

AEMC 2014 ELECTRICITY PRICE TRENDS REPORT

THIS REPORT LOOKS AT THE FACTORS DRIVING RESIDENTIAL ELECTRICITY PRICES OVER THE NEXT THREE YEARS TO 30 JUNE 2017

New South Wales market offer prices are expected to decrease by 9.7% in 2014/15 and 11% in 2015/16, before increasing by 2.2% in 2016/17

WHAT ARE THE COMPONENTS THAT MAKE UP A TYPICAL NEW SOUTH WALES ELECTRICITY BILL?



Competitive markets

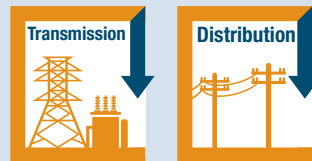
Wholesale costs are rising moderately and retail competition is effective



- Competitive market costs are expected to increase, on average, by 3% per year to 2016/17
- Wholesale costs are increasing moderately due to rising gas prices, although this is partly offset by the effect of an oversupply of generation capacity.
- By shopping around for a better deal, NSW consumers may have saved around 8% in 2013/14

Regulated networks

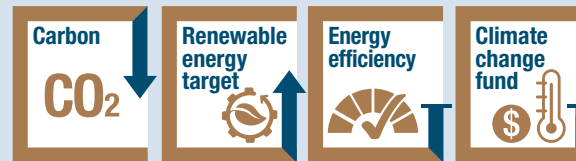
The cost of poles and wires is falling under new regulatory arrangements



- Regulated network prices are expected to decrease, on average, by 7.1% per year to 2016/17
- New rules made by the AEMC are being applied in NSW which better equip the regulator to set efficient network revenues, so consumers don't pay more than necessary
- A draft determination made by the regulator for NSW network businesses is one of the first to be made under the new rules and includes reductions in allowances for both capital and operating expenditure, and lower rates of return
- Benchmarking analysis undertaken by the regulator for draft determinations highlights the relative efficiencies of network companies

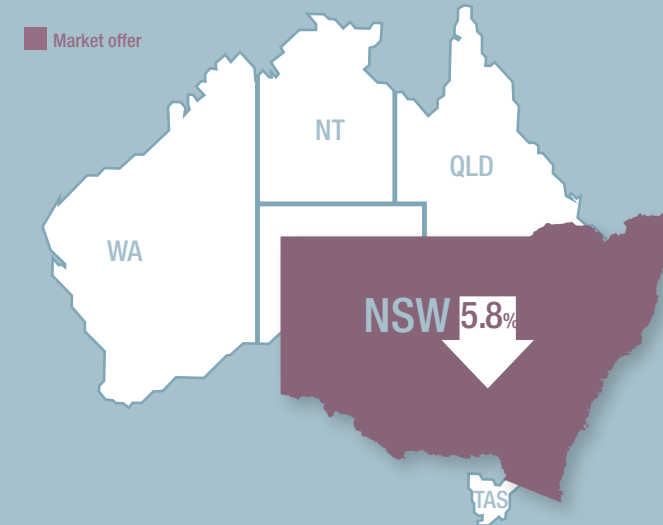
Environmental policies

Environmental policy costs including the Renewable Energy Target continue to impact prices

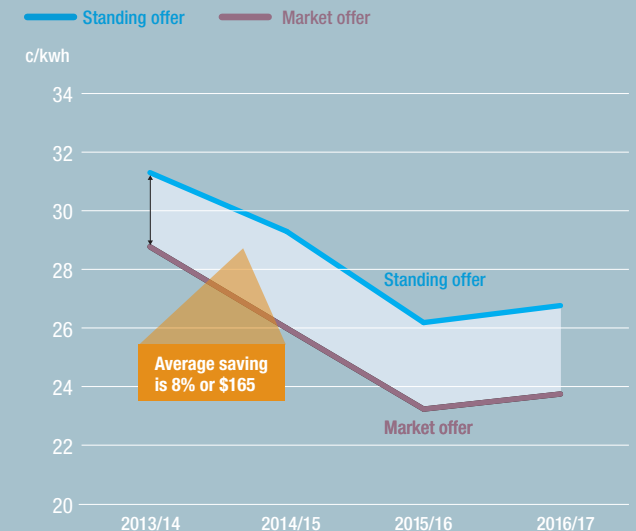


- Prices in the NSW are lower in 2014/15, mainly due to the removal of the carbon price
- Costs associated with the Renewable Energy Target are expected to rise, on average, by 4.6% per year to 2016/17
- Costs associated with other environmental policies such as the NSW Climate Change Fund and Energy Savings Scheme are expected to be stable to 2016/17

