Energy
Consumers
Australia

AEMC 2016 Retail Competition Review

Submission in response to the Approach Paper

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Executive Summary

The AEMC has been tasked with reporting on the effective competitiveness of energy markets in NEM jurisdictions. While the original purpose of the report has been to trigger jurisdiction commitments to deregulate retail prices once markets are effectively competitive, the AEMC has been asked to report on all jurisdictions.

Energy Consumers Australia notes that the long term interest of consumers is best served by highly effective competitive markets except in those aspects of the supply chain that are natural monopolies.

ECA is of the view that the current retail markets are competitive, but they have a long way to develop before they are at the level of competition required to fully promote the long term interests of consumers.

To provide a longer term focus on the ongoing development of an increasingly competitive retail market ECA proposes that the AEMC utilise the data currently assembled to provide the competitiveness report into a Retail Competitiveness Index that can be applied over future years to provide a more quantitative measure of the development of the market.

ECA also proposes that the AEMC place greater attention on retail gross margins rather than very ineffective measures of price movement.

Introduction

This submission is made by Energy Consumers Australia in response to the AEMC Approach Paper (the **Approach Paper**) for its 2016 Retail Competition Review (the **Review**).

Energy Consumers Australia (ECA) has been created by the Energy Council with the objective to:

> *To promote the long term interests of Consumers of Energy with respect to the price, quality, safety, reliability and security of supply of Energy services by providing and enabling strong, coordinated, collegiate evidence based consumer advocacy on National Energy Market matters of strategic importance or material consequence for Energy Consumers, in particular for Residential Customers and Small Business Customers.*

In this the ECA objective mirrors the objective of the Australian Energy Market Agreement.

The objectives of the three principal Acts that structure the energy market each state that the objective of each Law is to promote efficient investment in, and operation and use of, the relevant energy services. In doing so each law specifies that the reason for promoting efficiency is the long term interests of consumers (the **LTIC**).

Orthodox economic theory concludes that efficiency is best promoted through competitive markets, where they can operate.

The national energy markets have been structured on the principle of strictly separating natural monopoly elements in transmission and distribution networks from the competitive markets in generation and retail.

The annual retail competition review is therefore a critical determinant of how well the over-all market arrangements are delivering the objective of promoting the long term interests of consumers. It is only in the retail markets that consumers directly participate. If all the upstream elements of the operation of the wholesale market and the economic regulation of networks are working perfectly, the outcome for consumers will depend on the operation of retail markets.

The AEMC Retail Competition Review is therefore a critical element in determining how well the overall objective of the Australian Energy Market Agreement is being achieved.

ECA is particularly interested in the conduct of the review. The means by which ECA is to promote the long term interest of consumers includes “evidence based advocacy” on matters of strategic importance or material consequence for residential and small business customers. The data, information and reports provided by the market bodies (the AER, AEMC and AEMO) are one of the most important sources for evidence based policy. For effective advocacy the needs of consumer advocates in producing the data, information and reports is at least as important as the interests of industry participants, regulators and policy makers.

This need of information to support evidence based advocacy also raises an important issue about the use of data that might be provided by retailers with a claim of confidentiality. Experience in many industries is that claims of confidentiality often extend well beyond things for which an actual case for confidentiality can be made. ECA will make some comments about the operation of confidentiality in respect of specific measures of competitiveness.

The Terms of Reference

The terms of reference for the review transmitted to the AEMC in January 2014 commence with a background statement that:

> *Australian Governments have committed under the Australian Energy Market Agreement (AEMA) to remove energy price regulation where effective competition can be demonstrated. The Australian Energy Market Commission (AEMC) is tasked under the AEMA with responsibility for assessing the state of retail competition across jurisdictions within the National Electricity Market (NEM).*

ECA cannot find in the AEMA an explicit requirement for the AEMC to undertake assess the state of competition in retail markets. The AEMA refers to the AEMC being conferred all the relevant powers and functions in the National Energy Retail Law. The Law itself contains no explicit reference to the effectiveness of competition, though at s221(1)(b) it has the function and power for “market development functions”.

