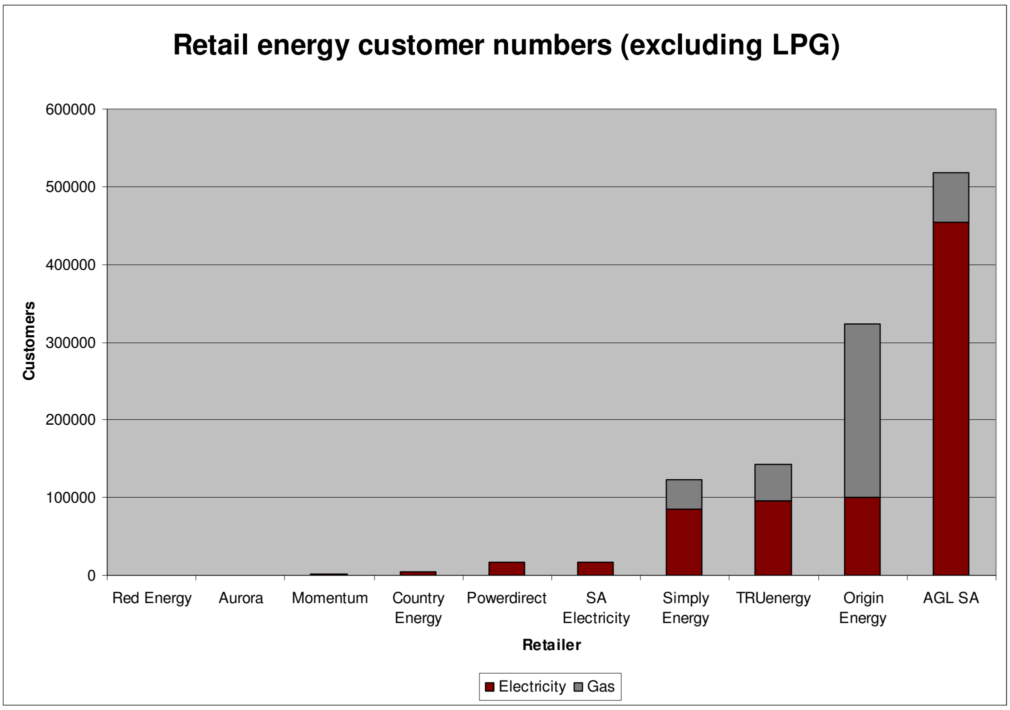
Large retailers, however, are expected to remain (or to become) vertically integrated into generation activities. Retailers expect a large standalone retailer would find it difficult to contract for sufficient volume of forward contracts, especially if other competing firms vertically integrate. A standalone retailer would also require a substantial balance sheet to back large volume forward contracts, whereas vertical integration may release efficiencies by allowing that capital to be invested directly in generation plant.

At a national level, the four largest retailers are vertically integrated; these firms are involved in wholesaling and retailing both gas and electricity and offer customers dual fuel. Several retailers suggested that there were additional business strategy considerations for dual fuel, vertically integrated, firms; gas could be used in electricity generation when electricity prices were relatively high and gas prices relatively low, and gas could be sold directly to end-use customers when electricity prices were low and gas prices high. Retailers operating in South Australia anticipate that the organisational structure of firms competing in the State will reflect these national trends.

Figure 5 below shows the number of electricity and gas customers for each retailer in South Australia in 2006/2007 (Source: ESCOSA Annual Performance Report)[3].

[3] AGL acquired Powerdirect in March 2007. Customer numbers are shown separately in the graph above.

Figure 5. SA retail energy customer numbers (excluding LPG)



3 Methodology

3.1 Retailer surveys

The retailer surveys sought qualitative and, to a lesser extent, quantitative information on retailer activity in the electricity and gas sectors in South Australia. Separate questionnaires were produced for the electricity and gas sectors; these questionnaires asked similar questions, but encouraged respondents to consider the gas and electricity components of their business separately if they competed in both sectors.

The surveys asked information about:

- **Company profile** – parent company, retail history, whether services are offered in all regions of South Australia;
- **Retailer rivalry** – price rivalry, incentives offered to obtain new customers and retain existing customers, branding and marketing, whether particular types of customers are targeted;
- **Customer participation and experience** – acquisition and retention costs, and customer enquiries and complaints; and
- **Conditions for entry, expansion and exit** – whether retailers are actively seeking new customers in South Australia, expansion plans, opportunities for entry and expansion, regulatory barriers, the impact of the structure of the gas sector on entry and expansion.

Managing Directors or Chief Executives were asked by the AEMC to sign off on surveys to ensure that responses gave an accurate reflection of the views held by the organisation.

The surveys were sent to fourteen retailers. Twelve retailers returned the surveys. Two of these retailers provided identical answers to the electricity and gas questions, completing one copy only. Two additional firms, not currently licensed to participate in the South Australian electricity and gas sectors, were interviewed.

A copy of the electricity survey distributed to retailers is included in Appendix 2 and a copy of the gas survey is included in Appendix 3.

3.2 Retailer interviews

Retailer interviews provided an opportunity to follow up and elaborate on the information gathered through the surveys. Retailers were asked to discuss their views on trends and specific issues arising from survey responses.

During interviews retailers were asked about similar topics to those outlined above for the survey. Key discussion questions included:

1. How effective is competition in the electricity and gas retail sectors in South Australia? How has this changed over time?
2. What aspects of competition or competitive threat do you monitor and control in your organisation?
3. In the survey you noted that you do not offer gas/electricity contracts to customers in all regions of South Australia. What are your reasons for this? (Had you made offers in any of these regions before?)
4. Do you have a preferred customer profile? If so, what is this profile? Are you able to accurately target this group?
5. How has customer targeting changed over time in South Australia?
6. What are the barriers to entry and expansion (if any) in the South Australia?
7. Have the conditions for entry or expansion improved or worsened over time and how?
8. What changes would you like to see made to allow you to compete more effectively in the South Australian market?
9. How would (a) your business and (b) the retail sector change if retail price controls were removed in South Australia?
10. What issues do you expect may impact on competition in the future?

Where agreed with the retailers, interviews were recorded and transcribed to assist with drafting this report.

To protect commercially sensitive information and encourage retailers to provide open and honest responses, the information gained from both the surveys and interview questions are not attributed in this report to particular retailers.

4 South Australian retailers

This section describes the retailers currently licensed to offer electricity and or gas retail services in South Australia. While we list various retailers as offering electricity and /or gas retail services, these retailers are not necessarily actively marketing their services at present, as outlined in section 2, key themes.

4.1 Retailers offering electricity and gas

Full retail competition commenced in the South Australian electricity sector in January 2003, and commenced in the gas retail sector from July 2004.

Retailers currently offering both electricity and gas for sale to small customers in South Australia include:

- **AGL** – is the host electricity retailer in South Australia and is Australia's largest energy company. AGL owns natural gas and electricity generation assets and operates in a number of other Australian states;

- **Origin Energy** – is the host gas retailer in South Australia and has held a retail gas licence since 1999 and has supplied electricity customers in South Australia since 2003. Origin owns gas-fired electricity generation assets;

- **Simply Energy** – owned by International Power (Retail) Pty Ltd – a gas- and coal-fired generator; Simply Energy has offered gas and electricity to consumers in South Australia since 2004. Simply Energy was formerly a partnership between International Power and EnergyAustralia under the EA-IPR Partnership; and

- **TRUenergy** – owned by CLP Power Asia, TRUenergy began as TXU. TRUenergy has been offering electricity since 2003 and offering gas since 2004.

4.2 Retailers offering electricity

Retailers currently offering only electricity for sale to small customers in South Australia include:

- **Aurora Energy –** offers electricity to small consumers via prepaid meter systems, known as Pay as You Go, and has held an electricity retailer licence since 2004;

- **Country Energy** – a New South Wales state owned corporation, Country Energy obtained its licence to operate in South Australia in 1999. Country Energy offers electricity, but not gas, to small consumers in South Australia;

- **Jackgreen Energy** – has been offering electricity to South Australian customers since mid 2007. Jackgreen supplies accredited GreenPower, at a minimum of 10% of energy. Jackgreen does not have a gas licence in South Australia;

- **Momentum Energy** – Melbourne based Momentum Energy has been supplying electricity to South Australian customers since early 2006;

- **Powerdirect** –owned by AGL Energy Limited, but formerly owned by Ergon Energy and Australian Energy Limited; Powerdirect has held a licence to operate in South Australia since 2003;

- **Red Energy** – owned by Snowy Hydro Limited, Red Energy offers electricity to small consumers in South Australia. Red Energy operates seven power stations and oversees a number of dams and reservoirs. Red Energy's licence to retail electricity in South Australia was issued in 2006; and

- **South Australia Electricity** –has been attracting electricity customers since 2006, having been granted an electricity licence in September 2005. South Australia Electricity was granted a gas licence at the same time, but has not yet exercised it.

4.3 Retailers not currently offering retail services in SA

Retailers who have been granted licences but are not currently offering electricity or gas in South Australia include:

- **Australian Power & Gas –** it was issued licences to retail electricity and gas in November 2007, but is not currently retailing electricity or gas in South Australia; and

- **Dodo Power & Gas** – Dodo, a supplier of internet and phone services, was granted a licence to retail electricity and gas in January 2008, but is not yet offering any energy services in South Australia.

- **Energy Australia** – was issued licences to retail gas and electricity in February 2008. Energy Australia is one the largest energy suppliers in Australia, but is not currently retailing electricity or gas in South Australia.

We also spoke to two additional firms that had considered, or were considering entering the South Australian electricity retail sector.

4.4 Service coverage

4.4.1 Electricity

Nine retailers responded that they either provide or plan to provide electricity in all regions of South Australia, while three do not. Regions that at least one retailer does not cover or will plan to exclude are those outside of their set criteria, and certain postcodes – one retailer provided services to areas defined by specific post codes due to regulatory restrictions related to the installation of specialist equipment.

4.4.2 Gas

Two retailers provide gas in all regions of South Australia, while five do not or do not intend to. Two retailers only provide gas to Adelaide (one to metropolitan Adelaide, and one to Adelaide excluding northern suburbs). A further retailer planned to provide gas to reticulated areas, within set company criteria, should it decide to actively market gas.

5 Retailer rivalry

This chapter summarises electricity and gas retailer responses to survey and interview questions on retailer rivalry including price rivalry; the offering of cash and in-kind incentives to obtain and retain customers; branding and marketing; and customer targeting.

Tables in this chapter and following chapters summarise survey responses, where retailers ranked the importance of certain factors on a Likert scale of one to five – from those not considered important to those considered very important. The dots in the tables record the number of retailer responses within each category (where a blank is equal to zero). Additional comment is included where the responses were expanded upon or clarified during the interviews.

5.1 Price rivalry

This section describes the factors influencing prices and the types of retail price structures offered for electricity and gas in South Australia.

5.1.1 Electricity

Factors influencing prices

When setting prices for electricity market contracts, six or more retailers rated the following factors as very important: wholesale electricity costs, target retailer margin/required return on investment and costs of distribution and transmission. Factors ranked important by six or more retailers included comparison of price with standing offer and competitor's prices.

In addition, other factors ranked as very important or important, but not included in this aspect of our survey, included available margin headroom, market liquidity in wholesale energy and customer profile.

Table 1: Factors influencing electricity prices

Factors influencing prices	Not considered	Considered	Moderately important	Important	Very important
Wholesale electricity costs				•	••••• ••••• •
Competitor's prices	•	•••	•	••••• •	•
Comparison of price with standard offer		••	••	••••• ••	•
Costs of distribution and transmission		••	•	•••	••••• •
Target retailer margin/required return on investment		•		•••	••••• •••
Your market share	••••	••••	•••	•	
Your competitors' market share	••••• •	••••	••		
Length of contract period	•	••••	••	••••	•
Pricing for dual fuel customers	•••••	•	••	••	•
Retail service standards		•••	••••	•••	••

Retailers reported during interviews that price remains the overwhelming factor in a consumer's decision to switch retailers. One retailed summed up their view as:

> *We will have to have a better price; that would be the bottom line. We could provide good service and all that, but I think that comes after, I think the foot in the door is the better price.*

All respondents noted in interviews that over the past 18 months or so, wholesale electricity prices in South Australia have risen significantly and spot price volatility has increased. Retailers generally perceived these wholesale price increases as having reduced substantially or eliminated the margin previously available between the wholesale price and the standing offer retail price. Hence, many argued that there was little or no margin over which to compete. One retailer commented:

> *because of the volatility that the market's experienced over probably the last 12 months I'd say demand is high [for forward contracts] therefore prices are high and people can't buy at a price that enables them to compete effectively given the limitations imposed by the retail price.*

A different retailer stated that:

> *… when that happens in the spot market [a period of volatility] that means that all the hedging products that are available become far more expensive … in South Australia [hedging products]have gone up so it's got to the point now where there are no margins, we can't offer competitive retail prices to customers in South Australia and earn a profit based on using those hedging products so basically we're not competing in South Australia any more, we used to but we actually don't have any sales teams operating...*

Most retailers attributed the recent fall in churn rates to the increase in the wholesale price against the regulated retail price:

> *it's not rocket science; you've seen the customer churn rates decline and that is driven overwhelmingly because of increased fuel costs, both electricity and gas over the past 12 months and as commodity prices go up and you're competing against a fixed regulated product which has got the commodity price locked in the margins will fall and the level of customer transfer decreases; it's as simple as that.*

New entrant retailers tended to contrast the current environment with market conditions prior to the recent spot price volatility, as in the following comment:

> *I think it's fair to say that up until the middle of last year it was a reasonable market to do business in … before the middle of last year there was reasonable head room for a retailer to offer a discount [to the prevailing maximum uniform tariff] plus retain enough of the gross margin to be competitive.*

Several retailers referred to the period of time over which the standing offer price is fixed; these retailers were concerned at the regulatory risk associated with buying in an open market and selling at terms which, although not controlled directly, were referenced to regulated rates. One retailer commented that:

> *I think you'd see a steep change in competition if retail price caps were removed ... with [the current] rigid retail structure and a fluid wholesale structure it's very difficult to [compete].*

Price structures

Electricity retailers responded to the survey questions saying that they offer a range of non-standard price structures and contract terms, the most popular being long term contracts, monthly rather than quarterly billing and bill smoothing, and charging exit fees. No one type of price structure stood out from the survey responses as being particularly important to competitive strategy, but prices that "track wholesale costs" and capped or fixed prices and exit fees ranked higher than other responses.

Our written question relating to "prices that track wholesale costs" appears to have been misinterpreted; we had intended from this question to find out whether retailers offer products that are variable and track changes in wholesale costs (e.g. on an hourly / daily / weekly basis). Some respondents, it seems, interpreted the question as asking whether retail prices were adjusted over time to reflect changes in retail costs. Following the interviews, we are not aware of any retailer that currently offers to small consumers a retail tariff that directly tracks wholesale costs.

Prompt payment discounts were rated as important by several retailers.

From the interviews with retailers, it is apparent that price offers are usually, but not exclusively, in the form of a discount to the standing offer. Those prices which are not structured as a discount to the standing offer are usually referenced against some other benchmark (for example, percentage off your current bill). Many retailers attribute a lack of innovation in price offers to the regulated standing offer, saying that in the absence of the standing offer they would align terms more with customer demands. However, retailers provided few specific examples of the changes they would make to contract terms to consumers.

Several retailers commented that customers did not appear to want a more complex price offer:

> *a more detailed, more structured, price structure; its not something which I've seen a demand for, but which we all have the capability to do … but I think it's more a demand driven question, I'm not sure the customers are interested.*

A number of retailers commented that offering 'a percentage off' the standing offer was a simple and effective method of communicating their offer to customers; in the absence of the standing offer they would look for some other, easily understood, bench mark.

> *If it [the standing offer] weren't there we'd probably have to use another benchmark; we're offering a discount off something so we're going to have to know what rate that person's on before we start offering them a discount … if it were a [retailer] dominated area you're probably start with the [retailer] rates … and offer discounts on those …*

Table 2: Price structures and contract terms that vary from standard offer

	Offered	Not considered	Considered	Moderately important	Important	Very important
Capped or fixed prices	●●●	●	●●		●●	●
Prices that track wholesale costs	●●		●●	●		●●
Long term contracts	●●●●● ●		●●	●●●	●	●
Monthly rather than quarterly billing	●●●●●		●●	●●		●
Bill smoothing	●●●●●	●	●●●●	●	●	
Exit fees	●●●●● ●●		●●	●●●	●●	●

5.1.2 Gas

Factors influencing prices

When setting prices for gas market contracts, retailers ranked wholesale gas costs, target retailer margin and costs of distribution and transmission as very important.

Table 3: Factors influencing gas prices

Factors influencing prices	**Not considered**	**Considered**	**Moderately important**	**Important**	**Very important**
Wholesale gas costs				•	•••••
Competitor's prices	•		•	••••	
Comparison of price with standard offer			•	••••	•
Costs of distribution and transmission			•	•	••••
Target retailer margin/required return on investment				••	••••
Your market share	••	••	•	•	
Your competitors' market share	••	••	••		
Length of contract period		••	•	••	•
Pricing for dual fuel customers	•		••	••	•
Retail service standards		•	••	••	

Retailers viewed wholesale prices for gas as high relative to the regulated retail prices. The gas retailers said that there had been little if any margin available between the wholesale gas prices and the regulated standing offer price for gas, and hence the scope to compete was diminishing. Most retailers noted that the Essential Services Commission of South Australia (ESCOSA) was currently reviewing the regulated retail gas price. Retailers emphasised their concern that this review should result in an adequate margin. One retailer commented that it would consider exiting gas retailing in South Australia if sufficient margins were not available following the review.

Price structures

Retailers were asked whether they offered non-standard price structures or contract terms and how important these were to their competitive strategy. Retailers reported that they offer bill smoothing and charge exit fees. Three retailers offer monthly billing and long term contracts. Retailers did not generally view these factors as important or very important. Exit fees and long term contracts ranked the highest in terms of importance to competitive strategy in the written responses.

Table 4: Price structures and contract terms that vary from standard offer

	Offered	Not considered	Considered	Moderately important	Important	Very important
Capped or fixed prices	•		•			•
Prices that track wholesale costs	•		•			•
Long term contracts	•••		•	••		•
Monthly rather than quarterly billing	•••		•	•		•
Bill smoothing	••••		•••	•	•	
Exit fees	••••		•	•••		•

As with electricity retailing, the predominant form of price offer (for market contracts) was in the form of a discount to the standing offer. Retailers anticipated that they would continue to offer gas against some readily understood benchmark, were the standing offer to be removed. Most retailers sought ways to simplify their price offers to assist customers to differentiate their offer from competitive offers.

Gas retailers (as did electricity retailers) referred to the period of time over which the standing offer price is fixed; these retailers were concerned at the regulatory risk associated with buying in an open market and selling at terms which, although not controlled directly, were referenced to regulated rates.

> *While you have a three year price control mechanism, based on someone taking a guess as to the dollar per gigajoule - to two decimal places – of the price gas is going to be in 2010, you are going to risk competitive development.*

5.2 Cash and in-kind incentives

This section summarises the types and levels of cash and in-kind incentives offered by retailers to obtain, and retain, electricity and gas customers.

