consumer.

5 November 2024

Electricity Authority
PO Box 10041
Wellington
By email: TaskForce@ea.govt.nz

Energy competition task force – request for level playing field measures

Thank you for the opportunity to provide our views on ways to improve the performance of the electricity market in the short to medium term.

Consumer NZ is an independent, non-profit organisation dedicated to championing and empowering consumers in Aotearoa. Consumer NZ has a reputation for being fair, impartial and providing comprehensive consumer information and advice.

New Zealand needs a fairer and more consumer-focused electricity market. We urge the Taskforce to ensure the upcoming market review prioritizes consumer outcomes over industry interests.

Firstly, we believe in the value of markets. A well-designed, well-functioning, and effectively regulated market will deliver positive outcomes for consumers by fostering innovation, providing choice, and maintaining downward pressure on prices. Unfortunately, this is not what we observe in the New Zealand electricity market.

For many years Consumer NZ has sought to raise awareness that outcomes for consumers we observe in the electricity market are inconsistent with those we would expect from a thriving competitive market.

There are several indicators that competition in the electricity sector is not delivering the expected benefits for consumers.

Market dominance of incumbent gentailers

Incumbent gentailers continue to hold a dominant share of the market. Despite, in general, offering less competitive prices and having lower customer satisfaction scores. The top

four gentailers currently maintain an 83.6% market share—nearly identical to their 83.2% share a decade ago[1].

In contrast, new entrants, often with more competitive pricing and innovative offerings, have faced significant challenges in gaining traction.

This persistent concentration suggests structural barriers that limit competition and restrict consumer access to better options.

Low switching rates despite available savings

Although households' commonly express concerns about electricity costs[2], switching rates remain notably low, with only around 7% of households changing providers over the past year, despite substantial potential savings[3].

Consumers are confused and disengaged meaning customer mobility is not the driver of competition it should be, despite ongoing efforts to encourage switching.

Retailer apathy around acquisition

We observe behaviours from retailers on the Powerswitch platform that diverge from those in other markets. Retailers, including incumbent gentailers, exhibit a surprisingly passive approach to attracting consumers looking to switch—a behaviour inconsistent with what we would expect in a competitive market where companies aggressively vie for market share.

Also, certain participants, typically smaller retailers, will on occasion withdraw from consumer acquisition efforts. This unusual market dynamic appears unique to this sector, raising questions about the effectiveness of the market in terms of stimulating and maintaining robust competition.

[1] EMI data.

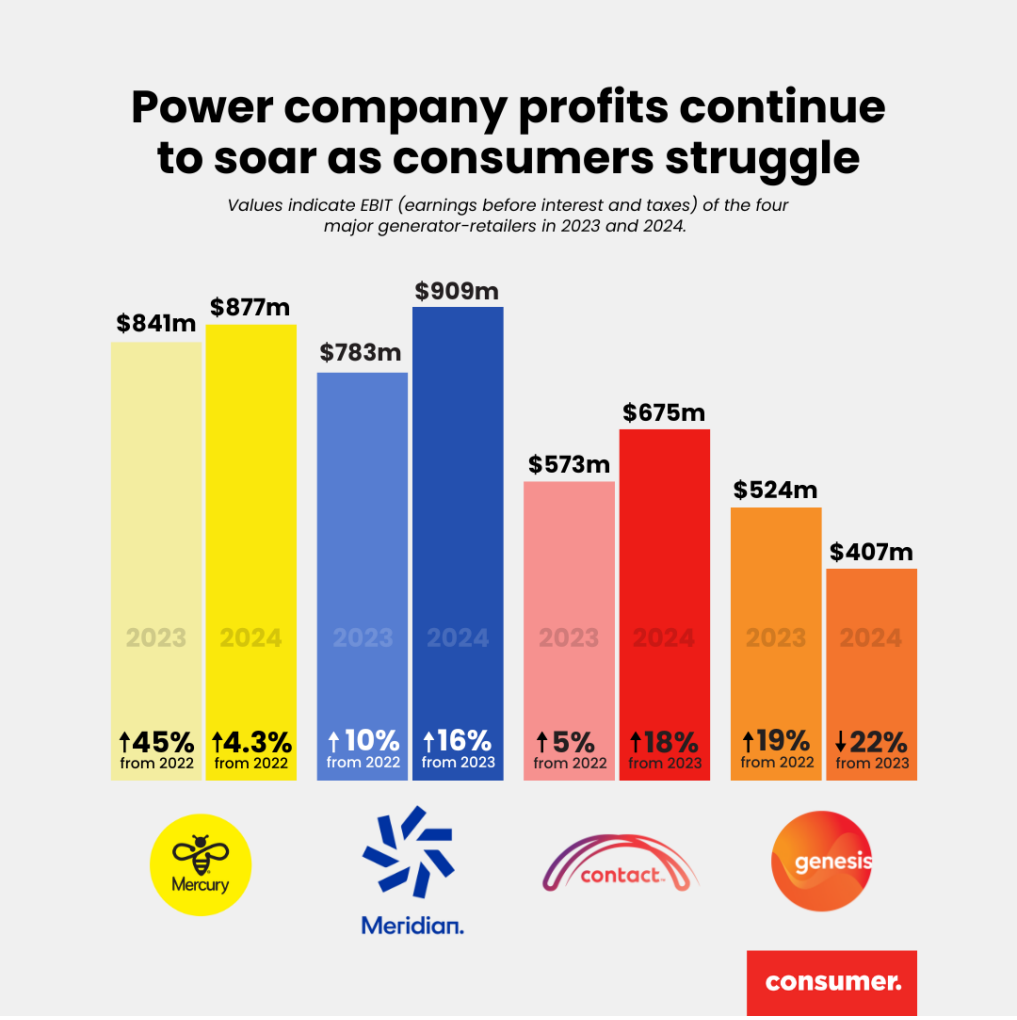
[2] In the 2024 Consumer NZ Energy survey, around 60% of consumers said they were concerned about their electricity costs and 19% of households reported they had experienced financial difficulty paying their monthly power bill in the last 12 months.

