Affordability in retail energy markets

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AUSTRALIAN ENERGY REGULATOR

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Introduction

What we pay for our energy has been front of mind for Australians for some time - the price we pay for our electricity and gas has gone up over the last decade.

At the same time as rising energy prices, income growth has been flat in many households.

People's lived experience of energy prices differs markedly. Customers pay different prices for their energy depending on where they live, how much network infrastructure is required to supply them, the intensity of competition among retailers in their local area and whether they are eligible for concessions.

Customers also use different amounts of energy depending on how many people live in their home, their local climate, the energy efficiency of their home and appliances, and whether they have access to gas or only electricity.

This *Affordability in retail energy markets report* provides a high-level analysis of energy affordability in New South Wales, Queensland, South Australia, the Australian Capital Territory, Victoria and Tasmania with a focus on the affordability of energy for low income households. It also provides an early analysis of the effect of the Default Market Offer arrangements introduced by the Australian Government in July 2019. These regulations, which are administered by the AER, place a cap on what retailers can charge customers on electricity standing offers in New South Wales, South East Queensland and South Australia.

In a departure from our usual practice of presenting this data as part of our *Annual report on compliance and performance of the retail energy market*, this year we have presented this data in a standalone form. The data contained in the report indicates some modest improvements in energy affordability over the past year, although energy is still difficult to afford by historical standards.

We know that paying energy bills is a major concern for many Australian households, especially those on low incomes. Our report shows that low income households on a typical market offer spent 4.8 to 7.6 per cent of their disposable income on electricity and 2.6 to 5.5 per cent on gas.

For customers on standing offers the cost of their energy is typically even higher. For example, for a low income household in South Australia, the difference between annual electricity bills on the median market offer relative to the median standing offer is $532. This translates into a difference between spending 9.9 per cent or 7.6 per cent of their disposable income on electricity.

We encourage households, where possible, to seek out the best possible deal they can for their circumstances. *EnergyMadeEasy* – our independent and free of charge price comparison website – provides the information you need to compare the various offers in your area so you can see if you would be better off under a different deal. Choosing the right deal can make a big difference to your energy bills.[1]

1 *EnergyMadeEasy* is available for customers in Queensland, NSW, SA, Tasmania and the ACT. Victorian customers can use the Victorian Energy Compare website.

1. How to navigate this report

The main purpose of this report is to look at how energy affordability changed over the period 2017 to 2019.

Chapter 2 helps set the scene. It provides an overview of how we characterise energy affordability and highlights the gap that has emerged between the rise in energy prices and income growth. We also look at measures being taken to help address energy affordability.

Chapter 3 provides a description of how we measure affordability, including a discussion of the key inputs for our analysis. These include income, gas and electricity offers for standing and market customers as well as energy usage. Chapter 4 discusses trends in these key inputs from 2017 to 2019 across the regions covered by this report.

In chapter 5 we bring this work together to show how energy affordability has changed over the past three years. Chapter 6 focuses on trends over the past three years in the use by retailers of conditional discounting as a tool for advertising energy offers. While the discounts look attractive, they have the potential to cause financial stress where customers don't, for whatever reason, meet the conditions they need to get the discounts. These conditional discounts can act like a penalty for households with limited capacity to pay.

To allow the reader an 'at a glance' snapshot of key information by region, including, amongst other measures, affordability, customer numbers, average usage and average annual bills, chapter 7 contains easy to read jurisdictional 'dashboards'.

For readers interested in delving into the detail behind the analysis contained in our report, appendix A contains our methodology used to analyse affordability. Appendix B contains our analysis of the early effects of the introduction of the Default Market Offer (DMO) on 1 July 2019, a key policy initiative to reduce excessive prices paid by electricity customers on standing offer contracts. Finally, appendix C contains the methodology we used to calculate representative DMO bills.

2. Background

Energy affordability has continued to be a key issue for many households, particularly those on lower incomes and for policymakers who are looking at options for improving affordability.

2.1 What is energy affordability?

We measure energy affordability based on how much of their disposable income households spend on energy bills. Disposable household income represents the income available to households to pay for goods and services after income taxes, levies and surcharges.

Energy bills and the prices customers pay for their energy will differ depending on where they live, how much network infrastructure is required to supply energy to them, how much competition there is among retailers in their area and what offer they are on. Some customers may also be eligible for a concession or rebate.

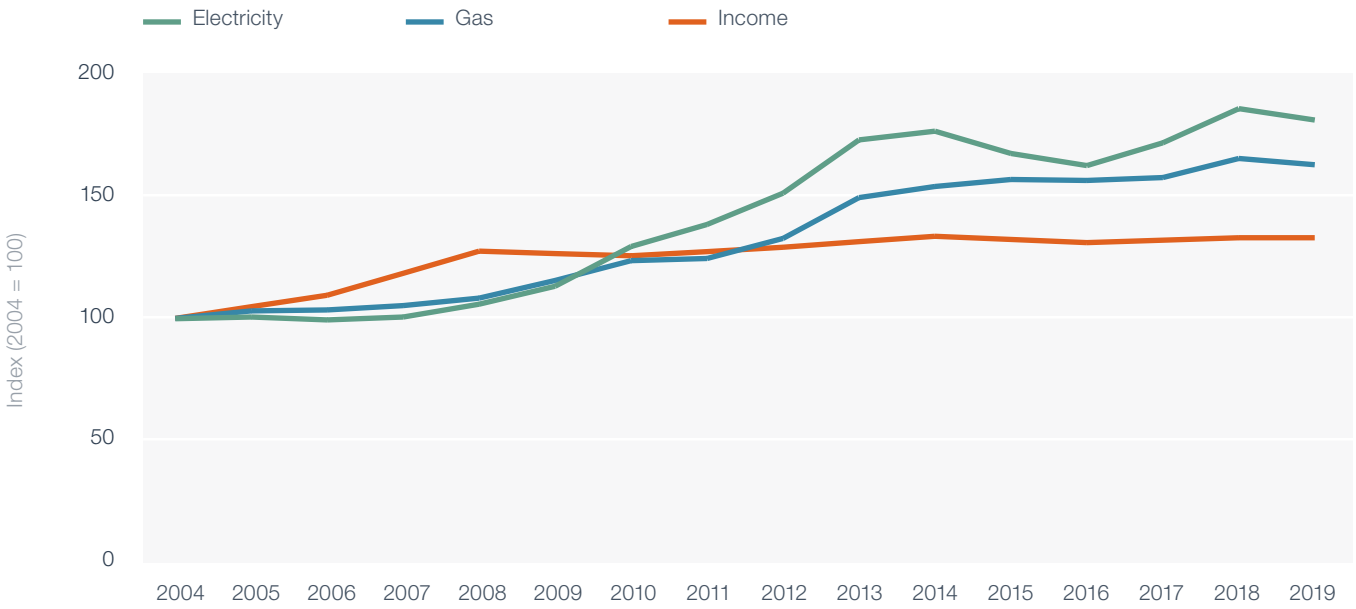
Customers use different amounts of energy depending on a range of factors, for example:

- how many people live in their home
- how the local climate impacts their heating and cooling needs
- the energy efficiency of their home and their appliances
- whether they have access to gas or only electricity
- what appliances they have and how they use these appliances within the home.

2.2 Energy prices remain high by historical standards

Figure 1 shows the widening gap between income and energy prices, with electricity and gas prices increasing markedly from about 2008 to 2014. Electricity prices increased by around 10 per cent annually over this period and gas prices increased by around 7 per cent annually. Electricity prices fell for two years from 2014 but then again rose sharply. They are currently just below the peak reached in 2018. Gas prices have grown at a similar pace to electricity prices over the past five years. And like electricity, although we've seen a fall in the most recent year, they are still much higher than they were in 2014. While the long term trend in energy prices over the past ten years has been upward, incomes have remained flat over the same period.

Figure 1: Long term trends in energy prices and income



Source: Electricity and gas index – Australian Bureau of Statistics (ABS), Consumer Price Index, cat. No. 6401.0, various years; income index – ABS, Household Income and Wealth, Australia, 2017-18.

2.3 Affordability is being tackled on a number of fronts

Rising electricity and gas prices, coupled with perceptions of poor retailer behaviour, contributed to a heightened focus on retail energy markets in recent years. This included several assessments of energy markets by governments, regulators and other bodies relevant to improving affordability.

Key assessments which have underpinned recent and ongoing policy intervention in energy markets are:

- The Australian Competition and Consumer Commission's (ACCC) 'Restoring electricity affordability and Australia's competitive advantage' review (Retail Electricity Pricing Inquiry - REPI) and subsequent Inquiry to monitor the effects of policy changes since REPI.[2]
- The 'Independent Review into the Electricity and Gas Retail Markets in Victoria' (Thwaites Review).[3]

These reviews made recommendations to improve outcomes across the energy supply chain, including reducing costs and increasing the effectiveness of competition. A number of recommendations were specifically focused on improving outcomes for customers facing difficulties meeting their energy costs, including changes to concession arrangements and hardship programs.

2 ACCC, Restoring electricity affordability and Australia's competitive advantage, Retail Electricity Pricing Inquiry—Final Report, June 2018. In August 2018, the then Treasurer directed the ACCC to hold a separate public inquiry to monitor the prices, profits and margins in the supply of electricity in the National Electricity Market (NEM).

3 Thwaites, T, Faulkner, P, and Mulder, T, *Independent review into the electricity and gas retail markets in Victoria*, August 2017. www.energy.vic.gov.au/about-energy/policy-and-strategy.

These recommendations were in addition to a body of work already underway in the energy sector to drive better outcomes for customers. Key processes implemented or initiated in recent years that will contribute to improved energy affordability include:

- reforms to customer hardship frameworks overseen by the Australian Energy Regulator (AER) and Essential Services Commission of Victoria (ESC) to strengthen protections for customers facing payment difficulties.
- rule changes to ensure customers are better informed about changes in the price they are charged for energy, and to allow easier comparison of offers in the market.
- the rollout of smart meters and ACCC work on implementing electricity consumer data rights – which will allow customers to make more informed energy choices.
- ongoing work by the AER to improve how network determinations are made and to provide more customer-focused outcomes.

While beyond the timeframe looked at in this report, measures were introduced on 1 July 2019 that will have an immediate positive effect on energy affordability for some customers on standing offers.

The DMO price, set by the AER, aims to remove the most expensive standing offers by capping the price that retailers can charge those customers. New rules will also assist customers to compare offers in the market, by using the DMO as a reference price in all advertising. See appendix B for more details.

The Victorian Default Offer (VDO), which flowed from the Thwaites Review, was also introduced on 1 July 2019. The VDO replaces standing offers in Victoria and aims to provide customers with access to a 'fair' priced electricity offer.

3. How we assess energy affordability

This section provides an overview of how we assess energy affordability over the past three years. See appendix A for further details.

This report focuses on the five regions where the AER has a regulatory role, and also covers Victoria. Western Australia and the Northern Territory are not covered.

To analyse affordability, we focus on the proportion of disposable household income spent on energy costs annually. We examine trends in energy prices, usage and income over the years 2017 to 2019 by region.

The key inputs into our analysis include:

1. **Offers**
   We sourced electricity and gas offers in each region from the *EnergyMadeEasy* website at June 2017, June 2018 and June 2019. For Victoria, we sourced offers at these same dates from the Victorian Energy Compare website. Our analysis is limited to generally available single rate offers.
2. **Usage**
   We estimated average annual residential electricity usage in each region based on data provided by distribution network businesses. This data is updated annually in response to Regulatory Information Notices issued by the AER. Gas usage levels were obtained though consumption benchmark surveys commissioned by the AER.
3. **Annual bills**
   We estimated annual bills for each offer by applying our usage assumptions to the usage charges in each offer, and then adding fixed charges. Our analysis is based on the median annual bill cost under both market and standing offers. For low income households, we adjusted annual bills to account for relevant government concessions.
4. **Income**
   We use ABS equivalised income data to represent household disposable income.[4] We present this data as the average for all households and also the average for low income households. This data is updated by the ABS every two years. Please see appendix A for more details.

4 An explanation of equivalisation is available under 'key concepts' in ABS, 6523.0 – Household income and wealth, Australia, 2015–16, available at https://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/6523.0~2015-16~Main%20Features~Key%20Concepts~3

4. Income, usage and offer trends 2017-2019

We separately analysed trends in the key drivers of energy affordability—income, retailer offers and usage. The combined effects of these factors determine the affordability of energy for households.