WHAT WILL EXPECTED AVERAGE ANNUAL PRICE TRENDS BE BETWEEN JULY 2014-17?



SWITCH AND SAVE: STANDING VS MARKET OFFER IN NSW



For further details including methodology, visit www.aemc.gov.au

AUSTRALIAN ENERGY MARKET COMMISSION

CHANGING THE ENERGY LANDSCAPE: NEW RULES FOR NETWORKS

AN INCENTIVE-BASED REGULATORY FRAMEWORK

NOVEMBER 2012:

Economic Regulation of Network Service Providers rule change

OUTCOMES OF THE 2012 RULE CHANGES

Setting revenue allowances for regulated networks

Regulation based on business efficiency means consumers don't pay any more than necessary for the reliable supply of electricity and gas.



NOVEMBER 2014:

Distribution Network Pricing Arrangements rule change

OUTCOMES OF THE 2014 RULE CHANGES

Structuring prices to empower consumers

Making network prices reflect the cost of providing network services to individual consumers means everyone can make informed decisions about how they use electricity. These rules cover how much individual households will pay for their network services.



Allowed revenues for network businesses are now set using the expenditure required by prudent, efficient operators as a benchmark

Companies have incentives to beat the benchmarks so they can keep some of their savings and pass the rest on to customers

By July 2017 the prices we pay will reflect the different ways we use electricity and the costs of providing it

The rules put consumers in the driving seat

The way we pay for power has to keep pace with our modern lifestyle. When prices reflect how much it costs to use different appliances at different times, consumers are able to make more informed decisions



AEMC rules are used by the Australian Energy Regulator (AER) to set the revenues that network businesses can recover as well as the maximum prices they can charge



The AER is able to review the efficiency of past capital expenditure overspends when assessing future revenue proposals



The AER works out revenues based on analysis of efficient costs including operating and capital expenditure, return on capital, depreciation, and tax liabilities



The AER has to release reports on network business performance to compare business performance across jurisdictions and over time



The rules include clear instructions for networks on the requirements to apply when determining how to structure network prices



There is more consumer consultation on how network prices are structured



Earlier notification of network prices allow retailers and consumers to better prepare for price changes



The right information on costs will help people choose energy services that are right for them – whatever technology changes lie ahead

NOVEMBER 2012

2013

27 NOVEMBER 2014

27 NOVEMBER 2014

2015

2017

AEMC makes new rules on setting network revenue allowances

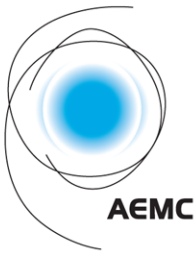
AER develops guidelines in response to the new rules and conducts public consultation under its Better Regulation Program

AER releases first draft revenue determinations under the new rules and guidelines

AEMC makes rules requiring cost reflective pricing for individual consumers

Network companies consult consumers and retailers on new tariffs and submit draft proposals to AER mid-year

Cost-reflective prices phased in no later than mid-year



NEWS

New South Wales electricity prices set to fall over the next two years

The Australian Energy Market Commission (AEMC) today released its 2014 Residential Electricity Price Trends report, which shows prices are set to fall by an average annual 5.8 per cent in New South Wales to 2016/17.

The report analyses trends in the competitive market sectors of the electricity industry; the regulated networks sector; and resulting from government environmental policies. The factors driving each of the three are different, so understanding price trends involves looking into each individually.

AEMC Chairman John Pierce said the factors which had previously led to significant price growth in New South Wales, including the cost of the regulated poles and wires, were now falling.