5.2.1 Electricity

Types of incentives offered

Most retailers offer some form of non-cash incentive to new customers switching to them, and to existing customers as a way of retaining them.

Incentives relating to contracts/electricity prices offered include: percentage discount, one month free after 12 months, tiered rebates, bill credits after year one, referral rebate, cash rebate at sign on, free installation, multi-utility bundling, prompt payment discounts, and cash rebates for retention.

Other incentives offered include: shopper dockets, company newsletter, voucher book/loyalty reward, wine, coffee machine, MYOB, loyalty card, DVD, renewable energy, frequent flyer points, RAA rebates, newspaper/magazine subscription, sporting club membership, free appliances, torch, centameter, movie tickets, DVD player and tree planting.

Green energy or renewable energy is becoming an increasingly important element of product offerings to many customers.

> *What we are trying to do – what any competitor is trying to do is move away from price based competition … we're doing our best to put green in the mix, things that have implied value.*

However, retailers have generally found that customers were not yet willing to pay a premium for green energy.

> *They're [small business] not looking to pay a premium at this point but they're starting to see it as something that can add value to their business … its no way yet to the point where a customer can reconcile enough to say I'll pay X for it. But it's something that we're driving as a point of differentiation.*

Other retailers made very similar comments, though a few retailers noted that customers would forego discounts of a few percentage points, or provide other consideration for green energy.

Obtaining new customers

Seven retailers have offered cash or in-kind incentives to customers at sign on. During interviews, retailers explained the primary reason for making non-cash offers was to gain the attention of the customer; retailers generally perceive that people like 'receiving gifts'. The number of retailers offering these incentives steadily increased from 2003 to 2007, and has dropped slightly this year.

Table 5: Incentives offered to obtain new electricity customers

Obtaining new customers	**2003**	**2004**	**2005**	**2006**	**2007**	**2008 (current)**
Incentives offered in calendar year	●●	●●●●	●●●●●	●●●●● ●	●●●●● ●●	●●●●● ●

Retailers' views were spread on the importance of incentives in their current marketing strategy to obtain customers. Nine electricity retailers ranked them as moderately to very important (despite not all of these retailers having offered incentives yet).

Table 6: Importance of incentives in current marketing strategy to obtain customers

Obtaining customers	Not considered	Considered	Moderately important	Important	Very important
Importance of incentives		●●	●●●	●●	●●●●

Ten retailers gave estimates of the cost of incentives offered in 2008 as a percentage of average monthly spends. Responses ranged from 0 to 20%, although only two retailers were willing to spend more than 10%.

Seven retailers offer these incentives as part of a national strategy; two offer them as part of a South Australia specific initiative and one retailer offers a mixture.

During follow up interviews, some commented that incentives were a good way of obtaining customers early on, but customers are becoming more interested in price and other product features as the market matures:

> *We do [not perceive] incentives to be as valued now as they were in the past, when the market opened it seemed to be very popular … we have found as the market has matured the steak knife approach has lost popularity and customers really are looking around price and features of the product but as the market opened absolutely incentives were a very good way of winning customers over.*

Retaining customers

Six electricity retailers have offered incentives to retain customers.

Table 7: Incentives offered to retain electricity customers

Retaining customers	2003	2004	2005	2006	2007	2008 (current)
Incentives offered in calendar year		●●	●●●	●●	●●●●●	●●●●

One retailer offers a cash incentive to customers in certain circumstances where customers have indicated they want to switch to another retailer.

From the written responses, incentives to retain customers appear to be less important to electricity retailers, than incentives to obtain customers. Six retailers view them as “moderately” to “very important”. However, all retailers in interviews emphasised that they typically place greater importance on retaining a (profitable) customer than on attracting new customers. A retailer incurs costs in attracting and switching a new customer that the retailer does not incur with its existing customer.

Table 8: Importance of incentives in current marketing strategy to retain electricity customers

Retaining customers	Not considered	Considered	Moderately important	Important	Very important
Importance of incentives		••	••••	•	•

Seven retailers gave estimates of the costs of these incentives, ranging from 0 to 12%. Five retailers offer incentives costing 5% or less.

Six of these retailers offer initiatives as part of a national initiative and one offers a mix of national and South Australian specific initiatives.

Most retailers (both gas and electricity) attempt to contact customers that have decided to switch to a new retailer, and attempt to 'win back' the customer before the switch is completed.

5.2.2 Gas

Types of incentives offered

Gas retailers offer a number of incentives to customers at sign on and to retain customers. These are very similar to those offered to electricity customers, with the addition of one month's free electricity for dual fuel being offered by one retailer.

Incentives relating to contracts/gas prices offered include: percentage discount, one month free after 12 months, tiered rebates, bill credits after year one, cash rebate at sign on, and cash rebates for customers to remain with the same retailer.

Other incentives offered include: shopper dockets/discounts, voucher book/loyalty rewards, frequent flyer points, RAA rebates, newspaper/magazine subscription, sporting club memberships, torch, movie tickets, and DVD players.

One retailer offers a cash incentive to retain customers in certain circumstances where customers have indicated they want to switch to another retailer.

Obtaining new customers

Retailers were asked if they offered cash or in-kind incentives to customers on sign on. Four retailers have offered incentives to obtain new customers since 2003.[4] Each of

[4] Full retail competition commenced for gas in 2004. Responses regarding incentives offered in 2003 may have referred to electricity, as some retailers provided gas and electricity responses on the same survey.

these retailers offered incentives over the four year period from 2004 to 2007, but one has stopped offering incentives this year.

As with electricity, some gas retailers commented that they had found customers to be less interested in gifts and other in-kind incentives as the market matured.

Table 9: Incentives offered to obtain new gas customers

Obtaining new customers	2003	2004	2005	2006	2007	2008 (current)
Incentives offered in calendar year	●●	●●●●	●●●●	●●●●	●●●●	●●●

Table 10: Importance of incentives in current marketing strategy to obtain customers

Three retailers ranked incentives as very important in their current marketing strategy.

Obtaining customers	Not considered	Considered	Moderately important	Important	Very important
Importance of incentives		●	●		●●●

* This table includes a response from one retailer who has not yet offered incentives

Five gas retailers gave estimates of the costs of incentives offered in 2008 (or planned to be offered in the case of one retailer) as a percentage of average monthly spend. Responses ranged from 0 to 20%, although only one retailer was willing to spend more than 7%.

Three gas retailers offer (or will offer) these incentives as part of a national strategy, one offers them as part of a South Australia specific initiative and one retailer offers a mixture.

Retaining customers

Three retailers have offered incentives to retain gas customers since 2004 (although not all three retailers within any one year). In the last two years, only two retailers have offered incentives to retain gas customers.

Table 11: Incentives offered to retain gas customers

Retaining customers	2003	2004	2005	2006	2007	2008 (current)
Incentives offered in calendar year		●	●●	●	●●	●●

Two retailers view incentives as “important” or “very important” in their current marketing strategy to retain gas customers.

Table 12: Importance of incentives in current marketing strategy to retain gas customers

Retaining customers	Not considered	Considered	Moderately important	Important	Very important
Importance of incentives		••		•	•

Two retailers estimated the cost of incentives offered in 2008 as a percentage of monthly spend per gas customer, and the estimate was 5% for each of the retailers.

Two retailers offer incentives as a result of national initiatives, while one offers them as a result of national and local initiatives.

5.3 Dual fuel

The four retailers currently offering gas to small customers also offer electricity – i.e. they provide dual fuel. However, not all retailers combine electricity and gas into one bill. Some retailers view the design of the bill as an opportunity to differentiate their product; for example by making the bill simple to understand. However there are limitations to the extent of which this may be possible due to the mandatory information that must appear on customer bills (this point is discussed further below in section 7.3).

Dual fuel is an important element of the marketing strategies for most retailers, especially larger retailers at least as a general proposition. Dual fuel is viewed as important by retailers because it allows the retailer to gain from cost synergies in acquiring and servicing a customer.

In acquiring a customer, retailers indicated in interviews that they would pay a commission to the door-to-door sales team of about $80 (for a single fuel) and about $110 for gas and electricity. In addition to the reduced acquisition cost, the retailer gains a second customer at little additional cost in terms of servicing that customer. As one retailer commented:

> *It's a simple proposition; if we've got a competitive operating cost platform that's scalable, then we're going to try and earn as much revenue off that cost base as we can. Dual fuel is the most logical single step in that direction.*

Retailers also drew attention to the relatively small volumes of gas sales; a combination of a low volume and a regulated low margin means that "*it's hard to make money out of gas*" and means that *"you never chase a gas customer alone; you would only chase it in conjunction with electricity."*

Retailers reported quite different views in relation to whether dual fuel customers were more or less likely switch to another retailer. Some retailers maintained that there was no difference between dual fuel and single fuel customers in terms of their propensity to switch:

If you knock on the door and it's a dual fuel customer I might win them. Equally if somebody knocks on my dual fuel customer's door I'll lose them. So there is no measurable difference in behaviour.

Other retailers maintained that dual customers were much less likely to switch because switching two fuels at the same time was a more significant event for the consumer, requiring more consideration.

… We do dual fuel campaigns, and that's just to lock in customers … the customer would tend not to leave because they have both their gas and electricity with you.

[Dual fuel customers are] sticky, yeah, yeah, much more sticky.

At the wholesale level, the larger retailers operate a dual fuel strategy. Gas could be used in electricity generation when electricity prices were relatively high and gas prices relatively low, and gas could be sold directly to end-use customers when electricity prices were low and gas prices high. These firms viewed themselves as "energy companies":

We're a retailer of electricity, we're a retailer of gas, we're … involved in the wholesale markets … [There is a] matrix between low and high prices in gas and electricity and there are spaces within that quadrant where we as an energy company would seek margin.

5.4 Branding and marketing

This section considers the type of branding and marketing retailers are using in South Australia and their views on how important these are to their customers.

5.4.1 Electricity

Factors important in obtaining or retaining customers

Electricity retailers rated reputation for customer service, brand recognition, provision of green energy products, and good corporate citizenship as the most important factors in obtaining/retaining electricity customers.

However, as discussed above, almost all retailers viewed price as the single biggest factor in its pitch to a new customer. Brand recognition, Australian ownership, good corporate citizen, and promotion of community events were means of gaining introductions to customers; the 'pitch' remained primarily about price.

Customer service is viewed by many retailers as an important element of their competitive strategy to retain customers. Several retailers commented that customers joined them because of price discounts but remained with them because of better service.

Factors generally not considered important by retailers include customers having an ownership interest, the host being the retailer at the connection site and reputation for providing in-kind benefits.

Table 13: Importance of factors in obtaining/retaining electricity customers

Factors in obtaining/ retaining customers	Not considered	Considered	Moderately important	Important	Very important
Reputation for low prices		••	•••	••••	•••
Reputation for providing in-kind benefits	•••	••••	•••	••	
Reputation for good customer service			•	••	••••• ••••
Provision of Green energy products		•	•	•••••	•••••
Energy saving and product advice		••	••••• ••	•	••
Offer dual fuel products	••••	•	•••	•	•••
Good corporate citizenship		••	••	•••	•••••
Customer has ownership interest	••••• •••	•	•••		
Brand recognition	•			••••• •	•••••
Host retailer at connection site	••••• •••		•	•••	

Promotion of service

Eleven retailers responded to the written question about the aspects of their electricity service they promote (or will promote). The factors which retailers promote the most include:

- Price per kWh;
- Comparison with the standing offer;
- Flexible payment options;
- Energy saving and product advice;
- Dual fuel;
- The retailer being an Australian company; and
- The retailer being an established retailer in other states.

Table 14: Aspects of electricity service that South Australian retailers promote

Aspects of service that may be promoted	Promote
Price	
Price customer required to pay for each kWh	●●●●● ●●●●
Comparison of price per KWh with other retailers	●●●●
Amount paid per payment period	●●
Comparison with amount charged to customer per payment period by other retailers	●●●
Comparison with standard offer (e.g. 5% off standard offer price)	●●●●● ●
Guaranteed price for a set period	●
Non-standard pricing structures	●●●
Early payment bonuses	●●●
Monthly rather than quarterly billing	●●●
Flexible payment options	●●●●● ●
Non-price benefits	●
In-kind benefits	●●●
Service	●
Responsiveness of call centre	
Energy saving and product advice	●●●●● ●●
Offer dual fuel	●●●●● ●
Other customer service aspects	●●●
Sells electricity appliances	●●
Corporate citizen	
Good corporate citizen	●●●●●
Ownership interest	
Customer is your shareholder	
Your business is a South Australian company	
Your business is an Australian company	●●●●● ●●●
Your business is an international company	●
Your business operates in multiple Australian states	●●●●●
Brand recognition	●
Long established retailer in South Australia	●●●

Aspects of service that may be promoted	Promote
You are the customer's existing retailer	•
Established retailer in other Australian state(s)	••••• ••

Retailers use a wide variety of channels to make customers aware of each aspect (i.e. price, non-price benefits, service etc) of their service. Retailers used their website or online advertisements, telesales and brochures for almost every aspect. Other channels mentioned included door-to-door sales agents, call centre, print media (such as price factsheets), PR, magazine advertisements, bills, customer mail, television commercials, and direct marketing. One retailer also mentioned the ESCOSA "estimator"[5] as a key channel for customers to become aware of their prices.

Importance of advertising media for obtaining customers

Door knocking was rated "very important" the most number of times by retailers in the written survey followed by inbound and outbound telesales for obtaining electricity customers.

During the interviews, all retailers characterised electricity and gas as low involvement commodities.

> *Gas and electricity are low involvement products, it's not something people go home every night and say hey I'm going to ring up and get a new gas and electricity provider; they generally don't think about it unless they're moving home or there's no power or gas when they get home.*

New and established retailers seeking to win customers from existing suppliers must actively market to those customers and provide offers which motivate them to switch to another retailer. Retailers noted that very few customers actively seek out retailers for competitive offers, except if moving house. Door-to-door sales were considered the most effective means of marketing, with outbound and inbound telesales the next most important.

A number of retailers found sponsorship effective, especially sponsorship of events identifiable with South Australia, as well as advertising in local or community newsletters. Established retailers tended to use mass marketing, such as television, more than new entrant retailers to promote their brand. However, new entrants seeking to be identified with a new product offer used television to promote the product, but then switched to door-to-door or telesales to complete on actual sales. Established retailers tend to use bill insertions for promotion and marketing more than new entrant retailers.

[5] http://www.escosa.sa.gov.au/site/page.cfm?u=18

The table below demonstrates that a range of media are at least “considered” by many retailers.

Table 15: Importance of advertising media for obtaining electricity customers

Importance of advertising media for general marketing	Not considered	Considered	Moderately important	Important	Very important
Television	●●	●●●	●	●●●	●
Radio	●	●●●●●	●●	●	●
Internet advertising		●●●	●●	●●●	●●
Newspapers and other print media		●●●●	●●●	●●●	
Outdoor advertising (e.g. bus shelters, billboards)		●●●●	●●●●	●●	
Direct mail	●	●●●	●●●	●●●	
Bill inserts	●●	●	●●●	●●	
Marketing with related products (affinity retailing)	●●	●	●●●●	●●	
Sponsorship	●●	●●●●		●●●	
Door knocking	●		●	●	●●●●● ●
Outbound telesales	●		●●	●●	●●●●
Inbound telesales			●●●	●●	●●●●

Importance of advertising media for customer retention

Inbound and outbound telesales were considered most important for customer retention. Telesales were also used to sell additional products to existing customers – because the retailer was calling an existing customer, the retailers were not caught by the ‘Do Not Call’ register. Established retailers tend to use bill insertions for promotion and marketing more than new entrant retailers.

A key method for customer retention for many retailers was ‘win-back’ strategies, where the retailer would seek to win back any (profitable) customer that had begun the process of switching or had advised the retailer that the customer had received a competitive offer by offering to match the offer received or providing a further discount.

Table 16: Importance of advertising media for retaining electricity customers

Importance of advertising media for general marketing	Not considered	Considered	Moderately important	Important	Very important
Television	●●	●●	●●●●	●●●	
Radio	●	●●●●	●●●●	●●	
Internet advertising		●●●	●●	●●●●	●●
Newspapers and other print media		●●●●●	●●●	●●	

		•			
Outdoor advertising (e.g. bus shelters, billboards)		••••	••••	••	
Direct mail		•	•	••••• ••	•
Bill inserts		•	•	•••••	••••
Marketing with related products (affinity retailing)	••	•	•••	••••	•
Sponsorship	•	••••• •	•	••	
Door knocking	•		••	•••	•••
Outbound telesales	•		••	•••	•••••
Inbound telesales		•	•	•••	•••••

5.4.2 Gas

Factors important in obtaining or retaining customers

Four gas retailers viewed reputation for good customer service as a very important factor in obtaining or retaining gas customers. Other factors viewed as important include brand recognition, and provision of green energy products. Customers having an ownership interest and the retailer being the host at the connection site were not considered by four retailers.

While recognising that retailers are not responsible for the safe delivery of gas (this is a responsibility of the distribution network companies), we sought to understand whether retailers perceived that this was a factor in customer choices. Written surveys were incomplete on this point. Some retailers commented in interviews that perceptions of safety were a factor in gas retailing that was not present in electricity retailing:

> *And then there are other concerns about gas sign up … there are safety and other issues that sit in the back of the mind so when we think … about switching suppliers, particularly the one that no one's ever heard of before, you know, new entrant; that's okay with electricity because nothing could go wrong with electricity. Electricity is a staple, it's a commodity, and everybody supplies it, that's easy. When it comes to my gas, mmm should I be worried about the pipes or what about smell? Those things pervade our research. We see more involvement [by the customer] in gas and therefore lower level of churn…*

Table 17: Importance of factors in obtaining/retaining gas customers

Factors in obtaining/retaining customers	Not considered	Considered	Moderately important	Important	Very important
Reputation for low prices		●●	●	●●	
Reputation for providing in-kind benefits	●●		●●	●	
Reputation for good customer service				●	●●●●
Reputation for gas expertise*		●			●
Provision of Green energy products				●●●●	●
Energy saving and product advice			●●●●		●
Offer dual fuel products			●●	●	●●
Good corporate citizenship		●		●●●	●
Customer has ownership interest	●●●●		●		
Brand recognition				●●●	●●
Host retailer at connection site	●●●●		●		

* Three retailers did not respond to this question as they used the electricity questionnaire for gas responses, which did not include this factor.

Promotion of service

The primary factors promoted by gas retailers, as reported in the survey responses, were:

- Price comparison with the standing offer; and
- Offer of dual fuel.

Second in importance behind these factors, were according to the survey responses:

- Energy savings and product advice; and
- Flexible payment options.