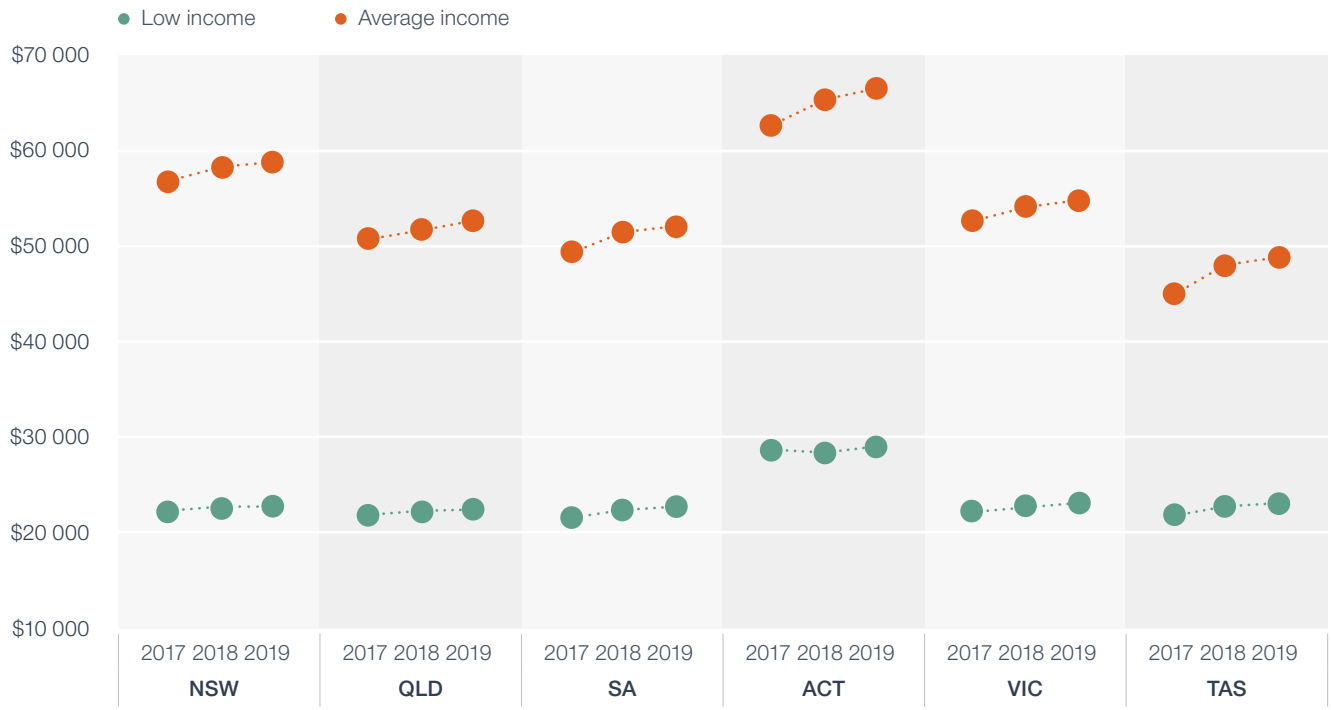
4.1 Income trends

The level of disposable income is a key element in assessing affordability of essential services such as energy.

In July 2019, the Governor of the Reserve Bank of Australia (RBA) noted there had been a protracted period of low income growth.[5] This includes the three year period covered by our analysis.

Low income households experienced lower income growth than other households over the past three years in NSW, Queensland, the ACT and Tasmania, increasing the affordability gap for households with the most limited capacity to pay. Income growth for low income households in Victoria and South Australia marginally exceeded other households in percentage terms. But this still represented less additional income in dollar terms over this period for low income households.

Figure 2: Low and average household incomes over three years



Note: Nominal disposable income. Uses ABS data points from 2016 and 2018. The data for the year 2017 are the average of 2016 and 2018. The 2019 data reflects the 2018 data adjusted for inflation.[6]

5 RBA Media release: 'Statement by Philip Lowe, Governor: Monetary Policy Decision', 2 July 2019. https://www.rba.gov.au/media-releases/2019/mr-19-18.html.

6 See appendix A for a more detailed methodology.

Incomes differ across regions. The variation in incomes is less pronounced for low income households than for all households. The average annual income for low income households was between $22 500 and $23 300 in 2019 across all regions except the ACT ($29 000). Average income across all households in 2019 ranged from around $49 000 in Tasmania, to $66 000 in the ACT. Higher average incomes in the ACT contributed to better energy affordability outcomes in that region.

4.2 Usage and price trends

The amount paid by households for energy is determined by the volume consumed and the price charged by retailers.

Energy prices will reflect both the underlying costs of producing and supplying energy to households, and the level of competition in the market. Usage will vary in response to changes in technology, consumer behaviour and climate.

Our analysis focuses on changes in price and usage at a regional level. We note, however, that the ability for particular households to access the lowest cost offers in the market, or to adjust their consumption, may be constrained.

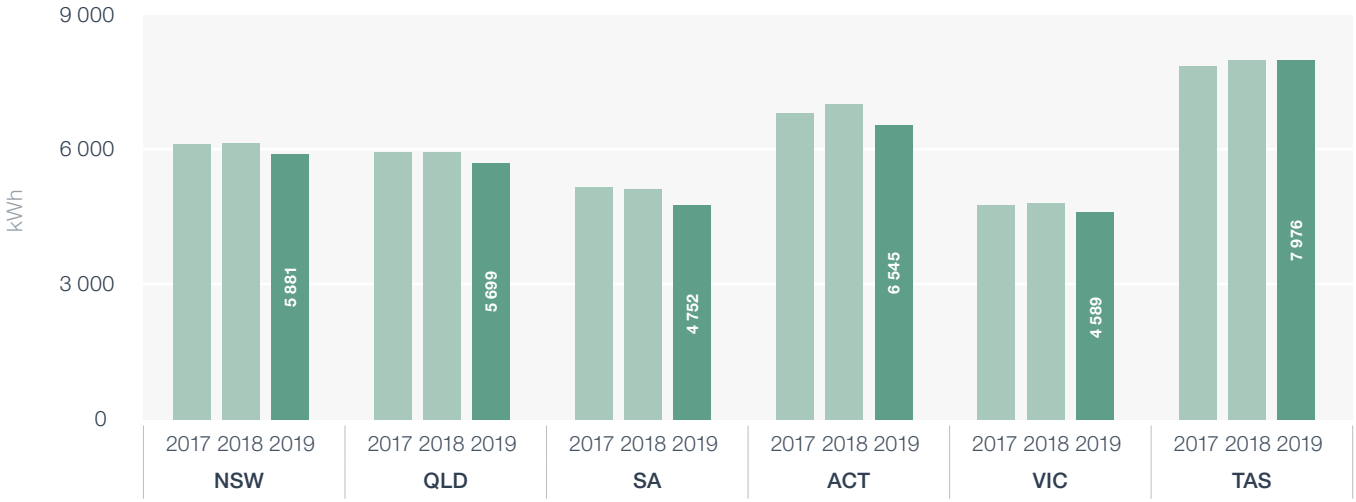
4.2.1 Trends in electricity usage

Usage charges represent the largest component of electricity bills for most households. The level of usage can therefore significantly impact on energy affordability.

As shown in figure 3, average household electricity usage in 2019 decreased from the previous year in all regions, although only marginally in some cases. This is consistent with a longer term trend of reduced usage, driven largely by the uptake of rooftop solar photovoltaic systems. Improving energy efficiency of homes and appliances has also contributed. Given the drivers of reduced usage, these average outcomes likely obscure a widening gap between usage for those households with the capacity to adopt new technology and other households. The former group would benefit from substantial reductions in usage, while usage of other households would be expected to be relatively consistent over time.

Electricity usage is highest in the ACT and Tasmania. Key drivers of electricity usage are climate (with greater heating and cooling requirements in some regions), and the penetration of gas as an alternative fuel. Tasmania in particular has low gas penetration for households. Conversely, most households in Victoria have both electricity and gas connections, resulting in the lowest average household electricity consumption.

Figure 3: Trends in average annual household electricity usage (kWh)



4.2.2 Trends in electricity offers

To analyse how retailers have changed their market and standing offers, we applied a consistent usage level (at 2019 levels) to all offers over the past three years.

In 2019 the median market offer for electricity decreased or was steady across all regions except Victoria (where it increased 3 per cent). Conversely, standing offers generally rose or were steady. This followed increases in the level of the median market and standing offer in nearly all regions between 2017 and 2018, which largely reflected increases in wholesale costs.

Market offers remain highest in South Australia, with customers paying over 40 cents per kilowatt hour (kWh) on the median offer in 2019. Offers are lowest in the ACT, with customers on the median market offer paying 26 cents per kWh. Regional differences are similar across standing offers, with South Australian offers the most expensive (54 cents per kWh) and ACT and Tasmanian offers the cheapest (31 cents per kWh).

Figure 4: Trends in median electricity market offer price (cents per kWh)

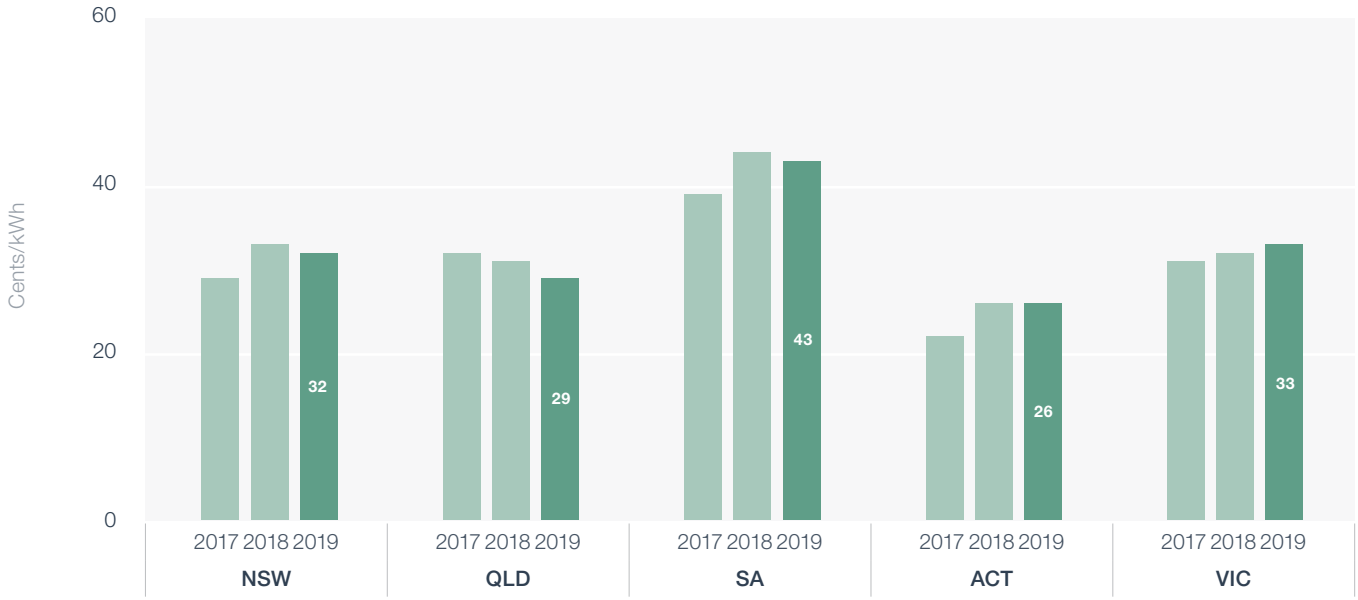
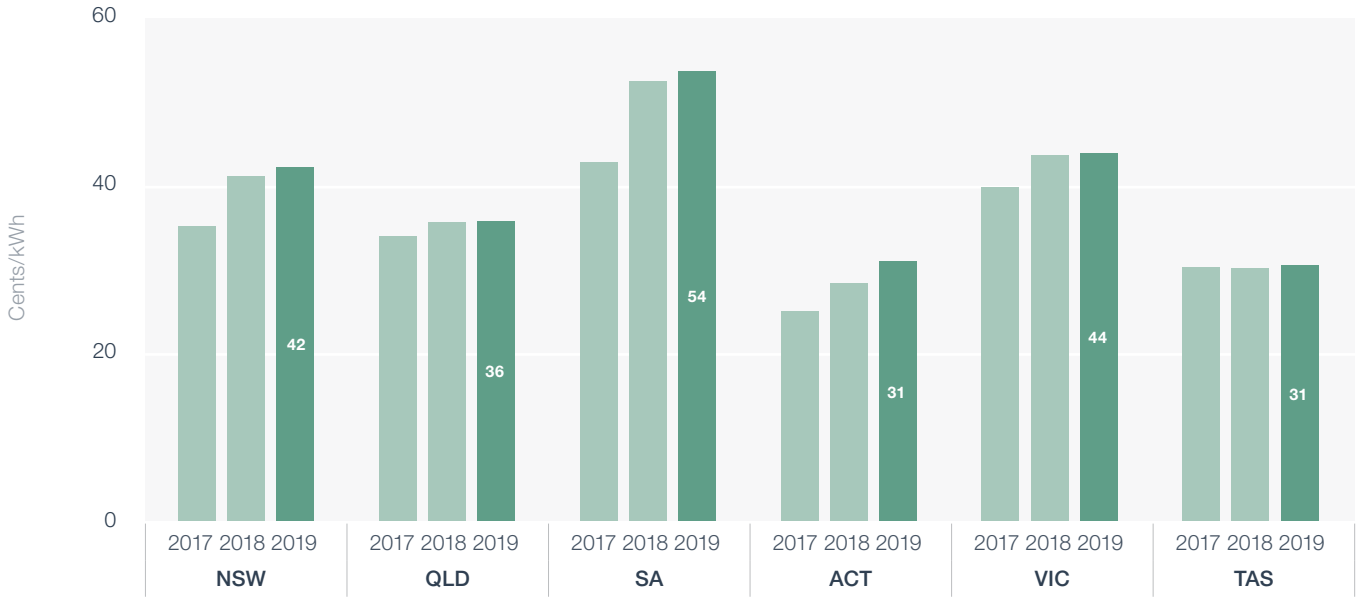