“The cost of supplying electricity in New South Wales has fallen by 9.7 per cent in 2014/15 following removal of the carbon price, and is expected to fall a further 11 per cent in 2015/16, before increasing by 2.2 per cent in 2016/17,” Mr Pierce said.

Mr Pierce said the main factor driving prices down in New South Wales was lower costs associated with the regulated poles and wires.

“The cost of the regulated network sector is set to fall substantially, including a 25 per cent reduction in distribution network revenues in 2015/16 under a new regulatory framework introduced by the AEMC which is now being applied by the Australian Energy Regulator.

“The proposed reductions in network revenues are based on the regulator’s draft determination last month which included lower capital and operating expenditure and rates of return than those put forward by New South Wales network businesses.

“The new rules better equip the regulator to set efficient revenue allowances for regulated network companies so people don’t pay more than necessary for the maintenance and upgrade of the poles and wires.”

Mr Pierce said competitive market costs are expected to rise by an annual average 3 per cent to 2016/17.

“Wholesale costs are increasing moderately due to rising gas prices in New South Wales, although this is partly offset by the effect of an oversupply of generation capacity mainly due to lower demand which is putting downward pressure on prices.

“Increased competition in the New South Wales electricity markets is also providing opportunities for consumers to switch electricity providers and save around 8 per cent on a better market offer – or \$165 on their annual bill.”

“We would encourage consumers to take advantage of competition between service providers by shopping around and choosing a better deal to save on their bills.”

The removal of the carbon price has cut electricity prices in 2014/15, however other environmental policies like the Renewable Energy Target continue to place upward pressure on prices in New South Wales.

"Costs associated with the Renewable Energy Target are expected to rise by an annual average 4.6 per cent to 2016/17 in New South Wales," Mr Pierce said.

The annual Residential Electricity Price Trends report is part of the AEMC's work to strengthen consumer engagement in energy markets.

The full report and further information is available at www.aemc.gov.au.

About the AEMC

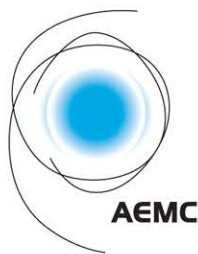
We are the independent body responsible since 2005 for providing advice to Australian governments on development of the electricity and gas sector. We make statutory energy market rules which are applied and enforced by the Australian Energy Regulator (AER).

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EMBARGOED 1pm AEDT, 11 December 2014



New South Wales: Household electricity price trends

New South Wales residential electricity prices expected to fall due to moderating network costs

The 2014 Residential Electricity Price Trends report identifies factors driving electricity prices over the three years to 2016/17 in all states and territories. By providing this information at the request of the COAG Energy Council, the AEMC is seeking to strengthen consumer engagement in the market.

The Residential Electricity Price Trends report presents expected movements in prices for a representative consumer in New South Wales (NSW), using an annual consumption level that was provided to us by the NSW Government.

- The annual consumption of the representative consumer in NSW is assumed be 6,500 kilowatt-hours (kWh).
- Average electricity prices are specific to the representative consumer and may not reflect the pricing outcomes for all residential consumers.

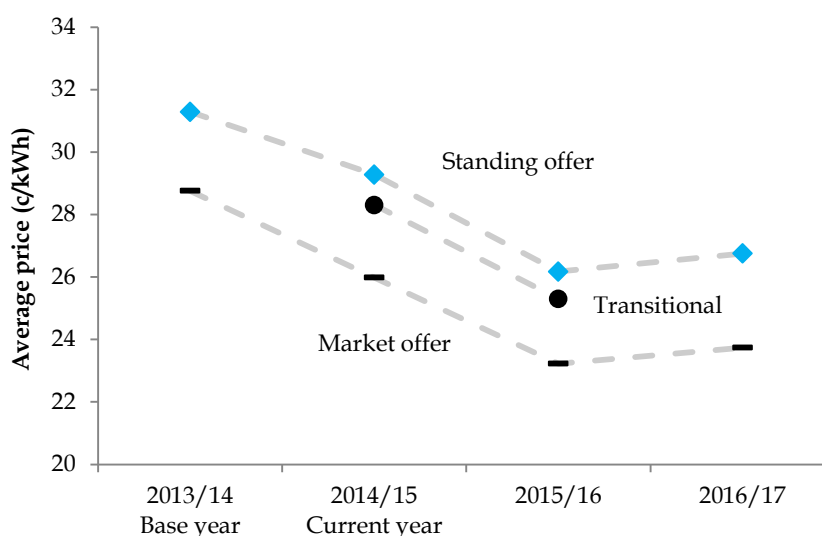
To undertake this work, we analysed trends in the wholesale and retail market sectors of the industry, the regulated networks sector and the impact of government environmental policies. We report on how these trends affect overall prices paid by residential consumers, in order to identify the relative contribution to the price movements of these drivers.

