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Dear Jenny

Market Design Review: Issues Paper - Survey of Market Performance

Introduction

1. Mighty River Power welcomes the opportunity to comment on the Electricity Commission's *"Issues Paper – Survey of Market Performance"*, 2007. No part of Mighty River Power's submission is confidential, and we are happy for it to be publicly released.

The Electricity Commission's work programme

2. Mighty River Power believes it is important for the Electricity Commission to periodically review its work programmes and priorities. The Electricity Commission has done this with its "big picture review" consultation.[1]
3. The appropriate framework for considering whether there are issues that warrant investigation and possible regulatory intervention is to ask whether there are any impediments to meeting the principal objectives and specific outcomes contained in section 172(N) of the Electricity Act 1992, and repeated in the Government Policy Statement on Electricity Governance 2006 (GPS).[2]
4. Market ideals are at the heart of section 172N and the regulation making provisions of the Electricity Act. In particular, every one of the specific outcomes is driven by efficiency considerations. The corollary of this is that the Electricity Commission should presume the principal objectives and specific outcomes are satisfied if no substantive and durable market failure(s) is identified in respect of any given Commission workstream.[3]
5. When the Electricity Commission was established it was faced with a considerable number of workstreams driven by the 2004 version of the GPS. The Electricity

[1] Letter dated 26 September 2006.
[2] This is a view we emphasised in detail in our submission to the Electricity Commission on *"The meaning and use of Section 172N of the Electricity Act 1992"*, 27 April 2007.
[3] The exception to the above is where the Government's electricity policy gets into the area of social policy. Aspects of the GPS section on Consumer Protection fit into this category; in particular, the low-fixed charge tariff requirements, and GPS requirements around protection of low income consumers.

Commission was also given a New Zealand Electricity Market (NZEM) handover package (Handover Package).[4]

6. Mighty River Power considers that the Electricity Commission's first priority should be to complete the work emanating from the GPS and the Handover Package. The Electricity Commission has done a considerable amount of work on the matters contained in the GPS, though there is still a significant way to go. The Handover Package also contains a large number of workstreams that remain relevant.
7. The Electricity Commission should be attending to these matters before considering potentially wider workstreams from the Market Design Review.
8. In Mighty River Power's view, the Handover Package that was provided to the Electricity Commission in February 2004 contained well developed market and rule changes. While Mighty River Power does not necessarily suggest they should all be implemented we are surprised they have not been consulted on. The matters dealt with in the Handover Package were in an implementable form, thereby requiring little work on the part of the Electricity Commission.
9. One of the issues "Demand Side Bidding and Forecasting" has only just been released for consultation after three years, despite the Handover Package indicating that the work was important to market development.[5]
10. Work streams that we believe have not been adequately resolved are:
    a. Settlement on real-time prices;
    b. Transmission capacity reserves (a transmission alternative); and
    c. Mixed constraints in Scheduling, Pricing and Dispatch (SPD).
11. Mighty River Power is also aware rule changes have been submitted to the Commission that have not been addressed in a timely fashion. The following rule changes are examples and Mighty River Power assumes there are more.
    a. Clarifying the rules around compliance of dispatch instructions; and
    b. The hybrid frequency regulating reserve selection methodology proposed by FIG and MEUG (this has been effectively rejected but the rejection is in some part due to the delays in addressing the rule change).
12. Mighty River Power is aware of a number of major issues with the electricity system the Electricity Commission must be aware of that either do not appear to be being addressed in a timely manner or are not being developed in the transparent manner. These include:
    a. Frequency market development is an area that appears to have had little priority from the Commission despite the fact that this market is worth up to $50m of annual costs.

[4] NZEM Rules Committee for the Electricity Commission *"Handover of Work Being Conducted Under NZEM"*, 12 February 2004.
[5] Electricity Commission *"Demand-side bidding and forecasting"*, 5 July 2007.

Mighty River Power considers that the frequency market is an area in urgent need of attention.

b. Mighty River Power acknowledges that the Commission has recently released a number of reports on investigations into wind generation integration it has conducted.[6] However, given the breadth of current operators and potential new entrants that require some regulatory certainty in the longer term around wind we are concerned so little has been openly discussed by the Commission about the subject of integration.

13. Mighty River Power is of the view that valuable market developments need to be done in a timely fashion and with good transparency and appropriate consultation. There is no doubt this takes time but the Electricity Commission takes too long to process rule changes and developments and often consults far too late in the policy development process.[7] The Electricity Commission should review its own processes to aim to be more efficient and effective in researching, consulting on, and developing the market and the rules.

14. In this context (and prioritising the list of options above) Mighty River Power recommends that the Electricity Commission:
    a. Streamline its processes and make them faster and more effective;
    b. Engage with interested parties earlier on in the policy development process;
    c. Give maximum possible urgency to the issues of the Frequency market and Wind Integration; and
    d. Commit to clearing the backlogs of work (including rule change proposals) from all its Advisory Groups.

15. A more strategic review of the electricity industry, and the way it is regulated, would be most appropriate after this work has been done.

Mighty River Power's general observations about the Issues Paper

16. Mighty River Power's evaluation of the Issues Paper is made against the framework provided by the Electricity Commission's principal objectives and specific outcomes, and identification of whether there are any *durable market failures* that impede the achievement of these objectives and outcomes.