There are also specific provisions for reviews to be directed by the Energy Council. It is unclear whether the annual competition review falls under the definition of an Energy Council directed review. In any case, it is unclear whether the AEMC is bound to limit the scope of the report of a directed review to the matters in the terms of reference or whether it can include additional information.

It is clear from the opening of the terms of reference that the Energy Council’s interest was in the threshold condition for price deregulation where “effective competition can be demonstrated.” This narrow reading of the purpose is further supported by the comment under “scope” that “the competition monitoring that occurs as part of the AEMC’s annual NEM-wide reviews will principally cover energy markets in jurisdictions that are subject to retail price regulation, but also markets in jurisdictions where prices have been deregulated – mainly for comparison purposes.”

However the actual requirement is not constrained in this regard. The first paragraph of the scope states:

> *The AEMC is required to publish an annual report assessing the current status (and possible future development) of retail competition in electricity and gas markets across all the NEM jurisdictions. This assessment is to be based upon objective measures and analysis. The AEMC’s reports should also comment on NEM-wide issues that are affecting retail competition*.

The section on the Assessment Framework (before listing the criteria which will be discussed later) states:

> *The AEMC should have regard to the following criteria where practicable, and subject to data availability and resourcing constraints, in assessing the effectiveness of retail competition in*

energy markets across and within NEM jurisdictions (i.e. they apply for both NEM-wide and any jurisdiction-specific reports).

As will be discussed below this raises the issue of whether the purpose of the report is merely to delineate those jurisdictions which are effectively competitive from those which are not; or is it a broader purpose to report on the development of competition and how to make it more effective.

It should also be noted that the AER is required to prepare an annual report on the retail market and also provides information on the retail market as part of its overall State of the Energy Market annual reports. Both these reports are prepared on a financial year end basis; the State of the Market Report is usually released in December. The AER retail report only covers those jurisdictions who have joined the National Energy Consumer Framework.

The AEMC also prepares an annual report on residential electricity price trends; the 2015 report was provided on 4 December. All this data is available to the AEMC in preparing its retail competitiveness report.

Related to this question is the issue of the SCER initiated review of Retail Reporting in the Energy Market. The Communique from the July meeting stated:

> *Review of Retail Reporting in the Energy Market – Opportunities for Improvement*
> *The Council was appreciative of stakeholders input into the recent consultation on retail reporting in the energy market. It was noted that generally stakeholders accepted that the current retail reporting framework was appropriate, with two national reporting bodies and jurisdictions reporting on the retail market as part of the transition to a deregulated retail price environment. Whilst most stakeholders considered reporting done by the two national reporting bodies was different, the data collection to inform the reports was the same. The Council therefore agreed to explore opportunities to harmonise or consolidate data collection for retail reporting. Stakeholders also recognised that pricing may become more complex with the introduction of flexible pricing. To ensure retail reporting is flexible in this changing environment, the Council agreed to ensure the AEMC has the necessary flexibility for its reporting on possible future price trends in electricity pricing.*

In their submission to the SCER review the Energy Retailers Association of Australia requested better coordination between the AER and AEMC (and jurisdictional regulators) on information requests, noting "From a reporting perspective, the ERAA urges the AEMC to implement arrangements to receive and share data with the AER, to remove the requirement on retailers to provide the relevant data for the reports to the AEMC, as this data is already available to the AER."

ECA supports this objective and, as will be discussed later, suggests that co-operation between the AER and AEMC should extend to the use of the AER's information gathering powers to assist in this process.

If there are any legislative barriers to this occurring the AEMC needs to propose legislative amendments to the Energy Council to have them removed.

What is effective competition and why does it matter?

Competition between providers in a market is essential for the objectives of the long term interest of consumers to be promoted.

In the static analysis of efficiency applied in determining that markets generate efficient outcomes, the assumption is made of "perfect" competition. Real world markets don't have the characteristics of an effectively infinite number of both suppliers and producers, consumers and providers are not perfectly informed about the preferences of each other before trades occur.

It is accepted, however, that there are levels of competition less than the ideal for which the same outcome as a competitive market would apply. Contestable market theory posited that so long as entry and exit costs were low the competitive outcome could be achieved with a monopoly provider faced with potential competitors.[1] Unfortunately real world entry and exit costs are never so low.