Key findings for NSW

On average, *market offer* prices in NSW have decreased by 9.7 per cent in 2014/15 for the representative consumer, and are expected to decrease by 11 per cent in 2015/16 before increasing by 2.2 per cent in 2016/17. This is equivalent to an annual average decrease of 5.8 per cent over the reporting period, as shown below.

Consumers may have saved around 8 per cent, or \$165, if they switched from the regulated offer to the representative *market offer* in 2013/14. Actual savings will depend on individual circumstances, such as level of consumption. More savings are possible if consumers shop around and choose the best *market offer* to meet their needs.

Trend in NSW *market offer* and *standing offer* price



The trend in NSW residential electricity prices over the reporting period is being driven by the repeal of the carbon price and expected decreases in network prices

In July 2014, there were 30 *market offers* available to residential consumers and the difference in the price between the highest and lowest offers was up to 8.1 c/kWh for the representative consumer.

The NSW Government has removed retail price regulation, effective 1 July 2014. Consumers on a regulated offer at this time were placed onto a transitional offer, although they may choose a *standing offer* or *market offer* at any time.

Drivers of price trends

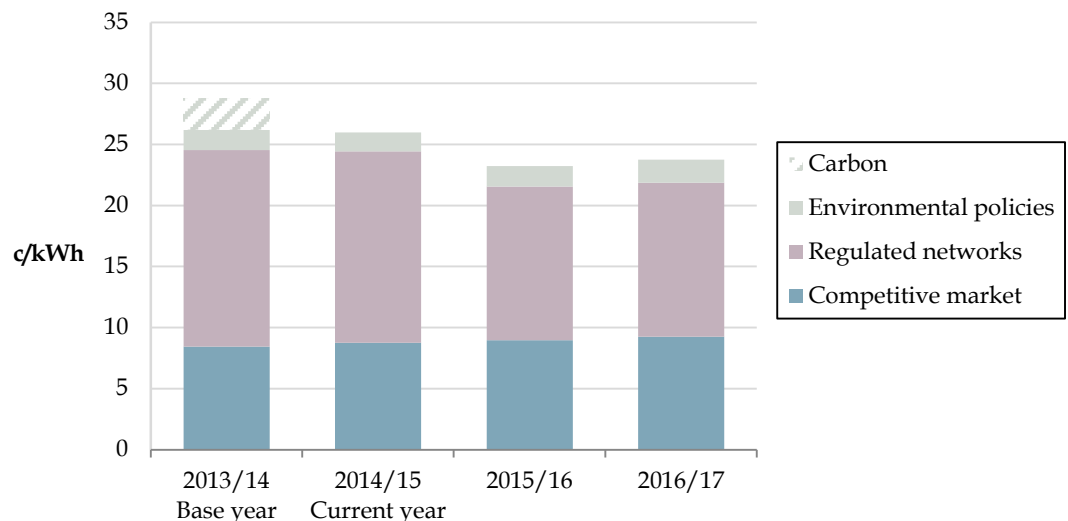
The key drivers of price decreases in NSW during the reporting period are the repeal of the carbon price and decreases in regulated network prices.

Market offer prices have fallen by around 9.7 per cent in 2014/15, mostly due to the removal of the carbon price. Distribution network prices are also lower due to the application of a lower regulated rate of return in the Australian Energy Regulator's transitional decisions for this year.