17. Mighty River Power believes there are two alternative perspectives that can be drawn from the Issues Paper; the glass is either considered to be half full or half empty.

[6] Electricity Commission, website at http://www.electricitycommission.govt.nz/opdev/comqual/windgen/wgip.

[7] Refer to the comments Mighty River Power made comparing the Electricity Commission's process for development of the hedge market and transmission pricing (favourable) with those made about the development of the benchmark agreement regime for electricity transmission (extremely unfavourable). For example, paragraphs 41 to 46 of Mighty River Power's *"Submission on the drafting of the Electricity Commission's Benchmark Agreement and Interconnection Rules"*, 18 April 2007

18. From the former perspective, the Issues Paper does not really identify any major problems in the retail and wholesale sectors of the electricity market, and points to a lot of evidence that the market (particularly, the wholesale sector) is operating well. From the latter perspective, while the Issues Paper does not identify any market failures it identifies a number of areas where further work ("more detailed analysis") is required to determine whether there is a problem or not.

19. Mighty River Power is of the view that the market is generally working well, though there is some scope for further improvement. We do not believe further major reforms are required or desirable. The electricity industry has already gone though 20 years of virtually continuous reform. Further major reforms should certainly not be contemplated in the absence of identification of substantial and durable market failures.

20. Regulatory intervention should be limited to addressing *durable market failures*; and should aim to address the market failures as directly as possible, i.e. address the causes of the problems rather than just the symptoms. The Market Design Review should focus on identifying what durable market failures exist that may mean the normal competitive operation of the (wholesale and retail) market cannot be relied on to ensure efficient outcomes. Any policy options the Electricity Commission considers should be directly targeted at addressing these market failures. That is, the regulation should aim to directly deal with the cause of the problem (where possible) rather than just the symptoms of the problem.

21. If no market failures are identified then regulatory intervention is not required.[8] Mighty River Power notes that we do not believe the Issues Paper has identified any durable market failures. Mighty River Power accordingly considers that more work is required before Stage 1 on problem definition is completed, and the Electricity Commission is in a position to move on to Stage 2 and identify solutions (solutions to what?).

Evidence from the Issues Paper that the electricity market is performing well

22. A lot of the content in the Issues Paper lends support to the view that the electricity market is performing reasonably well, and major changes are not needed (particularly in relation to electricity generation). For example:

> The general pattern of hydro/thermal linkage is evident through the entire period … Overall the patterns suggest a reasonably effective level of coordination between hydro storage, plant maintenance and thermal operation decisions.[9]
>
> Overall, there is no indication that the market has caused any increase in levels of spill, and if anything spill appears to have reduced in recent years.[10]
>
> Non-hydro plant generally appears to run in a merit order that corresponds with estimates of relativities among short run marginal costs.[11]

[8] The exception is where the Government is aiming to address social policy matters, such as protection of low income consumers.

[9] Paragraph 172.

[10] Paragraph 175.

> Shorter term wholesale price variations are considerably more volatile but appear to more strongly reflect prevailing hydro supply conditions than prior to market commencement.[12]

> This chart suggests that there is a degree of correlation between contract price indicators and dry year margin. In particular, the period of falling contract price indicators was associated with a rising dry year margin (1998-2000). Likewise, the more recent rise and subsequent fall in EnergyHedge and NZTF index price indicators coincides with a period when dry year margin was tighter than average, and is then projected to increase sharply (due mainly to scheduled commissioning of e3p).[13]

> The interaction between instantaneous reserves and energy markets and the level of competition to provide instantaneous reserves appears to suggest that the instantaneous reserves market is reasonably effective …[14]

> In terms of medium term demand response, there is evidence that large industrial users have responded to sustained movement in spot prices during extended periods of low inflows …[15]

23. These views accord with the Government's own electricity market review late in 2006. The Minister of Energy, for example, stated has that:

> I have recently undertaken a review of the electricity market … I concluded that the current competitive market arrangements should be retained but a range of improvements should be pursued to enhance security of supply and the operation of the market.[16]

> Officials consider the overall [wholesale] market design is in line with international best practices and is robust.[17]

> Performance on *timely investment in new generation* appears good … [18]

> On competitive and efficient prices, my review notes that prices have risen mainly as a consequence of the increased cost of existing and new thermal generation with the depletion of low cost Maui gas. Overall, however, prices appear to be tracking the long run cost of new generation … and New Zealand's prices continue to compare well with most other OECD countries …[19]

> My review also concluded that the current market arrangements reduce the risk of poor projects going ahead. Currently, capacity increments are coming from a diverse range of

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[11] Page 3-23.
[12] Page 3-23.
[13] Paragraph 250.
[14] Page 3-65.
[15] Page 4-17.
[16] Paragraph 2 of the Cabinet Policy Committee paper from the Minister of Energy *"Electricity Market Review: Improvements to Current Arrangements (Paper Two)"*, 2006.
[17] Paragraph 72, ibid.
[18] Paragraph 4a of the Cabinet Policy Committee paper from the Minister of Energy *"Electricity Market Review: Summary of Review (Paper One)"*, 2006.
[19] Paragraph 6, ibid.

investments regarding geographic location and type. It also concluded that the competitive market has delivered good innovation, pressure on costs and generally efficient dispatch of generation plant." [20]