Figure 5: Trends in median electricity standing offer price (cents per kWh)



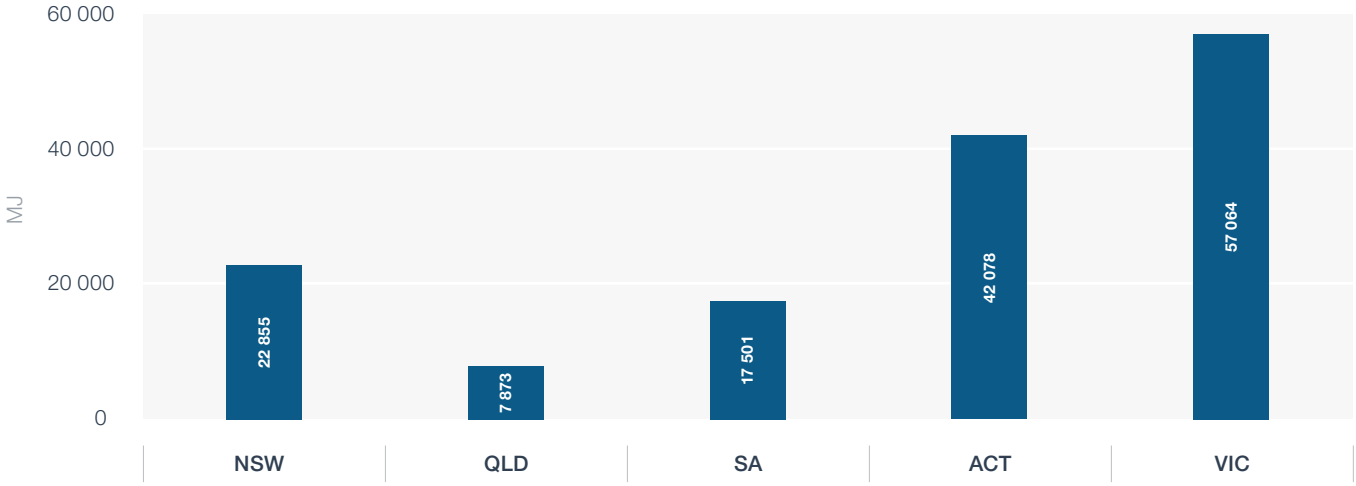
4.2.3 Gas usage

As for electricity, gas usage charges represent the largest component of gas bills for most households.

Gas is primarily used in residential homes for space heating, water heating and cooking. The requirement for space heating is heavily dependent on climate. Regions with colder climates, therefore, tend to use the most gas on average (such as Victoria and the ACT). The reverse is also true with Queensland using the least gas due to having a warmer climate.

For our gas analysis, we used ACIL Allen's 2017 *Energy Consumption Benchmarks* report, which estimates average gas usage of a household in each region.[7] This report was commissioned by the AER, with benchmarks updated every three years. Lack of annual data means that we are unable to explore changes in usage over our period of analysis.

Figure 6: Average annual household gas usage (MJ)



4.2.4 Trends in gas offers

We analysed how retailers changed their market and standing offers by applying a consistent usage level to all offers over the past three years.

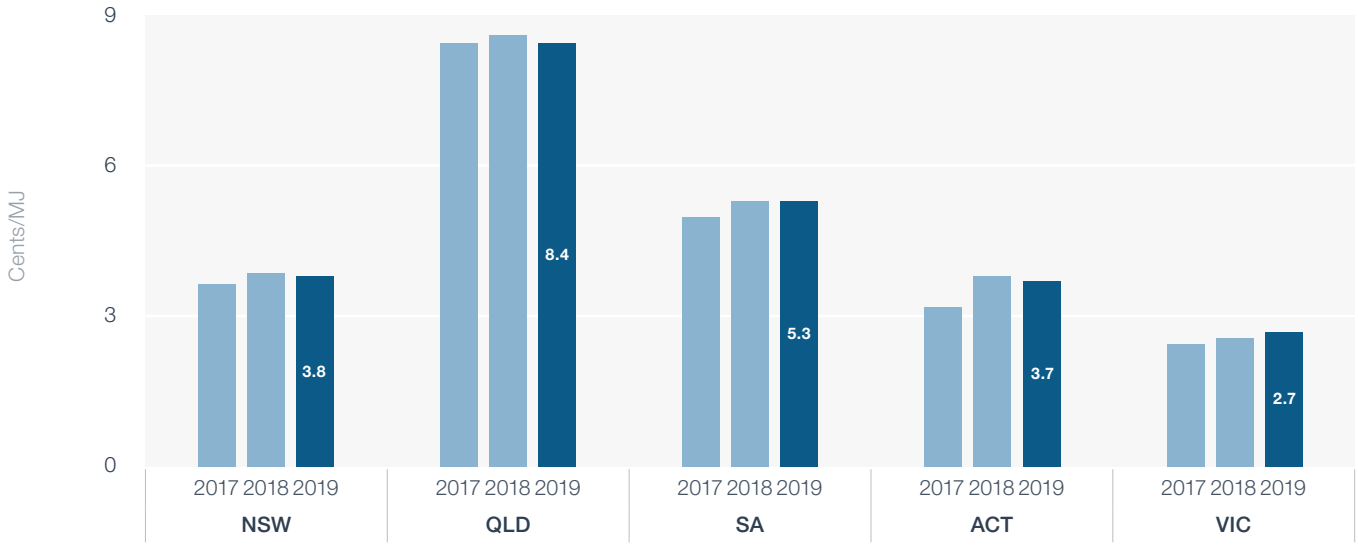
Gas market offers eased marginally or were steady in 2019 in all regions except Victoria, while standing offers generally rose or were steady. This followed increases in market and standing offers in all regions between 2017 and 2018. As with electricity, this rise largely reflected increases in wholesale costs as the supply-demand balance remained tight and domestic customers were exposed to international gas prices due to local demand competing with LNG exports.

The median market offer was cheaper than the median standing offer in all regions. The largest difference between the median standing and market offer was in Victoria, with standing offers 24 per cent more expensive. In other regions the difference between standing and market median offers ranges from 6 per cent (in Queensland) to 18 per cent (in NSW).

Gas is most expensive per unit in Queensland, with the median market offer at 8.4 cents per megajoule (MJ) in 2019. Gas is cheapest per unit in Victoria, at 2.7 cents per MJ. The lower price per unit in Victoria is likely related to a greater number of gas users in the region, creating savings due to economies of scale in the network costs for supplying gas. There is also higher household usage, meaning that fixed supply charges are spread over a greater base when assessing costs on a per unit of usage basis.

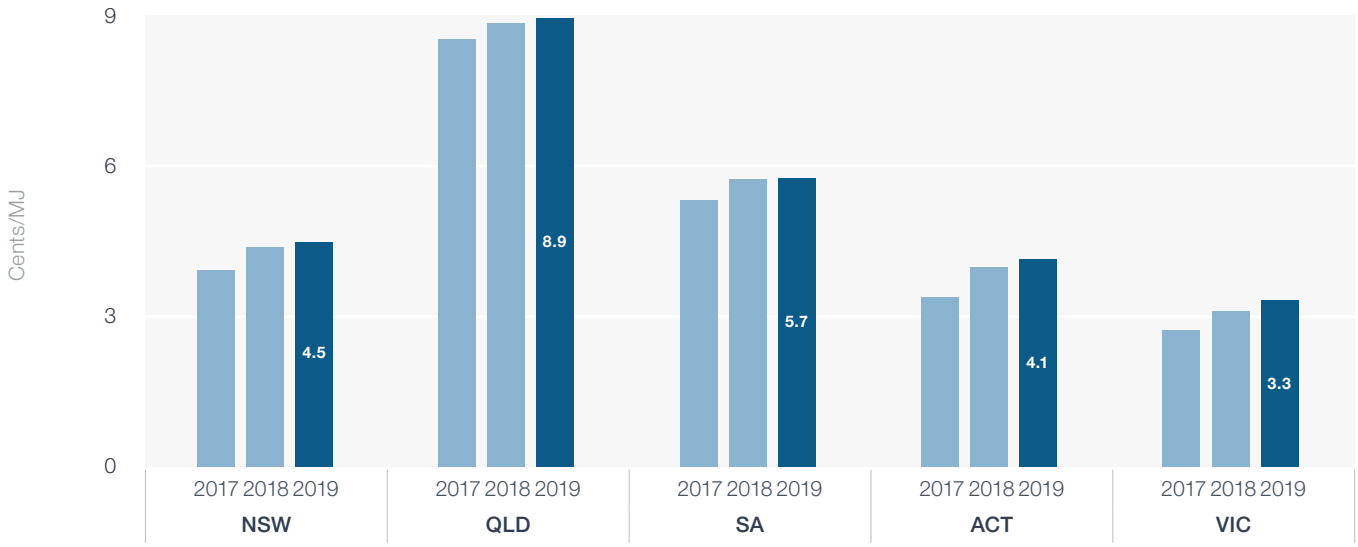
7 ACIL Allen Report to the AER, 'Energy Consumption Benchmarks', October 2017. See www.aer.gov.au/retail-markets/retail-guidelines-reviews/electricity-and-gas-bill-benchmarks-for-residential-customers-2017.

Figure 7: Trends in median gas market offer price (cents per MJ)



As with market offers, the gas median standing offer was most expensive in Queensland (8.9 cents per MJ) and least expensive in Victoria (3.3 cents per MJ).

Figure 8: Trends in median gas standing offer price (cents per MJ)



5. Bringing the analysis together – comparing energy affordability over the past 3 years

In this section, we bring together the work on income, electricity usage and retailer offers to provide an overall picture of changes to electricity affordability for households. This analysis is presented as the amount spent on electricity bills, based on a customer on the median market or standing offer, as a percentage of disposable household income. Our analysis focuses on low income households because these are the most likely to be affected by energy affordability. We separately repeat the analysis based on the average income across all households to provide an analysis of energy affordability more broadly.

Generally, energy affordability improved marginally for households in most regions in 2019, following a fall over the previous two years. Despite this improvement, energy affordability remains an issue for many households when assessed against longer-term outcomes. Low income households in particular continued to spend a significant part of their disposable income on energy.

5.1 Electricity affordability

Electricity bills fell across all regions between June 2018 and June 2019 for households on the median market offer, reflecting lower prices and lower usage. This followed rises in most regions between 2017 and 2018. Despite this improvement, electricity bills remained above 2017 levels everywhere except Queensland. This, combined with slow income growth, meant that electricity remained less affordable by historic standards and was a key concern for many households.

Figure 9 shows market and standing offer electricity bills for average income households as at June 2019. The bubbles above the bars in figure 9 show the percentage of disposable household income spent on electricity by average income households.

Consistent with previous years, bills for customers on standing electricity offers were more expensive than bills for customers on market offers in all regions at June 2019 (figure 9). Only a small number of customers are on standing offers but, to the extent that these are low income households, these will be the most affected by affordability issues.

Figure 9: Comparison of median market and standing offer electricity bills for average income household in 2019

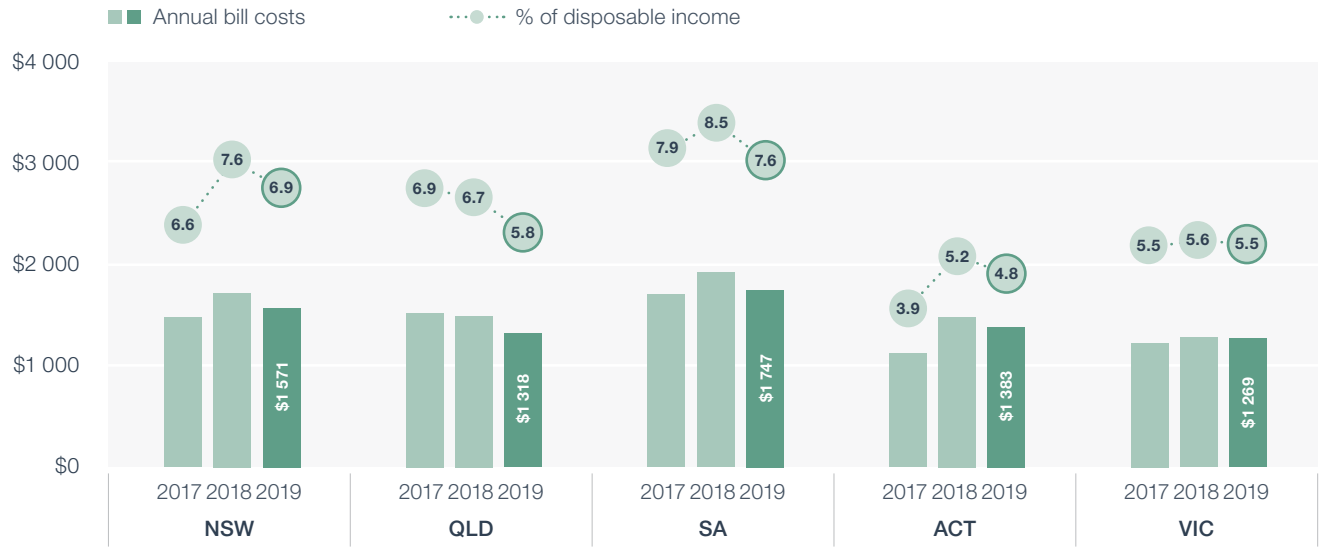
Note: Annual bills shown with no concessions applied. Differences are the same when concessions are applied.

