

29 November 2019

Submissions
Electricity Authority
By e-mail: submissions@ea.govt.nz

A strategic shift is required with a focus on delivery and improving retail and wholesale market outcomes for consumers

Electric Kiwi and Haast Energy Trading welcome the opportunity to submit on the Electricity Authority's 2020/21 Levy-funded appropriations. Our submission should be read in conjunction with the ecotricity, Electric Kiwi, energyclubnz, Flick Electric, Pulse Energy and Vocus joint submission.¹

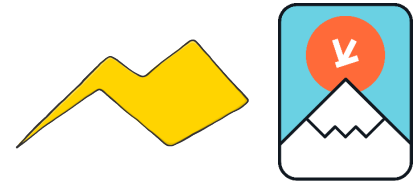
We recognise the Authority is going through a transition phase, where it is revising its strategic direction and looking at how it can do things better. We wholeheartedly support the Authority in this endeavour and look forward to engaging with the Authority as it develops its new thinking about its direction and strategy.

Our submission provides some initial thoughts on key areas we would like to see the Authority's strategy development focus on, including a stronger focus on retail and wholesale competition issues, and the types of KPIs the Authority should be setting for itself to drive success. Our thoughts substantially differ from the way the Authority currently sets its KPIs but highlight the kinds of changes needed if the Authority wants to become "a world-class electricity regulator".

Summary of Electric Kiwi and Haast's views

- We welcome the Authority's intention to undergo a new strategy development process over the next 6 months.
- It will be important not just to re-orient how the Authority's work programme and priorities are set, but also to develop a culture and capability focussed on delivery and success.
- It seems apparent there is a wide gap in perceptions about how well the Authority is performing, between stakeholders and the Authority. This seems to be partly driven by how the Authority sets and measures its performance KPIs. We would like to see a re-orientation of the KPIs to drive operational excellence and delivery.
- The majority of stakeholders would agree there is a need for a much greater focus on wholesale and retail market competition issues. Most of the EPR reforms the Government has tasked the Authority to implement are matters we, and other stakeholders with an interest in promoting a more competitive electricity market, have been urging the Authority to progress for a number of years.
- The immediate term priority must be on effective and timely delivery of the Government's EPR reforms. There is no reason why the Authority could not implement most, if not all, of the reforms prior to 2020/21. We reiterate the Authority can halt the TPM review in order to ensure the Government's EPR reforms are prioritised.
- The levy-funded appropriations consultation provides limited basis to comment on the Authority's proposed budget, absent details of the Authority's work priorities. We recognise that this, in part, reflects the transition the Authority is going through. However, the Authority proposes an additional \$2m in funding for the EPR reforms but does not provide any details of the reform work it expects to spill over into 2020/21.

¹ Ecotricity, Electric Kiwi, energyclubnz, Flick Electric, Pulse and Vocus, 2020/21 Levy-funded appropriations, 28 November 2019.



Electric Kiwi and Haast supports the Authority’s strategy reset

We welcome that the Authority has been upfront about its desire to improve its performance and organisational excellence. The Authority’s decision to undertake a strategic development review is both a timely and smart move. A focus on delivery will be a key element of the successful resetting of the Authority’s operational strategy.

We want to be fully engaged in supporting the Authority through the strategic changes it is attempting to make. We recognise the changes won’t happen over night or as a ‘big bang’ but rather as a process of incremental change and continuous improvement.

Some of the changes won’t necessarily seem that major, such as the apparent (and welcome) shift to posting submissions immediately after they are due, but are important changes from past practices.

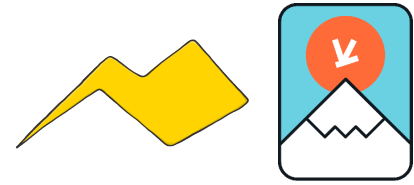
An obvious part of the reset is to consider how projects are prioritised and what being ‘high priority’ actually means in practice, but a broader, from the ground-up, reassessment is also warranted. Examples of the types of questions which merit consideration include:

- What is needed to become “a world-class electricity regulator” and what does that actually mean? What does excellence and success look like?
- How do we ensure a focus and culture of project delivery?
- How are KPIs set and what is their role in driving performance?
- How are projects managed?
- How do we ensure the Authority’s operation and decision-making is transparent? Has the Authority got its decision-making framework and criteria right? Are they well aligned with the statutory objective?
- What is the best way to engage with stakeholders and when (and how often)?
- Do stakeholders feel they are being listened to and their views are valued? What does the Authority do to demonstrate how stakeholder views impact its decisions and thinking?
- What should Advisory Groups be used for and how should they be governed?
- What lessons can be learnt from the Authority’s past performance and projects? What has worked, what hasn’t and why? What lessons can we learn from other regulators and agencies?