Level of competition in electricity retailing and generation

24. The Issues Paper makes the assertion that the retail and generation markets are not as competitive as they could/should be. Analysis of the competitiveness of the market is probably the most crucial part of the Issues Paper. Such an analysis directly aligns with the GPS. The specific outcomes the Government is seeking through the GPS include:

    > ... barriers to competition in electricity are minimised for the long-term benefit of end-users[21]
    >
    > ... delivered electricity costs and prices are subject to sustained downward pressure[22]

25. Likewise, paragraph 113 of the GPS states

    > ... the Government considers that retail competition is not as vigorous as it could be, and looks to the Electricity Commission to promote and facilitate retail competition, and to make recommendations to the Minister of Energy on any steps the Government should take, including regulating, to facilitate retail competition.

26. The Issues Paper lacks a methodical approach to assessment of the level of competition. Consequently, the Issues Paper does not provide adequate evidence in support of its propositions about the level of competitiveness of the retail and generation markets. The starting point should be to define the relevant market[23], and then to assess matters such as number of competitors, market concentration and whether there are barriers to entry. (A market can be highly competitive, even with few competitors, if there are low barriers to entry.)[24]

Market concentration

27. The Issues Paper asserts that *"The retail sector is highly concentrated, with the five largest parties ... accounting for over 90 percent of the market, based on ICP numbers"* and *"The generation market is highly concentrated, with the five main parties (all*

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[20] Paragraph 7, ibid.

[21] Paragraph 2c of the GPS.

[22] Paragraph 2f of the GPS.

[23] There are a number of potential dimensions to the market:

a. Product dimension – are other fuel types substitutes for electricity?

b. Geographic area – is the market(s) a national market or a series of regional markets?

c. Functional dimension – The level of the production or distribution chain.

d. Temporal dimension – the time frame or timing within which the market operates, where relevant.

e. Customer dimension – the different customer types within a market, where relevant.

[24] Assessment of the level of competition in markets is something that the Commerce Commission does on a regular basis, as part of its responsibilities under the Commerce Act 1986 and the Telecommunications Act 2001. See, for example, section 3 of the Commerce Commission's *"Mergers and Acquisitions Guidelines"*, 1 January 2004.

integrated generator-retailers) accounting for over 90 percent of the market by capacity."[25] But what is this highly concentrated compared to?

28. Figure 1 shows the market share for each electricity retailer and generator.

Figure 1: Market shares in the electricity market

Electricity Market Shares						
	Contact Energy	Genesis Energy	Mighty River Power	Meridian Energy	TrustPower	Other
Retailing[26]	27.0%	29.4%	18.4%	11.5%	11.5%	0.0%
Generation[27]	27%	19%	12%	30%	4%	8%

29. We believe this level of concentration is in line with overseas electricity markets where competition has been introduced. In the UK electricity retail market, which is 25 times the size of New Zealand, 6 retailers account for 99% of the market.[28] Likewise, in Victoria Australia 6 retailers account for 87% of the market.[29]

30. We also believe the electricity retail and generation markets level of concentration compares reasonably favourably with other markets in New Zealand.

31. One method of measuring the level of competition or level of market concentration in a market is the use of the Herfindahl-Hirschman Index (HHI) of market concentration. A monopoly would have an HHI of 10,000, while a perfectly competitive industry would have an HHI of zero. The electricity retail and generation markets have HHIs of 2196 and 2214, respectively, which are clearly closer to the perfectly competitive standard than the monopoly standard.

32. Figure 2 shows that the airline (domestic and trans-Tasman), telecommunications (mobile and fixed), banking (credit cards), supermarket and television markets all have higher levels of concentration than either the electricity retail or generation markets. This suggests that, from a national perspective, electricity retail and generation competition is relatively strong.

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[25] Chapter 3-61.

[26] Electricity Commission *"Retailer Market Share by ICP"* for May 2007.

[27] Page 126 of Ministry of Economic Development's Energy Data File, September 2006.

[28] BGT 22%, Powergen 20%, SSE 16%, npower 15%, EDF Energy 13%, ScottishPower 13%, Other 0%. Source: Figure 4.1 of the OFGEM report *"Domestic Retail Market Report – March 2006"*, 5 July 2006.

[29] Table 1 of the Essential Services Commission report *"Energy Retail Businesses Comparative Performance Report for the 2005-06 financial year"*, November 2006.

Figure 2: Level of concentration in different New Zealand markets[30]