The theory of Cournot oligopoly expressly stated the deviation that would occur from the efficient outcome with few providers who had to make commitments about the size of market share they wished to pursue.[2] Game theoretic solutions[3] and experimental solutions[4] indicate that the deviation from the competitive level can vary depending merely on the number of firms.

The real world purpose of markets, however, is not to achieve the price outcome foreshadowed by orthodox theory. Markets firstly are places of exchange and a well-functioning market is one in which the cost of exchange is minimised[5]. Markets are secondly places where, through the exchange of goods and services, information is exchanged. Consumers and producers are informed about each other's interests by the transactions that occurred in the market in previous time periods.[6]

One of the most important characteristics, but least understood, of the market is the extent to which there is "independent rivalry". That means that the focus of firms is competing **for the customers**, not competing **against each other**.

In determining the effectiveness of competition all of these characteristics are relevant. That is why the assessment framework criteria proposed by the Energy Council included a number of criteria. These were:

1. Independent rivalry within the market;
2. The ability of suppliers to enter the market;
3. The exercise of market choice by customers;
4. Differentiated products and services;
5. Price and profit margins; and
6. Customer switching behaviour.

The AEMC in the Approach Paper indicated that a different list of indicators would be used:

- Customer activity in the market;
- Customer satisfaction with market outcomes;
- Barriers to retailers entering, expanding or exiting the market;
- The degree of independent rivalry in the market; and
- Whether retail prices are consistent with a competitive market.

The adequacy of the identified indicators and the deviations from the Energy Council list will be discussed later in this submission.

The question to be addressed now is having recognised that there are a number of indicators of competition effectiveness how should they be combined, and what standard should be applied to declare a market sufficiently effectively competitive to meet the jurisdictional standard.

In the 2015 report the AEMC stated “there are no critical thresholds for these indicators that tell us when competition is operating effectively.” Unfortunately the AEMC has provided no guidance on how it determined, on the basis of the indicators taken collectively, to deem that a specific (geographic) market was, or was not, effectively competitive.

An extensive literature exists on the concept of “workable competition” starting with Clark.[7] Adopting the new term “effective competition” in 1968 Sosnick noted that the many writers on the topic have sought “both a standard against which functioning markets could be judged and guidelines for the formation and administration of antitrust and other public policies. Accordingly, each writer has tried to specify a realistic ideal, that is, a market situation that, unlike perfect competition, is both desirable and attainable.”

Sosnick goes on to develop seven principles for a writer to follow in defining effective competition;

- be specific about the issues,
- definite about his own views,
- explicit about necessary versus sufficient conditions,
- realistic about whether desirable conditions are attainable,
- discriminating in judging between a condition and its effects,
- comprehensive in listing market deficiencies,
- and stringent in describing his ideal.

Following these principles Sosnick assessed that a market was effectively competitive if and only if it was free of 25 flaws.[8] This work has not, unsurprisingly, been extensively cited by other writers. It is mentioned here as a description of what a thorough analysis of what effective competition might mean.[9]

It is clear from this survey that it is easier to compare the relative competitiveness of two markets than it is to declare whether a specific market meets a criterion of being effectively competitive.

The use of a “bright line test” on markets being effectively competitive before retail price controls are removed is also potentially an impossibility. By their very nature retail price controls suppress the product variety and pricing dimensions necessary as part of determining the effectiveness of competition.

As discussed above the continued promotion of competition in retail markets is required to promote the long term interest of end users. Were the National Energy Consumer Framework to be fully functioning across the country with no jurisdictional variation, the reporting on the effectiveness of competition for the single geographic market of the combined NEM jurisdictions will be valuable.

This suggests that the AEMC should take the step of determining how to use the multiple dimensions being assessed to derive a single Energy Retail Market Competitiveness Indicator.

