

From: Ralph Matthes
To: James Stevenson-Wallace; Andy Doube; Doug Watt; S9(2)(a); S9(2)(a)
Cc: John Harbord; S9(2)(a)
Subject: Wholesale market review - Questions from MEUG
Date: Friday, 29 October 2021 4:16:02 pm
Attachments: Refer to pages 2-3

Hi James, Andy, Doug, S9(2)(a) and S9(2)(a)
cc John (MEUG Chair) and S9(2)(a) (NZIER)

Attached is a memo with initial questions from MEUG.

Kind regards

Ralph

M S9(2)(a)

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29th October 2021 – not confidential

1. The 'INFORMATION' Report states (paragraphs 5.187 and 5.188), with text underlined for emphasis by MEUG:

"Concept found that forward prices have been above the cost of new electricity supply by about 50 percent, and this has been the case for longer than we would expect to see in a workably competitive market. This gap would suggest, to a casual observer, that more generation investment is signalled, at least over the term of the forward curve. It appears some investment is now happening, but because the signalled projects will not come on stream before 2023, the forward curve remains elevated."

Concept found that the divergence between forward prices and the cost of new supply exists primarily because the pipeline of build-ready projects has become very thin. In other words, while a number of projects are past the scoping (and sometimes consent) stage, they are not progressing to the final decision or commitment stage. The total quantity of definitely committed projects is 566 MW (see Table 6), which is not enough to replace existing thermal generation."

Two questions follow:

- What new initiatives are proposed in the consultation papers for further investigation or implementation that will lower prices between 2022 and 2024 to those expected in a workably competitive market compared to the status quo policy settings?
 - The final sentence of the quote above highlights the transition risks and care in setting policy settings for exiting existing thermal generation or new generation that can provide firming for wind and solar.¹ Addressing near-term gas supply issues has been highlighted by the Gas Industry Company (GIC) in their recent report on the Gas Market Settings Investigation for the Minister. Has the EA a view on the GIC recommendations?
2. In the Executive Summary of both the 'INFORMATION PAPER' and the 'DISCUSSION PAPER', the EA makes a series of observations about economic withholding including: 'Some offers do not reflect underlying conditions.', '... increased incentive and ability to economically withhold.', 'Differences in price between the North Island and South ...suggests some generators may have been economically withholding ...', 'The Lerner Index ... is sometimes high' etc.
 - Is the EA able to provide upper and bounds for the estimated effect of withholding on wholesale prices in the same way as the EA did for the Meridian/Tiwai contract?
 3. The Concept Consulting peer review (page 2) of the 'INFORMATION PAPER' quotes the EA *"However, some of the increase in prices since the Pohokura outage appears to be unexplained by the underlying conditions"* (page ii of the 'INFORMATION PAPER'). Concept comment, with text underlined by MEUG,

"We regard the regression analysis as among the most potentially informative evidence in the review because it allows diverse data to be assessed in an integrated

¹ An example of possible new thermal generation that is consented is Todd's Otorohanga gas peaker, staged units up to a total of 360 MW, with consents expiring 2027. Refer Concept Consulting report for EA, 'Review of generation investment environment.'

way. Putting aside the underlying cause of the apparent shift for now, it is striking that the analysis points to an unexplained upwards shift in average spot prices of almost \$40/MWh from late 2018 to mid-2021.

This is a material issue as \$40/MWh is around \$1.5 billion per annum. Helpfully Concept in their peer review undertook further analysis to see if they could determine drivers, though without success. Is the EA planning to continue investigation on this unexplained shift in prices of almost \$40/MWh?

4. Under Next Steps (see 'INFORMATION PAPER' page v), the EA states *'We are seeking feedback on our analysis, including the indicators used.'* However, the consultation questions released in the 'DISCUSSION PAPER' are heavily focused on the options for addressing future examples of the Meridian NZAS contract and the papers released do not include any of the quantitative data used to support the analysis presented in the 'INFORMATION PAPER'. Will the EA:
 - Release spreadsheets for the data used in the charts and equation fitting in the 'INFORMATION PAPER'?
 - Provide briefings and opportunities to ask questions about the analysis techniques used in Appendixes A to E of the 'INFORMATION PAPER'?
 - Issue a list of consultation questions that expands on the statement *'feedback on our analysis, including the indicators used.'* to a level of detail that is comparable to questions for the options?
5. Following on from the prior question, a topic of particular interest to MEUG is identifying and implementing useful metric to monitor aggregate sector economic profit trend. Can the EA publish the letter sent to the 4 largest suppliers requesting information in terms of section 46 of the Act, the data provided by suppliers to that request and other information used by Concept for the profitability analysis in the 'INFORMATION PAPER', and the analysis? The 42 questions in Appendix A of the 'DISCUSSION PAPER' do not include a request for feedback on the profitability analysis in the 'INFORMATION PAPER.' Is this consultation an opportunity for feedback on the profit analysis or should we engage separately with the EA?
6. The EA comments in the 'INFORMATION PAPER' about investment in generation include *'A reasonable number of signalled projects remain unbuilt, but only a small number of projects seem likely to proceed to the commissioning stage.'* and *'The total quantity of definitely committed investment projects is not enough to replace existing thermal generation. And at least 75 percent of this committed generation is from generator-retailers.'* These comments seem to be based largely on an interview-based analysis completed by Concept Consulting for the EA.
 - Does the EA intend to model scenarios for the potential effect of this outlook for generation investment on generator incentives and capacity for economic withholding in the short to medium term?
 - Has the EA compared the comments on the short-term outlook for generation in the Wholesale Market Review with the generation investment rules used in the TPM CBA modelling?