Market	HHI	Comment	Source
Airline – domestic	5,200-10,000	Based on 8 domestic routes observed in 2004 and 2005.	Tim Hazledine *"Pricing and Competition in Australasian Air Travel Markets".*
Airline – transTasman	2653 – 10,000	Based on 8 domestic routs observed in 2004 and 2005.	Tim Hazledine *"Pricing and Competition in Australasian Air Travel Markets".*
	4700	12 months to end of April 1998	Productivity Commission *"International Air Services Inquiry Report", Report No. 2, 11 September 1998*
Banking	1700 – 2500	2003. Various across services, e.g. home loans have the lowest HHI and credit cards the highest.	NZIER *"The Performance of the New Zealand Banking Sector – Report to the Reserve Bank of New Zealand",* 26 November 2004.
Electricity – retail	2196	May 2007.	Electricity Commission *"Retailer Market Share by ICP".*
Electricity – generation	2214		Page 126 of Ministry of Economic Development's Energy Data File, September 2006
Petrol retailing	2330	2001	The NZ Trade Consortium in Association with the NZIER calculated the HHI for the retail petrol industry in 2001 to be 2330 (*"The petrol industry deregulation, entry and competition"*, 2001).
Supermarket	3962	1998 sample of grocery shoppers	Philip Gendall, Katharine Hoskyn, Janet Hoek & Robert East *"Determinations Of Grocery Store Loyalty in New Zealand"*
Telecommunications – fixed	7978[31]	This has been estimated using liable persons (under the Telecommunications Act) share of the net cost of the TSO (Commerce Commission draft determination for 2003/04), with cellular netted out.	
Telecommunications	5016	Based on market share in	

[30] Figure 2 was derived from publicly available information. The Commerce Commission's decisions on mergers and acquisitions pursuant to the Commerce Act also include market share information but on a confidential basis. At the time of making this submission Mighty River Power had been unsuccessful at obtaining any of this information (or the resulting HHIs).

[31] Covec has calculated that the fixed-to-mobile origination market is highly concentrated, with an average HHI of 6,334. Covec Report prepared for Vodafone *"Regulating Mobile Termination: Pass-Through Issues"*, 14 July 2004.

Market	HHI	Comment	Source
– mobile[32]		December 2005.	
Television	3587	2005 Jan - Sep	Application from Sky TV to Commerce Commission pursuant to section 66(1) of the Commerce Act 1986 seeking clearance of a proposed business acquisition, 25 November 2005

33. The Issues Paper also contains various other information on the level of competition, including on service quality, price levels and profit margins, customer surveys, and customer switching. In the subsections below we look specifically at some of the information on the level of competition in the retail and generation markets, respectively. Before we do though we make the following observations.

34. The Issues Paper cites survey results which indicate some concern amongst market participants about the extent of competition in the contracts market,[33] making the claim that *"the survey indicates both users and suppliers have concerns about the competitiveness of the hedge contract market."*[34] Survey results are not an appropriate or valid basis for determining how competitive a market is.

35. Analysis of price and service quality is not very meaningful without an assessment of the competitiveness of the market.[35] It is difficult to robustly determine whether prices and service quality are appropriate without determining whether they reflect the outcome of a workably competitive market. Without this context the Issues Paper's analysis risks focussing on symptoms rather than causes of problems (if any). Due to the lack of competitive market assessment the Issues Paper lacks an adequate basis for concluding that the electricity retail and generation markets are not workably competitive.

36. The Issues Paper's analysis of service quality is not helped by the focus on electricity lines business (ELB) service quality measures rather than electricity retail measures. Measures such as SAIDI and CAIDI are determined by ELBs and electricity retailers have not control over them

37. Regardless of the above analysis, and consistent with our view on the need to undertake a market competitiveness assessment, we note the Minister of Energy's caution on reading to much into prices: [36]

> Concerns are sometimes raised that a lack of competition in the wholesale and retail markets is generating higher prices. It is important to note that it is not possible to identify non-

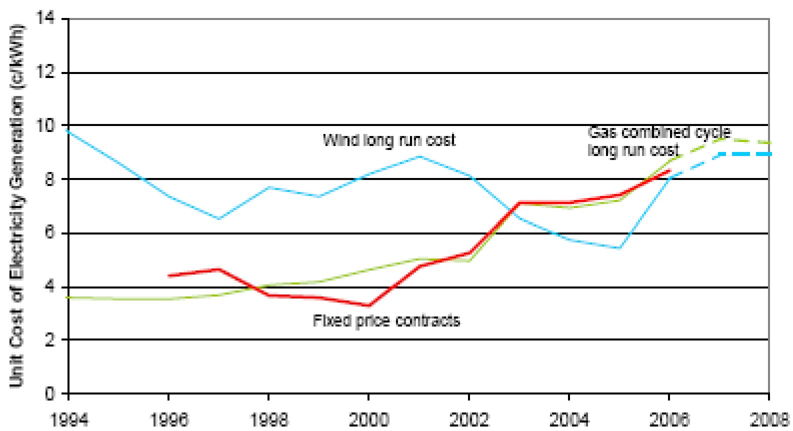
[32] Market share in December 2005 of:
Vodafone: 2,024,000
Telecom: 1,802,000
Total customers: 3,826,000.
[33] Figure 67.
[34] Chapter 3-45.
[35] More so if the service quality measures used are outside of the control of electricity retailers.
[36] Paragraph 43, ibid.

competitive pricing through observation of price levels alone. High prices are not necessarily evidence of lack of competition and, as noted, recent rises in wholesale prices have been accompanied by observable increases in underlying resource costs. Work to date by MED on retail margins indicates that margins are largely unchanged pre and post the market reforms of the late1990s.