The Authority’s performance over the last 12 months highlights opportunities for step change improvements

We revisited our 2018 submission on the Authority’s work priorities to assess how the Authority has performed on matters important for promotion of competition.

Electric Kiwi-Haast 2018 performance expectations for the Authority
Tighter and more focussed work programme
Greater emphasis on removal of barriers to entry and growth
Address the two-tier retail market (saves and winbacks) issue/prioritise completion
Address spot market trading conduct/prioritise completion
Address hedge market development (market making)/prioritise completion
Provide firm commitments for when each project will be completed
Build stakeholder confidence legislation won’t be needed for EA EPR implementation



We consider that an objective assessment of the Authority’s performance would fall short of where the Authority would like to be, or want to be perceived, as a regulator. We would hope there would be little debate the areas highlighted above are important for the Authority’s future success.

The Authority should be concerned about the absence of mid-sized electricity retailers

In our 2018 Appropriations submission we discussed the absence of a mid-sized tier of electricity retailers. The retail market is made up of a large tier of incumbent retailers, with a second small tier of retailers (all independents, with the exception of Nova). A comparison of this graph for October 2018² and 2019³ shows little perceptible change amongst the independent retailers other than that Electric Kiwi’s market share has doubled from 1% to 2% while Pulse has gone backwards (see Figures 1 and 2).

Figure 1: Retail Market share 2018

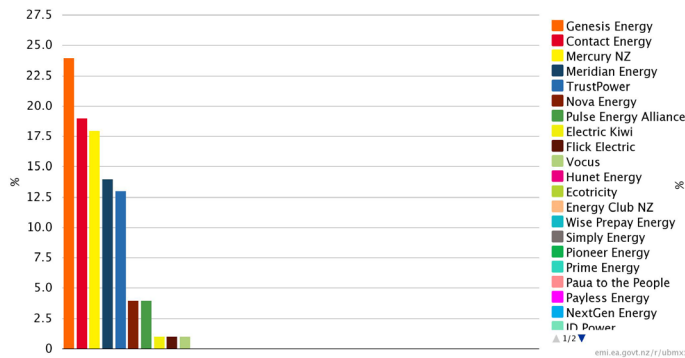
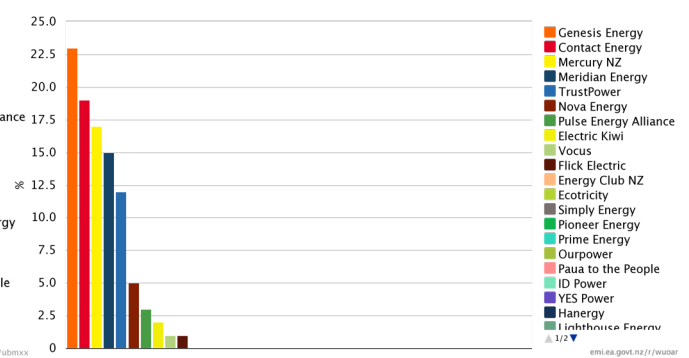


Figure 2: Retail Market share 2019



Consumer perceptions of the market are not surprising

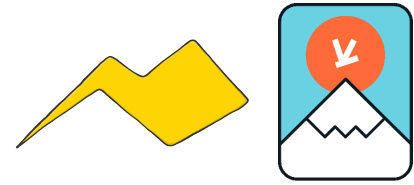
The Authority should be troubled that its consumer surveys indicate perceptions of competition worsening compared to 2017 survey results.⁴

HIGH-LEVEL RESULTS SOUGHT	HOW WE TRACK RESULTS	TARGET	RESULT
Widespread confidence among consumers in the competitiveness of electricity markets	Perception surveys: Percentage of survey respondents with an opinion on the matter who rate the electricity industry as neutral or better against the statements:	Overall improvement in survey results since Authority intervention began in 2011.	Perceptions of competition worsened in 2019 after a sustained period of improvement — see Figure 2 .
	“The current level of competition among electricity generators ensures they build the most efficient power stations and generate electricity as cheaply as possible.”		2011 result: 45% 2014 result: 51% 2017 result: 54% 2019 result: 48%
	“The current level of competition between electricity retailers ensures that prices consumers pay only rise in line with costs to the electricity companies.”		2011 result: 44% 2014 result: 45% 2017 result: 50% 2019 result: 50%