Table 18: Aspects of gas service that South Australian retailers promote

Aspects of service that may be promoted	Promote
Price	
Price customer required to pay for each GJ	●●●
Comparison of price per GJ with other retailers	
Amount paid per payment period	●
Comparison with amount charged to customer per payment period by other retailers	
Comparison with standard offer (e.g. 5% off standard offer price)	●●●●●

Aspects of service that may be promoted	Promote
Guaranteed price for a set period	
Non-standard pricing structures	
Early payment bonuses	•••
Monthly rather than quarterly billing	
Flexible payment options	••••
Non-price benefits	
In-kind benefits	•
Service	
Responsiveness of call centre	
Energy saving and product advice	••••
Offer dual fuel	•••••
Sells gas appliances	•
Other customer service aspects (e.g. gas use/service expertise)	•
Corporate citizen	
Good corporate citizen	••
Ownership interest	
Customer is a shareholder	
Your business is a South Australian company	
Your business is an Australian company	•••
Your business is an international company	•
Your business operates in multiple Australian states	••
Brand recognition	
Long established retailer in South Australia	••
You are the customer's existing retailer	
Established retailer in other Australian state(s)	•••

Importance of advertising media for obtaining customers

Retailers use a wide variety of channels to make customers aware of each category level aspect of their service. The channels used are very similar to those used to promote aspects of electricity services.

Door knocking is very important for obtaining gas customers for four out of five retailers that responded to this question. Other important mechanisms include outbound telesales, inbound telesales and direct mail.

Table 19: Importance of advertising media for obtaining gas customers

Importance of advertising media for general marketing	Not considered	Considered	Moderately important	Important	Very important
Television	•	•	•	••	
Radio	•	•	••	•	
Internet advertising			••	••	•
Newspapers and other print media		•	•••	•	
Outdoor advertising (e.g. bus shelters, billboards)		•	•••	•	
Direct mail		•		••••	
Bill inserts	•		•	••	•
Marketing with related products (affinity retailing)			••	•••	
Sponsorship		••	•	••	
Door knocking				•	••••
Outbound telesales			•	••	••
Inbound telesales			•	•	•••

Importance of advertising media for customer retention

Four out of five retailers that responded to this question rank direct mail, bill inserts, outbound telesales and inbound telesales as equally important mechanisms for retaining gas customers.

Table 20: Importance of advertising media for retaining gas customers

Importance of advertising media for general marketing	Not considered	Considered	Moderately important	Important	Very important
Television	•	••	•	•	
Radio	•	••	•	•	
Internet advertising		•	••	•	
Newspapers and other print media		••	••	•	
Outdoor advertising (e.g. bus shelters, billboards)		•	•••	•	
Direct mail			•	••	••
Bill inserts			•	••	••
Marketing with related products (affinity retailing)			•••	••	
Sponsorship		•••		••	
Door knocking	•		•	•	••
Outbound telesales			•	••	••

Inbound telesales			•	••	••

5.5 Targeting customers

This section outlines the types of customers targeted by retailers, the types of indicators used by retailers to recognise whether customers fall within this target and describes situations where customers would not be offered electricity or gas.

5.5.1 Electricity

Customer characteristics sought

Six electricity retailers responded to the survey reporting that they actively seek customers with particular characteristics. Six responded saying that they do not.

During interviews all retailers stated that they would accept any customer who met their credit criteria. However, almost all retailers explained that they do target or focus their marketing efforts. One retailer maintained they did not target at all, but took a "portfolio approach" to customer acquisition.

Customer characteristics viewed as important or very important by retailers include ability to pay and volume of energy consumption. Two retailers gave target customer energy consumption – at least 4MWh per annum for one retailer who has not yet entered South Australia, and up to 160MWh per quarter for another retailer.

Location within a given geographic area was the favoured method for identifying customers who had the ability to pay and higher than average energy consumption – the target neighbourhoods were not necessarily the most affluent (for example, a high income area populated by working couples might not have high electricity consumption).

> *energy retail is a volume based game and that's the sheer fact of it. Lower consuming customers just aren't profitable. You've got a fixed cost base … costs that you've got to recover on each customer. And it's pretty linear from there. The more a customer consumes the more profitable.*

The only neighbourhoods that some retailers reported as specifically excluding were a very limited number which the retailers associated with higher levels of crime, especially violence. Door knocking teams also tended to avoid 'gated apartments' because of access difficulties; competition for customers in apartments tended to be channelled through telesales.

Individual retailers targeted niche markets, such as customers who are more likely to favour green products or customer groups likely to be less attractive to other retailers, such as rural customers.

Some retailers focus only on residential customers and did not actively market to small business customers. Small business customers were more costly to acquire than residential customers, but more valuable once obtained. The decision-maker in a small business is often the owner or operator with many competing demands on his or her time. He or she may not have time to adequately consider any offers presented to them, especially as gas is likely to comprise only a small part of the cost structure of the firm. As one retailer commented:

> *Energy's generally a small proportion of their [small business] outgoings and they're got other things to worry about.*

In addition, business owners can generally only be contacted during business hours, decreasing the window of opportunity.

Table 21: Importance of customer characteristics when making electricity market offers

Customer characteristics	Not considered	Considered	Moderately important	Important	Very important
Volume of energy consumption		••	••	••••	••
Demand profile (time of day energy used)	••	•••	••	•••	
Ability to pay		•	••	••	•••••
Location within a given geographic area	••	••	•	•••	••
Likelihood of remaining on site for some time	••••	••	•	•••	
Desire for dual fuel	•••	••	•••	•	•

Electricity retailers were asked which indicators they use to identify electricity customers within their target group (identified above). The written responses suggested that retailers favoured characteristics that indicated the customer had a good income - indicators that were selected as most important include clear credit check and high household income, followed by affluent suburb and metropolitan area.

During the interviews, a number of retailers said they used quite sophisticated methods for 'credit washing' locations and for selecting defined areas to target door knocking teams. These target zones might be defined as precisely as particular streets, or parts of a street. However, as with the written responses, the retailers that targeted customer segments were not specific about the particular parameters or indicators they used to hone their targeting.

Having identified a target area, most retailers would instruct door knocking teams to contact each property in the target area (except for properties with access difficulties or dangers such as dogs). Earlier attempts to have door-knocking teams concentrate on houses with particular characteristics had mostly proved difficult to implement, as these characteristics would largely be ignored by commission based door knockers.

Table 22: Indicators of customer characteristics used and their importance

Customer characteristics and indicators of these	Indicator used	Not considered	Considered	Moderately important	Important	Very important
Volume of energy consumption	•					•
Large number of householders	••••		••••		••	
High household income	••••	•	••••	•	•	
Large house size (square metres)	•	•	••	•	•	
High volume of past energy consumption	•••	•	•	•	•••	
Affluent suburb	••••• •	•	•••	••	•••	•
Property appears to contain high volume appliances e.g. air-conditioning unit	•••	•••	••		•	
Property appears to house high energy users e.g. swimming pool, 4WD	••	••	••		•	
Demand profile		•				
Household includes children	••		••••			
Household has residents past retirement age	••	•	•••			
Householders are employed	•••	•	••••			
Home during the day when sales team phones/visits	••		•	••		••
Past energy profile matches demand profile sought (e.g. non-peak consumption)	••	•	••		•	
Past usage of dual fuel	•		•		•	•
Ability to pay						

Customer characteristics and indicators of these	**Indicator used**	**Not considered**	**Considered**	**Moderately important**	**Important**	**Very important**
High household income	•••	••		••	•	••
Residents own the house	••	••		••	•	
Householders are employed	••	••	••••			
Credit check is clear	•••••		••	•	•	•••
Good payment history with retailer	•••	••	••		••	•
Location within a given geographic area						
Affluent suburb	•••	•		••	••	•
Affluent region	••	•		•	••	•
Metropolitan area	•••	•	••		•••	•
Likelihood of remaining						
Residents own the house	••	•		•	••	
Not shared by a number of adults living together (i.e. flatting)		••	•			
Householder's age	•••	•	•••	•		

Declining to serve customers

Five retailers responded to the survey saying they would decline to serve customers with particular characteristics. Four retailers cited failed credit check or poor credit-worthiness as a reason to decline customers, while two may reject customers with a bad customer history with the company. One retailer, due to the special nature of the service it provides, will not offer service to residences that have medical life support systems that run on mains power, customers who do not have a single-phase power supply and customers who cannot safely access their own meter box. Two retailers exclude business customers.

Most retailers commented in interviews that their primary concern was in relation to customers that "won't pay" rather than those that "can't pay" at a particular time. These retailers recognised that most people want to pay for the services they take; the retailers expressed some pride in the arrangements that they have to provide customers with a managed path to pay their bills.

5.5.2 Gas

Customer characteristics sought

Two gas retailers actively seek customers with particular characteristics. Two do not. Three retailers responded that the question was not applicable to them because they were not actively seeking customers.

Responses were varied on the importance of different customer characteristics when making gas market offers. Ability to pay, volume of energy consumption and dual fuel were considered to be moderately to very important for three or more retailers.

Table 23: Importance of customer characteristics when making gas market offers

Customer characteristics	Not considered	Considered	Moderately important	Important	Very important
Volume of energy consumption		•	•	••	
Demand profile (time of day energy used)		•••	•		
Ability to pay			••	•	•
Location within a given geographic area		••		•	•
Likelihood of remaining on site for some time	••	••			
Desire for dual fuel		•	•		••

During the interviews, almost all retailers observed that the retail gas business in South Australia was a low volume business – households consumed less gas than say households in Victoria and a lower proportion of households are connected to gas.

> *In people's minds though gas is a discretionary fuel, gas it not an essential commodity, it's not a staple.*
>
> *You're looking at a gas customer that's using an average of around 20 to 25 [gigajoules] of gas per annum versus 60 to 65 [gigajoules] per annum of gas in Victoria, and your costs to serve are pretty much the same.*[6]

Almost all retailers said that they would only consider marketing gas as a dual fuel – that is to customers that also took electricity. None of the new entrants, or prospective entrant retailers, considered retailing gas as a standalone business.

[6] This quote was altered, replacing megajoules with gigajoules.

I think gas will always been seen as an add on product to electricity … I can't see that scenario changing.

Gas retailers use a limited number of indicators of customer characteristics and views were mixed on their importance. A clear credit check and location with an affluent suburb were more important characteristics. Several retailers use segmentation methods to identify customers by age, household income, and location. As gas was often marketed as part of a dual fuel offer, and as gas is typically the lower value product to the retailer compared with electricity, retailers actively seeking customers tend to target electricity customers and offer a dual fuel service if the targeted customer is also connected to gas.

Table 24: Indicators of customer characteristics used and their importance

Customer characteristics and indicators of these	**Indicator used**	**Not considered**	**Considered**	**Moderately important**	**Important**	**Very important**
Volume of energy consumption						
Large number of householders	•		•••			
High household income		•	•	•		
Large house size (square metres)		•	•	•		
High volume of past energy consumption		•	•	•		
Affluent suburb	•	•	•	•	•	
Property appears to contain high volume appliances (e.g. gas fired pool heater, gas central heating)	•	••	•			
Property appears to house high energy users (e.g. swimming pool, 4WD)	•	•	••			
Demand profile						
Household includes children			••			
Household has residents past		•	•			

Customer characteristics and indicators of these	**Indicator used**	**Not considered**	**Considered**	**Moderately important**	**Important**	**Very important**
retirement age						
Householders are employed		•	•			
Home during the day when sales team phones/visits			•	•		
Past energy profile matches demand profile sought (e.g. non-peak consumption)		•	•			
Past usage of dual fuel			•		•	
Ability to pay						
High household income		••		•		
Residents own the house		••		•		
Householders are employed		••	•			
Credit check is clear	•	•	•		•	•
Good payment history with retailer		•	•			•
Location within a given geographic area						
Affluent suburb	•	•		••		
Affluent region		•		•		
Metropolitan area		•			•	
Likelihood of remaining						
Residents own the house		•		•		
Not shared by a number of adults living together (i.e. flatting)		•	•			
Householder's age		•	•			

Declining service to gas customers

Two gas retailers decline to provide a market service to customers with particular characteristics. Reasons for declining service include poor payment history or credit rating and location within certain geographical areas.

Similar to the electricity responses, retailers tend to actively target products to certain customers, while offering the core service to all; retailers are generally more concerned about customers who won't pay rather than customers who can't pay (the latter group can be assisted through various "hardship" programs managed by the retailers).

6 Customer participation and experience

This chapter summarises retailer responses to survey questions on acquisition and retention costs; and customer enquiries and complaints.

6.1 Acquisition and retention costs

In this section we outline the acquisition and retention costs faced by retailers in South Australia. To encourage retailers to provide responses in what is a commercially sensitive area, we requested ranges rather than actual figures. One retailer commented during an interview that based on their responses it appeared that its spend remained constant over time, while its spend had increased over time but remained within the same range category.

6.1.1 Electricity

Acquisition costs for customer purchases

One electricity retailer reported that it had purchased residential customers from another retailer in the last three years and one retailer has purchased small business customers over the last three years. One retailer who undertook such a transaction did not have figures available.

We have not included in this report the cost data provided to us relating to purchases of customer bases as the sample size was too small to retain confidentiality. Costs, as reported to us, have risen between 2005 and 2006. The costs reported to us for purchasing a customer base tend to be higher than the costs reported for acquiring customers through marketing campaigns. We were not able to establish why these costs were different – for example, whether a purchased customer base might retain a large number of customers who were less likely to switch than customers gained through a marketing campaign. As one retailer commented:

> *the incumbents do have a certain advantage in that for a body of customers it doesn't matter how many times you ring them or try and knock on their door they're not going to listen; they're just too busy, they've got other things in life; the cost of electricity just isn't that important to them and they're never going to churn. An incumbent is really in quite a good position to hold onto that core and I don't know how big that core is, whether it's 50% of customers or 80% of customers but there's certainly an advantage in incumbency…*

Acquisition costs for obtaining new customers (through marketing etc)

Eight retailers have funded direct marketing/advertising, direct sales, back office costs, incentives and/or switching costs to obtain residential customers in the last three years. Costs ranged from $10 to $150 per customer in 2005 and 2006, and have increased to $101 to $200 in 2007.

Some caution should be taken in interpreting these numbers. Retailers were asked to include the same categories of costs in their estimates and divide by the number of acquisitions per annum. However, the figures may have been calculated differently (for example, retailers might have taken different approaches to allocating common costs), and the variations in results might reflect variations in approach to estimating the costs rather than differences in actual costs.

Table 25: Average acquisition cost per residential customer obtained through general sales/marketing/walk ins

Residential customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125	•	•	•••
$126-$150	••••	••••	•••
$151-$175			•
$176-$200			•
$201-$250			
$251-$300			
$301+			

Seven retailers have funded direct marketing/advertising, direct sales, back office costs, incentives and/or switching costs to obtain small business electricity customers in the last three years. Costs ranged from $126 to over $301 per customer over the last three years. Acquisition costs are higher for small business customers than for residential customers.

Table 26: Average acquisition cost per small business customer obtained through general sales/marketing/walk ins

Small business customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150	••	•	•
$151-$175	•	••	••
$176-$200			•
$201-$250			
$251-$300			
$301+	••	••	••

Retention costs

Eight retailers faced costs associated with direct marketing/advertising to existing residential customers, direct sales to existing customers, back office costs, additional customer service above normal levels and/or offered incentives for their customers to remain on file. Seven retailers faced retention costs for small business customers.

For both customer groups, estimates of retention costs were lower than estimates for acquisition costs and appear to be increasing slightly over time.

Table 27: Average retention cost per residential electricity customer

Residential customers	2005	2006	2007
$0 - $50	••	••	•••
$51-$100	•	•	•
$101-$125	•	•	••
$126-$150	•	•	••
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Table 28: Average retention cost per small business electricity customer

Small business customers	2005	2006	2007
$0 - $50	•	•	•
$51-$100	•	•	•
$101-$125	•		•
$126-$150		•	•
$151-$175			
$176-$200	••	••	••
$201-$250			
$251-$300			
$301+			

6.1.2 Gas

Acquisition costs for customer purchases

No gas retailers responded as having purchased residential customers from other retailers in the last three years.

Acquisition costs for obtaining new customers (through marketing etc)

Five retailers who responded to this question, spent between $0 and $200 on average per customer to acquire residential customers between 2005 and 2007. The number of retailers paying acquisition costs increased in 2007.

One retailer provided total costs for electricity and gas customers, and suggested a percentage allocation between the two. The tables below give the proportion relating to gas only.

Table 29: Average acquisition cost per residential customer obtained through general sales/marketing/walk ins

Residential customers	2005	2006	2007
$0 - $50	•	•	•
$51-$100			
$101-$125	•	•	••
$126-$150	•	•	•
$151-$175			
$176-$200			•
$201-$250			
$251-$300			
$301+			
Not applicable	••	••	••

Acquisition costs for small business customers vary widely by retailer – from $0 to $50, $151-175, to over $301. Acquisition costs remained relatively steady over time for small business customers.

Table 30: Average acquisition cost per small business customer obtained through general sales/marketing/walk ins

Small business customers	2005	2006	2007
\$0 - \$50	•	•	•
\$51-\$100			
\$101-\$125			
\$126-\$150			
\$151-\$175	•	•	•
\$176-\$200			•
\$201-\$250			
\$251-\$300			
\$301+	•	•	•
Not applicable	••	••	••

Retention costs

Gas retailers spent up to \$125 in 2005 and 2006 and up to \$150 in 2007 to retain residential gas customers. Two further retailers began funding active customer retention in 2007.

Table 31: Average retention cost per residential gas customer

Residential customers	2005	2006	2007
\$0 - \$50	••	••	••
\$51-\$100			
\$101-\$125	•	•	••
\$126-\$150			•
\$151-\$175			
\$176-\$200			
\$201-\$250			
\$251-\$300			
\$301+			
Not applicable	••	••	••

Retention costs for small business customers were higher than for residential customers, with spends of up to \$200 per customer per annum.

Table 32: Average retention cost per small business gas customer

Small business customers	2005	2006	2007
$0 - $50	•	•	•
$51-$100	•	•	•
$101-$125			•
$126-$150			
$151-$175			
$176-$200	•	•	•
$201-$250			
$251-$300			
$301+			
Not applicable	••	••	••

6.2 Customer enquiries and complaints

This section discusses how customer complaints are dealt with in South Australia and outlines retailer responses to customers who cannot or will not pay for energy consumed.

6.2.1 Electricity

Referrals to complaint handling bodies

Retailers operating in South Australia have had a number of complaints referred to the Energy Industry Ombudsman of South Australia (EIOSA), an independent service which *"can investigate and resolve disputes between customers and electricity and gas companies"*. Many retailers did not respond to the survey question asking for complaints referred to complaint handling bodies, therefore we are unable to comment on trends from the survey information. (EIOSA publishes complaint numbers in its annual report).

Customers who cannot/will not pay

South Australian retailers tend to distinguish between customers who cannot pay and those who will not pay. Broadly, retailers offer support to customers who cannot pay and refer to debt management those who will not pay (while still meeting regulatory obligations to customers).

All retailers described internal policies and procedures to deal with customers (in particular residential customers) who cannot pay. Some approach it by following the Victorian Essential Services Commission Hardship Policy, which is seen as a national benchmark by some retailers, or the Energy Retail Code. Others described detailed policies, offering individuals who met certain criteria (usually showing some willingness to try and pay), entry into a programme, with tailored individual payment plans offered by case managers and protection from disconnection provided that payments are not repeatedly missed. Customers are given referrals to community welfare organisations, suggestions for financial counselling, no additional fees and in some cases energy saving advice.

Most retailers appeared sympathetic to customers who cannot pay. One retailer commented that there are many reasons that customers' ability to pay can change such as illness, diminished income due to drought or other natural disasters, or other changes in circumstances.