The trend in 2015/16 and 2016/17 reflects a decrease in distribution network prices in 2015/16, as set out in the Australian Energy Regulator's draft decisions for the 2014-19 regulatory period. The potential impact of these decisions is discussed below.

In 2014/15, it is expected that the total electricity bill for a representative consumer in NSW will consist of around 60 per cent regulated network prices, 34 per cent competitive market costs and 6 per cent environmental policy costs, as shown below.

Trend in NSW supply chain components



Regulated network prices

Regulated network prices consist of the costs of the transmission and distribution networks.

- In 2014/15, it is expected that transmission network prices will make up around 14 per cent of the total bill for the representative consumer and distribution network prices will make up 47 per cent.
- Regulated network prices are expected to decrease at an average annual rate of 7.1 per cent between 2013/14 and 2016/17.

In November 2012, the AEMC made new rules relating to how networks are regulated by the Australian Energy Regulator. The new rules improve the capacity of the regulator to determine network prices. Under the new rules, the regulator is better equipped to develop methods and processes to achieve efficient outcomes for consumers, including how the rate of return on capital is set.

The new rules apply to the transitional determination for 2014/15 and, ultimately, the final determination for the 2014-19 regulatory period, which will be made in April 2015. For this report we have estimated network prices based on the Australian Energy Regulator's draft decisions for 2014-19, which were released on 27 November 2014.

The Australian Energy Regulator has proposed large reductions in the regulated rate of return, and capital and operating expenditure, compared to the 2009-14 regulatory period. The draft decision reflects changed financial market conditions, expected falls in peak

demand, changes to risk management practices and potential efficiencies in how network services are provided.

Actual network prices will depend on the Australian Energy Regulator's final determination to be made by 30 April 2015.

Transmission network

- Transmission network prices have increased by around 4.5 per cent between in 2014/15 and are expected to decrease by 1.3 per cent in 2015/16 and 4.9 per cent in 2016/17. The trend in 2015/16 includes an adjustment for \$71 million of revenue that was under-recovered by TransGrid in 2013/14.
- In its draft decision, the Australian Energy Regulator has proposed a regulated rate of return of 7.24 per cent, which is less than the 10.05 per cent allowed during the previous regulatory period. Proposed capital and operating expenditure is also notably less than actual spending by the networks in 2009-14.

Distribution network

- Distribution network prices have fallen by around 4.3 per cent in 2014/15 and are expected to decrease by 25 per cent in 2015/16 before increasing by 2.1 per cent in 2016/17.
- In its draft decision, the Australian Energy Regulator has proposed a regulated rate of return of 7.15 per cent for all three distribution network businesses, which is less than the 10.02 per cent allowed during the previous regulatory period. Proposed capital and operating expenditure is also materially lower than actual spending by the networks in 2009-14.
- The Australian Energy Regulator is currently consulting on whether the proposed reduction in operational expenditure should be implemented as a step-change in 2015/16 or implemented more gradually over multiple years. The price trend presented in this report is based on all savings being implemented in 2015/16, which reflects the Australian Energy Regulator's draft decision.

Competitive market costs

Competitive market costs include the wholesale energy component and the costs associated with retailing electricity to residential consumers.

- Between 2013/14 and 2016/17, competitive market costs are expected to increase at an average annual rate of 3.1 per cent. Wholesale energy costs are expected to be relatively constant, increasing by around the rate of inflation due to the current oversupply of generation in the market.

The AEMC's 2014 Retail Competition Review found that there are 14 competing retailers in NSW and 60 per cent of consumers are on a *market offer* contract. About 18 per cent of consumers changed their retailer in 2013.

Environmental policy costs

Environmental policies that apply in NSW during our reporting period are the:

- carbon pricing mechanism;
- Renewable Energy Target;
- Climate Change Fund; and
- NSW Energy Savings Scheme.

Costs associated with the carbon pricing mechanism apply only in the base year of our reporting period (2013/14) as the policy was repealed with effect from 1 July 2014.

- In 2013/14, these costs made up around 8.8 per cent of the total bill for the representative consumer in NSW.