While figure 9 above shows outcomes for average income households, low income households on the median market offer in each region paid about twice the proportion of their disposable income for electricity compared to the average income household. For example, in 2019, low income households on the median market offer spent between 4.8 per cent (in the ACT) and 7.6 per cent (in South Australia) of disposable income on electricity (see figure 10). By comparison, the average income household spent between 2.6 per cent (in the ACT) and 3.9 per cent (in South Australia) (see figure 12 below).

Electricity costs and affordability for low income households[8]

Figure 10 shows that, in 2019, low income households in South Australia spent the highest percentage of their disposable income on market offer electricity bills (7.6 per cent), while low income households in the ACT spent the lowest (4.8 per cent). All regions saw marginal improvements in affordability over the past year, based on the reduction in bills and a slight rise in incomes. Improvements ranged from 0.1 per cent of income in Victoria, to 0.9 per cent of income in Queensland and South Australia.

Figure 10: Annual electricity bills for low income households on a median market offer



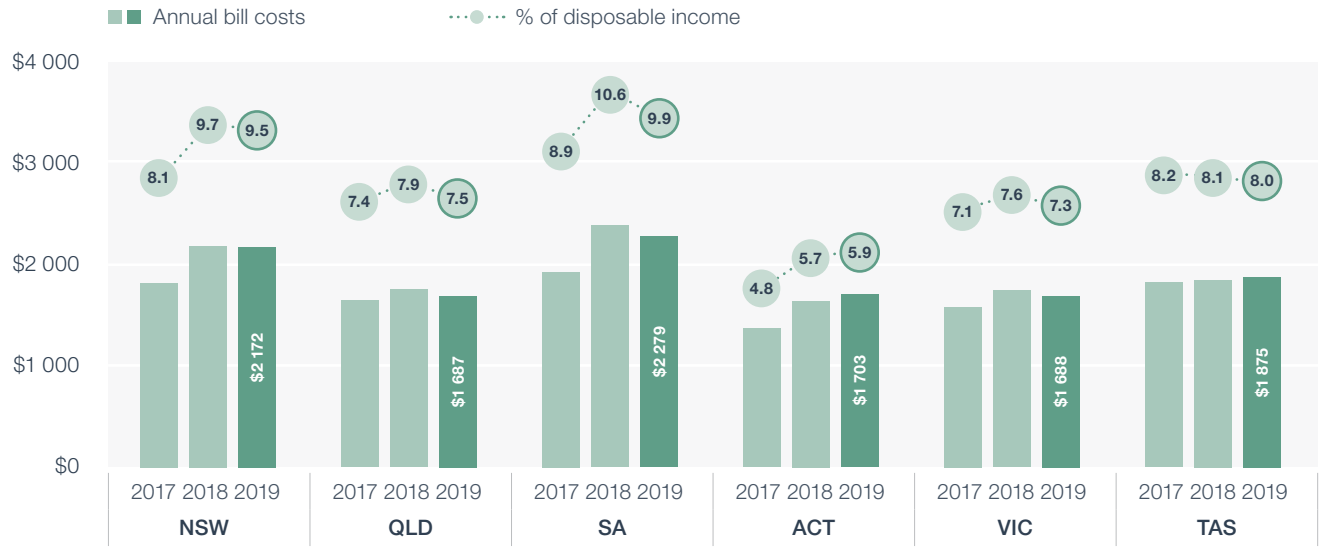
Retailers' median standing electricity offers were more expensive than the median of their market offers in all regions. So, low income households on standing offers spent a higher proportion of their disposable income on electricity than customers on market offers.

Figure 11 shows the annual bill cost for low income households on a median standing offer. As a proportion of annual disposable income, annual standing offer bill costs remained relatively steady from 2018 to 2019 in NSW and Tasmania and rose slightly in the ACT. Low income households on standing offers in Queensland, South Australia and Victoria experienced improved affordability as a result of lower usage and flat prices.

Low income customers on standing offers in South Australia and NSW faced the least affordable electricity in 2019, with 9.9 per cent and 9.5 of income going towards electricity costs respectively. ACT customers, despite seeing a slight deterioration in affordability, continued to pay the lowest proportion of their income on electricity, at 5.9 per cent.

8 The analysis of the impact of electricity bills on low income houses takes account of government concessions which lower the bills for these households.

Figure 11: Annual electricity bills for low income households on a median standing offer



Electricity bill costs and affordability for the average household

Annual bills for market electricity offers followed a similar trend for the average household as for low income households.[9]

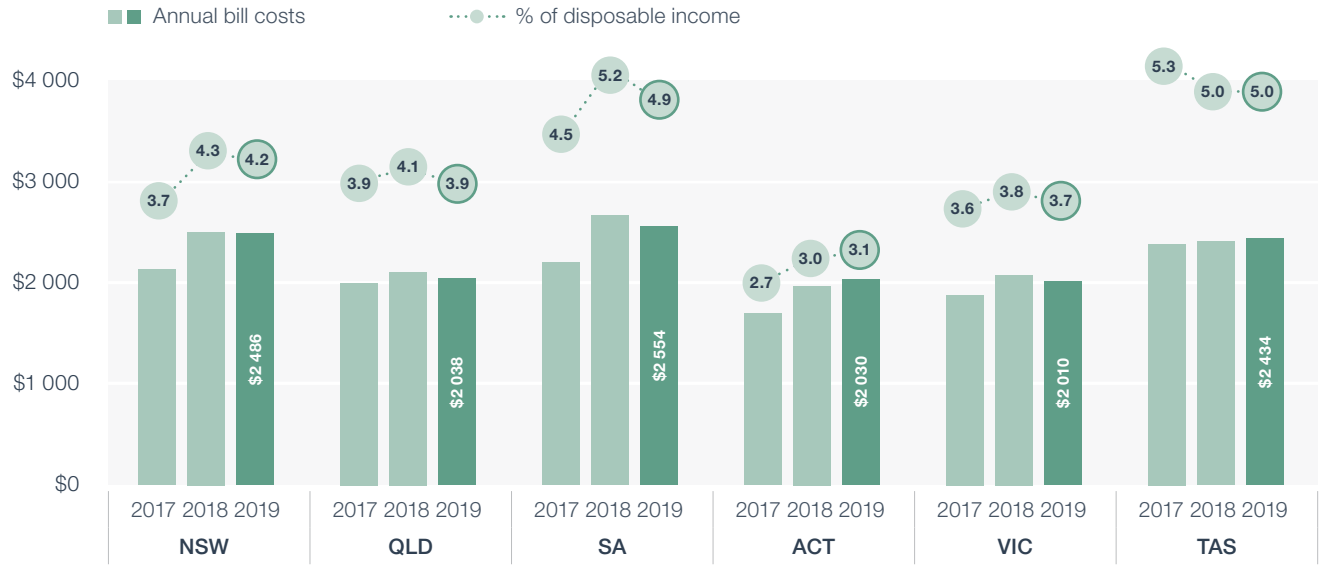
The key difference between the household groups is that the average household spent a significantly lower proportion of their income on market offer electricity bills relative to what low income households spent on energy. In South Australia, the most expensive region, the average household on the median market offer spent 3.9 per cent of their income on electricity bills compared to 7.6 per cent for low income households.

Figure 12: Annual electricity bills for the average income household on a median market offer

9 A point of difference to note here is that, unlike for low income households above, we do not account for government concessions for the average household.

Similarly, the average household on a standing offer spent a significantly lower proportion of their disposable income on electricity than low income households on these offers. The greater impact of standing electricity offer bills on low income households compared to the average household is particularly stark. In South Australia, for example, low income households on standing offers spent 9.9 per cent of their disposable income on electricity while the average household spent 4.9 per cent.

Figure 13: Annual electricity bills for the average income household on a median standing offer



5.2 Gas affordability

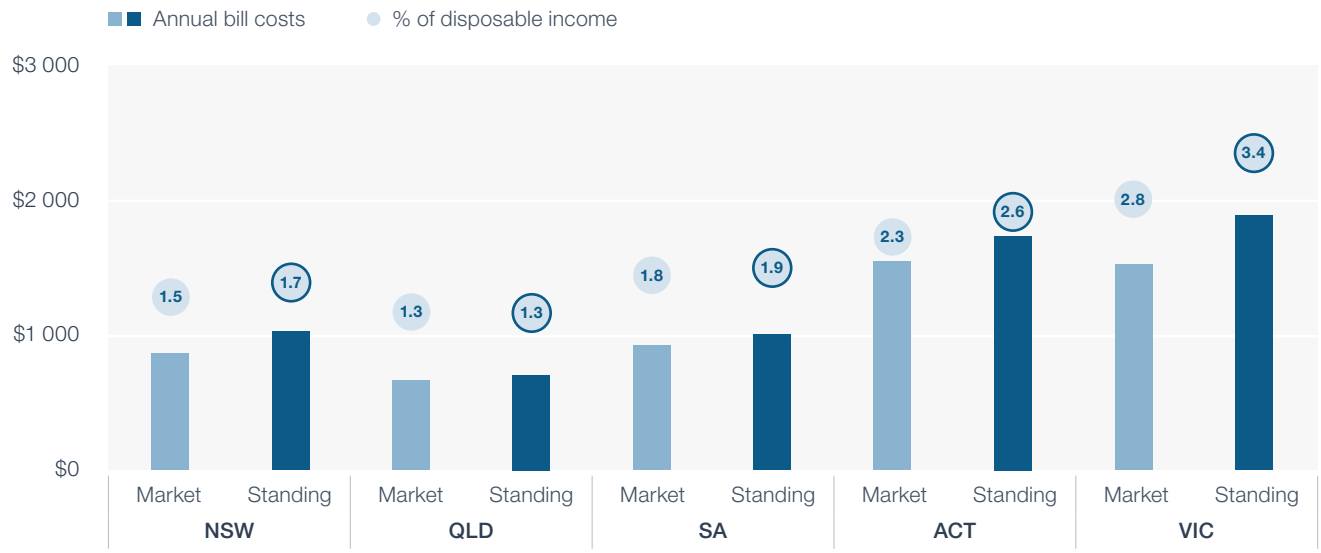
We combine the above analysis of income, gas usage and retailer offers to provide an overall picture of changes to gas affordability for households. This analysis is presented as the amount spent on gas bills, based on a customer on the median market or standing offer, as a percentage of disposable household income. We repeat the analysis for low income households and, separately, the average household, as we did for electricity.

Gas affordability improved for those on market offers in all regions between June 2018 and June 2019, except Victoria where affordability declined marginally. This improvement was primarily due to falls in retailer offers. However, bills in all regions remained at or above 2017 levels.

Victorian and ACT households paid the highest gas bills irrespective of whether they were on a standing offer or market offer. This is largely because households in these regions used more gas than other regions—57 064 MJ per year in Victoria and 42 078 MJ per year in the ACT. Given this higher usage, Victorian households pay a significantly higher proportion of disposable income on gas than all other regions. For ACT households, large annual gas costs were partly offset by higher average incomes. On average, Queensland households use the least gas at 7873 MJ per year and spend the least on their gas bills despite gas prices being highest there when assessed on a per unit basis.

Gas standing offers remained higher than gas market offers across all regions, although the difference between standing and market offers is smaller than for electricity. Figure 14 shows median annual bill costs for market and standing offers as a proportion of disposable income at June 2019.