[3] The average savings on Powerswitch by changing retailer over the last 12-months was $494 per annum.

Excessive profits for incumbent gentailers[4]

In the past financial year, incumbent gentailers reported approximately $2.7 billion in operating profits, reflecting an 18% increase from the previous year—equivalent to around $7.4 million in daily profits[5]. This trend is not an isolated occurrence; gentailers have consistently achieved record profits over several consecutive years.

These sustained high profits suggest that current market conditions may be enabling excessive returns for incumbents, raising questions about the effectiveness of competition.



[4] Gentailers claim profit levels are aligned with a reasonable return on investment. However, a study by the Council of Trade Unions showed the circular process of high returns driving asset revaluations. High returns justify increasing asset valuations, which justify high returns, and so on. In the year 2000 the combined asset value of the gentailers came to around $7B. By 2022 the combined asset value was $23.7B. While new assets were created in that time, 46% of the assets value increase ($11B) was through asset revaluations.

[5] Online article, August 31 2023: https://www.stuff.co.nz/business/132841291/big-four-power-companies-earning-7-million-every-day

Insufficient investment in new generation capacity

Since 2019, forward electricty prices have been significantly above the estimated cost of new supply[6]. Yet despite persistently high prices and record profits, the anticipated investment in new generation capacity has not materialized at the levels required. Given the long-standing price signals from the market, this lack of investment, and the negative outcomes for consumers, is concerning and warrants closer examination.

One of the primary drivers for establishing the market was to stimulate non-government investment in new electricity generation. However, in the 25 years since the market's inception, New Zealand's total generation capacity has only increased by 16%[7]. This modest growth highlights a discrepancy between the market's original intent and the actual rate of capacity expansion, raising questions about whether the market structure effectively encourages the necessary level of investment in generation infrastructure.

This shortfall arises from a critical flaw: a significant lag exists between when price signals indicate the need for new generation and when new capacity can realistically be brought online. Planning, consenting, and constructing new generation facilities typically requires at least 18 months to three years—or even longer—creating a delay that hampers timely responsiveness to market signals.

But regardless of physical constraints, we believe the current market structure incentivises scarcity, rewarding gentailers who delay investment in new capacity. This dynamic suggests that the structure itself may deter timely investment – always being a little late rather than on time or early - ultimately affecting supply and creating sustained periods of elevated prices.

Prioritizing industry interests over consumer and economic outcomes

There is an old adage that "markets should be the servant, not the master." Yet often it appears that electricity consumers and the New Zealand economy is being asked to accommodate the needs of the electricity system rather than the other way around!

Persistently elevated prices are portrayed by some in the industry as an inherent feature of the New Zealand energy system. However, we find this perspective hard to accept.