Some of these policies are only available to residential, not business customers. Retailers were also less lenient with customers who will not pay, and follow normal debt management procedures. Retailers did explain that customers who do not meet their payment obligations may be disconnected and those that switch retailers will be subject to normal collection processes.

6.2.2 Gas

Referrals to complaint handling bodies
As above, gas retailers have had customer complaints referred to EIOSA.

Customers who cannot/will not pay
Gas retailers follow the same processes in dealing with customers who cannot and will not pay as described above for electricity retailers.

7 Conditions for entry, expansion and exit

This chapter summarises retailers' views on the conditions for entry, expansion and exit in the South Australian electricity and gas markets. It covers expansion plans, opportunities for entry and expansion, regulatory barriers, and the impact of market structure.

7.1 Expansion plans

This section outlines retailers' responses to questions asking whether they are actively seeking new customers, what changes to their business model they are considering and whether they are considering expanding or contracting.

7.1.1 Electricity

Seeking new customers

Five electricity firms responded saying they were actively marketing for new customers in South Australia.

These responses need to be interpreted carefully. One of the retailers who stated that it is actively seeking new customers is only doing this through their internet site, while another who said that it is not actively marketing and only attracting customers through inbound telesales and online sales. This suggests retailers have different perspectives on what active marketing involves.

Importantly, four electricity retailers ceased or suspended active marketing in South Australia over the past 24 months. One retailer has suspended marketing for three periods of up to one month for each period, but is now seeking new customers. Three retailers have suspended active marketing (two of these since mid 2007). All retailers who have suspended active marketing pointed to wholesale electricity prices as all or part of the reason for this move. Several of the responses from retailers in relation to the wholesale price were quoted in section 5.1 above. Quotes from the written responses include.

> *Volatile wholesale electricity prices and limited liquidity of hedges in market made continued sales unviable.*
>
> *Poor wholesale contract market. Market Liquidity – unable to get competitive energy prices short, medium and long term.*
>
> *…suspended active marketing due to increases in wholesale costs of electricity.*
>
> *1) High wholesale prices. 2) Refocus on launch of [another state] retail gas business*

Changes to business model

Dual fuel forms an important element for most retailers, and two retailers currently supplying a single fuel report having definite plans to offer dual fuel and standardise systems nationally, while one has definite plans to vertically integrate. Others may consider changes to their business model in future.

Retailers in South Australia generally perceive a national trend towards a small number of large, vertically integrated, dual energy (electricity and gas) companies. Within this emerging market structure, retailers generally expect there would continue to be room for new standalone entrants as well as small, and niche market, retailers. The retailers emphasised that this was a general statement and that high and volatile spot prices meant that there were few if any opportunities currently for standalone retailers in South Australia.

Large retailers, however, are expected to remain (or to become) vertically integrated into generation activities. Retailers expect a large standalone retailer would find it difficult to contract for sufficient volume of forward contracts, especially if other competing firms vertically integrate. A standalone retailer would also require a substantial balance sheet to back large volume forward contracts, whereas vertical integration may release efficiencies by allowing that capital to be invested directly in generation plant.

At a national level, the four largest retailers are vertically integrated; these firms are involved in wholesaling and retailing both gas and electricity and offer customers dual fuel. Several retailers suggested that there were additional business strategy considerations for dual fuel firms, as discussed in section 5.3. Retailers operating in South Australia anticipate that the organisational structure of firms competing in the State will reflect these national trends.

Table 33: Changes to electricity business models being considered by retailers

Factors impacting on business model	**Factor already in place**	**Definite plans**	**May consider in future**
Launching an electricity retail business in South Australia	●●●●● ●●●●		
Vertically integrating with electricity generation	●●●●●	●	●●●●
Vertically integrating with energy network business			●●
Offering dual fuel	●●●●●	●●	●●
Standardising retail systems nationally (to the extent that this is possible)	●●●●● ●●	●●	●

Retailers commented that they were increasingly interested in green energy, and one retailer reported that it was considering investing directly in green generation. During the follow up interview this retailer stated that *"we want to get into the green market as quickly as we can… its common sense now… with all the schemes coming through and levies"*. The retailer went on to explain that suppliers tend to want to sell green energy in large blocks and tend to negotiate better deals with larger suppliers, and suggested that smaller retailers would need to invest in green energy with a joint venture partner.

Expansion or contraction

Eight retailers have already commenced retail in other states.

A number of retailers pointed to possible expansion plans. One retailer has definite plans to acquire the customer base of another state's retailer, while six may consider it in the future. Six retailers may consider acquiring the customer base of another South Australia retailer in the future.

Four retailers also commented that contraction - selling their existing customer base and exiting the South Australian market - as possible considerations in the future.

Table 34: Expansion or contraction being considered by electricity retailers

Factors impacting on expansion	Factor already in place	Definite plans	May consider in future
Acquiring the customer base of another SA retailer			●●●●● ●
Commencing retail in another state	●●●●● ●●●		
Acquiring the customer base of another state's retailer		●	●●●●● ●
Exiting the SA market			●●●●
Selling your existing customer base			●●●●

7.1.2 Gas

Seeking new customers

Three gas retailers are actively seeking new customers in South Australia. Two other retailers who responded to this question are not actively seeking customers.

One retailer suspended active marketing in mid 2007 due to an increase in wholesale costs. The retailer is still accepting customers through inbound telesales and online sales.

One retailer stated that while it always had services on offer, *"the level of proactive and direct marketing of product offers will vary depending on customer margins and the business strategy at that point in time"*.

Changes to business model

Five retailers have stated that they have already launched gas retail businesses in South Australia. Four retailers have vertically integrated with an energy supplier and offer dual fuel, while one has definite plans to offer dual fuel. Three have attempted to standardise retail systems nationally, while two have definite plans to do this. Vertical integration may be considered by one retailer.

Table 35: Changes to gas business models being considered by retailers

Factors impacting on business model	Factor already in place	Definite plans	May consider in future
Launching a gas retail business in South Australia	●●●●●		
Vertically integrating with energy supplier	●●●●		●
Vertically integrating with energy network business			●
Offering dual fuel	●●●●	●	
Standardising retail systems nationally (to the extent that this is possible)	●●●	●●	

Expansion or contraction

Two retailers may consider expansion through acquiring the customer base of another South Australia retailer and/or another state's retailer. Exit and sale of customer base is being considered by one retailer.

Table 36: Expansion or contraction being considered by gas retailers

Factors impacting on expansion	Factor already in place	Definite plans	May consider in future
Acquiring the customer base of another SA retailer			●●
Commencing retail in another state	●●●●		
Acquiring the customer base of another state's retailer		●	●●
Exiting the SA market			●
Selling your existing customer base			●

7.2 Opportunities for entry and expansion

Retailers were asked if they were comfortable that they could do the following in order to enter into the market or expand their market share:

1. Source the energy supply required;

2. Put in place effective methods for managing price and volume risk;

3. Access the network infrastructure required;

4. Switch customers in a timely and efficient manner

Two electricity and gas retailers did not answer questions related to 2-4 above, as they are not seeking to expand.

7.2.1 Electricity

Sourcing energy supply

Five retailers stated that they were comfortable that they can source the energy supply required to expand. Retailers explained that access to own generation and a liquid wholesale market gave them the energy supply required. Retailers' views are quoted below:

> *Energy is sourced (physically) from the pool and purchased from NEMMCO, hence sourcing the energy is very easy.*
>
> *In addition to our existing generation capacity, portfolio of hedges and access to the spot market (either within the state or via interconnector flows), [retailer] is comfortable that a sufficiently transparent and active contract market exists. [retailer] is able to purchase contracts from generators or wholesales either "Over the Counter" or via the futures market.*
>
> *The market has a good level of liquidity, therefore offering enough options to purchase wholesale contract cover.*

Five retailers stated that they were not comfortable that they can source the energy supply required to expand. When pressed in interviews, almost all of these retailers commented that they could obtain supply, but that they could not obtain supply at a price that would allow them to compete for customers profitably. Retailer views on these issues were discussed above in section 5.1. Quotes from the written responses include:

> *Fine demand and supply balance; most generation capacity has been contracted out; remaining capacity is used by generators for potentially 'gaming' the market; large vertically integrated entities 'controlling' access and creating barriers to entry*
>
> *…are comfortable that we can source the energy supply required from existing supply side market participants. However, current volatility in the wholesale market …increases the difficulty in securing cost effective wholesale agreements (especially for small new entrant 2nd tier retail suppliers). In addition, the uncertainty about the impending CTS in 2010 restricts the ability of any retailer to contract for the medium term.*
>
> *The total regional capacity and regional demand (including the record demand of 10 January 2008) equate to about 9% of the NEM. The nameplate South Australian generation capacity comfortably meets demand with a significant buffer of 30% of South Australian capacity based on record demand against all*

NEM registered generators in South Australia. Although the physical generation is not being offered to the market as financial contracts.

During the interviews, all of these retailers suggested that the situation had become difficult for them over the past 12 to 18 months because of the high and volatile spot market prices.

Managing price and volume risk

Four retailers felt comfortable that they could put in place effective methods for managing price and volume risk. Two retailers explained that they are able to access (physical and market) instruments to cover price (and volume) risk. One of these retailers also stated that it is expanding its generation capacity to help manage price and volume risk.

Five retailers were not comfortable that they could put in place effective methods for managing price and volume risk. Contracts were available but at prices which would make it uneconomic for the retailer to compete for customers. Reasons given for the high price of contracts included the current volatility and difficulty securing appropriate agreements in the wholesale market; low risk agreements require premiums that make retail offers uncompetitive; difficulty predicting load requirements and load flexing particularly during very hot days (which is more of an issue for South Australia as it is a temperature sensitive region); and the dominance of host generator/retailers – which these retailers view as a barrier to entry.

In detailed comments during interviews, retailers explained that the primary difficulty related to managing volume risk. Retailers generally feel they can manage price, but smaller retailers were concerned about managing volume risk. The smaller retailers generally commented that:

liquidity of risk management products (futures and OTC contracts) is thin and variable.

Retailers commented that liquidity was acceptable previously, though has always been less than Victoria. A number of retailers commented that the situation had been made worse by the operation of TIPS in 2007/2008 and the exit of financial intermediaries.

One retailer referred us to Sydney future exchange data which shows that traded forward contracts for South Australia amounted to about 70% of the underlying physical demand, whereas in Victoria, forward contracts traded in volume terms at about 190% of the underlying physical demand.

The more established retailers suggested that periods of volatility are inherent in electricity markets and that poor risk management by some retailers should not be blamed on the market.

A question for those guys [complaining about volatility] is, were contracts available before summer that would have left you with a profit? The answer is, yes for sure… did these guys want more profit, did they want to grow quicker, *are they prepared to take risks to do that and cut corners and I think the answer to that is absolutely yes.*

Accessing network infrastructure

All eight retailers who responded to this survey question stated that they were comfortable that they can access the network infrastructure required to expand. Comments included *"genuinely open access", "design is very effective"* and *"given the regulated nature... no discernable constraints"*.

Retailers did mention some issues they had however, which largely focused on credit arrangements:

- Development of alternative market products has been limited;
- Credit arrangements are severe compared to Victoria and processes for "B2B" should be more aligned with other states; and
- Would prefer availability of an insurance option and or approaches that recognised payment history, rather than a cash backed bank guarantee – a particular issue for small new entrants who have not been established long enough to acquire an acceptable credit rating and will have to provide a guarantee.

The credit arrangements implement by the network distribution companies in Victoria were referred to as providing a better model.

Switching customers in a timely and efficient manner

Seven retailers feel able to switch customers in a timely and efficient manner. One retailer stated that South Australian systems are comparable with those in other states, while another stated that systems have proven effective. One of these retailers was comfortable, but would still like to see the use of new technologies to speed up the transfer process and make it more efficient.

Two retailers did not feel comfortable that they can switch customers in a timely and efficient manner. Complaints included level of manual rework required and timing issues. One stated that timing is *"a moving target that can happen from days to months"* while the other would prefer next day transfers (but recognised that the rules and systems do not allow for this).

7.2.2 Gas

Sourcing energy supply

Three retailers stated that they were comfortable that they can source the energy supply required to expand. One retailer explained that South Australia is supplied by two gas transmission pipelines and multiple producers, therefore there is little impediment to securing gas supply. This may be strengthened by coal seam methane transported via Moomba.

Three retailers stated that they were not comfortable that they can source the energy supply required to enter the market. One explained that gas is sold in large volumes on a take or pay basis which is not viable for smaller retailers without a large customer base (despite a number of attempts on their part to secure this). In the interviews a retailer explained the problem as follows:

> *Generally gas contracts are bought with fairly rigid terms so they're a little bit harder to risk manage… Managing take or pay is quite difficult when you're penetrating a market and your volume is growing… That's where the Victorian system, where you have a pool market and it makes it a bit easier to go long or short on gas; you have a disposal or acquisition mechanism.*

The retailer commented that the residential market is very driven by temperature, and hence consumption volumes were volatile. To retail gas in South Australia, the retailer had to:

> *Buy the transportation as well as buy the physical fuel and nominate how much gas you wanted every day… In the case of electricity, NEMMCO does all that for you.*

Another retailer expressed concern about market volatility and the inability to purchase through cost effective agreements. A third retailer pointed to the limited number of gas suppliers and producers, and the volumes held for electricity generators, and the potential for market gaming as factors affecting the availability of gas supply.

Accessing network infrastructure

Three retailers stated that they were comfortable that they can access the gas distribution network infrastructure required to expand. One retailer gave the following reasons: the regulated nature of access; existing access arrangements; significantly more transmission capacity than demand; willingness of pipeline operators to consider requests for shipping contracts or on selling from existing shippers to third parties. Another agreed that it could access the infrastructure but that the level of credit support and requirement of a bank guarantee were onerous for small retailers.

Two retailers stated that they were not comfortable that they can access the network infrastructure required to expand. During interviews, these retailers explained that there concerns were primarily about the difficulty and cost of managing volume risk in transporting gas.

Switching customers in a timely and efficient manner

Three retailers felt comfortable that they can switch customers in a timely and efficient manner. One retailer felt that REMCo market systems are in place and functioning effectively. Another noted that there is still room for improvement, in the utilisation of new technologies to make it more efficient.

Two retailers did not feel comfortable that they can switch customers in a timely and efficient manner. One retailer stated that the REMCo system and process requirements are complicated and not robust compared to other systems.

7.3 Regulatory barriers to entry and expansion

This section summarises retailers' views on barriers to entry and expansion in the South Australian energy retail markets. Retailers' were asked specifically about the impact of standing offers, climate change and rising fuel prices; and were also asked about other regulatory barriers and changes they would like to see.

7.3.1 Electricity

Standing offers

In written responses, the electricity retailers had different views on whether the existence of standing offers limited their ability to run their business, particularly on pricing and targeting of low volume customers. Retailers tended toward the view that the standing offers were limiting their ability to maintain a competitive profit margin. However, a number of retailers also responded that the standing off had not limited their ability to launch retail in South Australia.

During interviews, retailers clarified that the standing offer had not limited their ability to enter the market historically as there had been 'head room' between the standing offer price and the wholesale price. Most retailers believed that situation had changed, and a lack of margin was now impeding competition for customers.

As discussed above, the lack of margin between the wholesale spot price and the standing offer had led a number of retailers to cease actively marketing in South Australia.

Table 37: Extent to which standing offers limit retailer's ability to enter or expand

How existence of standing offers may limit ability to alter business	Not at all limiting	A consideration	Moderate limitation	Limiting	Very limiting
Launch an electricity retailing business in South Australia	●●●●●	●	●●	●●	
Introduce a greater range of innovative products	●●●	●●	●●	●●●	●
Offer more innovative pricing structures	●●●	●	●●	●●	●●●
Offer prices that reflect the efficient costs to service	●●	●●●	●	●●	●●●
Maintain a competitive profit margin		●	●●	●●	●●●●●
Target low volume consumers	●●●	●●●●	●●	●	●●

One retailer explained that it is a *"strong advocate for the removal of retail price regulation when a market is deemed to be demonstrating effective competition"*. The retailer argues that this is the case in South Australia due to the level of customer churn from standing offer to market contracts and as South Australia was ranked third in the world for switching (World Energy Retail Ranking).

The retailer also explained that standing offers that are set inappropriately *"may inadvertently result in the erosion of retailer margins due primarily to the inability to recover costs"*. As discussed in section 5, all retailers in the interviews echoed the concern that over the past 18 months the standing offer did not reflect actual wholesale prices. Retailers perceived a regulatory risk that the standing offer would not be adjusted to reflect higher costs – a number of retailers referred to the current price for oil not being anticipated when the standing offer price was set.

Climate change and rising fuel prices

Seven retailers believe that policies to address climate change and rising fuel prices are likely to affect entry and competitive conditions for electricity. Four believe that they will not. One retailer provided a mixed response that climate change policies and rising fuel prices would have an adverse affect only if retailers are not allowed to reflect costs in retail tariffs.

The key initiatives discussed included:

1. **Proposed REES (Residential Energy Efficiency Scheme)** – a scheme proposed for South Australia which will require electricity retailers to offer incentives to households to adopt energy saving measures such as energy efficient appliances and insulation. For example, they may replace light bulbs or provide discounts on installation of insulation.[7]

2. **Proposed NETS (National Emissions Trading Scheme)** – this is being designed now and is expected to be in place by 2010. The scheme will be a cap and trade scheme, which will aim to drive investment in low emission technologies and renewable energy, complemented by policies to improve household energy efficiency, in order to reduce emissions by 60% by 2050.[8]

3. **Increases in MRET (Mandatory Renewable Energy Target)** – a national target of 20% renewable energy in Australia's electricity supply by 2020. Proposed changes are being made which will be put in place by early 2009.[9]

Retailer's responses tended to fall into three groups. We paraphrase and summarise responses under these groupings below.

[7] http://www.dtei.sa.gov.au/images/energy_efficiency_scheme.pdf

[8] http://www.greenhouse.gov.au/emissionstrading/about.html

[9] http://www.greenhouse.gov.au/renewabletarget/index.html

1. **The policies will have an impact on competition**

   Some retailers were concerned that these policies will impact on competition by disadvantaging small or non-vertically integrated retailers who are unable to absorb increased costs or by reducing the benefits of operating in multiple jurisdictions, reducing the likelihood that retailers will do so. Responses included:

   - Uncertainty regarding implementation of the Emissions Trading Scheme is impeding investment. Compliance costs from schemes such as REES are *"extremely onerous and costly to implement"* for smaller retailers, which will see them withdraw from the market or taking a very cautious approach to expansion, reducing competitiveness if thresholds are not put in place.

   - Costs will be difficult to pass on to end users, but vertically integrated retailers will have an advantage, impacting on the level of competition.

   - Retailers operating across jurisdictional boundaries will face an additional burden where climate change policies have inconsistent obligations and reporting requirements.

2. **The policies will lead to changes, but these will affect all retailers alike, therefore there will be no impact on competition**

   - Changes will affect all retailers alike if the cost of carbon and fuel prices are reflected fully in contracts and price tariffs.

   - All retailers are required to meet the same proportion of MRETs, and can source these competitively priced Renewable Energy Certificates (REC) from the secondary REC trading market.

   - All retailers are likely to be faced with the same proportional impacts under the proposed South Australia energy scheme.