Figure 14: Comparison of median market and standing offer gas bills for average income households in 2019



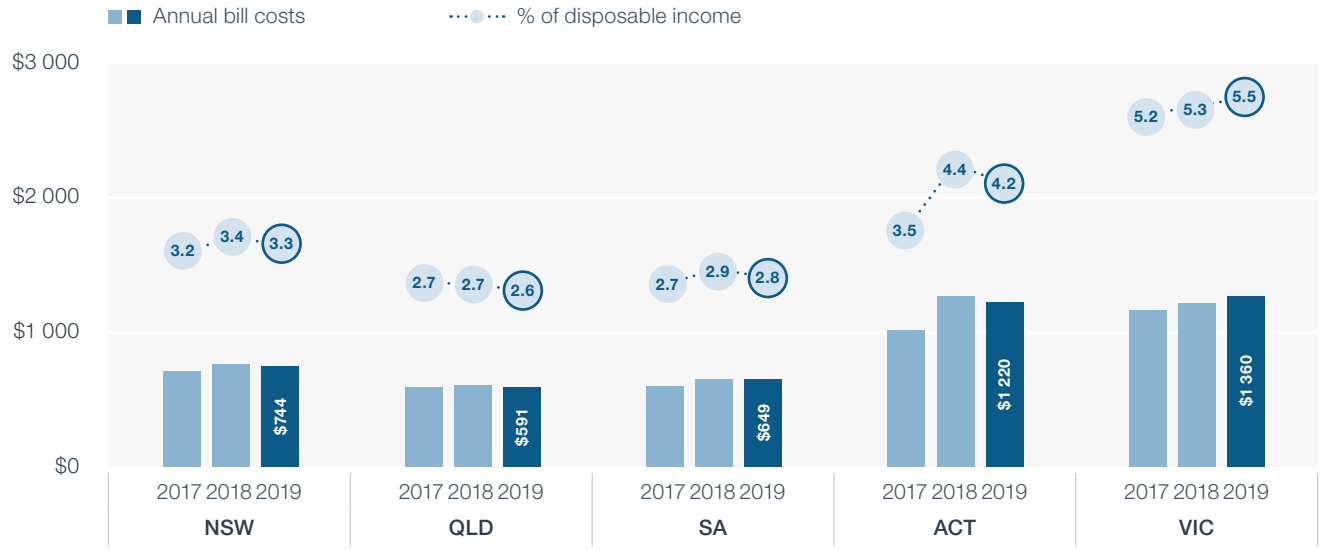
Note: Annual bills shown with no concessions applied. Differences are the same when concessions are applied.

For most regions, low income households spent roughly double what the average household spent on gas bills (as a percentage of their income). In Victoria, for example, a low income household spent 6.8 per cent of disposable income on standing offer gas bills while the average household spent 3.4 per cent.

Gas costs and affordability for low income households

All regions except Victoria saw steady or marginal improvement in gas affordability for low income households between June 2018 and June 2019. For low income households on market offers, the percentage of disposable household income spent was greatest in Victoria (at 5.5 per cent of income). Other regions range from 2.6 per cent of income in Queensland to 4.2 per cent in the ACT. As mentioned above this is because of higher usage of gas by Victorian households. While usage is also high in the ACT, this is partly offset by higher average income.

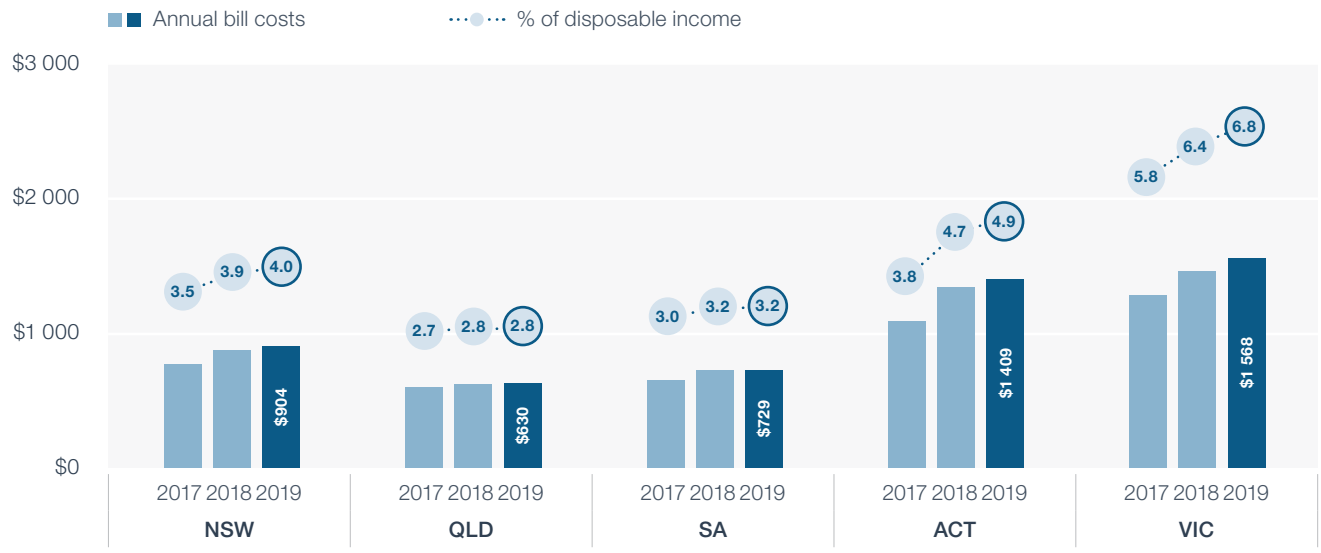
Figure 15: Annual gas bills for low income households on a median market offer



For low income households on standing offers, in 2019 affordability remained steady in NSW, Queensland and South Australia. Affordability worsened in Victoria and the ACT. Low income households paid 6.8 per cent of disposable income in Victoria (up from 6.4 per cent) and 4.9 per cent in the ACT (up from 4.7 per cent). By contrast, Queensland households spent 2.8 per cent of their disposable income on standing offer gas bills.

For gas, there is less of a difference between market and standing offer annual bills than there is for electricity. The difference in the proportion of disposable income for gas market offer versus standing offer bills ranged from 0.2 per cent of disposable income in Queensland to 1.3 per cent in Victoria.

Figure 16: Annual gas bills for low income households on a median standing offer



Gas bill costs and affordability for the average household

Annual bills for gas market offers followed a similar trend for the average household as for low income households. Affordability for the average household remained relatively steady for both market and standing offers across all regions.

The average household spent a smaller proportion of their disposable income on gas bills. In South Australia across both standing and market offers, low income households paid around 1 per cent more of disposable income on gas than the average household, through to around 3 per cent more in Victoria.

Figure 17: Annual gas bills for average income households on a median market offer

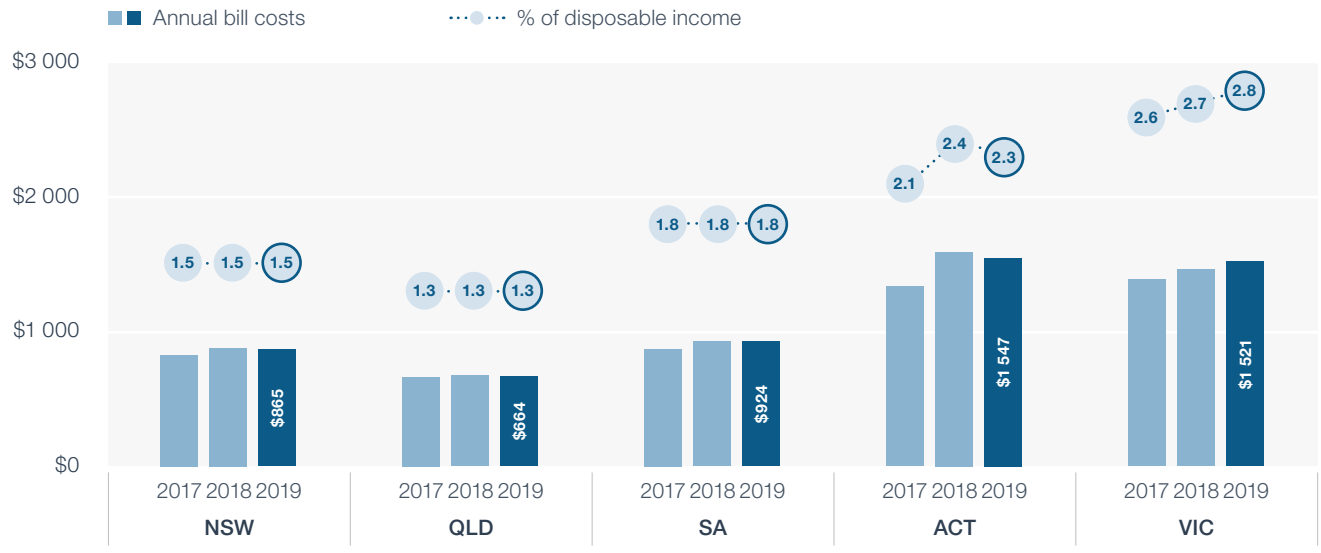
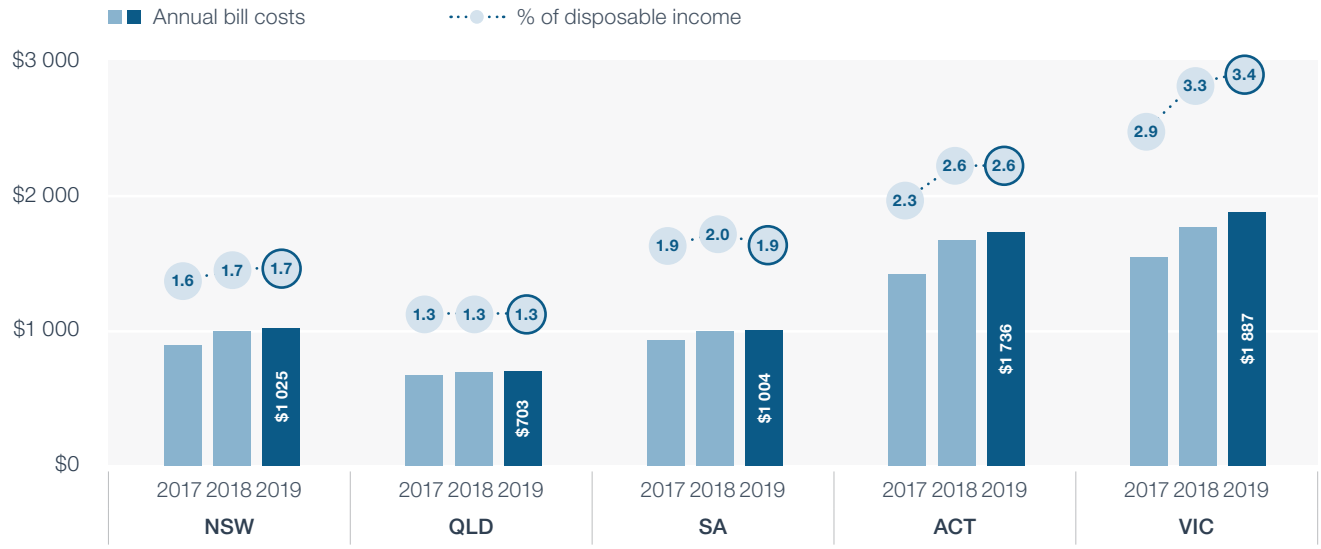


Figure 18: Annual gas bills for average income households on a median standing offer



6. Discounting practices

Retailers often provide discounts to customers who meet certain requirements, such as paying bills on time or by paying via direct debit. At June 2019, these 'conditional discounts' could reduce a customer's bill by up to 42 per cent.[10] Our analysis in this report assumes that consumers achieve the maximum discount by meeting all conditions of their offers. However, as REPI reported, pay on time discounts 'are achieved only 56 per cent of the time for payment plan customers and only 42 per cent of the time for hardship customers. Customers who do not pay on time are, in effect, paying very large late payment penalties, often amounting to hundreds of dollars per year.'[11]

Given the potential significance of missed conditional discounts to the costs customer face for electricity and gas each year, we examined conditional discounts over the same timeframe as our affordability analysis (up to June 2019).

The figures below illustrate the proportion of market offers that had a conditional discount, and the average value of those discounts, for electricity and gas respectively over the past three years.

We note that retailer discounting practices appear to be undergoing a shift, evidenced by a general trend away from conditional discounts. There is likely to be a range of factors that have influenced retailers' approach to discounting, for example new discounting regulations came into effect in 2018 (the AEMC's *Preventing discounts on inflated energy rates* rule change) and new regulatory interventions are being consulted on (the *Regulating conditional discounting* rule change consultation). Major regulatory interventions affecting retailers' ability to advertise conditional discounts also came into effect in Victoria, South East Queensland, South Australia and NSW on 1 July 2019 under the respective VDO and DMO frameworks.

While analysing future trends into 2019-20 is out of scope for this report, appendix B includes analysis of how discounting practices changed after 1 July 2019 in regions where the DMO applies.

10 This reflects offers available on the ***EnergyMadeEasy*** website.

11 ACCC, *Restoring electricity affordability and Australia's competitive advantage, Retail Electricity Pricing Inquiry—Final Report*, June 2018, p. xi.