Level of competition in electricity generation

38. The Minister of Energy has provided some useful analysis in relation to electricity generation. This analysis indicates, reflected in Figure 3, wholesale contract prices have largely tracked the long run cost of new gas thermal generation. As the Minister notes *"This is the efficient price level to encourage optimal new generation investment and consumption decisions."*[37]

Figure 3: Comparison of wholesale contract prices and new generation costs



Source: Minister of Energy[38]

39. The Issues Paper confirms this position noting *"Wholesale electricity prices, as indicated by EnergyHedge appear to track close to LRMC for the period 2004-2009."*[39]

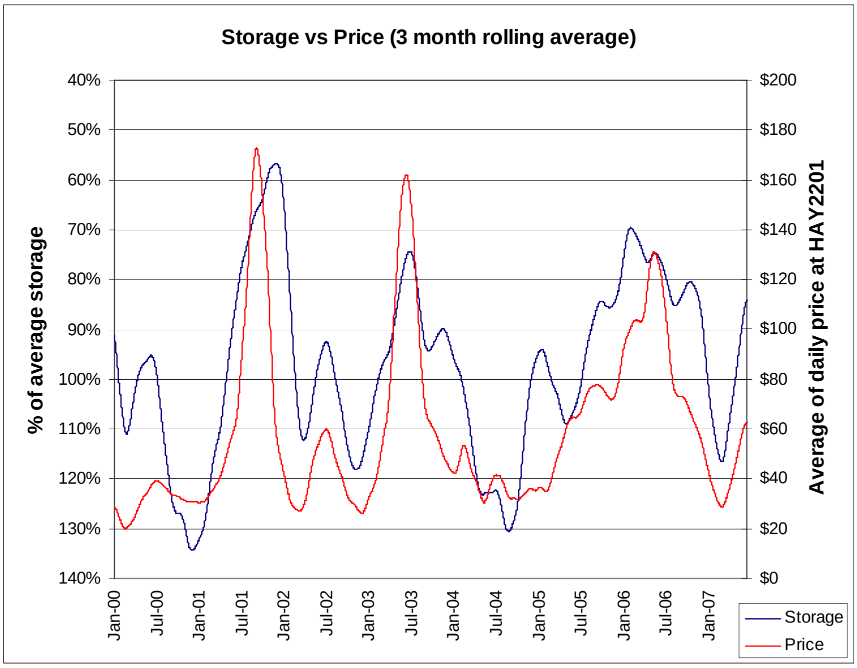
40. Mighty River Power believes that the electricity generation market's management of security of (energy) supply risk demonstrates the market is operating in a competitive manner, and satisfying the principal objective in the GPS to *"ensure that electricity is produced and delivered to all classes of consumers in an … reliable … manner"*. We also consider that the market can be relied on to achieve the GPS's specific outcome *"risks (including price risks) relating to security of supply are properly and efficiently managed"*.[40]

[37] Paragraph 38 of the Cabinet Policy Committee paper from the Minister of Energy *"Electricity Mt Review: Summary of Review (Paper One*)", 2006.
[38] Figure 5, ibid.
[39] Paragraph 262.
[40] Paragraphs 1 and 2(b) of the GPS.

41. We believe that the dry years of 2001, 2003 and 2006 – where there was the potential for electricity shortages, but none actually occurred – provide sufficient evidence to support this view.[41]

42. The risk of dry-year, and the resulting potential scarcity of electricity, is signalled through increases in spot and hedge prices in the wholesale electricity market. As the risk of a dry-year increases so to have spot and hedge prices. This is reflected in Figures 4 and 5.

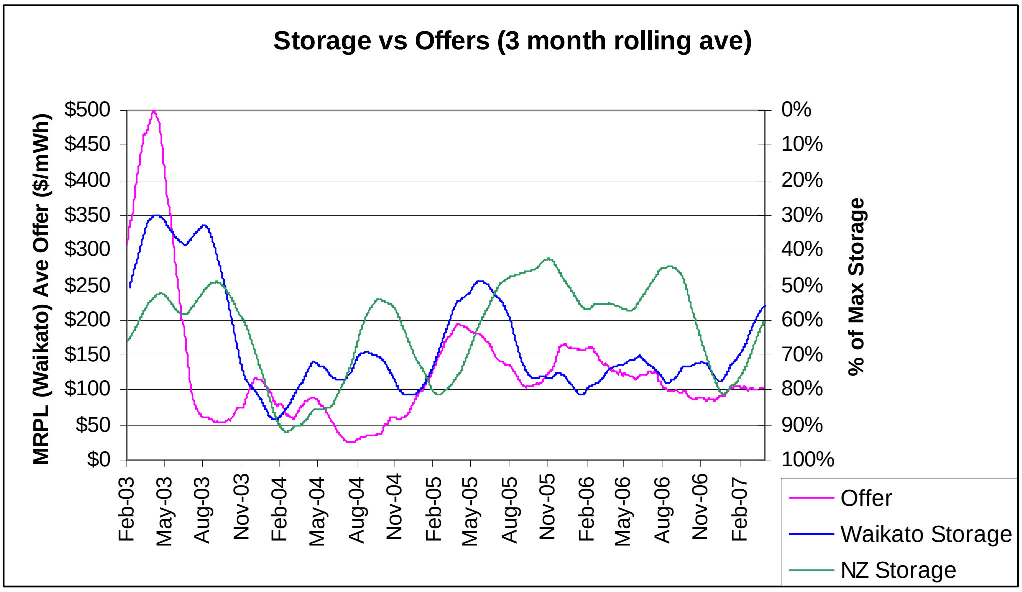
Figure 4: Relationship between storage capacity and spot prices



43. Figure 5 shows the relationship of Mighty River Power's offers with national and Waikato River storage levels. The Figure shows that Mighty River Power's offers have a higher correlation with their Waikato storage, than with national storage.