   - While emissions trading schemes will impact on overall energy costs, "there will be no material impact on retail competition or entry conditions".

3. **The policies will have an impact, due to increased costs [without linking this to competitive effects]**

   - Retail businesses will face a *"real and very significant"* cost burden as retailers comply with scheme conditions and *"implement required changes to strategies, systems and processes, reporting and resourcing"*.

   - Initiatives will increase cost and therefore squeeze retail margins.

   - Regulated prices have not fully accounted for rising fuel prices, reducing margins

One retailer explained that it is *"monitoring Government policy to address climate change and the carbon trading schemes in each state are considered when deciding which markets we target"*.

Other regulatory barriers

Seven retailers discussed other regulatory barriers (in addition to standing offers and the climate change regulation discussed above) concerning them.

Specific barriers discussed include:

- Prudential requirements from the coordination agreement with ETSA Utilities, as they *"impose significant and unnecessary costs on retailers"*. These were considered a barrier to entry because large retailers with credit histories were not required to provide the cash backed guarantees required from smaller and new entrant retailers (this issue was discussed above).

- Reporting requirements are viewed by two retailers as more onerous in South Australia than other States.

- Overly prescriptive regulation: most retailers expressed concern that South Australia (and other State regulators) regulated aspects of service standards which the retailers believed should be determined by competition. For example, one retailer told how that it attempted to simplify the bills to customers in response to customer demand but found that it could not because of regulatory requirements:[10]

  > *we thought well we can do something here because there was far too much information [on customer bills]… we spoke to 1000 customers and we said what would you like, and they said they'd like something simple because we can't understand what we've got. And when we went through it we thought well it's a low engagement category, people can't spend the time trying to understand it, and so it actually doesn't serve a purpose and so anyway we looked at simplifying the bill only to find that 98% of the information there is mandatory, so actually you've got choice over colour and you've probably got choice over the type of paper you use… I think it is that crazy… by taking these things away [overly prescriptive regulation] you create the opportunity where people will be more engaged and then you drive genuine innovation and the customer benefits over time.*

More general concerns included compliance costs, policy directives and signalling, and the number of environmental schemes in place. The most common complaint from retailers was inconsistency of policy between jurisdictions, which means that retailers cannot work efficiently across a number of states. Examples included schemes on retail

[10] This retailer has the same concerns in relation to regulatory requirements in Victoria.

codes, energy efficiency, hardship, debt management, consumer protection, solar fuel and metering policies (including pre-pay and advanced metering). These retailers called for a nationally consistent approach.

Four retailers listed no further regulatory barriers of concern – with one pointing to retailer rivalry and the level of customer churn as evidence of this.

Potential changes to government policy

Retailers suggested the following changes to policy to enable more effective competition in South Australia. We have grouped these by theme.

Improve the consumer protection framework

A number of retailers requested improvements to the consumer protection framework, to reduce the burden on retailers largely by aligning with other States' requirements and providing greater scope for retailer differentiation and innovation. Retailer views are summarised below:

- Alter detailed customer service protections (as discussed above) such as telephone response times as they limit the ability to differentiate on the basis of service and cost, are more onerous than in other states and may deter entry because of cost impacts (mentioned by more than one retailer). Associated with this, retailers called for a nationally consistent ombudsman and consumer protection schemes.

- Remove business customer coverage from the energy consumer protection framework.

Act to promote innovation

Most retailers sought removal of retail price regulation, and some sought intervention to allow new technology and innovation to be put in place. Paraphrased responses included:

- Remove standing offer prices/retail price regulation to encourage innovation and cost-reflective pricing, and eliminate future pricing risk for retailers. This change was mentioned by most retailers.

- Take a "light handed" approach to regulation to promote product innovation and adoption of new technology; by 'light handed' the retailer meant that regulation should be designed to rely more on incentives and less on prescriptive approaches.

- Consider the installation of prepayment meters as a distributor included service, spreading the costs across the entire regulated market.

Improve national policy consistency

Retailers want a more nationally consistent approach to energy regulation, with one set of rules. For example, around responses to greenhouse gases:

- Improve policy consistency between jurisdictions and remove state specific programs (mentioned by more than one retailer). Develop national rules or regulatory framework (mentioned by more than one retailer).

- Agree on greenhouse mitigation measures nationally and implement them as soon as possible to provide certainty.

- Some policy differences between the States were perceived as having the potential to segment the operations in different jurisdictions. One example of such a policy difference raised in interviews related to smart meters; were Victoria to proceed with installing smart meters and South Australia to retain non-interval meters, retailers operating in each state would receive vastly different information flows and would begin to package retail products in Victoria and South Australia differently; and eventually the operations across different jurisdictions may become segmented.

Reduce compliance costs

Retailers called for reduced compliance costs and processes which ensure that future compliance costs are minimised:

- Reduce compliance reporting or make it consistent across all states.

- Consult with retailers before making changes which impose compliance costs than cannot be adequately recovered.

- Alter prudential requirements such as with ETSA Utilities.

Regulate vertical integration

Smaller retailers expressed concerns about the level of vertical integration in the market and some called for regulation, including:

- Stronger regulation of the retailer/network relationship.

- Restricting the level of generation capacity that can be owned by host retailers, to reduce the level of vertical integration and open the market for competition.

7.3.2 Gas

Standing offers

Retailers believe the existence of gas standing offers limits the ability of gas retailers to offer more innovative pricing structures, maintain a competitive profit margin, offer prices that reflect efficient costs of service and introduce a greater range of innovative products. It was not considered by most to limit the targeting of low volume customers.

During interviews gas retailers said that there had been little if any margin available between the wholesale prices and the regulated standing offer price for gas, which combined with the low level of gas usage in South Australia compared with other states explains the limitations described above. Retailers did note that ESCOSA is reviewing the regulated gas price, as discussed above.

Table 38: Extent to which standing offers limit retailer's ability to enter or expand

How existence of standing offers may limit ability to alter business	Not at all limiting	A consideration	Moderate limitation	Limiting	Very limiting
Launch a gas retailing business in South Australia	••		•	•	
Introduce a greater range of innovative products	•		••	••	•
Offer more innovative pricing structures	•		•	••	••
Offer prices that reflect the efficient costs to service		••	•	••	•
Maintain a competitive profit margin		•	•	•	••
Target low volume consumers	••	••			•

Climate change and rising fuel prices

Three retailers believe that policies to address climate change and rising fuel prices will affect entry and competitive conditions for gas. Four retailers believe that they will not.

Views specific to gas retailing or discussed by retailers in relation to gas only included:

- Environmental policies will not affect competition at present, but may in future as the calls on gas for end use may increase, reducing wholesale liquidity further.

- As Australia moves to a carbon constrained economy there may be greater demand for lower intensity fuels such as natural gas, although this will affect all retailers and may not impact on competition

- The National Emissions Trading scheme will add costs and there may be an issue as to how costs will be passed through and accounted for, particularly for those players that are not vertically integrated.

- Gas market liquidity is unlikely to change as a result of an emissions trading scheme being introduced, allowing retailers to participate on a level playing field.

Other regulatory barriers

Six retailers who responded to this question discussed other regulatory barriers (in addition to standing offers and the climate change regulation discussed above) concerning them. These included:

- The market rules *"are just too complex and impose too many risks for being out of balance."* Limited information, training or advice available from REMCO on gas market rules, forcing reliance on competitors "*to assist us through the maze of market rules"*.

- As with electricity, gas retailers were concern about South Australia specific environmental programs:

  > *The advent of additional government programs specifically for South Australia and the required compliance by both incumbent and second-tier retailers with the new regulations can also hinder entry into the South Australian gas market. Retailers primarily compete on a national level and any additional entry costs to satisfy a specific jurisdiction has system and process costs that impact competition in that jurisdiction.*

- Retail code coverage of business customers.

More general concerns included jurisdictional differences (e.g. for customer protection), compliance costs, policy directives and signalling and the regulated retail price.

One retailer did not raise any concerns, citing South Australia's ranking as the third hottest market in the world for customer switching as evidence of lack of barriers.

Potential changes to government policy

Retailers suggested a number changes to government policy to allow entry or more effective competition in South Australia. These are very similar to the suggestions outlined above under electricity, with the addition of a request to improve transmission and distribution access arrangements (including prudential requirements and penalty structures).

7.4 Impact of market structure on entry and expansion

This section covers three main areas: structural features of the market; firm size; and changes over time. It considers the structural features and other factors facilitating or hindering entry or expansion in the South Australian energy retail markets. It also outlines retailers' views on whether economies of scale and a particular critical mass are required to be competitive in South Australia. Finally, it outlines retailers' views on whether conditions are improving or worsening over time and what measures of competitive threat are monitored internally.

7.4.1 Electricity

Structural features

Retailers view access to generation as a very important factor in being competitive in the South Australian market, with vertical integration with energy supply being viewed as important by most. Access to capital, operation in another jurisdiction and size of customer base were also ranked as important by most retailers.

Vertical integration with energy distribution and position as host retailer were not considered to be important by most retailers.

Table 39: Importance of structural features for retailers to be competitive

Factors impacting on competitiveness	Not considered	Considered	Moderately important	Important	Very important
Vertical integration with energy supply		●	●●	●●●	●●●●●●
Access to generation			●●	●●	●●●●●●●●
Vertical integration with energy distribution	●●●●●●	●●	●	●	●
Position as a host retailer	●●●●●	●●	●●●●●		
Size of customer base in South Australia (local economies of scale)	●	●●●	●●●●●	●●●●	
Operation in another Australian jurisdiction		●●●	●●	●●●●	●●●
Size of customer base in other parts of Australia (national economies of scale)	●●	●	●	●●●●●●	●●
Access to capital	●		●●●	●●●●	●●●●

A number of the smaller retailers commented that the structure of the South Australian electricity sector mean that one vertically integrated retailer could periodically exercise market power.

Factors affecting entry into South Australia

The table below goes into more detail about factors that retailers see as providing incentives or deterrents to entry (the next table focuses on expansion). As discussed above, the two major deterrents to entry for retailers were regulatory uncertainty and access to energy supply at reasonable cost. Other deterrents include regulatory differences between jurisdictions, and access to risk mitigation products. Retailers listed few major incentives to enter, with market share being a factor for two retailers. Other factors providing some incentive to enter include distribution of market shares between retailers and customer engagement with energy products.

Table 40: Factors facilitating or hindering entry into South Australia electricity market

Factors impacting on competitiveness	**Major deterrent to entry**	**A hindrance to entry**	**No impact**	**Some incentive to enter**	**Major incentive to enter**
Retail market structure					
Large number of retailers currently supplying customers		●●	●●●●● ●●	●	●
The distribution of market shares between retailers		●	●●●●● ●	●●●●	
The market share of the host retailer		●●	●●●	●●●●	●●
The scope of services offered by competitors		●●●	●●●●● ●	●	●
Current levels of competition between retailers	●	●●	●●●●●	●●●	
Wholesale market and infrastructure					
Access to energy supply at reasonable cost	●●●●●	●●●	●●	●	●
Access to risk mitigation products	●●●	●●●●●	●●	●	●
Access to adequate transmission and distribution services	●●	●	●●●●● ●	●●	●
Regulatory framework					
Extent of state consumer protection and other regulation	●●	●●●●● ●●	●●		
Regulatory differences between jurisdictions	●●●	●●●●● ●	●●		
Regulatory uncertainty	●●●●●	●●●●	●●		
Standing offer price legislation	●●	●●●●	●●●●●		
Marketing					
Brand awareness		●●	●●●●●	●●●	
Brand loyalty to other retailers	●	●●●●●	●●●●●		
Customer inertia	●	●●●	●●●●● ●●		
Customer engagement with energy products		●●●●	●●	●●●●	
Access to sufficient customer data to make offers		●	●●●●● ●●	●●●	
Customer transfer process					
Customer fears or concerns regarding the process of		●●●●●	●●●●●		

Factors impacting on competitiveness	Major deterrent to entry	A hindrance to entry	No impact	Some incentive to enter	Major incentive to enter
switching to another retailer			•		
Time delays before transfer implemented	•	••••• •••	••		
Exit or termination fees for some customer contracts	•	•••	••••• ••		
Investment requirements					
Marketing		••••	•••••	••	
Call centre		••	••••• ••	•	
Billing system	•	•••	••••• •	•	

Five retailers listed other factors which they believe facilitate or hinder entry into the South Australian electricity market. Retailers' views are illustrated with selected quotes or portions of quotes below:

- **Market liquidity –** *South Australian demand equates to about 9% of the NEM yet the open interest of Futures contracts (as a region in the NEM) on the SFE equate to a little under 3% of the total contracts held. This illustrates that there are far less financial contracts traded in the South Australian region than in other regions within the NEM.*

- **Power of the host retailers** – *The domination of the South Australian market by the Incumbent Generators and Retailers and the lack of liquidity of financial contract coverage are in themselves a natural barrier to entry to new and expanding retailers…The ability of the generators to rebid surplus reserve capacity in a temperature sensitive region has in turn reinforced the dominance of the incumbent participants via the pool price outcomes…The tight control of surplus reserve capacity and the ability of the region to experience significant price spikes…further reinforce the concentrated power.*

- **Set up costs** – *There are some set-up costs of establishing a retail electricity business for South Australia because of the need to comply with certain South Australia obligations such as the rebate schemes and their service level requirements….However, the development of various retail operating models, such as outsourcing back-office functions to third parties allows … retailers to enter the market without necessarily incurring the full set-up costs.*

- **Jurisdictional differences** – *The current complexity and differences in regulatory requirements across the various jurisdictions impose significant compliance costs upon participants in the energy market. This complexity in* *turn diminishes the benefits that would otherwise flow from energy market reform.*

Factors affecting expansion in South Australia

The table below summarises retailers views on factors facilitating or hindering expansion within the South Australian electricity market. The major deterrent to expansion for five retailers is access to energy supply at reasonable cost. Other deterrents include regulatory uncertainty, access to risk mitigation products, and regulatory differences between jurisdictions. Incentives to expand include market share of host retailer, access to risk mitigation products and brand awareness. Factors influencing expansion are similar to those influencing entry.

Table 41: Factors facilitating or hindering expansion within the South Australia electricity market

Factors impacting on competitiveness	**Major deterrent to expansion**	**A hindrance to expansion**	**No impact**	**Some incentive to expand**	**Major incentive to expand**
Retail market structure		●			
Large number of retailers currently supplying customers		●●●	●●●●● ●	●	●
The distribution of market shares between retailers		●	●●●●●	●●●●	
The market share of the host retailer		●●	●●●●	●●●●	●
The scope of services offered by competitors		●●	●●●●● ●●	●	●
Current levels of competition between retailers	●		●●●●● ●●●	●●	
Wholesale market and infrastructure					
Access to energy supply at reasonable cost	●●●●●	●●	●●●	●	●
Access to risk mitigation products	●●●	●●●●	●	●●●	●
Access to adequate transmission and distribution services	●●	●●	●●●●●	●●	●
Regulatory framework					
Extent of state consumer protection and other regulation	●	●●●●● ●●	●●●		
Regulatory differences between jurisdictions	●●	●●●●● ●	●●●		
Regulatory uncertainty	●●●	●●●●●	●●●		
Standing offer price legislation	●●	●●●●	●●●●●		

Factors impacting on competitiveness	**Major deterrent to expansion**	**A hindrance to expansion**	**No impact**	**Some incentive to expand**	**Major incentive to expand**
Marketing					
Brand awareness		●●	●●●●	●●●●●	
Brand loyalty to other retailers	●	●●●●●	●●●●●		
Customer inertia	●	●●	●●●●● ●●●		
Customer engagement with energy products		●●	●●●●●	●●	●
Access to sufficient customer data to make offers		●●	●●●●● ●	●●●	
Customer transfer process					
Customer fears or concerns regarding the process of switching to another retailer	●	●●●●	●●●●● ●		
Time delays before transfer implemented	●	●●●●● ●●●	●●		
Exit or termination fees for some customer contracts	●	●●●	●●●●● ●		
Investment requirements					
Marketing		●●	●●●●● ●	●●●	
Call centre			●●●●● ●●	●●●	
Billing system		●●	●●●●● ●	●●●	

Six retailers listed other factors which facilitate or hinder expansion within the South Australian electricity market. These include:

- Requirements for retailers to purchase meters and then pass them on to the distribution company for installation – access to meters and competitive installation costs are an issue.
- Regulatory changes which retailers must implement at their own cost.
- Price regulation imposing a price cap – "*the single biggest issue affecting our ability to expand*".
- Jurisdictional differences and complexity.

- Policies related to renewable energy/greenhouse gases.

- High level of competitive activity and customer churn make it increasingly difficult to win customers.

Critical mass

Retailers were asked if a critical mass in terms of customer numbers or volume of electricity was required to be a viable competitor in South Australia. Five retailers believe a critical mass is required and five retailers did not believe a critical mass was required. One gave a mixed response (only if services are not provided in other jurisdictions).

Three retailers suggested a set critical mass, ranging from 5,000-10,000 active customers; 10,000-20,000 customers if established in another state or 100,000 customers for South Australia alone; to 100,000 customers at a minimum. Two retailers agreed that economies of scale were useful, but did not give a set critical mass (one suggested that different business models and outsourcing could reduce the size needed to gain benefits of scale). Retailers pointed to a number of benefits of scale including: an improved ability to negotiate with third party suppliers, ability to comply with energy efficiency schemes, to provide a reasonable platform and due to the greater focus on retention that larger retailers tend to take.

Generally, retailers did not perceive difficulty in achieving critical mass in the electricity sector, but were more cautious about the ease with which critical mass could be achieved in gas retailing.

Economies of scale

Retailers were asked whether economies of scale (if important) need to be achieved through South Australia alone or whether they can be achieved through operating in other Australian states or through contracting out.

Views were mixed on whether a retailer expanding to a larger scale would encounter issues of investment scale. Some retailers maintained that the models adopted by new entrants were feasible only for relatively small scale operations; others took the view that recent entrants were advantaged by not having legacy systems that were difficult and costly to change.

We have grouped responses in terms of achieving economies of scale under four headings – economies of scale must be achieved in South Australia alone; economies of scale can also be achieved through operating in other States; economies of scale can be achieved through operating in other jurisdictions or contracting out; and mixed views on where economies of scale must be achieved.

Economies of scale must be achieved in South Australia alone

One retailer explained that due to the divergent requirements on retailers imposed by different Australian states, a retailer will need to maintain a large customer base in

South Australia in order to enjoy the benefits of scale. This suggests that customer numbers in other States become irrelevant when assessing the ability of retailers to enter into the South Australian market or expand within it.

> *Whilst there is a continued jurisdiction divergence around the regulatory framework, compliance obligations and energy efficiency schemes these economies of scale will be jurisdictionally based.*

Economies of scale can be achieved through operating in other States

Two retailers believe that economies of scale can be achieved by operating in other states. One noted that while there are regulatory differences between states they can be handled (refer to the quote below), while the other did not provide an explanation.

> *A consolidated approach is feasible in that customer base aggregated from all jurisdictions can deliver economies of scale (and scope). There are uniqueness in regulatory requirements in SA that can be dealt to without requiring infrastructure and process co-location.*

Economies of scale can be achieved through operating in other States or contracting out

Two retailers stated that economies of scale can be achieved through operating in other States or contracting out. This suggests that if retailers are not spread across States, they can still enjoy the benefits of economies by contracting out part of their functions (such as call centre support).