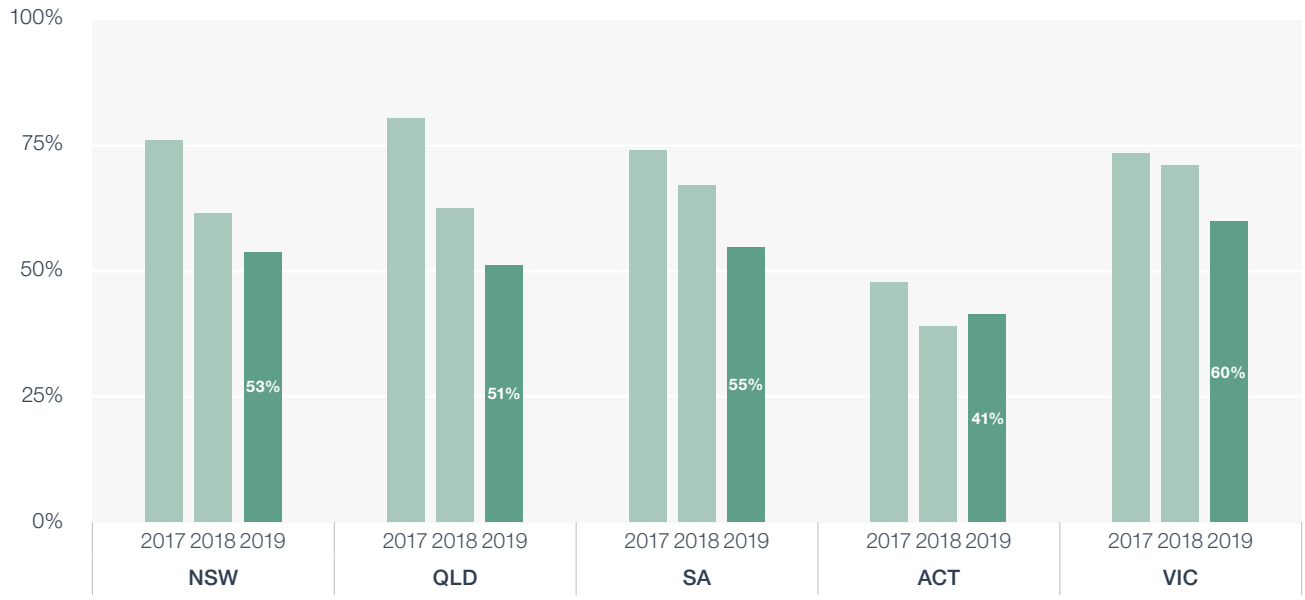
6.1 Conditional discounting in electricity

In electricity over the previous year, customers saw a smaller proportion of offers with a conditional discount. However, the value of available discounts continued to increase in all regions (except Victoria).

A downward trend in the proportion of electricity offers with conditional discounts continued from the previous year across all regions, except for in the ACT where conditional discounts increased from 39 to 41 per cent of all market offers. The largest decrease in the proportion of offers with discounts with in South Australia, which shifted from 67 per cent of all offers in June 2018 to 55 per cent of all offers in June 2019.

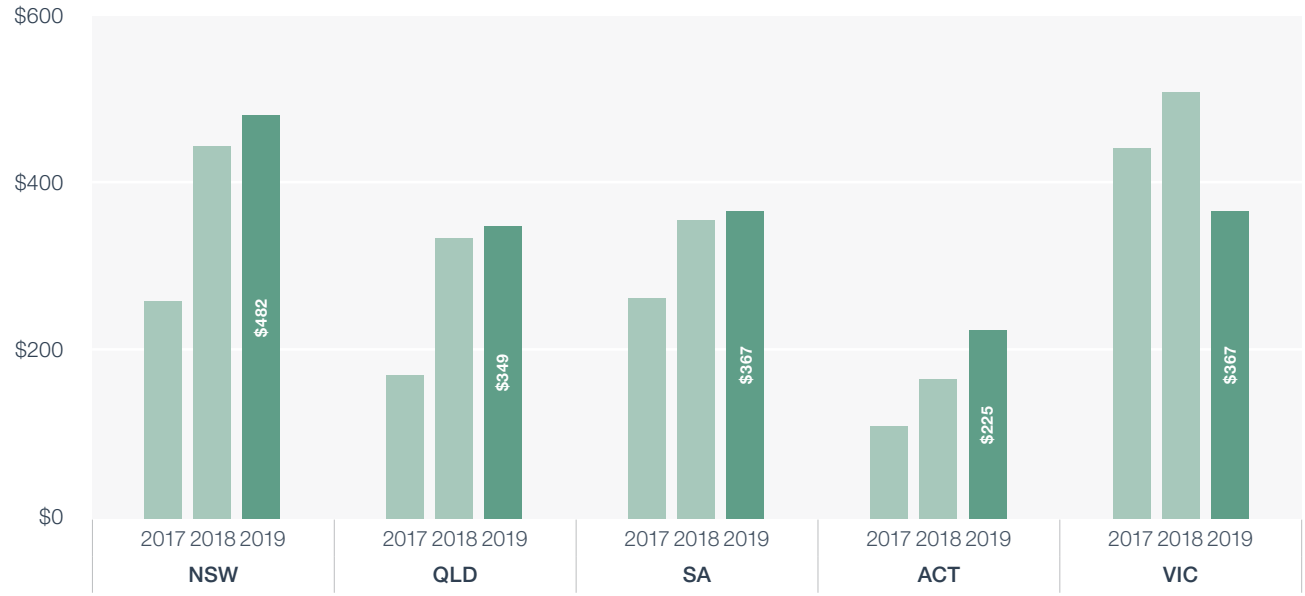
In appendix B we extend our analysis to capture trends up to July 2019 for relevant regions. In that analysis we see an acceleration in the decline of the proportion of offers with conditional discounts.

Figure 19: Proportion of electricity market offers that have conditional discounts



For all regions except Victoria, the average value of conditional discounts for electricity increased between 3 per cent and 35 per cent. The ACT experienced the most significant increase in the average value of conditional discounts, raising from $167 to $225 for the year. Customers in Victoria saw a steep fall in the value of conditional discounts of approximately 28 per cent, from $510 to $367.

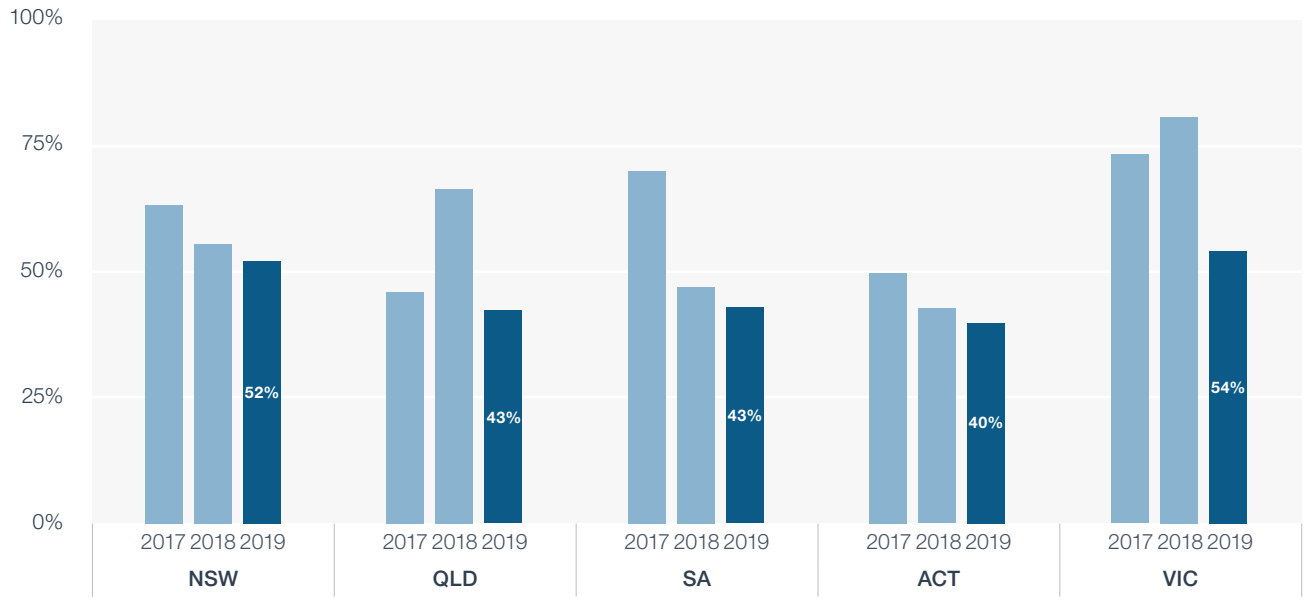
Figure 20: Average value of conditional discounts for electricity market offers



6.2 Conditional discounting in gas

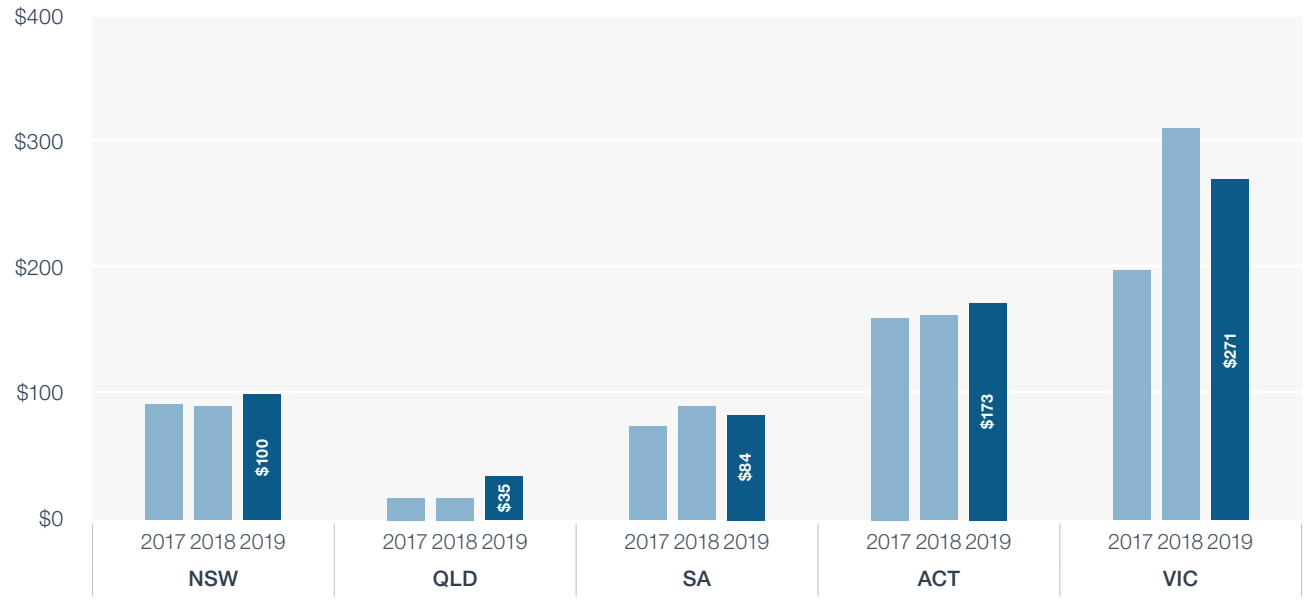
For gas, the trend in proportion of offers with conditional discounts was similar to that of electricity over the previous year. The proportion of gas offers with conditional discounts fell across all regions, with the biggest movements in Queensland and Victoria. In 2018, 67 per cent of all offers in Queensland contained conditional discounts and this fell to 43 per cent in June 2019. In Victoria, 81 per cent of all market offers comprised conditional discounts in 2018 and this decreased to 54 per cent of all offers in June 2019.

Figure 21: Proportion of gas market offers that have conditional discounts



Changes to the average value of conditional discounts for gas was inconsistent across regions from 2018 to 2019. The value of conditional discounts increased 6 to 10 per cent in the ACT and NSW respectively. In Queensland where customers use much less gas than customers in other regions, the value of gas discounts doubled from a low base of $18 in 2018 to $35 in 2019. The largest fall in the value of conditional discounts was in Victoria, from $312 in 2018 to $271 in June 2019.

