

ELECTRICITY AUTHORITY REVIEW:

COMPETITION IN THE WHOLESALE ELECTRICITY MARKET

In March 2021 the Electricity Authority announced its review into competition in the wholesale electricity market. The review responds to sustained elevated electricity prices since Spring 2018 and focuses on the period from January 2019 to June 2021.

The Authority has published two papers for consultation:

- A review paper: *Market monitoring review of structure, conduct and performance in the wholesale electricity market*
- Issues and options paper: *Inefficient price discrimination in the wholesale electricity market*

Key observations from the Review

- Elevated prices do not always match underlying supply and demand conditions
- Not as many build ready investments in renewable energy as expected
- The New Zealand Aluminium Smelter (NZAS) was offered a low electricity price to encourage it to stay and this may have resulted in other consumers having to pay more.

The Authority's immediate focus is on the market settings enabling the NZAS arrangements and whether they are in the interest of all consumers.

The Tiwai contracts and inefficient price discrimination

The Authority is looking at whether the arrangements involving Contact, Meridian and NZAS encouraged NZAS to stay in New Zealand, but in doing so led to greater electricity demand, higher wholesale electricity prices, and more gas and coal generation. All generators seem to benefit from higher prices, but consumers are paying more.

The Authority is concerned that inefficient price discrimination is allowing generators to in effect subsidise NZAS by up to \$500m, resulting in higher prices for all other consumers. This could add up to \$200 to household electricity bills each year.

The current rules haven't necessarily been broken (although if the Authority does find they have we will take the appropriate action). The Authority is looking at whether the settings that allowed this to happen need changing for the long-term interests of consumers.

As a first step, the Authority is publishing an issues paper that seeks comment on its analysis of this issue and looking for feedback on potential steps we can take to prevent inefficient pricing from happening in the future.

Other observations from the Review

Addressing the potential issues the Tiwai situation raises is the first step in responding to the Review and we are consulting on all options. The wider review of wholesale market competition signals the continuation

of the Authority's focused programme of work on the wholesale market. The Authority welcomes the input from all stakeholders on the review and their views on the actions that should stem from it.

Supporting a low emissions future

Sending the right price signals is critical for an affordable and reliable electricity supply. The current and future electricity prices help investors make decisions about where and when to invest in renewable energy sources. This investment is critical to decarbonising the New Zealand economy. The Authority

considers the uncertainty of Tiwai and the gas situation have impacted on investment decisions. Much more investment in renewables is necessary to keep up with the pace of change required to move away from relying on gas and coal in the future.

Competition enables innovation and gives consumers choice

In a competitive market the wholesale electricity price largely reflects underlying supply and demand conditions. For example, how much water we have in our hydro lakes (including stored water); how much we consume; how much gas is available; and the cost of fuel including the price of carbon emissions. These factors help determine the price generators offer and in doing so, signal the cost of electricity in New Zealand at any one time.

Since 2018, there has been increasing demand; less water; decreasing gas supply and increased fuel costs. These factors have contributed in large part to the increase in spot prices however the Authority considers other factors have also contributed to elevated high prices.

What's next?

The papers and information about consultation is on our website at ea.govt.nz. Consultation ends Wednesday 8 December 2021. After considering feedback, the Authority will consult on recommendations in early 2022.

THE AUTHORITY'S ROLE

The Authority regulates the electricity industry for the long term benefit of consumers. We oversee the operation of the electricity system and markets, making and enforcing the rules participants must follow.