² As at 31 October 2018: https://www.emi.ea.govt.nz/Retail/Reports/R_MSS_C?Percent=Y&DateTo=20181031&_si=v|3

³ As at 31 September 2019: https://www.emi.ea.govt.nz/Retail/Reports/R_MSS_C?Percent=Y&_si=v|3

⁴ Electricity Authority, 2018/19 Annual Report, page 12.



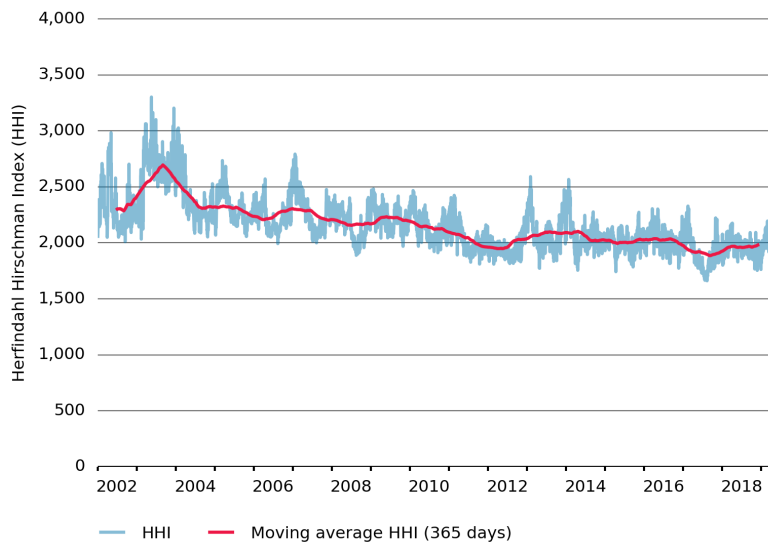
Impediments to a fully competitive market outcomes need to be removed

According to the 2018/19 Annual Report, the Authority has achieved an “overall improvement in a suite of competition statistics”.⁵ This includes the HHI index and CR4 (market share of the largest 4 retailers). Electric Kiwi and Haast consider that this presents an entirely false and misleading impression of how competition is improving and the Authority’s achievements.

Overall improvement across a suite of statistics on electricity market competition	Measures covering residential, spot, hedge and ancillary service markets. Statistics will also address entry and exit data, dynamic efficiency, and information about investment and innovation.	Overall improvement in suite of competition statistics.	Achieved. There was a continued improvement in the suite of competition statistics during 2018/19.*
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The suite of statistics the Authority has selected on electricity market competition ignore the wholesale electricity market. It is notable the Authority has not applied the HHI index and CR4 for the wholesale market as part of its electricity market measure performance. The EA has acknowledged in internal communication that “there is very little change since 2010”.⁶ The HHI and Concentration Ratios for the wholesale electricity market has changed very little since the Authority was established, and the HHI deteriorated around 2017/18 (see Figures 3, 4 and 5). The Authority should remedy this substantial gap for future monitoring of electricity market competition.

Figure 3: Wholesale electricity market HHI trend



⁵ Electricity Authority, 2018/19 Annual Report, page 12.

⁶ OIA release: 1219633 - Generation HHI_1229212_1.PDF.