Figure 22: Average value of conditional discounts for gas market offers



New South Wales
Electricity 2018-19

3
DISTRIBUTORS

33
RETAILERS

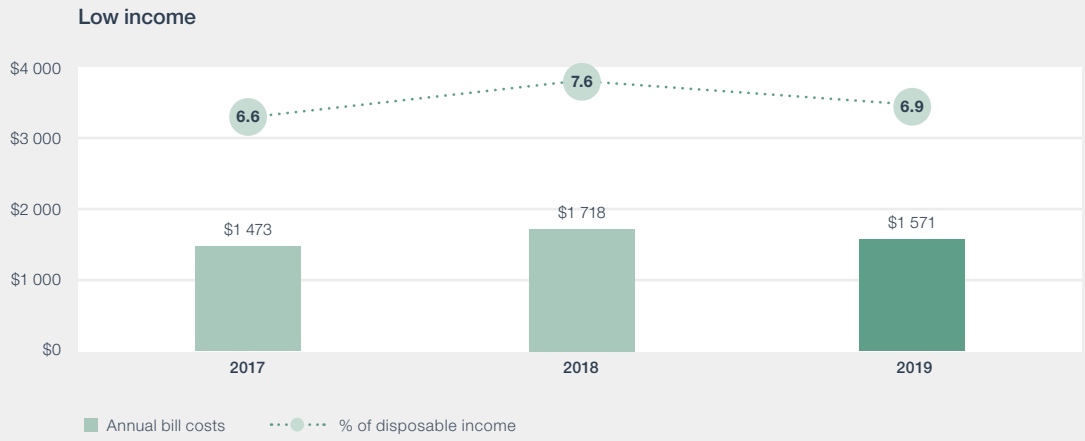
3 182 309
CUSTOMERS

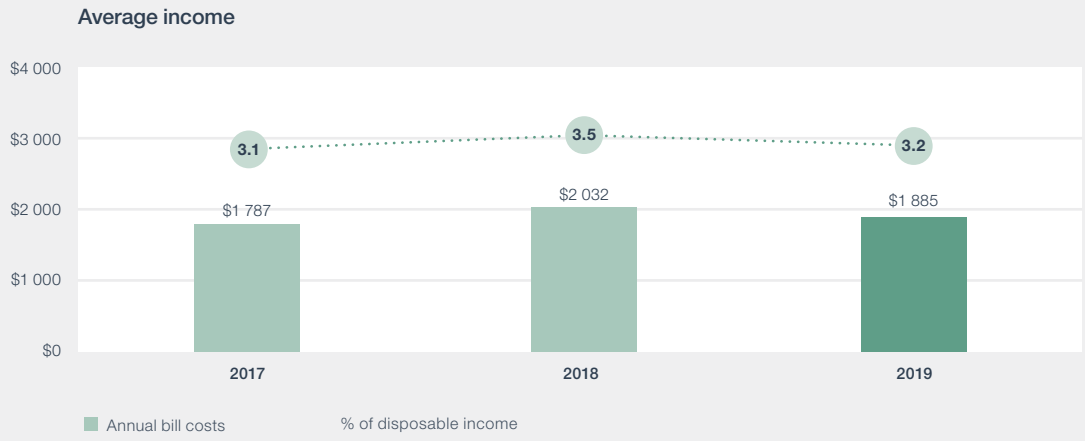
5 881
AVERAGE USAGE KWH

$1 571
ANNUAL BILL LOW INCOME

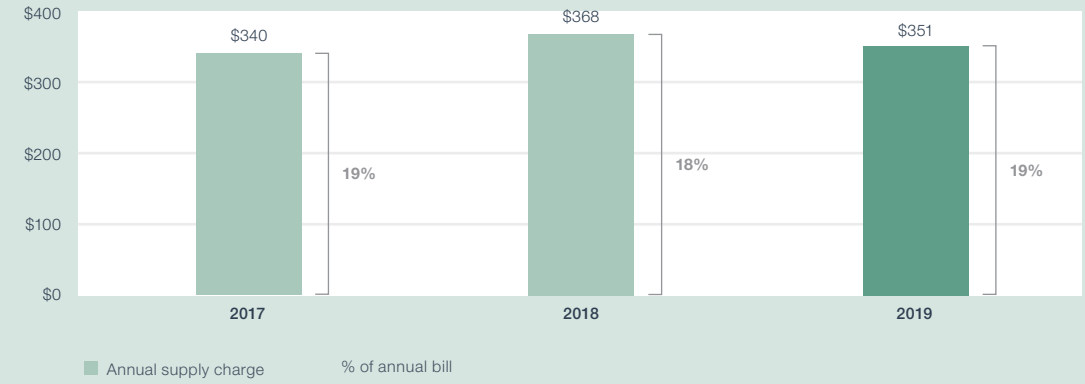
$1 885
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



New South Wales
Gas 2018-19

4
DISTRIBUTORS

12
RETAILERS

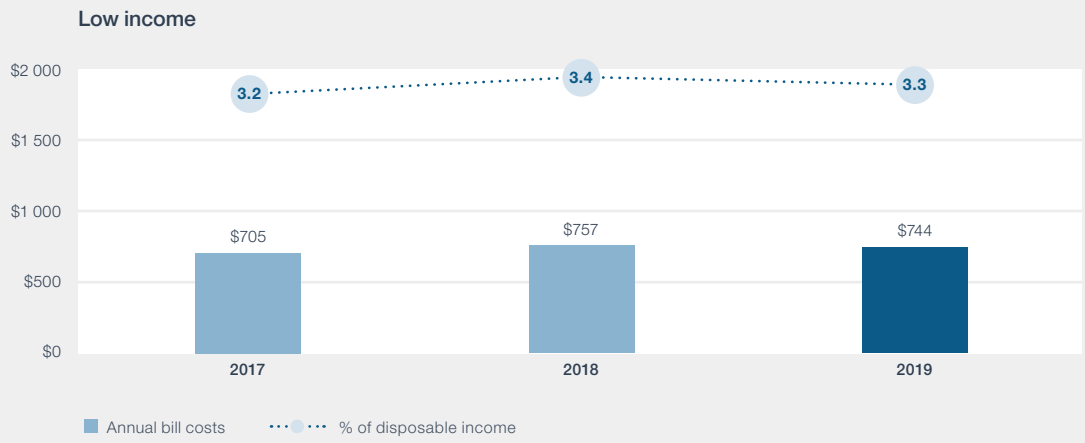
1 390 525
CUSTOMERS

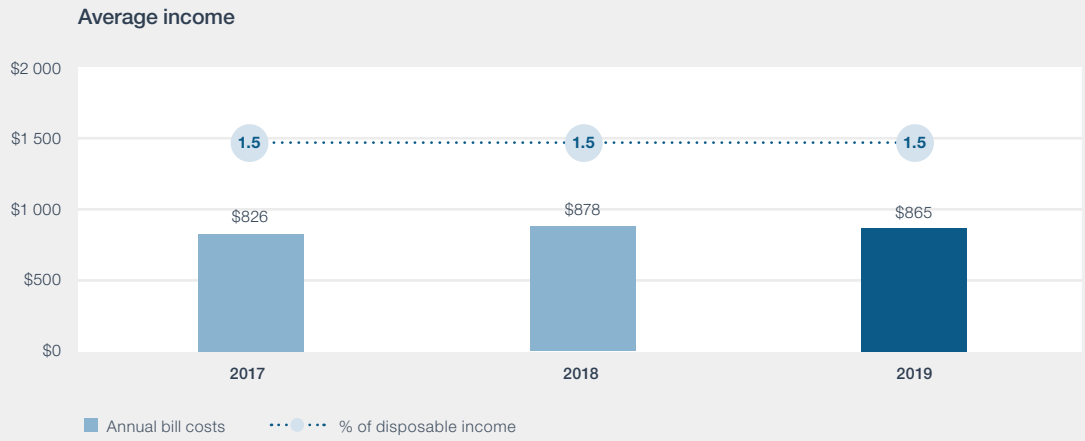
22 855
AVERAGE USAGE MJ

$744
ANNUAL BILL LOW INCOME

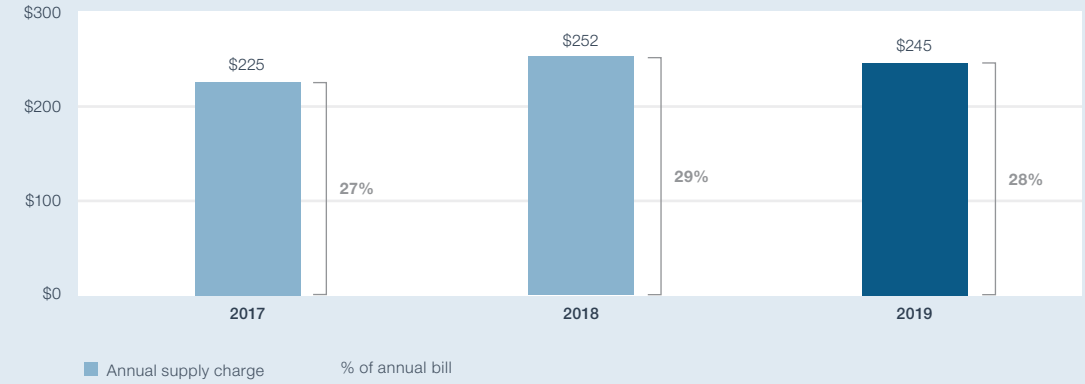
$865
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Queensland
Electricity 2018-19

2
DISTRIBUTORS

30
RETAILERS

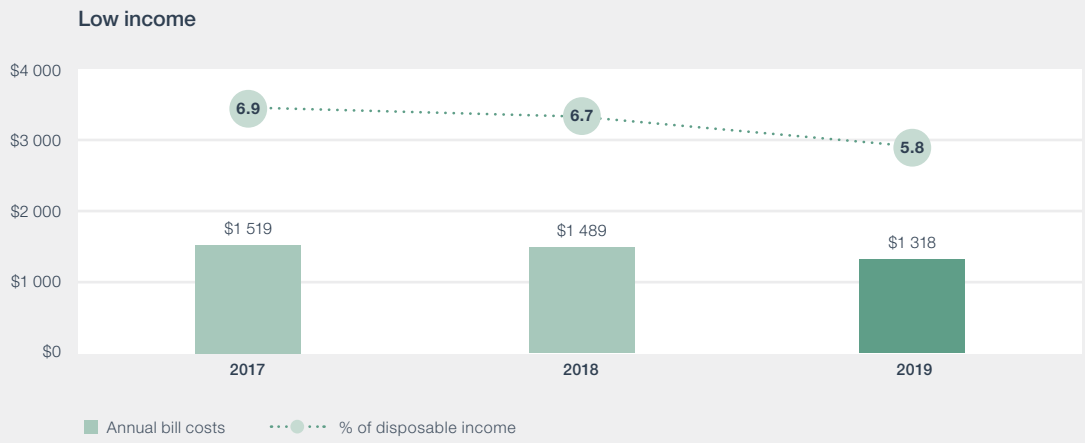
2 003 354
CUSTOMERS

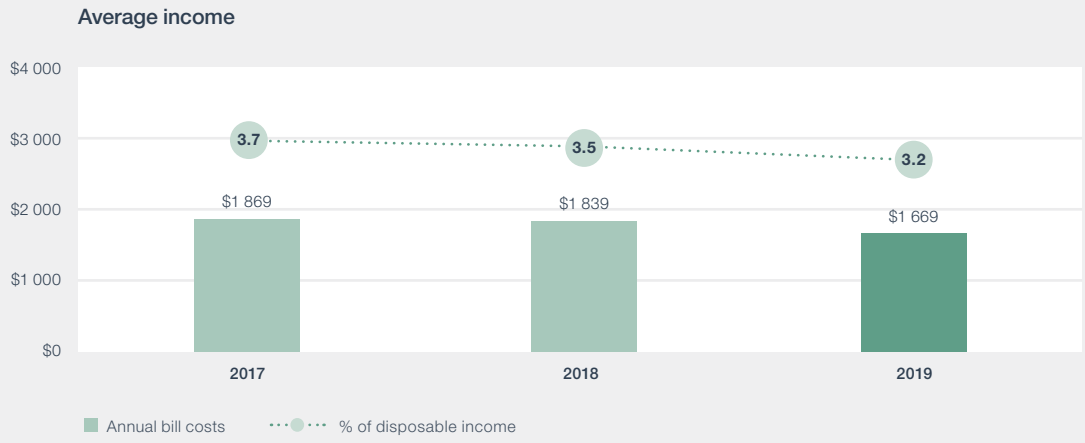
5 699
AVERAGE USAGE KWH

$1 318
ANNUAL BILL LOW INCOME

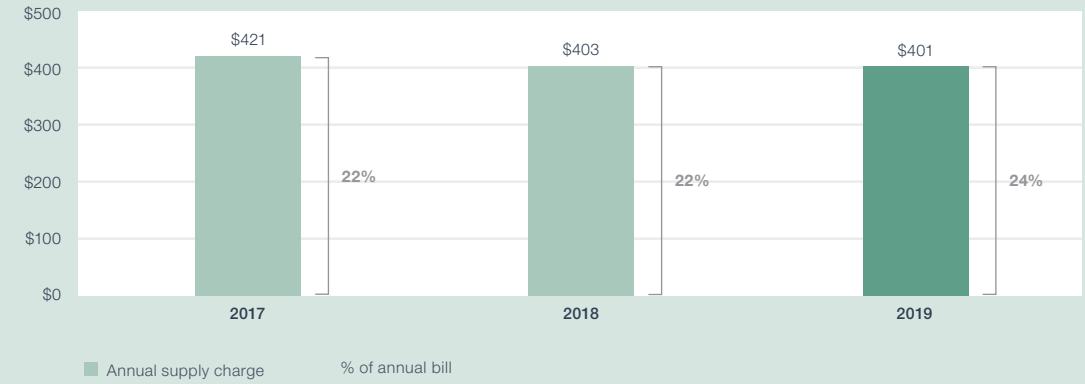
$1 669
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Queensland
Gas 2018-19