Composite Indicators (**CIs**) are being increasingly utilised as a useful tool for policy analysis and public communication. They are particularly used in a variety of comparisons of countries and are used by government agencies and policy advocates. Examples include the World Economic Forum's Global Competitiveness Index[10], the Global Innovation Index[11], the ITU's ICT Development Index[12], the European Union's Digital Economy and Society Index[13], and the OECD's Better Life Index.[14] Locally the Regional Australia Institute has developed a regional competitiveness index (it is actually a suite of indicators).[15]

The *OECD Handbook on Constructing Composite Indicators* provides the following description[16]:

> *An indicator is a quantitative or a qualitative measure derived from a series of observed facts that can reveal relative positions in a given area. When evaluated at regular intervals, an indicator can point out the direction of change across different units and through time. In the context of policy analysis, indicators are useful in identifying trends and drawing attention to particular issues. They can also be helpful in setting policy priorities and in benchmarking or monitoring performance.*
>
> *A composite indicator is formed when individual indicators are compiled into a single index on the basis of an underlying model. The composite indicator should ideally measure multidimensional concepts which cannot be captured by a single indicator, e.g. competitiveness, industrialisation, sustainability, single market integration, knowledge-based society, etc.*

The OECD handbook notes the following as benefits from using a composite indicator:

- Can summarise complex, multi-dimensional realities with a view to supporting decision makers.
- Are easier to interpret than a battery of many separate indicators.
- Can assess progress of countries over time.
- Reduce the visible size of a set of indicators without dropping the underlying information base.
- Thus make it possible to include more information within the existing size limit.
- Place issues of country performance and progress at the centre of the policy arena.
- Facilitate communication with general public (i.e. citizens, media, etc.) and promote accountability.
- Help to construct/underpin narratives for lay and literate audiences.
- Enable users to compare complex dimensions effectively.

The potential disadvantages include:

- May send misleading policy messages if poorly constructed or misinterpreted.
- May invite simplistic policy conclusions.
- May be misused, e.g. to support a desired policy, if the construction process is not transparent and/or lacks sound statistical or conceptual principles.

- The selection of indicators and weights could be the subject of political dispute.
- May disguise serious failings in some dimensions and increase the difficulty of identifying proper remedial action, if the construction process is not transparent.
- May lead to inappropriate policies if dimensions of performance that are difficult to measure are ignored.

All the dimensions the AEMC considers in assessing retail market competiveness constitute indicators. Figure 2.1 of the 2015 Retail Competition Review provided an indication of the way the data could be structured in the development of a composite index.

The development of a composite indicator from the underlying indicators could potentially be done in such a way that the data from the two preceding reports could also be included to commence a time series of the composite indicator. The composite index would provide a more thoughtful policy tool for comparing the geographic markets, and would provide an indicator for the ongoing promotion of competition in the national market.

The challenge in developing a composite index is in converting the original data into a normalised data set (this may include the process to convert qualitative data into a quantitative measure), and then developing the weight to be associated to each indicator and the means of combining them. Even were it to be decided that a composite indicator was not viable, the consideration of the normalisation and weighting processes would provide greater clarity about the relative significance of the various indicators.

ECA does not have the resources to progress the development of the AEMC data into a sample composite index but would be happy to assist the AEMC if this idea was seen to have merit. The remainder of the comments in this paper will be based on the assumption that the AEMC retail competition review will not be based on providing a composite index. However, where appropriate thoughts on how an indicator could be quantified and normalised will be offered.

Competitive Market Indicators

In this section ECA will focus on the competitive market indicators being proposed for the 2016 review as included in section 3.3 of the Approach Paper. This will begin with a review of the overall indicators to be used, followed by a consideration of each of them.

List of indicators

The different propositions advanced by the EC and the AEMC for the list of indicators has already been discussed above.

The ACCC has also had reason to consider the definition of “effective competition” in its regulatory proceedings. In a May 2015 declaration inquiry in telecommunications the ACCC wrote[17]:

> *The concept of ‘effective competition’ recognises the practical limitations of the theory of perfect competition, especially when applied to the fixed line telecommunications markets. Some characteristics of effective competition are that it:*
>
> - *is more than the mere threat of competition – it requires that competitors are active in the market, holding a reasonably sustainable market position*

- *requires that, over the long run, prices are determined by underlying costs rather than the existence of market power*
- *requires that barriers to entry are sufficiently low and that the use of market power will be competed away in the long run, so that any degree of market power is only transitory*
- *requires that there be 'independent rivalry in all dimensions of the price/product/service [package]', and*
- *does not preclude one party from holding a degree of market power from time to time but that power should 'pose no significant risk to present and future competition'.*

These five factors are indicators of the extent to which competition constrains market participants to supply products and services of a given quality at prices that are based on efficient costs.