[41] The operation of Whirinaki in 2006 helped reduce the risks, and dampened spot prices, but does not change this conclusion.

Figure 5: Relationship between storage capacity and Mighty River Power's offers

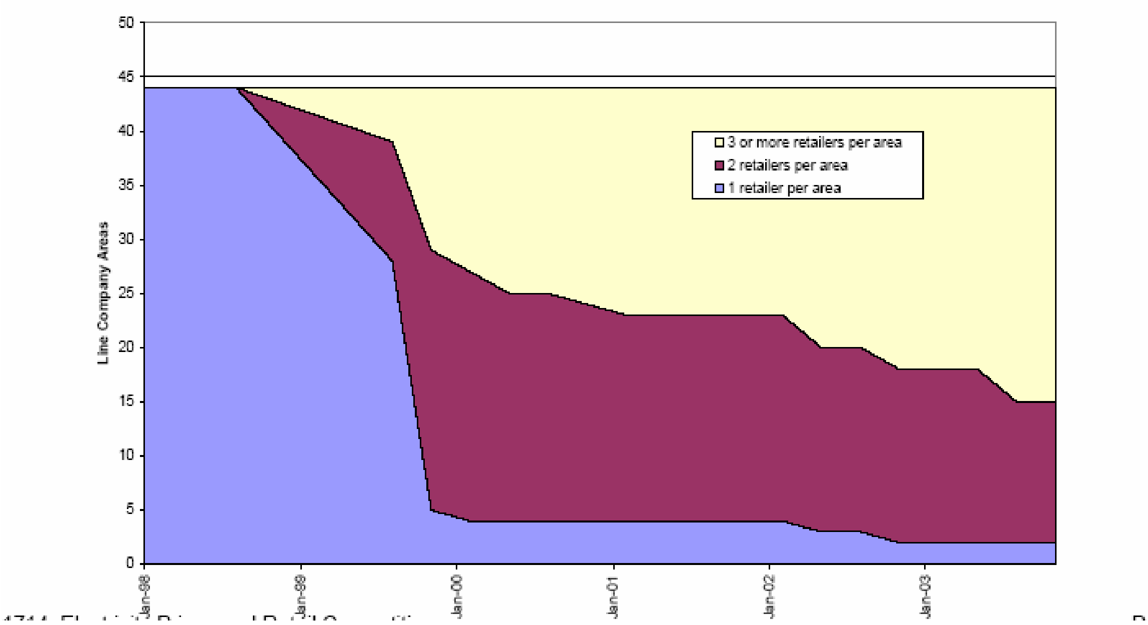


44. The increases in wholesale electricity prices resulting from lower storage levels send a signal to electricity generators to increase use of thermal generation (which is made economic by the higher spot prices), and to 'store' electricity in hydro dams (which can be sold at a later time, at a higher price). End-users in turn face strong incentives to reduce electricity demand. Either because of exposure to high spot prices, or the opportunity to profit from on-selling hedge contracts. This is how the market is intended to work, and how it did work in 2001, 2003 and 2006. The lights stayed on, despite these being some of the driest years that New Zealand has experienced.

Level of competition in the electricity retail market

45. Information from the Ministry of Economic Development supports the proposition that retail competition is relatively strong, and increasing. Figure 6 shows that the number of retailers in each ELB network area is increasing over-time.

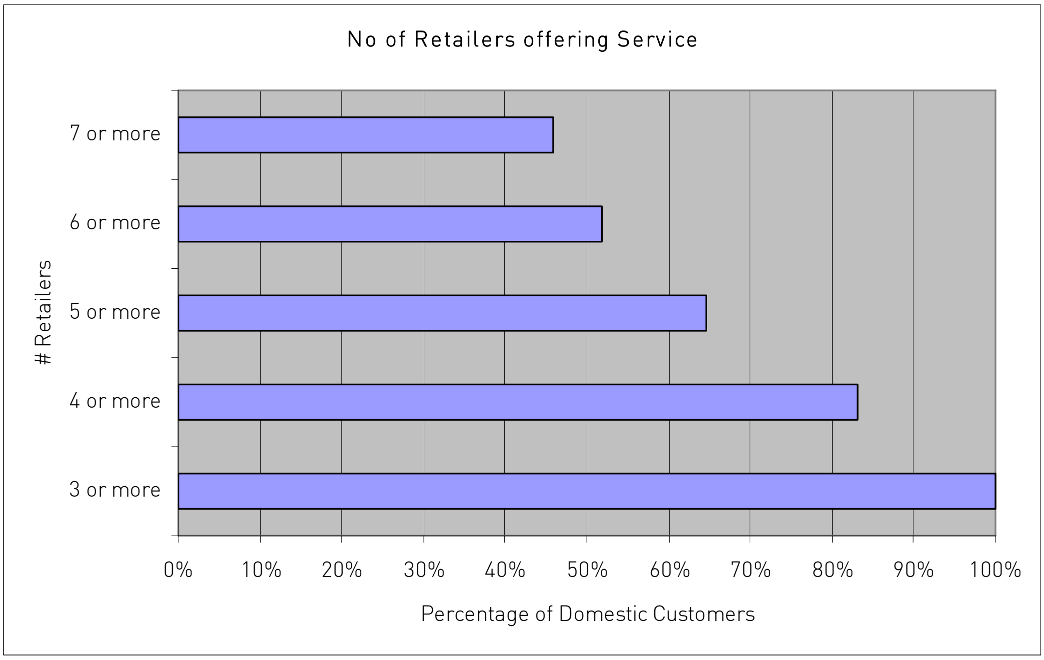
Figure 6: Increase in retailer competition for domestic consumers (showing number of retailers in each ELB area)



Source: MED.