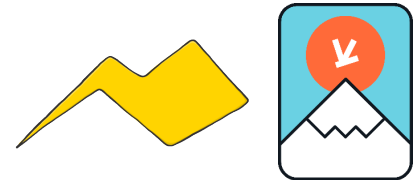


Figure 4: Wholesale electricity market CR1 trend

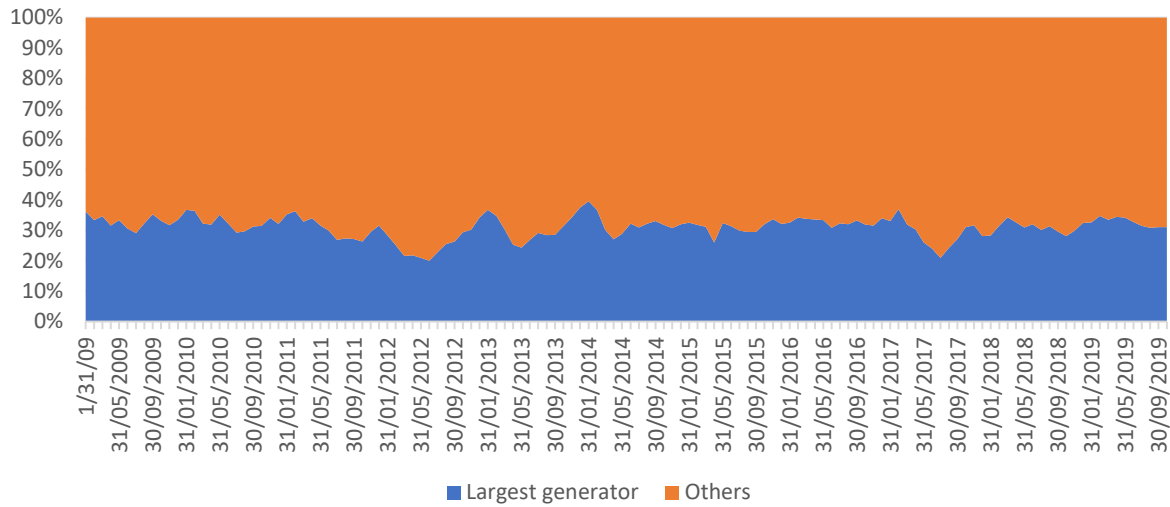
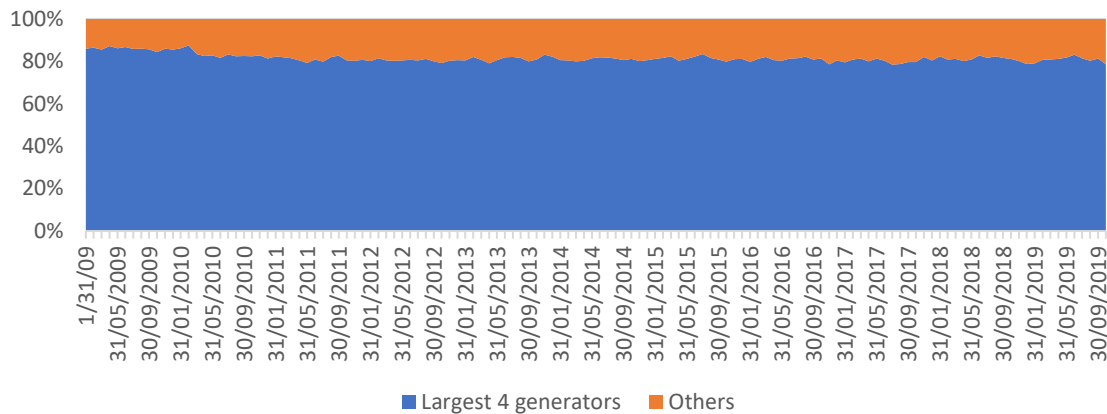
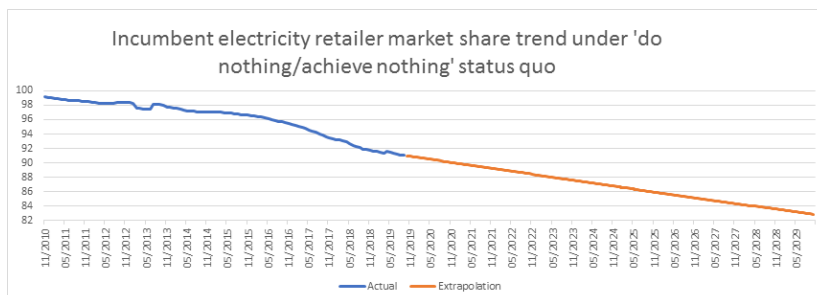


Figure 5: Wholesale electricity market CR4 trend



Market concentration statistics, for the retail market, such as HHI and CR4 can be expected to improve, unless something is seriously going wrong in the market, even without the Authority actually doing anything. This is illustrated by Figures 6 and 7 which projects out the trend in the CR1 and HHI concentration measures under the status quo if the Authority, respectively.