When assessing whether effective competition exists in a relevant market, the ACCC examines certain structural and behavioural factors in the market, including but not limited to:

- *structural factors, including the level of concentration in the market*
- *the potential for the development of competition in the market including planned entry, the size of the market and the existence and height of barriers to entry, expansion or exit in the relevant market*
- *the dynamic characteristics of the market, including growth, innovation and product differentiation as well as changes in costs and prices over time, and*
- *the nature and extent of vertical integration in the market.*

A footnote to the list stated "This is not intended to be an exhaustive list of the characteristics of effective competition."

The table below relates the five indicators the AEMC proposes to use for its assessment and aligns them with the requests from the Energy Council and the ACCC's indicators.

AEMC	EC	ACCC
The degree of independent rivalry in the market	Independent rivalry within the market	requires that there be 'independent rivalry in all dimensions of the price/product/service [package]'
Barriers to retailers entering, expanding or exiting the market	The ability of suppliers to enter the market	requires that barriers to entry are sufficiently low and that the use of market power will be competed away in the long run, so that any degree of market power is only transitory
Customer activity in the market;	The exercise of market choice by customers & Customer switching behaviour	
Whether retail prices are consistent with a competitive market.	Price and profit margins	requires that, over the long run, prices are determined by underlying costs rather than the existence of market power
	Differentiated products and services	the dynamic characteristics of the market, including growth, innovation and product differentiation as well as changes in costs and prices over time

Customer satisfaction with market outcomes;		

The AEMC's inclusion of customer satisfaction with market outcomes is a particularly useful inclusion over and above the indicators chosen by the EC and ACCC. It could be argued that customer satisfaction would be a derivative measure that reflects the combination of all the other indicators. However, it works as a very effective quantitative measure that will incorporate dimensions that might not otherwise be captured. If the AEMC pursues the option to develop a Composite Index the relationship between the satisfaction indicator and the overall indicators could be instructive.

The other noteworthy deviations are that the AEMC and EC both include a dimension of customer activity (and here the ECs two entries of exercise choice and switching have been combined) which the ACCC doesn't, while the EC and ACCC have included product and service differentiation which the AEMC has not. It could be argued that the ACCC's "dynamic characteristics of the market" could be interpreted to include customer activity. The AEMC has included "Product differentiation and number of offers available" as a sub-indicator in independent rivalry. The suitability of that will be considered in the discussion of the indicators.

Customer activity in the market

Customer activity in the market is not merely as the AEMC describes it a "desirable outcome"; it is an essential characteristic of effective competition. It is a significant measure of the degree of independent rivalry in the market.

The difficulty is that it is not directly observable (except in a limited sense by switching data) though well-structured market research can assist. The AEMC proposes three sub-indicators.

- Customer engagement in choosing energy offers (AER data and customer surveys)
- Customer attitudes – key drivers for shopping around and issues inhibiting
- Customer switching – customer survey and AEMO data

The measure could perhaps more appropriately build a story, as follows:

- Consumer awareness
  How aware are customers that they have a choice and the extent of that choice.
- Retailer engagement
  How many retailers have approached the customer.
- Consumer engagement
  How confident are customers that they can make a choice, how satisfied are they with the choice available.
- Consumer attitude
  This should measure the extent to which consumers who aren't satisfied have taken any action, or simply "couldn't be bothered."The measure is the customers who say they aren't satisfied (including don't know) who have not switched or actively investigated an alternative offer.

- Consumer switching
  Would be useful to know if customers investigated alternative plans but didn't switch, why they didn't.
  Correlate customer survey to AEMO data. Measure switching as proportion of those who considered or were approached who actually did switch. Separate category is new switchers – people for whom switch in last 12 months was first in five years.
- Consumer confidence
  A straightforward metric from the consumer survey asking how confident consumers are they can choose the offer that is right for their household.