In 2013/14, Renewable Energy Target costs made up around 4.3 per cent of the total bill for the representative consumer, Climate Change Fund costs made up 1.4 per cent and Energy Savings Scheme costs made up 0.2 per cent.

Price drivers vary between states and territories, although there are some common underlying trends.

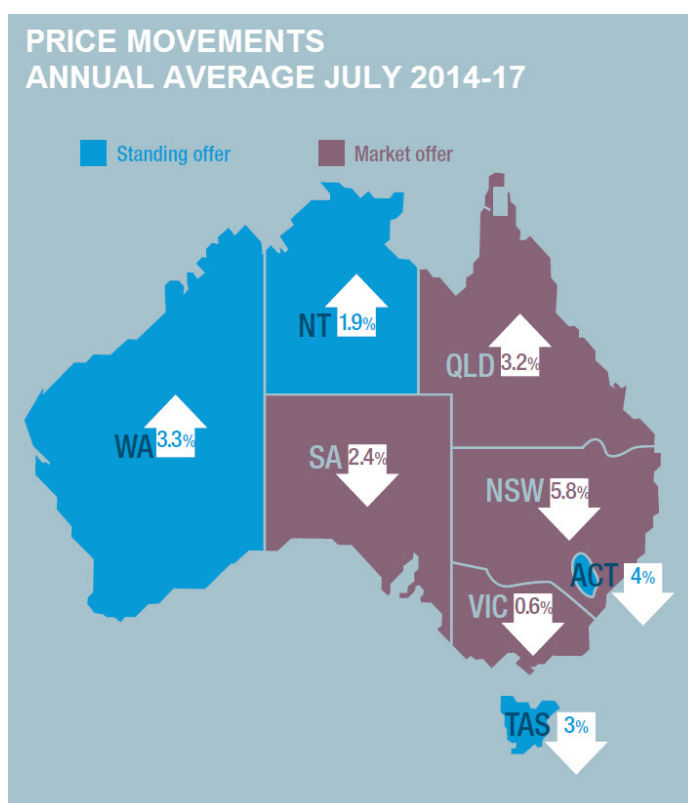
- Based on the current Renewable Energy Target legislation, scheme costs in NSW are expected to increase, on average, by 4.6 per cent per year between 2013/14 and 2016/17.
- The costs associated with the Climate Change Fund and Energy Savings Scheme are not expected to change substantially during the reporting period.

Jurisdictional price trends

Trends in residential electricity prices differ between states and territories. In most jurisdictions, prices are expected to have fallen in 2014/15 following the removal of the carbon pricing mechanism. The extent of this decrease varies between jurisdictions, as the savings are offset by other factors. In 2015/16 to 2016/17, price movements are mixed, reflecting different jurisdictional drivers.

On average across the three year period from 2013/14 to 2016/17, prices are relatively stable or decreasing in most jurisdictions. The exceptions to this trend are Western Australia, Queensland and the Northern Territory, where prices are expected to increase, on average, during the same period.

Our analysis of trends in *market offers* covers Queensland, NSW, Victoria and South Australia. In other jurisdictions, our analysis is based on trends in the regulated *standing offer* price. In jurisdictions where both *standing* and *market offers* are available, residential consumers are able to shop around for the best offer from retailers.



Information sources

Information for this report has been sourced from jurisdictional governments and regulators. We also sourced information from the Australian Energy Regulator in relation to transmission and distribution network costs and from retailers operating in the relevant states for our analysis of *market offer* prices.

The AEMC also commissioned independent modelling of wholesale energy purchase costs, carbon pricing mechanism costs and Renewable Energy Target costs. Our modelling was undertaken based on current knowledge and assumptions as well as existing legislation and is available on our website.

About the AEMC

The Australian Energy Market Commission is the independent body responsible for providing policy advice to Australian governments on the electricity and gas sector. It makes rules that are applied and enforced by the Australian Energy Regulator.

The Residential Electricity Price Trends report is part of the AEMC's work to empower families, businesses and industry to participate confidently in all parts of the energy supply chain, where they desire to do so. It provides annual information to help consumers better understand the factors which drive residential electricity prices.

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