> *Economies of scale can be achieved both through operating in other jurisdictions, and/or contracting out services.*

> *Contracting out various activities to reduce cost to serve as well as building on economies of scale by operating in multiple jurisdictions. Please note that these jurisdictions need to operate on the same regulatory framework to allow for a streamlining of processes and systems.*

Mixed views on whether economies of scale can be achieved through South Australia alone or through operating in other States

Three retailers stated that economies of scale can be achieved through operation in other States, but two cautioned that the benefits are diminished when regulatory differences are too great; and one noted that some activity will still need to be state focused.

> *Operational economies of scale such as call centre requirements etc can be achieved by a presence in multiple states to a certain degree. Differences in regulations between states however diminish these efficiency gains. Economies of scale that lead to better hedging arrangements in South Australia due to large and diverse customer base etc can only be achieved in South Australia.*

Depends on the retail model involved and which cost factors are being considered…. Many retail functions such as billing and customer management systems and general retail processes such as marketing, call centres and customer management can be averaged across the national customer base. However …there is a very tight limit to the amount to which under-recovered costs in one state can be effectively "subsidised" by operations in other states… In addition, some retail cost elements, such as product development for South Australia, will be specific to the jurisdiction because of the specific regulations involved… Moreover, energy purchase costs are calculated on a state specific basis, due to differences in NSLP demand profiles, market settlements, intraregional connectivity and specific regional wholesale risks.

Some costs can be shared across businesses in other States; however differences in regulations have potential to reduce inter-State synergies.

Changes over time

Ten retailers stated that conditions for entry and expansion have changed over time. Two stated that they have not (e.g. "remained buoyant").

Improvements described by retailers included the development of different retail operating models (such as outsourcing back office functions) which has allowed smaller retailers to compete.

Worsening of conditions described centre around wholesale prices and access to supply. Retailers commented that high wholesale prices and poor access to supply (through lack of generation, and the number of vertically integrated retailers) has made it difficult to offer prices that compete with the standing offer and thereby attract customers, due to increased supply costs which aren't reflected in the regulated price. The power of the host retailers was raised, as well as poor market liquidity.

Other worsening of conditions discussed by retailers included greater regulatory requirements, particularly uncertain requirements or those that diverge from other jurisdictions. Risks due to the uncertainty of new environmental schemes and how costs will be reflected in regulated rates, was associated with this. One retailer was also concerned about increased compliance reporting requirements, "demanding and unrealistic deadlines are set".

Internal measures of competitive threat

All electricity retailers report that the monitor competitive threat. Retailers reported that they monitor and include in internal management reports the measures of competitive threat listed below. Factors commonly considered include other retailers' advertising/marketing, customer gains and losses, market share, offers, and regulatory changes. Most retailers report that they monitor at least three aspects of competitive threat.

Where competitors are marketing, what they are offering, the level of their media spend, and customer perception.

Competitor advertising, pricing promotions.

Market Share, Customer Gains & Losses, Anecdotal Competitor Activity Reports, TARPS, Competitor Advertising Content.

…customer transfers, both its own and it's competitors; other retailers wholesale portfolio; energy products being offered by other retailers; and any increase in marketing activity. Take-up of [retailer] products is also monitored closely to determine what is being valued by customers and appropriate action is then taken.

Competitor offers, market share and forecast of wholesale position.

…CI Program.

Reports that analyse losses and competitor activity. Also review market developments and regulatory changes.

Churn results (i.e. % monthly customer transfers); Other retailers' offers in the marketplace; Door to door activity.

Competitor activity (Pricings and offerings); Regulatory uncertainty or changes (Price reviews, introduction of new schemes that require retailer administration); Political environment.

Churn indicators primarily.

One retailer (who is currently not actively marketing) stated that this question was not applicable. One retailer did not respond to this question. While retailers were willing to discuss internal monitoring of competitors in general terms, retailers were generally not willing to discuss specifics or share with us examples of their internal monitoring documents.

7.4.2 Gas

Structural features

All retailers who responded to the survey stated that access to gas supply and access to capital are important or very important to enable entry or to be a competitive player in the South Australian market. Other features considered to be important by many retailers include operation in another jurisdiction and size of customer base. Views diverged on the importance of vertical integration and position as host retailer.

Table 42: Importance of structural features for retailers to be competitive

Factors impacting on competitiveness	Not considered	Considered	Moderately important	Important	Very important
Vertical integration with gas supply	●	●●		●●	●●
Access to gas supply				●●	●●●●●
Vertical integration with energy distribution	●●●●		●●	●	
Position as host retailer	●●	●●		●	●

Factors impacting on competitiveness	Not considered	Considered	Moderately important	Important	Very important
Size of customer base in South Australia (local economies of scale)		•	••	••••	
Operation in another Australian jurisdiction		••	•	••	••
Size of customer base in other parts of Australia (national economies of scale)		•••		••	••
Access to capital				••••	•••

Factors affecting entry into South Australia

The table below summarises gas retailers views on whether a set of structural factors facilitate entry, hinder entry or have no impact. Major deterrents for four out of seven retailers include access to energy supply at reasonable cost, access to risk mitigation products and access to adequate transmission and distribution services. Five retailers viewed regulatory uncertainty, regulatory differences between jurisdictions, and extent of state consumer protection as a hindrance or major hindrance to entry. Customer inertia appears not to be an issue in South Australia, with six retailers citing it as having no impact. Factors considered being some incentive or a major incentive to enter by three retailers include market share of host retailer, and current levels of competition. The responses to this survey question appear to depend largely on the position of the retailer.

Table 43: Factors facilitating or hindering entry within the South Australia gas market

Factors impacting on competitiveness	Major deterrent to entry	A hindrance to entry	No impact	Some incentive to enter	Major incentive to enter
Retail market structure					
Small number of retailers currently supplying customers			••••	•	•
The distribution of market shares between retailers			••••	••	
The market share of the host retailer		•	••	••	•
The scope of services offered by competitors		•	•••	•	•
Current levels of competition between retailers		•	••	•••	
Wholesale market and infrastructure					
Access to energy supply at reasonable cost	••••		•	••	
Access to risk mitigation products	••••		•	••	

Factors impacting on competitiveness	**Major deterrent to entry**	**A hindrance to entry**	**No impact**	**Some incentive to enter**	**Major incentive to enter**
Access to adequate transmission and distribution services	••••	•	•	•	
Regulatory framework					
Extent of state consumer protection and other regulation		•••••	•		
Regulatory differences between jurisdictions	•	••••	•		
Regulatory uncertainty	•••	••	•		
Standing offer price legislation	•	•••	••		
Marketing					
Brand awareness		•	•••	••	
Brand loyalty to other retailers		••	••••		
Customer inertia			••••• •		
Customer engagement with energy products		••	•••	•	
Access to sufficient customer data to make offers		•	••••	•	
Customer transfer process					
Customer fears or concerns regarding the process of switching to another retailer		••	••••		
Time delays before transfer implemented		••••	••		
Exit or termination fees for some customer contracts		••	••••		
Investment requirements					
Marketing		•	••••		•
Call centre		•	••••		•
Billing system		••	•••		•

Other factors impacting on entry into the South Australia gas market include set up costs, and dealing with complex rules that may be different from other jurisdictions:

- Initial set up costs to establish a gas business associated with contracting gas supply and transport, installing retail systems and setting prices to comply with strict South Australian service level agreements (although outsourcing some back office functions can assist).

- Lack of assistance from the market operator.

- Complex rules.
- Penal balancing arrangements.
- Need to source gas and transport capacity favours vertically integrated retailers and doesn't support incremental growth.
- Jurisdictional differences and complexity.
- Uncertain national greenhouse gas mitigation schemes.

Factors affecting expansion within South Australia

Gas retailers gave similar views on factors facilitating and hindering expansion. Brand awareness became more important as an incentive to expand.

Table 44: Factors facilitating or hindering expansion within the South Australia gas market

Factors impacting on competitiveness	Major deterrent to expansion	A hindrance to expansion	No impact	Some incentive to expand	Major incentive to expand
Retail market structure					
Small number of retailers currently supplying customers			••••	•	
The distribution of market shares between retailers			••••	••	
The market share of the host retailer			••••	•	•
The scope of services offered by competitors			••••	•	•
Current levels of competition between retailers			•••	•••	
Wholesale market and infrastructure					
Access to energy supply at reasonable cost	•••	•	•	••	
Access to risk mitigation products	•••	•	•	••	
Access to adequate transmission and distribution services	•••	••		••	
Regulatory framework					
Extent of state consumer protection and other regulation		••••	••		
Regulatory differences between jurisdictions	•	•••	••		
Regulatory uncertainty	••	•••	•		

Factors impacting on competitiveness	Major deterrent to expansion	A hindrance to expansion	No impact	Some incentive to expand	Major incentive to expand
Standing offer price legislation	•	•••	••		
Marketing					
Brand awareness		•	•	•••	
Brand loyalty to other retailers		••	••••		
Customer inertia			••••• •		
Customer engagement with energy products		•	••••	•	
Access to sufficient customer data to make offers			••••	••	
Customer transfer process					
Customer fears or concerns regarding the process of switching to another retailer		••	••••		
Time delays before transfer implemented		••••	••		
Exit or termination fees for some customer contracts		••	••••		
Investment requirements					
Marketing		•	•••	••	
Call centre			••••	••	
Billing system		•	•••	••	

Other factors affecting the ability of South Australia retailers to expand include:

- REMCo costs and extent of services.
- Price regulation capping prices.
- Jurisdictional differences and complexity.
- Uncertain greenhouse gas mitigation regimes.
- Difficulty winning customers with the high level of competitive activity and customer churn.

Critical mass

Three gas retailers believe that a critical mass of customer numbers or volume of gas is required in order to be a viable competitor in South Australia. Two do not. One believes that economies of scale are important, but there is not one set critical mass. This retailer stated that this depends on the business model selected; some retailers may depend on a certain number of petajoules of gas based on their supply and transport contracts; while others may require a certain number of customers.

Two retailers gave estimates of required critical mass – over 20,000 customers according to one retailer, between 5,000 and 10,000 active customers for another.

Two gas retailers explained why they argued that a critical mass is required. One retailer who believes that a critical mass is required explained that a larger customer base provides economies of scale, in part because it is cheaper to retain customers than sign new customers, and larger retailers may have a stronger focus on retention. Another retailer emphasised that critical mass *"provides a reasonable revenue platform from which to move forward, additionally this base provides a greater ability in the negotiation of service provision from third party suppliers"*.

Economies of scale

One retailer argued that economies of scale are only useful within South Australia due to jurisdictional differences in regulation. One stated that they can be achieved in other jurisdictions. Three gave a mixed response, some aspects (such as hedging and product development) can only occur in South Australia, while others such as back office functions can occur in other states (with the rider that regulatory differences are eroding the efficiencies). One mixed response stated that economies of scale can be exercised either in other states or through contracting out.

Changes over time

Five retailers stated that conditions for entry and expansion have changed over time. One stated that conditions have not changed. One gave a mixed response – noting that the same hurdles exist now as they did three years ago, but noted that the "access to market information and assistance with interpreting rules [is] worse".

Improvements to the conditions described above include:

- Competitive viability has improved due to removal of physical infrastructure restraints and improved upstream competition and access to diversified sources of gas.
- Development of various operating models (such as outsourcing).
- Access arrangements have improved (although commercial impediments remain to access gas and pipeline capacity contracts).
- Retail tariffs have been regulated to a realistic level.

Worsening of conditions described includes:

- Wholesale access and pricing regime.

- Increasing supply costs not reflected in regulated prices.

Internal measures of competitive threat

Five gas retailers responded that they use identical measures of competitive threat for the gas market as they do for the electricity market. These retailers focus on what their competitors are marketing, customer transfers, customer response, and in some instances market share and the regulatory environment.

> *Where competitors are marketing, what they are offering, the level of their media spend, and customer perception.*
>
> *Market Share, Customer Gains & Losses, Anecdotal Competitor Activity Reports, TARPS, Competitor Advertising Content.*
>
> *…customer transfers, both its own and it's competitors; other retailers wholesale portfolio; energy products being offered by other retailers; and any increase in marketing activity. Take-up of [retailer] products is also monitored closely to determine what is being valued by customers and appropriate action is then taken.*
>
> *Churn results (i.e. % monthly customer transfers); other retailers' offers in the marketplace; Door to door activity.*
>
> *Competitor activity (Pricings and offerings); Regulatory uncertainty or changes (Price reviews, introduction of new schemes that require retailer administration); Political environment.*

One retailer measures *"competing offers, wholesale and network costs and portfolio review"* for the gas market.

Appendix 1: Retailers invited to participate

The following retailers were invited to participate in this review.

1. AGL
2. Aurora Energy
3. Australian Power & Gas
4. Country Energy
5. Dodo Power & Gas
6. EnergyAustralia
7. Jackgreen
8. Momentum Energy
9. Origin Energy
10. Powerdirect
11. Red Energy
12. Simply Energy
13. South Australia Electricity
14. TRUenergy

In addition two organisations considering entry participated in short interviews.

Appendix 2: Electricity survey

Copy of electricity survey provided to participants (with white space removed).

Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia

Survey Questionnaire for South Australian Electricity Retailers

Background

This research was commissioned by the Australian Energy Market Commission (Commission) as part of its review of the effectiveness of competition in the electricity and gas retail markets in each national electricity market jurisdiction. If the Commission finds competition to be effective, it is required to provide advice on ways to phase out retail price regulation or, if it is found not to be effective, ways to promote competition. The South Australian Review is the second such review, following the review of Victoria completed in February this year.

The Commission is asking each energy retailer operating, or preparing to operate, in South Australia to complete a survey (or two surveys if they sell electricity and sell, or are licensed to sell, gas) and then participate in a follow up interview discussion. The results of the surveys and interviews will be considered by the Commission as part of its assessment of retail competition in South Australia. The Commission has engaged LECG, an economic consulting firm with particular expertise in competition and energy markets and McGregor Tan, a market research consultancy, to assist with the surveys and interviews.

Purpose

This questionnaire is designed to obtain factual information and, in some cases, value judgments about the following from the perspective of each retailer:

- Company profile;
- Retailer rivalry;
- Customer participation and experience;
- Conditions for entry, expansion and exit.

The results of the survey will be used as a springboard for discussion and exploration of issues during the follow up interview.

Completing the survey

The Commission appreciates that completing this survey will take some time and effort on your part; however the Commission asks that you do prioritise this so that the South Australian Review can be as accurate as possible. You may need to work with others in your organisation to complete the survey.

Please complete this electricity survey if you sell electricity in South Australia, the gas survey if you sell, or are licensed to sell, gas in South Australia, and both surveys if you sell (or are licensed to sell) both types of energy.

Please complete this electricity survey with small consumers only in mind, i.e. those who use less than 160MWh per annum. Include both business and residential consumers who fall within this threshold.

Please complete the survey with your South Australian business in mind.

If possible, please use calendar years when completing questions.

If possible, please complete the survey electronically in Microsoft Word and return it by email. Alternatively, the survey can be completed on a paper copy, then scanned and emailed, or faxed.

Confidentiality

Your responses to the surveys will be treated as confidential. Your responses will form part of a report prepared by LECG to the Commission but this report will contain aggregated information so as not to identify individual retailers. This report will be published on the Commission's website.

A copy of your survey responses will be provided to McGregor Tan in order that they can lead the follow up interviews.

Returning the survey

Please return the completed survey by **Friday, 18 April 2008** to both:

Kieran Murray, Director
LECG Limited
kmurray@lecg.com
+64 4 4720596 Fax
+64 4 4720590 Phone

and

Catherine McKay, Senior Advisor
Australian Energy Market Commission
catherine.mckay@aemc.gov.au
+61 2 8296 7899 Fax
+61 2 8296 7800 Phone

If you have any queries about the survey please contact Kieran Murray. If you have any questions about the broader review, please contact Catherine McKay.

Thank you for your input.

PART ONE: COMPANY PROFILE

1. Legal name ______________________________

2. Trading name ______________________________

3. Parent company(s) ______________________________

4. Please provide a brief summary of your firm's retail history in South Australia since the introduction of full retail competition in 2003, including the date your firm entered the South Australian electricity market, and any subsequent mergers, acquisitions or divestments.

5. Do you offer electricity market contracts to customers in all regions of South Australia? Yes_____ No______

6. If you answered no to question 5, please list those South Australian regions where you **DO** offer electricity market contracts.

7. If you do not offer electricity contracts in certain regions of South Australia, we will ask you to explain why during the follow-up interviews.

PART TWO: RETAILER RIVALRY

Price rivalry

8. When you set prices for electricity market contracts how important are the following factors? If there are additional factors, please specify these and their importance.

Factors influencing prices	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Wholesale electricity costs					
Competitor's prices					
Comparison of price with standard offer					
Costs of distribution and transmission					
Target retailer margin/required return on investment					
Your market share					
Your competitors' market share					
Length of contract period					
Pricing for dual fuel customers					
Retail service standards					
Other (please specify)					

9. Do you offer your small electricity customers price structures or contract terms that vary substantially from the structure of the standard offer? Examples of different price or contract structures might include capped or guaranteed prices, or prices that track the wholesale market. If so, how important are these non-standard offers to your competitive strategy? *Please mark an X in the first column if you do offer these, and then rank their importance.*

	Offered	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Capped or fixed prices						
Prices that track wholesale costs						
Long term contracts						
Monthly rather than quarterly billing						
Bill smoothing						
Exit fees						
Other (please specify)						

Cash or in-kind incentives – obtaining new customers

10. Have you offered cash or in-kind incentives to electricity customers when they sign on? For example, free electricity for one month, a gift voucher or a magazine subscription. *Please mark X below in each of the years where you have offered incentives. Please mark N/A for any years you were not retailing electricity in South Australia.*

Obtaining	**2003**	**2004**	**2005**	**2006**	**2007**	**2008 (current)**
Incentives offered in calendar year						

11. If you have offered incentives, please outline what these were and the time period over which they were offered. Examples of some commonly offered incentives are provided.

Incentive offered	**2003**	**2004**	**2005**	**2006**	**2007**	**2008 (current)**
Magazine subscription						
Sporting tickets						
Sporting club membership						
Frequent flyer points						
Free appliance						
Cash rebate at sign-on						
Wine						
Shopper dockets or discounts						
Movie tickets						

12. How important are these incentives in your current marketing strategy to obtain customers?

Obtaining customers	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Importance of incentives					

13. Please estimate the cost of the incentives you offered in 2008 as a percentage of average monthly spend on electricity per customer (of customers in the category receiving the benefit). For example, if your customers spend an average of $100 per month and the incentive costs you $10, the percentage would be 10%. ______________%

14. Are these incentives currently offered as part of a national or South Australian initiative? ______________

Cash or in-kind incentives – retaining customers

15. Have you offered cash or in-kind incentives for electricity customers to remain with you? For example loyalty programmes such as discounts after remaining for one year. *Please mark X below in each of the years where you have offered incentives. Please mark N/A for any years you were not retailing electricity in South Australia.*

Retaining customers	**2003**	**2004**	**2005**	**2006**	**2007**	**2008 (current)**
Incentives offered in calendar year						

16. If you have offered incentives, please outline what these were and the time period over which they were offered.

17. How important are these incentives in your current marketing strategy to retain electricity customers?

Retaining customers	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Importance of incentives					

18. Please estimate the cost of the incentives you offered in 2008 as a percentage of average monthly spend on electricity per customer (of customers in the category receiving the benefit). For example, if your customers spend an average of $100 per month and the incentive costs you $10, the percentage would be 10%. ______________%

19. Are these incentives offered currently as part of a national or South Australian initiative? _______________

Branding and marketing

20. How important are the following factors to you in obtaining/retaining electricity customers?

Factors in obtaining/ retaining customers	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Reputation for low prices					
Reputation for providing in-kind benefits					
Reputation for good customer service					

Factors in obtaining/ retaining customers	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Provision of Green energy products					
Energy saving and product advice					
Offer dual fuel products					
Good corporate citizenship					
Customer has ownership interest					
Brand recognition					
Host retailer at connection site					
Other (please specify)					

21. Please place an X next to the aspects of your electricity service that you promote. For each that you mark, please list the key channels or media through which customers are made aware of this aspect e.g. TV, radio, bill inserts, internet, billboard advertising.