Figure 6: Reduction in incumbent electricity retailer market share under status quo



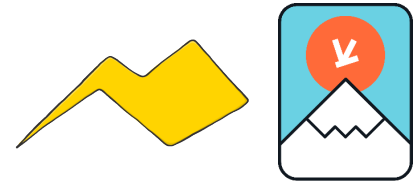
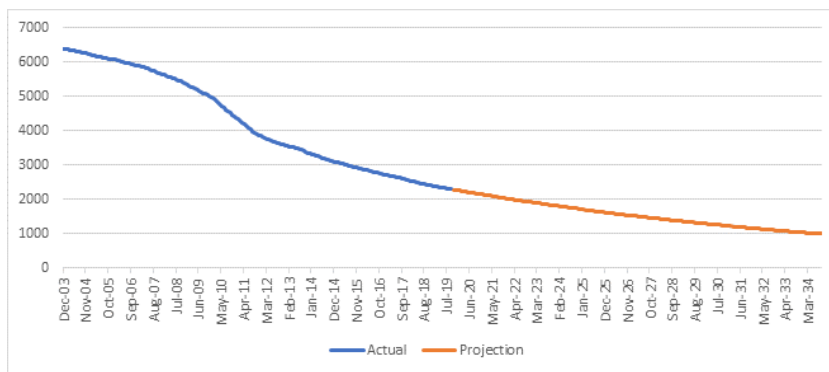


Figure 7: Reduction in HHI under status quo



Figures 8 and 9 also show the slow progress in reducing the HHI in Auckland and Tauranga network regions, respectively.

Figure 8: Reduction in HHI in the Auckland network region under status quo

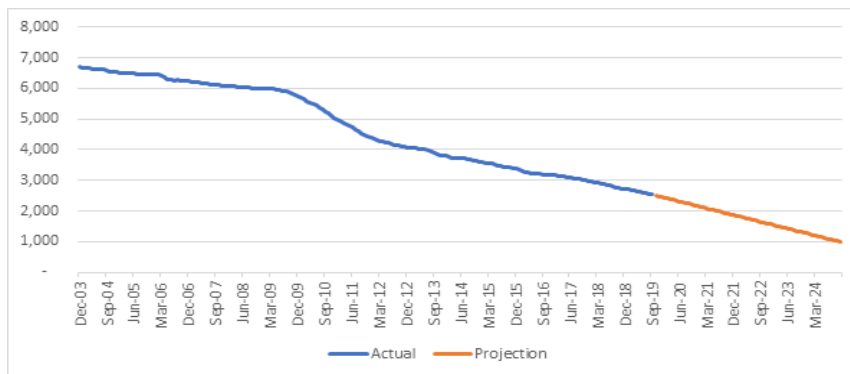
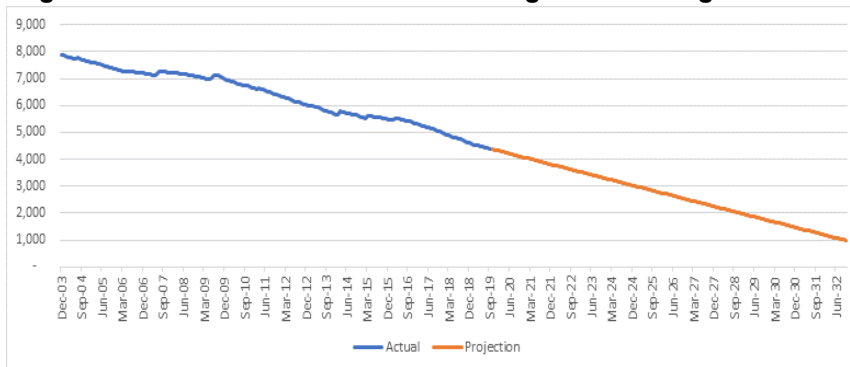


Figure 9: Reduction in HHI in the Tauranga network region under status quo



Whether or not the Authority has achieved its competition KPIs should be measured in terms of whether it accelerates the improvement in these statistics, not just on whether the statistics improve i.e. the Authority will only be successful in promoting competition if incumbent market share/market concentration declines faster than the orange lines above. For example, there was a discernible increase in the rate in which the national and Auckland HHI statistics improved which immediately slowed back down after the Authority was established. This is the type of improvement the Authority should be seeking to achieve and sustain to ensure fully competitive electricity retail and wholesale markets develop.