High prices put a strain on consumers, with an increasing number facing energy hardship, while businesses struggle to remain viable. Although the market continues to generate substantial profits for electricity retailers, these outcomes are not only detrimental to

[6] Generation investment survey 2022 – prepared for the Electricity Authority by Concept Consulting.
[7] Past and Present Electricity Pipeline. Concept Consulting 11 October 2024

consumers—they pose a significant risk to the broader New Zealand economy.

We need market adaptation at a time of technological change and greater electrification of the economy

We are at a critical juncture, having reached a point of inflection where emerging technologies, combined with advancements in AI, have the potential to deliver significant benefits for consumers and the broader economy. However, these innovations may disrupt the status quo for incumbent gentailers, potentially challenging their ability to sustain high profit margins.

There is a clear incentive for some in the industry to resist these changes and normalize current outcomes. Without careful attention to market design, there is a real risk that these benefits could be stifled by efforts to protect existing interests, undermining the potential of new technologies to improve affordability and efficiency for consumers. It is essential that we seize this opportunity to get the framework right.

We suggest the following need to be investigated in the initial market review:

1. Greater separation between generation and retail functions

In our view, achieving greater separation between generation and retail functions is essential to promoting a fairer and more competitive electricity market. While a move to complete ownership separation could be highly disruptive and presents certain risks, implementing targeted measures to enforce functional separation within existing ownership structures can create a more level playing field without the need for drastic structural changes.

Regulatory measures should be introduced to ensure that independent retailers are able to procure electricity on terms and rates that are genuinely comparable to those available to gentailers. This would reduce current disparities, enabling independent retailers to compete more effectively and, ultimately, deliver better choices and outcomes for consumers.

However, it is important to consider complete ownership separation as a backstop option if these measures do not achieve the desired results. Full separation should remain a viable policy alternative if functional separation fails to address the existing competitive imbalances, ensuring that the market remains accountable, and consumer interests are protected.

2. Address consumer apathy and barriers to switching

For too long, a combination of apathy, confusion, mistrust, and certain retailer behaviours has denied consumers the promised benefits of a competitive retail electricity market.

Despite electricity being one of the largest household expenses, disengagement has become so prevalent that around 20% of consumers do not even open their monthly bills[8]. Although substantial savings are available and consumers are increasingly concerned about rising electricity costs, relatively few take the steps to regularly compare providers and switch.

This disengagement largely benefits incumbent providers, who face minimal pressure to enhance transparency, service quality, or improve consumer engagement.

Increasing switching activity among consumers is crucial to promoting a genuinely competitive market. Making it straightforward for consumers to compare options would directly encourage more switching, increase competitive pressure, help stabilize prices, and drive much-needed innovation.

The solution is straightforward: mandating and standardizing essential elements of electricity billing, as has been done in other countries, would allow consumers to easily compare offers and make informed choices. User-friendly bills with standardised elements and consistent terminology would eliminate much of the confusion that currently discourages consumers from engaging with the market and taking advantage of potential savings.

This is not simply a desirable improvement; it is essential to ensuring that electricity retail evolves in a way that truly benefits consumers. By making bills more transparent and comparable, the market can encourage greater consumer participation, resulting in a healthier, more competitive, and more equitable electricity market.

3. Address the market not providing reliability

New Zealand's electricity system is highly renewable and is likely to become even more so. While this shift supports the country's climate goals, it also exposes the system to increased reliability risks due to the variable nature of weather-dependent generation. In a predominantly renewable system, managing these weather-related contingencies requires significant overbuild in generation capacity. However, under the current market structure, there is little to no incentive for investment in plants designed to cover dry-year contingencies, as these plants would remain idle most of the time, making such investments economically unviable.

As the proportion of renewables continues to grow, this issue will intensify. The decreasing availability of gas, coupled with climate change impacts that may make dry years more frequent, compounds the urgency of addressing this structural gap.

We believe that viable solutions to enhance system resilience and reliability lie in establishing a capacity market or procuring capacity outside of the existing market

[8] 2024 CNZ energy survey results

structure. This could take the form of direct contracts to build and maintain new generation specifically for dry-year and contingency needs. Alternatively, the System Operator could procure this additional capacity as an ancillary service, similar to how it already procures reserves, black-start capability, and frequency-keeping services.

By implementing these measures, New Zealand could maintain a resilient and dependable electricity system, balancing climate ambitions with the practical requirements of supply stability.

Yours sincerely,

Jon Duffy
Chief Executive
Consumer NZ