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Australian Energy Market Commission  
PO Box A2449  
Sydney South NSW 1235

Lodged online: [www.aemc.gov.au](http://www.aemc.gov.au)

### **Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales – Issues paper**

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Australian Energy Market Commission's (AEMC) Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales – Issues paper.

The esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of 36 electricity and downstream natural gas businesses. These businesses own and operate some \$120 billion in assets, employ more than 51,000 people and contribute \$16.5 billion directly to the nation's Gross Domestic Product.

Continued retail price regulation remains a key outstanding reform area preventing a competitive retail electricity market from flourishing in NSW. As the esaa has consistently argued in its submissions to a number of reviews, retail price regulation is a barrier to competition and an obstacle to the further development of Australia's electricity markets.

The combination of fixed regulated retail prices, inherently volatile wholesale energy costs and thin margins means that retailers contemplating operating in a market under the shadow of price regulation expose themselves to the risk of error by jurisdictional regulators (an unavoidable risk given that the regulator is effectively required to predict the future pattern of wholesale energy prices and other costs) and the consequent financial and commercial implications. Importantly the risks with price regulation in a contestable market are asymmetric. While prices set too low will stifle the development of competition (this occurred in NSW during the 2007-10 Retail Price Determination), excess returns from regulated prices set too high would be eroded away by competition.

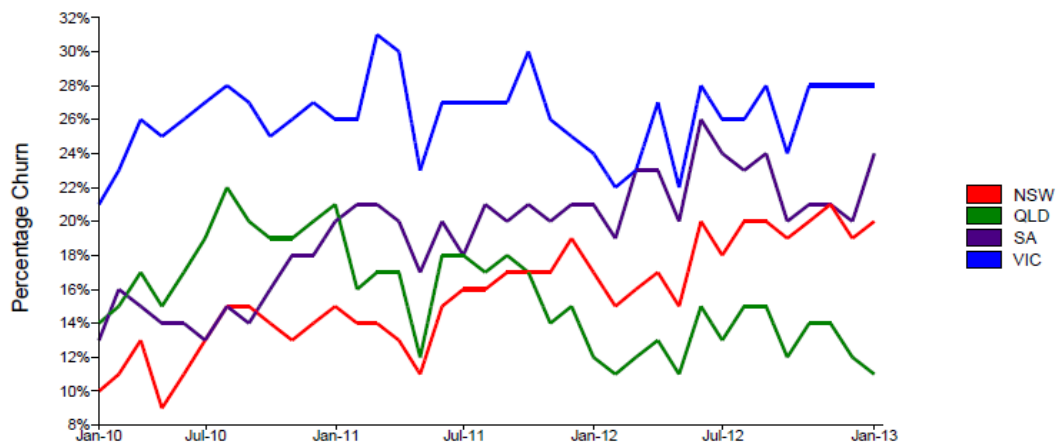
The contrast between the dynamics of market competition and administrative price setting is stark. While competitive markets naturally encourage prices to be efficient – that is, as low as is sustainably possible while businesses still make an appropriate return, retail price regulation is an inherently fallible and risk laden exercise. The value of competitive markets in setting prices in Australia will become increasingly important in the coming years as the impact of a floating carbon price materialises. Competitive markets are far more capable of processing the complex impacts of climate change policies on supply and demand than a regulator and are more likely to find the most appropriate pricing structures and encourage competition in the development of alternative products and levels of service.

When judging whether competition is present and sufficient in a retail market the esaa believes the greatest weight should be given to the ability of suppliers to enter the market. As long as the credible threat of new entry exists through low barriers to market entry, incumbent retailers will maintain their price and service offerings at cost reflective, competitive levels or risk losing market share to new entrants. In such a situation, actual entry does not need to be observed as the implied threat will act to discipline participant behaviour. As such, competitive

pricing can be observed in markets with limited participants. This observation has particular relevance to the NSW retail energy market where relatively large shares of the competitive electricity and gas markets are held by a couple of retailers. The aggressive marketing campaign by AGL in the wake of missing out in the retail privatisation process and the presence of second tier retailers demonstrates that the barriers to entry are sufficiently low to allow effective competition.

This view is supported by the increasing level of switching in the NSW retail market. Since the 2010 Retail Price Determination switching rates have risen and are now at comparable levels to South Australia (which was deemed by the South Australian government to be sufficient to allow deregulation).

**Historical Monthly Annualised Transfer Rate<sup>1</sup>**



Any questions about our submission should be addressed to Kieran Donoghue, by email to [kieran.donoghue@esaa.com.au](mailto:kieran.donoghue@esaa.com.au) or by telephone on (03) 9205 3116.

Yours sincerely

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<sup>1</sup> The graph represents the historical one month annualised transfer rate over a 3 year rolling window – Australian Energy Market Operator.