Customer satisfaction

As the AEMC asserts a consequence of an effectively competitive market should be consumers who are generally satisfied.

The dimension should not, however, be cluttered with anything other than the simple measure of consumer satisfaction overall and whether consumers are receiving value for money.

Other characteristics suggested in the Approach Paper for inclusion under this metric (aspects of specific products, customer complaints) belong in either the independent rivalry metric or the product variety metric.

In future iterations of the research the satisfaction and value for money could be converted from an absolute to a relative scale by also asking consumers the same questions about other services they acquire like mobile phones, broadband, credit cards and water.

The AEMC should also review the literature to determine whether the Net Promoter Score provides a better customer value measure than satisfaction.

Barriers to entry, exit or expansion

Under the traditional structure-conduct-performance model these are among the most important dimensions for measuring competition effectiveness. They are, however, primarily lead indicators; or an early hurdle to competitiveness.

As noted in the Approach Paper there are reasons to be sceptical about the validity of the conclusions drawn from the retailer survey. The quantitative measures of new entry and expansion by relatively new entrants are better indicators than the survey data; however these need to be moderated by the existing structure. It can be much harder to enter a market with low entry barriers that is already crowded than to be the second person into a market which had higher entry compliance costs.

The change in share of retailers is more effectively captured in the overall concentration measure and is an indicator of rivalry.

The measures of contract liquidity are an important factor that could becoming increasingly relevant as a combination of gentailers and prosumers drive out uncommitted capacity.

Independent Rivalry

This is the fundamental concept of the market and hardest to directly measure. The single best measure is market concentration measured using the HHI.

Given the structure of the existing market a top three firms concentration ratio is also a useful indicative measure in addition to the HHI.

The level of switching is a measure of rivalry – but only to the extent that the whole "customer activity in the market" suite of measures can be seen to be part of the measure of rivalry. It should not be counted again in this measure.

Product variety is a particularly good measure and can be captured in two ways.

The first is by an overall count of the average number of products being offered by retailers. In doing so an "offer" that constitutes a discount for either a term commitment or a payment arrangement or both should not be classed as a product variety – it is a pricing element only.

The second is by a total count of new product offerings in the market. This captures the degree of innovation. Retailers should be expected to be retiring older products with the introduction with new ones so over time the average number of offers will stabilise but the new offerings should still be vibrant.

Competitive Retail Prices

It is a common fallacy that a wide variety of prices is indicative of effective competition. In a supposedly perfectly competitive market all providers charge the same price.

In fact, wide price variations can be indicative of ineffective competition because there is clearly a lack of rivalry if a high priced offer can be sustained. Further, the use of breadth of prices can be gamed by retailers choosing to put a high priced plan in the market merely to create the appearance of price variation.

Economists primarily measure competitiveness by mark-up. The Approach Paper dismisses this approach for a variety of reasons. The first is the difficulty of computing "net" margins. This is understood because it involves the internal costs of the company and the allocation of these across markets.

However gross margins do not suffer from this deficiency and the input costs of distribution charges and wholesale energy costs are relatively easy to identify. Revenue is equally easy to identify. Ultimately all the necessary data could be extracted from public sources.

Gross margin is also a more useful measure because it not only captures the potential net margin mark-up from market power, but it also includes the measure of the internal productive efficiency of the retailers.

The AEMC notes that it does not have information gathering powers. That is not a reason not to ask the retailers to voluntarily provide the information in the required format given that it could be acquired by other means. The metric to be determined would be gross margin for the entire market, not by retailer.

It is irrelevant whether the appropriate level of net or gross margin for effective competition is known. A lower margin reflects a progress to being more effectively competitive.

In short prices alone provide very little information about competitiveness, it is only prices related to costs that performs this task.

Other Issues

The research in relation to vulnerable customers and alternative energy offerings (that is, not from the current retailer model) is useful for a better understanding of the market. The challenges faced by the former group actually place limitations on the development of effective competition. The latter will become a more significant as a source of competition in future years and will need to be incorporated in future indices.