Targeting accelerated rates of improvement in retail and wholesale market competition would deliver better consumer outcomes, faster

We consider that the Authority should aim to ensure there are NO concentrated or highly concentrated retail markets by 2025 at the very latest. We also consider that the Authority should adopt KPIs aimed at narrowing the gap in competitiveness in different electricity retail markets by improving the outcomes in the worse performing regions (King Country, Tauranga and Central Hawke's Bay):

- On current projections, from the trend since the Authority was established, it won't be until November 2035 before Auckland incumbent retailer market share drops below 80%. In November 2019 (10 years from now) the incumbent retailer market share will still be 85%.
- The Commerce Commission uses $CR3 < 70\%$ and $CR1 < 40\%$ as tests to determine whether a market is concentrated. Based on current trajectories it won't be until 2034 before there are no concentrated retail markets in New Zealand. King Country, Tauranga, Central Hawke's Bay will all take over a decade before they are no longer concentrated, while Southern Hawke's Bay, Buller, North Canterbury, and Waitaki will take around 5 years (2024-25).
- The UK Competition and Markets Authority uses thresholds of HHI higher than 2000 for highly concentrated, between 1000 and 2000 for concentrated, and under 1000 for unconcentrated. Under these measures 100% of electricity retail markets in New Zealand are concentrated and 64.1% are highly concentrated. On current projections it will be nearly 10 years before there are no highly concentrated retail markets and over 13 years before there are no concentrated retail markets.
- There appears to be little prospect of the wholesale electricity market ever becoming unconcentrated, with little or no change in concentration measures since the Authority was established.

These trends are simply not good enough and don't reflect that the Authority is achieving its competition targets. Electric Kiwi and Haast want the electricity market to not only shift away from being heavily concentrated, but to also become fully competitive.

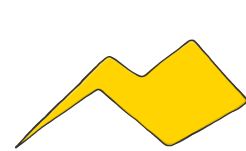
Concluding remarks – moving to operational excellence and delivery in the promotion of competition

The Authority has acknowledged "that the retail market is highly concentrated".⁷ The retail and wholesale markets are presently oligopolistic in nature, with a long-tail of small new entrants. This is illustrated by the following:

- Based on current projections, from the trend since the Authority was established, the incumbent retailers' market share in Auckland will still be over 85% in 10 years' time and won't drop below 80% until towards the end of 2035.
- Based on the Commerce Commission's market concentration tests it won't be until 2034 before there are no concentrated retail markets.
- Based on the UK Competition and Markets Authority's concentration tests it will be nearly 10 years before there are no highly concentrated markets and over 13 years before there are no concentrated markets.
- In the Authority's own words "there is very little change [in wholesale electricity market HHI] since 2010".⁸ There has also been very little movement in Concentration Ratios since the Authority was established.

⁷ Electricity Authority, Saves and Winbacks Code Amendment, 5 November 2019, paragraph 2.19.

⁸ OIA release: 1219633 - Generation HHI_1229212_1.PDF.



There can be little question that this is simply not good enough. New Zealanders deserve better and deserve a fully competitive electricity market. The Authority has substantial opportunity to improve competition and lift the performance of the retail and wholesale electricity markets. The first step should be to eliminate market concentration within the next 5-years.

We welcome the Authority' desire to "[set] a foundation so all retailers – large and small, old and new – have equal opportunity to compete for customers"⁹ and the acknowledgement of the importance of independent and "new entrant retailers [being able] to expand in size, increas[e] competitive pressure on incumbent retailers and [foster] innovation in business models, processes and product offerings".¹⁰

Our interest is in ensuring a strong and thriving competitive landscape where retailers operate on a level playing field, and aren't hindered from providing consumers, including those currently missing out on the benefits of competition, competitive prices and service.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'L. Blincoe'.

Luke Blincoe
Chief Executive, Electric Kiwi Ltd
luke.blincoe@electrickiwi.co.nz
+64 27 601 3142

A handwritten signature in black ink, appearing to be 'P. Anderson'.

Phillip Anderson
Managing Director, Haast Energy
phill@haastenergy.com
+64 21 460 040

⁹ <https://www.ea.govt.nz/about-us/media-and-publications/media-releases/2019/electricity-authority-welcomes-electricity-price-review-report-2/>

¹⁰ Electricity Authority, Saves and Winbacks Code Amendment, 5 November 2019, page ii.