46. The latest figures, reflected in Figure 7, we have indicate that all ELB network areas have at least 3 electricity retailers competing for domestic consumers, and over half the network areas have 6 or more electricity retailers. All major urban centres have 6 or 7 retailers. Also the information that the Issues Paper contains (Figure 34) is not up-to-date. There are two new entrants that have requested switches from us, Ezy Networks and Simply Energy.

Figure 7: Number of retailers competing for domestic consumers

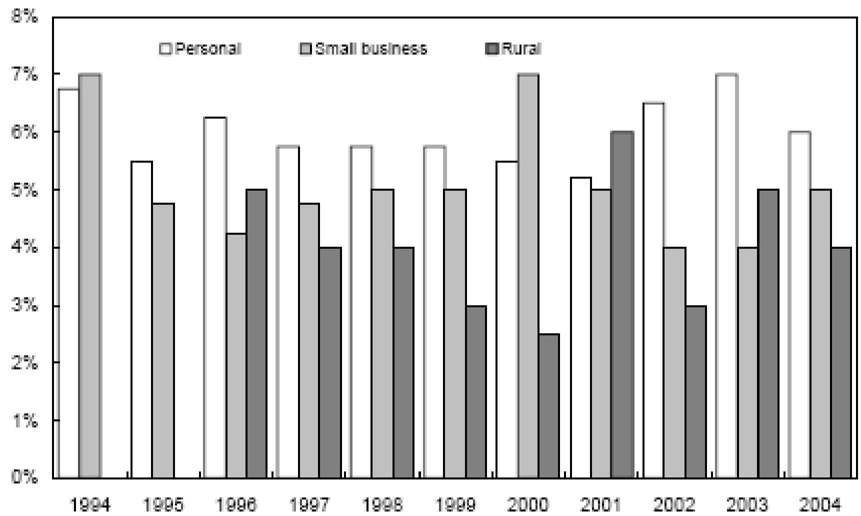


47. The Issues Paper has a substantial discussion around trends in retail margins and prices. It notes there has been substantial tariff rebalancing amongst customer groups. This is a matter that was directly covered off in the Minister of Energy's market review where he noted: [42]

> … aggregate real electricity prices have been relatively constant for most of the past 25 years. However, there has been 15 years of increasing real *domestic* prices and falling *commercial* prices, due primarily to the progressive removal of cross-subsidies from commercial to domestic consumers.

48. The Minister of Energy went on to provide context to the increases in domestic electricity prices by noted they *"… are not out of line with other OECD countries …"* which is illustrated by Figure 18 in the Issues Paper.
49. As well as market concentration, the Issues Paper uses customer switching to measure the level of retail competition.
50. Care needs to be given to any comparisons of switching. The level of switching will depend on what stage of development the market is in. This is reflected in Figure 37 which shows a high level of switching when competition was introduced into the electricity retail market in New Zealand, which then steadied around the 8 – 10% mark.
51. The switching figures raise questions of how they compare with other industries. Mighty River Power has not done an investigation of this, but we note that the electricity retail switching figures are higher than for the banking industry which ranges between 3 and 7% (depending on type of customer). This is shown in Figure 8.

Figure 8: Percentage of customers who have switched main bank



Source: NZIER *"The Performance of the New Zealand Banking Sector"*, November 2004

52. Care also needs to be given using switch numbers as they can understate the level of customer switching between retailers. Switch numbers do not accurately reflect the

[42] Paragraph 41 of the Cabinet Policy Committee paper from the Minister of Energy *"Electricity Market Review: Summary of Review (Paper One)"*, 2006.

number of consumers who move between retailers, they measure the numbers of ICPs (or physical premises) that move between retailers. If a Mercury Energy customer moves to a new house/premise that was say supplied by Genesis Energy, and the customer then switched to Genesis Energy this would not show up in the switching statistics.

53. Figure 38 of the Issues Paper shows a ranking of competitive electricity retail markets by level of switching. New Zealand is ranked 5th out of 13 which appears reasonably good. It is worth looking behind the rankings, and at the actual level of switching, which is shown in Figure 9. This shows that between 3rd and 8th have very similar levels of switching. Only Victoria and Great Britain have substantially more switching than New Zealand.