Conclusion

It is possible for the AEMC to develop a set of quantitative indicators that can then be combined into a single retail competitiveness index to facilitate comparison between markets and to provide analysis over a series of years.

ECA encourages the AEMC to adopt this approach.

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[1] William J. Baumol, John C. Panzar, & Robert D. Willig (1982). *Contestable Markets and the Theory of Industry Structure*.

[2] That is the total mark up is proportional to the sum of the square of market shares (the Hirschman-Herfindal Index) divided by the own price elasticity of demand.

[3] Selten, R. (1973), "A Simple Model of Imperfect Competition, where Four Are Few and Six Are Many", *International Journal of Game Theory*, 2, 141-201.

[4] Huck, Steffen; Normann, Hans-Theo; Oechssler, Jörg 'Working Paper: Two are Few and Four are Many: Number Effects in Experimental Oligopolies' Bonn Econ Discussion Papers, No. 12/2001

[5] George Yarrow 'The political economy of markets' Essays in Regulation. No 51 2015 Regulatory Policy Institute

[6] Friedrich Hayek 'The Use of Knowledge in Society' American Economic Review, XXXV, No. 4; September, 1945, 519-30.

[7] J. M. Clark 'Toward a Concept of Workable Competition' *The American Economic Review*, Vol. 30, No. 2, Part 1 (Jun., 1940), pp. 241-256. Sosnick identifies eighteen writers who have offered definitions of workability. Stephen H. Sosnick 'A Critique of Concepts of Workable Competition' *The Quarterly Journal of Economics* Vol. 72, No. 3 (Aug., 1958), pp. 380-423

[8] Stephen H. Sosnick 'Toward a Concrete Concept of Effective Competition' *American Journal of Agricultural Economics*, Vol. 50, No. 4 (Nov., 1968), pp. 827-853

[9] The Google Scholar count of citations is 847 for Clark 1940, 159 for Solnick 1958 and only 44 for Solnick 1968.

[10] http://www.weforum.org/reports/global-competitiveness-report-2014-2015

[11] https://www.globalinnovationindex.org/content/page/GII-Home

[12] http://www.itu.int/en/ITU-D/Statistics/Documents/publications/mis2014/MIS2014_without_Annex_4.pdf

[13] https://ec.europa.eu/digital-agenda/en/desi

[14] http://www.oecdbetterlifeindex.org/#/11111111111

[15] http://www.regionalaustralia.org.au/in?ljsight/

[16] OECD *Handbook on Constructing Composite Indicators: Methodology and User Guide* 2008 Available at http://www.oecd.org/std/42495745.pdf

[17] ACCC *Superfast Broadband Access Service declaration inquiry: Discussion paper* May 2015 Available at https://www.accc.gov.au/regulated-infrastructure/communications/superfast-broadband-access-service-declaration-inquiry/discussion-paper

Questions posed by AEMC

Questions on the approach

1. **Is the approach described above appropriate for this year's review of competition and why?**

   As described in commentary above, ECA is generally supportive of the approach. However we disagree that price is an effective measure of competitiveness and recommend that the approach utilise gross margin instead.

   The utility of the Retail Competitiveness Review would be enhanced by the development of a composite index of effectiveness of competition.

Questions on the competitive market indicators

2. **Is there any new evidence about how customers are behaving in retail energy markets and what does that evidence tell us about the level of competition in those markets?**

   Recent research by ECA indicates that as many households are considering installing solar PV as have already installed it. In addition 80% of those with PV are considering batteries while 25% of those considering PV are also considering batteries.

   This indicates that there is a new wave of consumers looking to find alternatives to their existing retailers as a way to managing energy costs. This could be an indicator that consumers are dissatisfied with the options available to them from existing retailers.

   That said, the big three retailers have become quite active in these markets and so the survey response could be a reaction to their market behaviour.