Aspects of service that may be promoted	**Promote**	**Key channels/media customers become aware of this**
Price		
Price customer required to pay for each kWh		
Comparison of price per KWh with other retailers		
Amount paid per payment period		
Comparison with amount charged to customer per payment period by other retailers		
Comparison with standard offer (e.g. 5% off standard offer price)		
Guaranteed price for a set period		
Non-standard pricing structures		
Early payment bonuses		
Monthly rather than quarterly billing		
Flexible payment options		
Non-price benefits		
In-kind benefits		
Service		

Aspects of service that may be promoted	Promote	Key channels/media customers become aware of this
Responsiveness of call centre		
Energy saving and product advice		
Offer dual fuel		
Other customer service aspects		
Sells electricity appliances		
Corporate citizen		
Good corporate citizen		
Ownership interest		
Customer is your shareholder		
Your business is a South Australian company		
Your business is an Australian company		
Your business is an international company		
Your business operates in multiple Australian states		
Brand recognition		
Long established retailer in South Australia		
You are the customer's existing retailer		
Established retailer in other Australian state(s)		
Other (please specify)		

22. How important are the following advertising media for obtaining electricity customers?

Importance of advertising media for general marketing	1 Not considered	2 Considered	3 Moderately important	4 Important	5 Very important
Television					
Radio					
Internet advertising					
Newspapers and other print media					
Outdoor advertising (e.g. bus shelters, billboards)					
Direct mail					
Bill inserts					

Marketing with related products (affinity retailing)					
Sponsorship					
Door knocking					
Outbound telesales					
Inbound telesales					
Other (please specify)					

23. How important are the following advertising media for retaining electricity customers?

Importance of advertising media for general marketing	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Television					
Radio					
Internet advertising					
Newspapers and other print media					
Outdoor advertising (e.g. bus shelters, billboards)					
Direct mail					
Bill inserts					
Marketing with related products (affinity retailing)					
Sponsorship					
Door knocking					
Outbound telesales					
Inbound telesales					
Other (please specify)					

Targeting customers

24. Do you actively seek electricity customers with particular characteristics (as opposed to seeking new customers generally)?

Yes_______ No______

25. If you target electricity customers based on volume of total energy consumption, please state the annual volume you target customers above.

_______MWh per annum

26. Please rate the importance to you of each of the following customer characteristics when you are making electricity market offers to small customers.

Customer characteristics	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Volume of energy consumption					
Demand profile (time of day energy used)					
Ability to pay					
Location within a given geographic area					
Likelihood of remaining on site for some time					
Desire for dual fuel					
Other (please specify)					

27. For each of the customer characteristics listed above, please mark X next to the indicators that you use to identify electricity customers within the target group and rank their importance.

Customer characteristics and indicators of these	**Indicator used**	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Volume of energy consumption						
Large number of householders						
High household income						
Large house size (square metres)						
High volume of past energy consumption						
Affluent suburb						

Customer characteristics and indicators of these	**Indicator used**	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Property appears to contain high volume appliances e.g. air-conditioning unit						
Property appears to house high energy users e.g. swimming pool, 4WD						
Demand profile						
Household includes children						
Household has residents past retirement age						
Householders are employed						
Home during the day when sales team phones/visits						
Past energy profile matches demand profile sought (e.g. non-peak consumption)						
Past usage of dual fuel						
Ability to pay						
High household income						
Residents own the house						
Householders are employed						
Credit check is clear						
Good payment history with retailer						
Location						

Customer characteristics and indicators of these	**Indicator used**	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
within a given geographic area						
Affluent suburb						
Affluent region						
Metropolitan area						
Likelihood of remaining						
Residents own the house						
Not shared by a number of adults living together (i.e. flatting)						
Householder's age						
Other (please specify)						

28. Do you decline to provide a service to electricity customers with particular characteristics, and if so what are those characteristics?

PART THREE: CUSTOMER PARTICIPATION AND EXPERIENCE

Switching behaviour

The AEMC will shortly send a data template to your Regulatory Manager requesting a range of data about the switching behaviour of your customers. This information will be used in conjunction with data obtained from NEMMCO to better understand the switching behaviour of small customers in South Australia.

Acquisition and retention costs

For the following acquisition and retention cost questions (questions 29-31) please base your responses on your electricity business only if possible. If you also retail gas and are unable to separate costs for the two, please provide total *figures for both aspects of your business, note that you have done this and give a suggested split.*

Electricity and gas combined: No_____

Yes____: if so, _____% electricity _____% gas

29. Please place an X in the box corresponding to your average acquisition cost per residential and small business customer, for those customers whom you have purchased from another retailer over the last three years:

Residential customers	**2005**	**2006**	**2007**
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Small business customers	**2005**	**2006**	**2007**
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

30. Please place an X in the box corresponding to your average acquisition cost per customer for residential and small business electricity customers that you have obtained through general sales/marketing/walk ins etc over the last three years

Please calculate these costs by adding up your total annual spend on:

- *direct marketing / advertising to new customers (e.g. 'door knocking', advertising, TV campaign costs)*
- *direct sales to new customers (e.g. sales commissions)*

- *back office costs (e.g. devising marketing campaign, deciding on incentives, procuring additional purchase options)*
- *incentives to new customers*
- *NEMMCO switching costs*

and dividing by the number of customers acquired during that year.

Residential customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Small business customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

31. Please place an X in the box corresponding to your average retention cost per customer for residential and small business customers over the last three years.

Please calculate these costs by adding up your total annual spend on:

- *direct marketing/ advertising to existing customers (e.g. printing of brochure)*
- *direct sales to existing customers (e.g. sales commissions)*
- *back office costs (e.g. devising retention campaign, deciding on incentives)*
- *additional customer service above normal levels to existing customers*
- *incentives to remain*

and dividing by the number of customers on file for that year.

Residential customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Small business customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Customer enquiries and complaints

32. Please explain how incoming calls and other communications are classified as complaints (or otherwise) within your organisation. You may wish to provide a copy of your internal policies and procedures for classifying and handling enquiries and complaints.

33. For electricity complaints received between 2005 and 2007, please list the number that were referred to the following complaint handling bodies:

Complaint handling body	2005	2006	2007
Office of Consumer and Business Affairs SA			
Other (please specify)			

34. Please explain your policies and procedures for handling electricity customers who cannot or will not pay the amount invoiced (distinguishing between residential and small business customers if possible/appropriate). You may wish to provide a copy of these policies and procedures.

PART FOUR: CONDITIONS FOR ENTRY, EXPANSION AND EXIT

Expansion plans

35. Are you actively seeking new electricity customers in South Australia?

Yes_______
No_______

36. If you have ceased or suspended actively marketing for electricity customers at any time during the past 24 months, please state the number of periods, the approximate length of time (in days), and the reasons why you ceased or suspended actively marketing for customers.

Cessation/suspension of active marketing	**Response**
Number of periods for which marketing ceased or was suspended	
Approximate period of time (in days) for which marketing ceased or was suspended	
Reasons for ceasing or suspending marketing	

37. What changes to your electricity business model are you considering? *Please mark an X under the columns as appropriate. If a factor is already in place (for instance, you are already vertically integrated), please mark that column.*

Factors impacting on business model	**Factor already in place**	**Definite plans**	**May consider in future**
Launching an electricity retail business in South Australia			
Vertically integrating with electricity generation			
Vertically integrating with energy network business			
Offering dual fuel			
Standardising retail systems nationally (to the extent that this is possible)			

Other (please specify)			

38. What expansion or contraction in electricity retailing are you considering? *Please mark an X under the columns as appropriate. If a factor is already in place (for instance, you already operate in another jurisdiction), please mark that column.*

Factors impacting on expansion	**Factor already in place**	**Definite plans**	**May consider in future**
Acquiring the customer base of another SA retailer			
Commencing retail in another state			
Acquiring the customer base of another state's retailer			
Exiting the SA market			
Selling your existing customer base			
Other (please specify)			

Opportunities for entry and expansion

Where the answers to any of the following questions about opportunities for entry and expansion (questions 39-42) is yes, the survey asks you to explain why. You may wish to provide brief explanations as additional information about these issues will be sought during the confidential follow-up interviews.

39. If you considering entering the South Australian retail electricity market or are working to expand your existing market share, are you comfortable that you can source the energy supply required? Please answer yes/no and briefly explain why. Yes_______ No_______

40. If you considering entering the South Australian retail electricity market or are working to expand your existing market share, are you comfortable that you can put in place effective methods for managing price and volume risk? Please answer yes/no and briefly explain why. Yes_______ No_______

41. If you considering entering the South Australian retail electricity market or are working to expand your existing market share, are you comfortable that you can access the network infrastructure required? Please answer yes/no and briefly explain why. Yes_______ No_______

42. If you considering entering the South Australian retail electricity market or are working to expand your existing market share, are you comfortable that you can switch customers in a timely and efficient manner? Please answer yes/no and briefly explain why. Yes_______ No_______

Regulatory barriers to entry and expansion

Where the answer to any of the following questions about regulatory barriers to entry and expansion (44-46) is yes, the survey asks you to explain. You may wish to provide brief explanations as additional information about these issues will be sought during the confidential follow-up interviews.

43. Please rate the extent to which the existence of electricity standing offers limits your business' ability to do each of the following:

How existence of standing offers may limit ability to alter business	**1** Not at all limiting	**2** A consideration	**3** Moderate limitation	**4** Limiting	**5** Very limiting
Launch an electricity retailing business in South Australia					
Introduce a greater range of innovative products					
Offer more innovative pricing structures					
Offer prices that reflect the efficient costs to service					
Maintain a competitive profit margin					
Target low volume consumers					
Other (please specify)					

44. Are policies to address climate change and rising fuel prices likely to affect entry and competitive conditions for electricity? If so, please explain how these issues will impact on competition.

45. Are there any other regulatory barriers in place which limit your ability to enter the South Australian retail electricity market (if applicable) or to compete for electricity customers? If so, please explain what they are, whether they are as a result of federal or state regulation, and why they are a barrier to competition.

46. In your view, are there any changes that could be made to the government policy framework that would allow you to enter the South Australian retail electricity market or to compete more effectively within it? If so, please explain what changes you would like to see and why.

Impact of structure of electricity market on entry and expansion

Where the answer to any of the following questions about the impacts that the electricity market structure has on entry and expansion (49 and 51-55) is yes, the survey asks you to explain. You may wish to provide brief explanations as additional information about these issues will be sought during the confidential follow-up interviews.

47. How important are the following structural features for you to be a competitive retailer in the South Australian electricity market?

Factors impacting on competitiveness	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Vertical integration with energy supply					
Access to generation					
Vertical integration with energy distribution					
Position as a host retailer					
Size of customer base in South Australia (local economies of scale)					
Operation in another Australian jurisdiction					
Size of customer base in other parts of Australia (national economies of scale)					
Access to capital					
Other (please specify)					

48. Please rate how important the following factors are in facilitating or hindering entry into the South Australian electricity market at the present time. If you have not yet entered the market, please rate how important these factors are in facilitating or hindering your entry.

Factors impacting on competitiveness	**1** Major deterrent to entry	**2** A hindrance to entry	**3** No impact	**4** Some incentive to enter	**5** Major incentive to enter
Retail market structure					
Large number of retailers					

Factors impacting on competitiveness	**1** Major deterrent to entry	**2** A hindrance to entry	**3** No impact	**4** Some incentive to enter	**5** Major incentive to enter
currently supplying customers					
The distribution of market shares between retailers					
The market share of the host retailer					
The scope of services offered by competitors					
Current levels of competition between retailers					
Wholesale market and infrastructure					
Access to energy supply at reasonable cost					
Access to risk mitigation products					
Access to adequate transmission and distribution services					
Regulatory framework					
Extent of state consumer protection and other regulation					
Regulatory differences between jurisdictions					
Regulatory uncertainty					
Standing offer price legislation					
Marketing					
Brand awareness					
Brand loyalty to other retailers					
Customer inertia					
Customer engagement with energy products					
Access to sufficient customer data to make offers					
Customer transfer process					
Customer fears or concerns regarding the process of switching to another retailer					
Time delays before transfer implemented					
Exit or termination fees for					

Factors impacting on competitiveness	1 Major deterrent to entry	2 A hindrance to entry	3 No impact	4 Some incentive to enter	5 Major incentive to enter
some customer contracts					
Investment requirements					
Marketing					
Call centre					
Billing system					
Other (please specify)					

49. Are there any other factors not listed above which in your view facilitate or hinder entry into the South Australian electricity market? If so, please list and explain.

50. Please rate how important the following factors are in facilitating or hindering your expansion within the South Australian electricity market at the present time. If you have not yet entered the market, please rate how important these factors are likely to be in facilitating or hindering your expansion.

Factors impacting on competitiveness	1 Major deterrent to expansion	2 A hindrance to expansion	3 No impact	4 Some incentive to expand	5 Major incentive to expand
Retail market structure					
Large number of retailers currently supplying customers					
The distribution of market shares between retailers					
The market share of the host retailer					
The scope of services offered by competitors					
Current levels of competition between retailers					
Wholesale market and infrastructure					
Access to energy supply at reasonable cost					
Access to risk mitigation products					
Access to adequate transmission and distribution services					
Regulatory framework					
Extent of state consumer protection and other					

Factors impacting on competitiveness	**1** Major deterrent to expansion	**2** A hindrance to expansion	**3** No impact	**4** Some incentive to expand	**5** Major incentive to expand
regulation					
Regulatory differences between jurisdictions					
Regulatory uncertainty					
Standing offer price legislation					
Marketing					
Brand awareness					
Brand loyalty to other retailers					
Customer inertia					
Customer engagement with energy products					
Access to sufficient customer data to make offers					
Customer transfer process					
Customer fears or concerns regarding the process of switching to another retailer					
Time delays before transfer implemented					
Exit or termination fees for some customer contracts					
Investment requirements					
Marketing					
Call centre					
Billing system					
Other (please specify)					

51. Are there any other factors not listed above which in your view facilitate or hinder expansion (including by you) within the South Australian electricity market? If so, please list and explain.

52. Is there a critical mass required in terms of customer numbers or volume of electricity required in order to be a viable competitor in the South Australian electricity market? If so, please state what you believe the threshold to be and why.

53. If economies of scale are important, do these need to be achieved in South Australia alone or can they be achieved through operating in other Australian States or through contracting out various activities? Please explain.

54. Have the conditions for entry and expansion in the South Australian electricity market changed over time? Describe any improvements or worsening of conditions.

55. What measures of competitive threat, if any, do you monitor and include in internal management reports?

56. If there is something in particular you would like to discuss during the follow up interview, please note below.

Thank you for completing this survey. The Commission and LECG look forward to discussing the results of the survey with you during an interview.

Declaration

I, ……………………………………………….., the Managing Director / Chief Executive Officer of…………………………………… (name of Retailer), declare that the responses to this survey are an accurate reflection of the views held by ……………………… (name of Retailer).

Appendix 3: Gas survey

Copy of gas survey provided to participants (with white space removed).

Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia

Survey Questionnaire for South Australian Gas Retailers

Background

This research was commissioned by the Australian Energy Market Commission (Commission) as part of its review of the effectiveness of competition in the electricity and gas retail markets in each national electricity market jurisdiction. If the Commission finds competition to be effective, it is required to provide advice on ways to phase out retail price regulation or, if it is found not to be effective, ways to promote competition. The South Australian Review is the second such review, following the review of Victoria completed in February this year.

The Commission is asking each energy retailer operating, or preparing to operate, in South Australia to complete a survey (or two surveys if they sell electricity and sell, or are licensed to sell, gas) and then participate in a follow up interview discussion. The results of the surveys and interviews will be considered by the Commission as part of its assessment of retail competition in South Australia. The Commission has engaged LECG, an economic consulting firm with particular expertise in competition and energy markets and McGregor Tan, a market research consultancy, to assist with the surveys and interviews.

Purpose

This questionnaire is designed to obtain factual information and, in some cases, value judgments about the following from the perspective of each retailer:

- Company profile;
- Retailer rivalry;
- Customer participation and experience;
- Conditions for entry, expansion and exit.

The results of the survey will be used as a springboard for discussion and exploration of issues during the follow up interview.

Completing the survey

The Commission appreciates that completing this survey will take some time and effort on your part; however the Commission asks that you do prioritise this so that the South Australian Review can be as accurate as possible. You may need to work with others in your organisation to complete the survey.

Please complete this gas survey if you sell, or are licensed to sell, gas in South Australia, the electricity survey if you sell electricity in South Australia, and both if you sell (or are licensed to sell) both types of energy.

Please complete this gas survey with small consumers only in mind, i.e. those who use less than 1TJ of gas per annum. Include both business and residential consumers who fall within this threshold.

Please complete the survey with your South Australian business in mind.

If possible, please use calendar years when completing questions.

If possible, please complete the survey electronically in Microsoft Word and return it by email. Alternatively, the survey can be completed on a paper copy, then scanned and emailed, or faxed.

Confidentiality

Your responses to the surveys will be treated as confidential. Your responses will form part of a report prepared by LECG to the Commission but this report will contain aggregated information so as not to identify individual retailers. This report will be published on the Commission's website.

A copy of your survey responses will be provided to McGregor Tan in order that they can lead the follow up interviews.

Returning the survey

Please return the completed survey by **Friday, 18 April 2008** to both:

Kieran Murray, Director
LECG Limited
kmurray@lecg.com
+64 4 4720596 Fax
+64 4 4720590 Phone

and

Catherine McKay, Senior Advisor
Australian Energy Market Commission
catherine.mckay@aemc.gov.au
+61 2 8296 7899 Fax
+61 2 8296 7800 Phone

If you have any queries about the survey please contact Kieran Murray. If you have any questions about the broader review, please contact Catherine McKay.

Thank you for your input.

PART ONE: COMPANY PROFILE

1. Legal name ________________________________

2. Trading name ________________________________

3. Parent company(s) ________________________________

4. Please provide a brief summary of your firm's retail history in South Australia since the introduction of full retail competition in 2004, including the date your firm entered the South Australian gas market, and any subsequent mergers, acquisitions or divestments.