Figure 9: ICP Switching – International Market Rankings

Jurisdiction	Ranking	Switching
Victoria	1	21%
Great Britain	1	20%
South Australia	3	11%
Texas	4	7%
Norway	5	7-10%
New Zealand	6	8%
Netherlands	7	7-15%
Sweden	8	6-7%
NSW	9	6%
Finland	10	5%
Flanders	11	<5%
New York	12	<5%
Denmark	13	<5%

Source: First Data Utilities and VaasaEMG Utility Customer Switching Project

54. The switching figures also warrant the context of market share trends since the introduction of retail competition. Since 2001 Mercury Energy has targeted northern networks with aggressive door-to-door campaigns, supported by television and direct marketing. Our market share has increased by 50,000 customers over this time. We have had a particular focus and success in the United Network's Waitemata network capturing over 25% of customers in the market. We have also made significant inroads in a half dozen other networks including Counties Power and Thames Valley. We have also seen aggressive activity from our competitors, particularly Contact Energy and Genesis Energy in Auckland.[43]

[43] Between May 2003 and 2007, Mighty River Power's retail market share has increased from 15.5% to 18.4%.

Level of retail competition in different network areas

55. One interesting observation the Issues Paper makes on the level of retail competition is that *"A significant variation in margins across network areas is apparent. Furthermore, estimated margins are generally lower in the main urban areas, and higher in the regional areas."*[44] This lends support to Mighty River Power's view that the large number of ELBs in New Zealand (and the small size of many of them) makes competing in some areas more costly/difficult.[45]

56. Figure 10 generally shows that the smaller the ELB (in terms of number of customers) the less competition/the higher the largest retailer's market share will tend be.

Figure 10: Market share by ELB network area

ELB	Largest retailer market share (%)	ICPs
Northpower	49.3	50,005
Electra	58.9	40,403
United Networks	59.8	353,073
Unison Network	63.3	101,816
Nelson Electricity	67.2	8,962
Orion New Zealand	67.7	179,045
Alpine Energy	68.1	29,239
Buller Electricity	71.8	4,219
Average	73.8	64,533
Electricity Ashburton	74.7	15,270
Waipa Power	77.1	21,646
Powerco	78.3	290,698
Aurora Energy	78.9	76,840
Vector	78.9	301,296
Central Hawkes Bay Power	79.8	7,680
Otago Power	81.2	14,605
Counties Power	81.7	34,139
Marlborough Lines	82.8	22,683
The Lines Company	83.4	23,157

[44] Paragraph 99.
[45] Mighty River Power *"Response to the Electricity Commission's Consultation Paper: Indicators of retail market activity in the New Zealand electricity market"*, 28 April 2006.

ELB	Largest retailer market share (%)	ICPs
Scanpower	83.4	6,643
The Power Company	86.8	32,366
W E L Energy Group	89.1	76,533
Waitaki Power	89.7	11,647
MainPower NZ	91.5	30,711
Electricity Invercargill	91.6	16,907
Network Tasman	91.8	34,059
Eastland Network	92	24,845
Westpower	92.6	11,949
Top Energy	93.9	27,852
Horizon Energy Distribution	96.5	23,157

Source: Electricity Commission, February 2006.

57. Mighty River Power believes this reflects that:

    a. The smaller the ELB's network area the smaller the potential benefits from entry (in terms of potential customers/revenue gained)[46]; while

    b. There are significant costs of entry that do not vary with customer numbers eg determining the access arrangements; establishing billing systems; setting retail prices (exacerbated by the need to set low-fixed charge tariffs) for residential customers.

58. Mighty River Power believes the combination of a large number of ELBs that exist and the small size of many of the ELBs (coupled with the varying nature of line charge levels, structures, contractual arrangements and fault responsibility) in New Zealand may mean that retail competition is not as strong as it otherwise could be. Mighty River Power believes this is an aspect of the Issues Paper that warrants further consideration.

Concluding remarks

59. It is important for the Electricity Commission to periodically review its work programmes and priorities. The Electricity Commission has done this with its "big picture review" consultation.

60. We feel that there is a significant amount of work that the Electricity Commission already has that it should undertake; notably, matters arising in the New Zealand Electricity Market (NZEM) handover package (Handover Package).

[46] There are notable exceptions to this, however. In Northpower, the largest retailer (Meridian Energy) has a market share of less than 50%, even though Northpower only has 50,000 customers.

61. Mighty River Power considers that the Handover Package contains a large number of work streams that remains relevant. To this extent we do not think the Commission should be considering anything new of significant magnitude. This view is reinforced by our review of the Issues Paper.

62. Mighty River Power's view on the Issues Paper is:

    a. The limited evidence it provides indicates the electricity generation and retailing markets are working reasonably well, and no substantial regulatory reforms are needed.

    b. In areas where it identifies that there could potentially be a minor problem, e.g. the hedge market, the Electricity Commission has already initiated workstreams.

    c. It does not provide any real evidence of durable market failures. Further analysis (particularly around the level of competition in the electricity generation and retailing markets) would be required before further regulatory reforms could be justified (if at all).

63. This is consistent with the view the Government reached in its review of the electricity market. The market is fundamentally sound, and only fine-tuning of the regulatory regime is justified.

64. Mighty River Power **recommends** that, before progressing the next stage of the Market Design Review, the Electricity Commission conduct further analysis to identify whether there are any durable market failures impeding the achievement of the principal objectives and specific outcomes in the GPS.

65. If you have any queries regarding this submission, or would like further information, please do not hesitate to contact either me (on 09 308 8259 or robert.allen@mightyriver.co.nz).

Yours sincerely

Robert Allen
Regulatory Manager