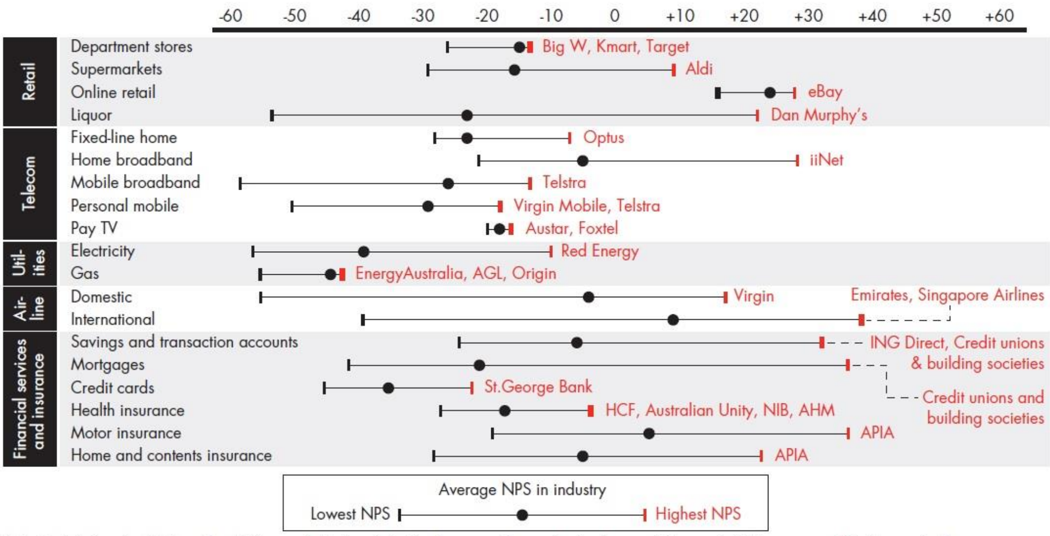
3. **What are the barriers to some customers (such as, customers that remain on standing offers) seeking out a new market offer that better suits their needs?**

   Standing offers are not meant to be uncompetitive offers, they are offers that come with certain explicit consumer protections not available under market offers (e.g. the standard contract). The number of customers on standing offers should not be used as an indicator of competitiveness.

4. **Is there any new evidence about what the outcomes are for customers in retail energy markets (such as their level of satisfaction with their experiences) and what does that evidence tell us about the level of competition in those markets?**

   Industry has learnt that the metric known as a Net Promoter Score correlates better with commercial success than does the simple measure of customer satisfaction.

   Energy suppliers are the worst performing of all industries in two relatively recent comparisons. A 2012 study by Bain & Company[1] rated energy suppliers worst of all industries:



Note: Excludes brands with fewer than 100 respondents. Some industries have more than one leader, because differences in NPS scores are within the margin of error.
Source: Bain & Company NPS Consumer survey, December 2012

More recently the August 2015 NPS benchmarking by Customer Monitor also rated energy suppliers as the worst industry with an NPS of minus 40.[2]

5. **What is the nature of any current or expected barriers to entering, exiting or expanding in any NEM jurisdictions for electricity or natural gas retailers?**

   The cost of multiple jurisdictional compliance requirements is probably more significant than the specific hurdles in any one jurisdiction.

6. **Is there any new evidence that retailers are competing in retail energy markets on price, product and service differentiation to acquire new, and retain existing, small customers, and what does this evidence tell us about the level of competition in those markets?**

   It is always important in assessing market activity to determine whether it is pro-competitive activity or not. Programs in retailers that are designed to "increase customer stickiness" including offerings with fixed terms that do not recover any upfront cost of the retailer are not indicators of a genuinely effectively competitive market.

Questions on the key issues for this year's review

7. **What are the differences between the experiences of vulnerable customers in retail energy markets and other customers; and what do these tell us about how effectively vulnerable customers are able to participate in retail energy markets?**

   One difficulty with the consideration of the way vulnerable customers engage with competitive markets is their limited degrees of freedom of choice. Most notably they have less ability to enter into fixed term contracts, and less ability to trade a capital expenditure now for a lower energy bill in the future.

8. **8. Is there any evidence that new products and services are currently impacting competition in retail energy markets and if so, what is that impact?**

See comments above.

[1] Katrina Bradley and Richard Hatherall *The powerful economics of customer loyalty in Australia* Bain and Company 2012

[2] Customer Monitor *Australia NPS Benchmarking* August 2015