5. Do you offer gas market contracts to customers in all regions of South Australia? Yes________ No________

6. If you answered no to question 5, please list those South Australian regions where you **DO** offer gas market contracts.

7. If you do not offer gas contracts in certain regions of South Australia, we will ask you to explain why during the follow-up interviews.

PART TWO: RETAILER RIVALRY

Price rivalry

8. When you set prices for gas market contracts how important are the following factors? If there are additional factors, please specify these and their importance.

Factors influencing prices	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Wholesale gas costs					
Competitor's prices					
Comparison of price with standard offer					
Costs of distribution and transmission					
Target retailer margin/required return on investment					
Your market share					
Your competitors' market share					
Length of contract period					
Pricing for dual fuel customers					
Retail service standards					
Other (please specify)					

9. Do you offer your small gas customers price structures or contract terms that vary substantially from the structure of the standard offer? Examples of different price or contract structures may include capped or guaranteed prices, or prices that track the wholesale market. If so, how important are these non-standard offers to your competitive strategy? *Please mark an X in the first column if you do offer these, and then rank their importance.*

	Offered	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Capped or fixed prices						

	Offered	1 Not considered	2 Considered	3 Moderately important	4 Important	5 Very important
Prices that track wholesale costs						
Long term contracts						
Monthly rather than quarterly billing						
Bill smoothing						
Exit fees						
Other (please specify)						

Cash or in-kind incentives – obtaining new customers

10. Have you offered cash or in-kind incentives to gas customers when they sign on? For example, free gas for one month, a gift voucher or a magazine subscription. *Please mark X below in each of the years where you have offered incentives. Please mark N/A for any years you were not retailing gas in South Australia.*

Obtaining	**2003**	**2004**	**2005**	**2006**	**2007**	**2008 (current)**
Incentives offered in calendar year						

11. If you have offered incentives, please outline what these were and the time period over which they were offered. Examples of some commonly offered incentives are provided.

Incentive offered	**2003**	**2004**	**2005**	**2006**	**2007**	**2008 (current)**
Magazine subscription						
Sporting tickets						
Sporting club membership						
Frequent flyer points						
Free appliance						
Cash rebate at sign-on						

Incentive offered	2003	2004	2005	2006	2007	2008 (current)
Wine						
Shopper dockets or discounts						
Movie tickets						

12. How important are these incentives in your current marketing strategy to obtain gas customers?

Obtaining customers	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Importance of incentives					

13. Please estimate the cost of the incentives you offered in 2008 as a percentage of average monthly spend on gas per customer (of customers in the category receiving the benefit). For example, if your customers spend an average of $100 per month and the incentive costs you $10, the percentage would be 10%. _____________%

14. Are these incentives currently offered as part of a national or South Australian initiatives? ______________

Cash or in-kind incentives – retaining customers

15. Have you offered cash or in-kind incentives for gas customers to remain with you? For example loyalty programmes such as discounts after remaining for one year. *Please mark X below in each of the years where you have offered incentives. Please mark N/A for any years you were not retailing gas in South Australia.*

Retaining customers	2003	2004	2005	2006	2007	2008 (current)
Incentives offered in calendar year						

16. If you have offered incentives, please outline what these were and the time period over which they were offered.

17. How important are these incentives in your current marketing strategy to retain gas customers?

Retaining customers	1 Not considered	2 Considered	3 Moderately important	4 Important	5 Very important
Importance of incentives					

18. Please estimate the cost of the incentives you offered in 2008 as a percentage of average monthly spend on gas per customer (of customers in the category receiving the benefit). For example, if your customers spend an average of $100 per month and the incentive costs you $10, the percentage would be 10%. ______________%

19. Are these incentives offered currently as a result of a national or South Australian initiative? _______________

Branding and marketing

20. How important are the following factors to you in obtaining/retaining gas customers?

Factors in obtaining/retaining customers	1 Not considered	2 Considered	3 Moderately important	4 Important	5 Very important
Reputation for low prices					
Reputation for providing in-kind benefits					
Reputation for good customer service					
Reputation for gas expertise					
Provision of Green energy products					
Energy saving and product advice					
Offer dual fuel products					
Good corporate citizenship					
Customer has ownership interest					
Brand recognition					
Host retailer at connection site					
Other (please specify)					

21. Please place an X next to the aspects of your gas service that you promote. For each that you mark, please list the key channels or media through which customers become aware of this aspect e.g. TV, radio, bill inserts, internet, billboard advertising.

Aspects of service that may be promoted	**Promote**	**Key channels/media customers become aware of this**
Price		
Price customer required to pay for each GJ		
Comparison of price per GJ with other retailers		
Amount paid per payment period		
Comparison with amount charged to customer per payment period by other retailers		
Comparison with standard offer (e.g. 5% off standard offer price)		
Guaranteed price for a set period		
Non-standard pricing structures		
Early payment bonuses		
Monthly rather than quarterly billing		
Flexible payment options		
Non-price benefits		
In-kind benefits		
Service		
Responsiveness of call centre		
Energy saving and product advice		
Offer dual fuel		
Sells gas appliances		
Other customer service aspects (e.g. gas use/service expertise)		
Corporate citizen		
Good corporate citizen		
Ownership interest		
Customer is a shareholder		
Your business is a South Australian company		
Your business is an Australian company		
Your business is an international company		
Your business operates in multiple Australian states		
Brand recognition		

Aspects of service that may be promoted	Promote	Key channels/media customers become aware of this
Long established retailer in South Australia		
You are the customer's existing retailer		
Established retailer in other Australian state(s)		
Other (please specify)		

22. How important are the following advertising media for obtaining gas customers?

Importance of advertising media for general marketing	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Television					
Radio					
Internet advertising					
Newspapers and other print media					
Outdoor advertising (e.g. bus shelters, billboards)					
Direct mail					
Bill inserts					
Marketing with related products (affinity retailing)					
Sponsorship					
Door knocking					
Outbound telesales					
Inbound telesales					
Other (please specify)					

23. How important are the following advertising media for retaining gas customers?

Importance of advertising media for general marketing	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Television					
Radio					
Internet advertising					
Newspapers and other print media					
Outdoor advertising (e.g. bus shelters, billboards)					
Direct mail					
Bill inserts					
Marketing with related products (affinity retailing)					
Sponsorship					
Door knocking					
Outbound telesales					
Inbound telesales					
Other (please specify)					

Targeting customers

24. Do you actively seek gas customers with particular characteristics (as opposed to seeking new customers generally)? Yes_______ No_______

25. If you target gas customers based on volume of total energy consumption, please state the annual volume you target customers above.

_________GJ per annum

26. Please rate the importance to you of each the following customer characteristics when you are making gas market offers to small customers.

Customer characteristics	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Volume of energy consumption					
Demand profile (time of day energy used)					
Ability to pay					
Location within a given geographic area					
Likelihood of remaining on site for some time					
Desire for dual fuel					
Other (please specify)					

27. For each of the customer characteristics listed above, please mark X next to the indicators that you use to identify gas customers within the target group and rank their importance.

Customer characteristics and indicators of these	**Indicator used**	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Volume of energy consumption						
Large number of householders						
High household income						
Large house size (square metres)						
High volume of past energy consumption						
Affluent suburb						
Property appears to contain high volume appliances (e.g. gas fired pool						

Customer characteristics and indicators of these	**Indicator used**	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
heater, gas central heating)						
Property appears to house high energy users (e.g. swimming pool, 4WD)						
Demand profile						
Household includes children						
Household has residents past retirement age						
Householders are employed						
Home during the day when sales team phones/visits						
Past energy profile matches demand profile sought (e.g. non-peak consumption)						
Past usage of dual fuel						
Ability to pay						
High household income						
Residents own the house						
Householders are employed						
Credit check is clear						
Good payment history with retailer						
Location within a given geographic area						
Affluent suburb						
Affluent region						

Customer characteristics and indicators of these	**Indicator used**	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Metropolitan area						
Likelihood of remaining						
Residents own the house						
Not shared by a number of adults living together (i.e. flatting)						
Householder's age						
Other (please specify)						

28. Do you decline to provide a service to customers with particular characteristics, and if so what are those characteristics?

PART THREE: CUSTOMER PARTICIPATION AND EXPERIENCE

Switching behaviour

The AEMC will shortly send a data template to your Regulatory Manager requesting a range of data about the switching behaviour of your customers. This information will be used in conjunction with data obtained from REMCo to better understand the switching behaviour of small customers in South Australia.

Acquisition and retention costs

For the following acquisition and retention cost questions (questions 29-31) please base your responses on your gas business only if possible. If you also retail electricity and are unable to separate costs for the two, please provide total figures for both aspects of your business, note that you have done this and give a suggested split.

Gas and electricity combined: *No_____*

Yes____: if so, _____% gas _____% electricity

29. Please place an X in the box corresponding to your average acquisition cost per residential and small business gas customer, for those customers whom you have purchased from another retailer over the last three years:

Residential customers	**2005**	**2006**	**2007**
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Small business customers	**2005**	**2006**	**2007**
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

30. Please place an X in the box corresponding to your average acquisition cost per customer for residential and small business gas customers that you have obtained through general sales/marketing/walk ins etc over the last three years.

Please calculate these costs by adding up your total annual spend on:

- *direct marketing / advertising to new customers (e.g. ‘door knocking’, advertising, TV campaign costs)*
- *direct sales to new customers (e.g. sales commissions)*
- *back office costs (e.g. devising marketing campaign, deciding on incentives, procuring additional purchase options)*
- *incentives to new customers*
- *REMCo switching costs*

and dividing by the number of customers acquired during that year.

Residential customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Small business customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

31. Please place an X in the box corresponding to your average retention cost per customer for residential and small business gas customers over the last three years.

Please calculate these costs by adding up your total annual spend on:

- *direct marketing/ advertising to existing customers (e.g. printing of brochure)*
- *direct sales to existing customers (e.g. sales commissions)*
- *back office costs (e.g. devising retention campaign, deciding on incentives)*
- *additional customer service above normal levels to existing customers*
- *incentives to remain*

and dividing by the number of customers on file for that year.

Residential customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Small business customers	2005	2006	2007
$0 - $50			
$51-$100			
$101-$125			
$126-$150			
$151-$175			
$176-$200			
$201-$250			
$251-$300			
$301+			

Dual fuel

31A. Of the customers to whom you currently supply both electricity and gas, what percentage are supplied pursuant to a single market contract?

________%

Customer enquiries and complaints

32. Please explain how incoming calls and other communications are classified as complaints (or otherwise) within your organisation. You may wish to provide a copy of your internal policies and procedures for classifying and handling enquiries and complaints.

33. For gas complaints received between 2005 and 2007, please list the number that were referred to the following complaint handling bodies:

Complaint handling bodies	2005	2006	2007
Office of Consumer and Business Affairs SA			
Other (please specify)			

34. Please explain your policies and procedures for handling gas customers who cannot or will not pay the amount invoiced (distinguishing between the residential and small business customers if possible/appropriate). You may wish to provide a copy of these policies and procedures.

PART FOUR: CONDITIONS FOR ENTRY, EXPANSION AND EXIT

Expansion plans

35. Are you actively seeking new gas customers in South Australia?

Yes_______ No_______

36. If you have ceased or suspended actively marketing for gas customers at any time during the past 24 months, please state the number of periods, the approximate length of time (in days), and the reasons why you ceased or suspended actively marketing for customers.

Cessation/suspension of active marketing	Response
Number of periods for which marketing ceased or was suspended	
Approximate period of time (in days) for which marketing ceased or was suspended	
Reasons for ceasing or suspending marketing	

37. What changes to your gas business model are you considering? *Please mark an X under the columns as appropriate. If a factor is already in place (for instance, you are already vertically integrated), please mark that column.*

Factors impacting on business model	Factor already in place	Definite plans	May consider in future
Launching a gas retail business in South Australia			
Vertically integrating with energy supplier			
Vertically integrating with energy network business			
Offering dual fuel			
Standardising retail systems nationally (to the extent that this is possible)			
Other (please specify)			

38. What expansion or contraction in gas retailing are you considering? *Please mark an X under the columns as appropriate. If a factor is already in place (for instance, you already operate in another jurisdiction), please mark that column.*

Factors impacting on expansion	Factor already in place	Definite plans	May consider in future
Acquiring the customer base of another SA retailer			
Commencing retail in another state			
Acquiring the customer base of another state's retailer			
Exiting the SA market			
Selling your existing customer base			
Other (please specify)			

Opportunities for entry and expansion

Where the answers to any of the following questions about opportunities for entry and expansion (questions 39-42) is yes, the survey asks you to explain why. You may wish to provide brief explanations as additional information about these issues will be sought during the confidential follow-up interviews.

39. If you are considering entering the South Australian retail gas market or are working to expand your existing market share, are you comfortable that you can source the energy supply required? Please answer yes/no and briefly explain why. Yes_______ No_______

40. If you are considering entering the South Australian retail gas market or are working to expand your existing market share, are you comfortable that you can put in place effective methods for managing price and volume risk? Please answer yes/no and briefly explain why. Yes_______ No_______

41. If you are considering entering the South Australian retail gas market or are working to expand your existing market share, are you comfortable that you can access the network infrastructure required? Please answer yes/no and briefly explain why. Yes_______ No_______

42. If you considering entering the South Australian retail gas market or are working to expand your existing market share, are you comfortable that you can switch customers in a timely and efficient manner? Please answer yes/no and briefly explain why. Yes_______ No_______

Regulatory barriers to entry and expansion

Where the answer to any of the following questions about regulatory barriers to entry and expansion (questions 44-46) is yes, the survey asks you to explain. You may wish to provide brief explanations as additional information about these issues will be sought during the confidential follow-up interviews.

43. Please rate the extent to which the existence of gas standing offers limits your business' ability to do each of the following:

How existence of standing offers may limit ability to alter business	**1** Not at all limiting	**2** A consideration	**3** Moderate limitation	**4** Limiting	**5** Very limiting
Launch a gas retailing business in South Australia					
Introduce a greater range of innovative products					
Offer more innovative pricing structures					
Offer prices that reflect the efficient costs to service					
Maintain a competitive profit margin					
Target low volume consumers					
Other (please specify)					

44. Are policies to address climate change and rising fuel prices likely to affect entry and competitive conditions for gas? If so, please explain how these issues will impact on competition.

45. Are there any other regulatory barriers in place which limit your ability to enter the South Australian retail gas market (if applicable) or to compete for gas customers? If so, please explain what they are, whether they are as a result of federal or state regulation, and why they are a barrier to competition.

46. In your view, are there any changes that could be made to the government policy framework that would allow you to enter the South Australian retail gas market or to compete more effectively within it? If so, please explain what changes you would like to see and why.

Impact of structure of gas market on entry and expansion

Where the answer to any of the following questions about the impacts that the gas market structure has on entry and expansion (questions 49 and 51-55) is yes, the survey asks you to explain. You may wish to provide brief explanations as additional information about these issues will be sought during the confidential follow-up interviews.

47. How important are the following structural features for you to enter the South Australian retail gas market (if applicable) or to be a competitive retailer in it?

Factors impacting on competitiveness	**1** Not considered	**2** Considered	**3** Moderately important	**4** Important	**5** Very important
Vertical integration with gas supply					
Access to gas supply					
Vertical integration with energy distribution					
Position as host retailer					
Size of customer base in South Australia (local economies of scale)					
Operation in another Australian jurisdiction					
Size of customer base in other parts of Australia (national economies of scale)					
Access to capital					
Other (please specify)					

48. Please rate how important the following factors are in facilitating or hindering entry (including by you) into the South Australian gas market at the present time. If you have not yet entered the market, please rate how important these factors are in facilitating or hindering your entry.

Factors impacting on competitiveness	**1** Major deterrent to entry	**2** A hindrance to entry	**3** No impact	**4** Some incentive to enter	**5** Major incentive to enter
Retail market structure					
Small number of retailers currently supplying customers					
The distribution of market shares between retailers					
The market share of the host retailer					
The scope of services offered by competitors					
Current levels of competition between retailers					
Wholesale market and infrastructure					
Access to energy supply at reasonable cost					
Access to risk mitigation products					
Access to adequate transmission and distribution services					
Regulatory framework					
Extent of state consumer protection and other regulation					
Regulatory differences between jurisdictions					
Regulatory uncertainty					
Standing offer price legislation					
Marketing					
Brand awareness					
Brand loyalty to other retailers					
Customer inertia					
Customer engagement with energy products					
Access to sufficient customer data to make offers					
Customer transfer process					
Customer fears or concerns					

Factors impacting on competitiveness	**1** Major deterrent to entry	**2** A hindrance to entry	**3** No impact	**4** Some incentive to enter	**5** Major incentive to enter
regarding the process of switching to another retailer					
Time delays before transfer implemented					
Exit or termination fees for some customer contracts					
Investment requirements					
Marketing					
Call centre					
Billing system					
Other (please specify)					

49. Are there any other factors not listed above which in your view facilitate or hinder entry into the South Australian gas market? If so, please list and explain.

50. Please rate how important the following factors are in facilitating or hindering your expansion within the South Australian gas market at the present time. If you have not yet entered the market, please rate how important these factors are likely to be in facilitating or hindering your expansion.

Factors impacting on competitiveness	**1** Major deterrent to expansion	**2** A hindrance to expansion	**3** No impact	**4** Some incentive to expand	**5** Major incentive to expand
Retail market structure					
Small number of retailers currently supplying customers					
The distribution of market shares between retailers					
The market share of the host retailer					
The scope of services offered by competitors					
Current levels of competition between retailers					
Wholesale market and infrastructure					
Access to energy supply at reasonable cost					
Access to risk mitigation products					
Access to adequate transmission and distribution services					

Factors impacting on competitiveness	1 Major deterrent to expansion	2 A hindrance to expansion	3 No impact	4 Some incentive to expand	5 Major incentive to expand
Regulatory framework					
Extent of state consumer protection and other regulation					
Regulatory differences between jurisdictions					
Regulatory uncertainty					
Standing offer price legislation					
Marketing					
Brand awareness					
Brand loyalty to other retailers					
Customer inertia					
Customer engagement with energy products					
Access to sufficient customer data to make offers					
Customer transfer process					
Customer fears or concerns regarding the process of switching to another retailer					
Time delays before transfer implemented					
Exit or termination fees for some customer contracts					
Investment requirements					
Marketing					
Call centre					
Billing system					
Other (please specify)					

51. Are there any other factors not listed above which in your view facilitate or hinder expansion (including by you) within the South Australian gas market? If so, please list and explain.

52. Is there a critical mass required in terms of customer numbers or volume of gas required in order to be a viable competitor in the South Australian retail gas market? If so, please state what you believe the threshold to be and why.

53. If economies of scale are important, do these need to be achieved in South Australia alone or can they be achieved through operating in other Australian states or through contracting out various activities? Please explain.

54. Have the conditions for entry and expansion in the South Australian gas market changed over time? Describe any improvements or worsening of conditions.

55. What measures of competitive threat, if any, do you monitor and include in internal management reports?

56. If there is something in particular you would like to discuss during the follow up interview, please note below.

Thank you for completing this survey. We look forward to discussing the results of the survey with you during an interview.

Declaration

I, ……………………………………………….., the Managing Director / Chief Executive Officer of…………………………………… (name of Retailer), declare that the responses to this survey are an accurate reflection of the views held by ……………………… (name of Retailer).