2
DISTRIBUTORS

5
RETAILERS

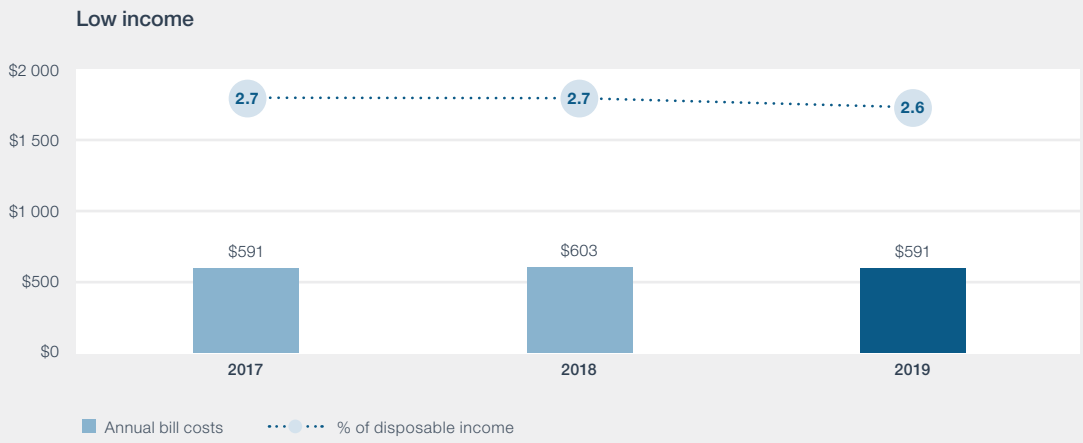
196 765
CUSTOMERS

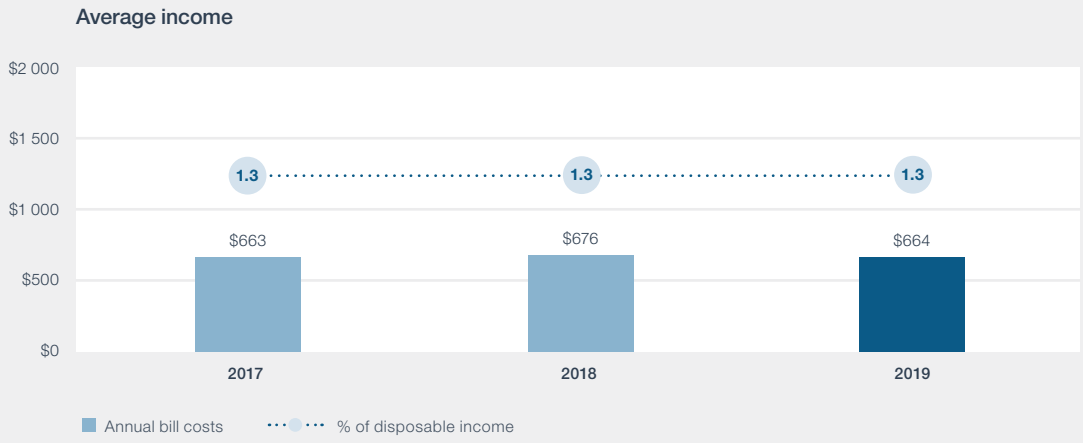
7 873
AVERAGE USAGE MJ

$591
ANNUAL BILL LOW INCOME

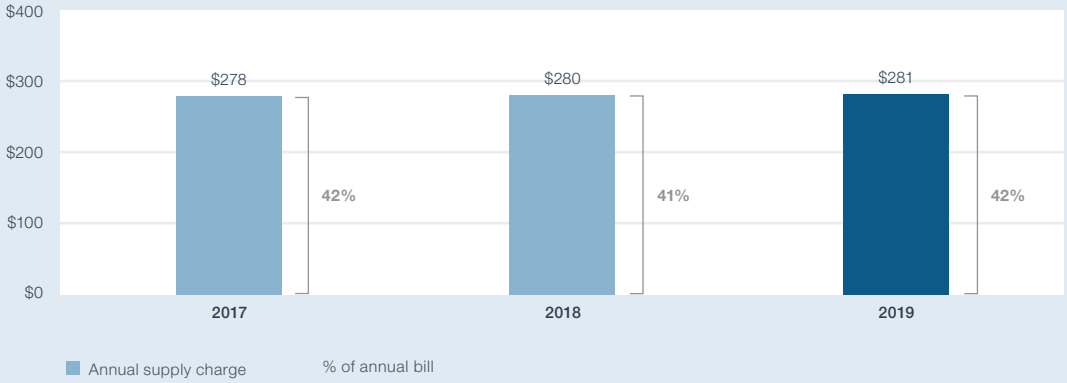
$664
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



South Australia
Electricity 2018-19

1
DISTRIBUTOR

20
RETAILERS

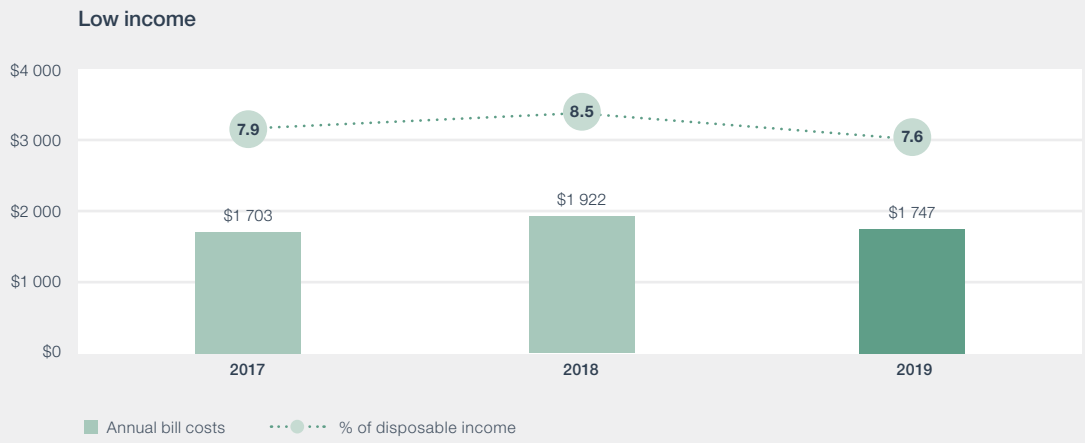
776 382
CUSTOMERS

4 752
AVERAGE USAGE KWH

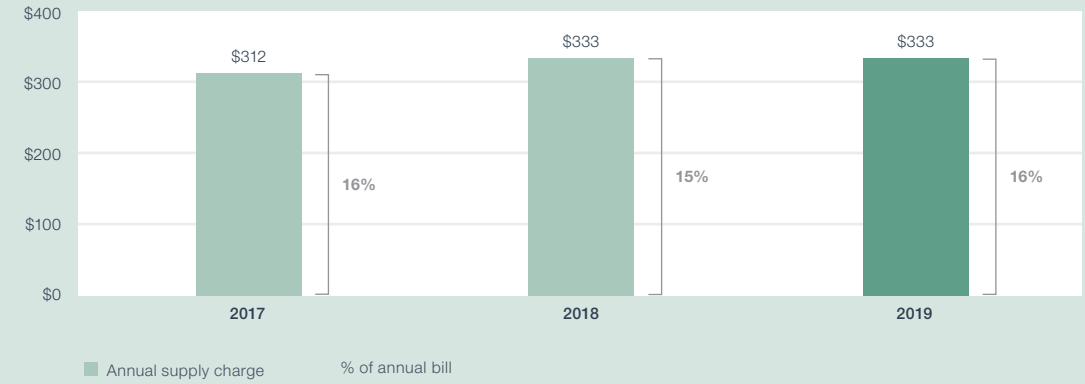
$1 747
ANNUAL BILL LOW INCOME

$2 022
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income



Annual electricity supply charge and proportion of annual bill



South Australia
Gas 2018-19

1
DISTRIBUTOR

8
RETAILERS

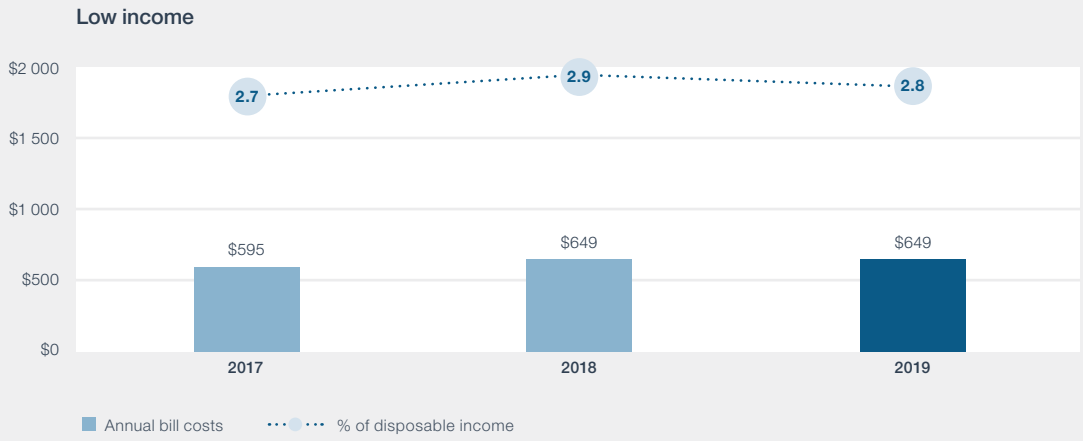
432 772
CUSTOMERS

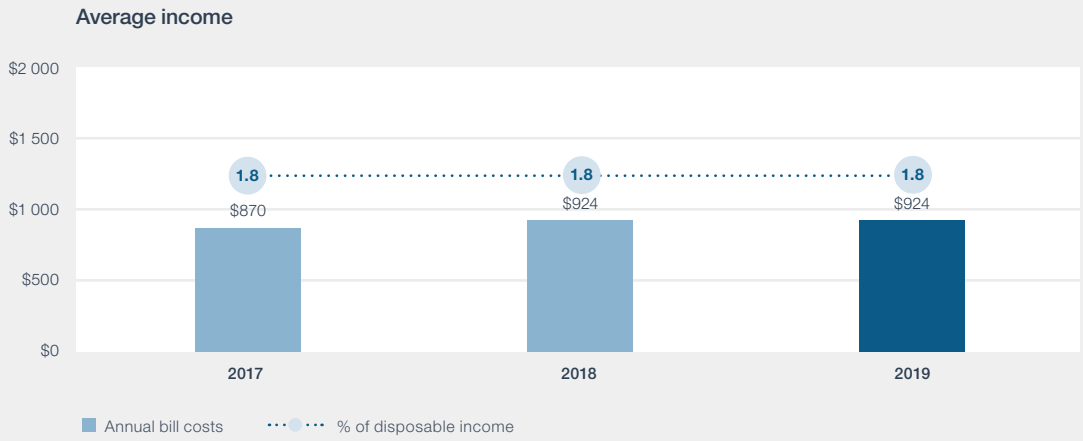
17 501
AVERAGE USAGE MJ

$649
ANNUAL BILL LOW INCOME

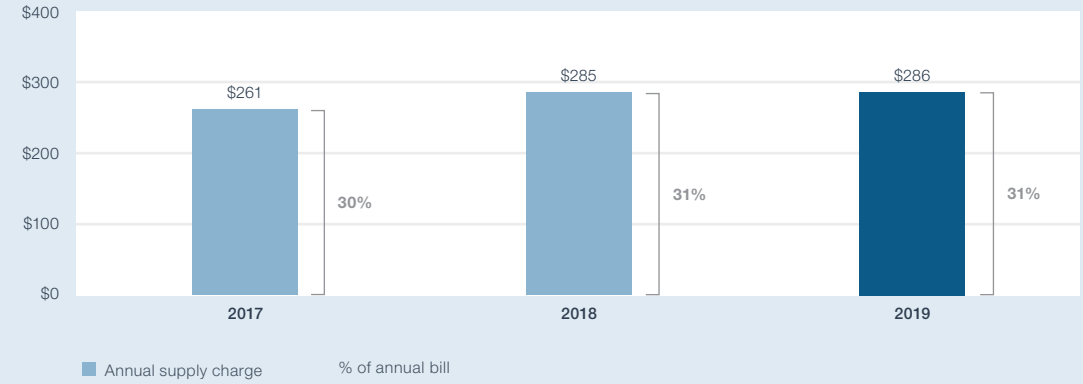
$924
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Australian Capital Territory
Electricity 2018-19

1
DISTRIBUTOR

7
RETAILERS

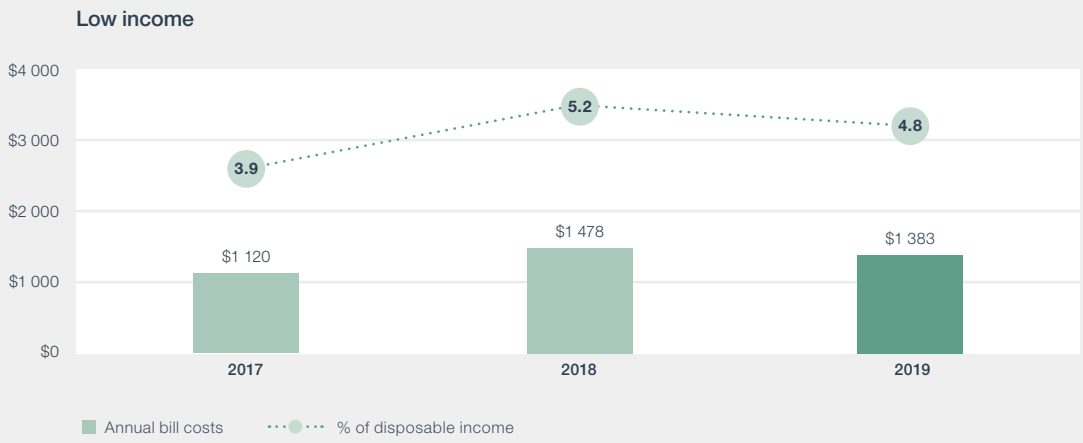
174 739
CUSTOMERS

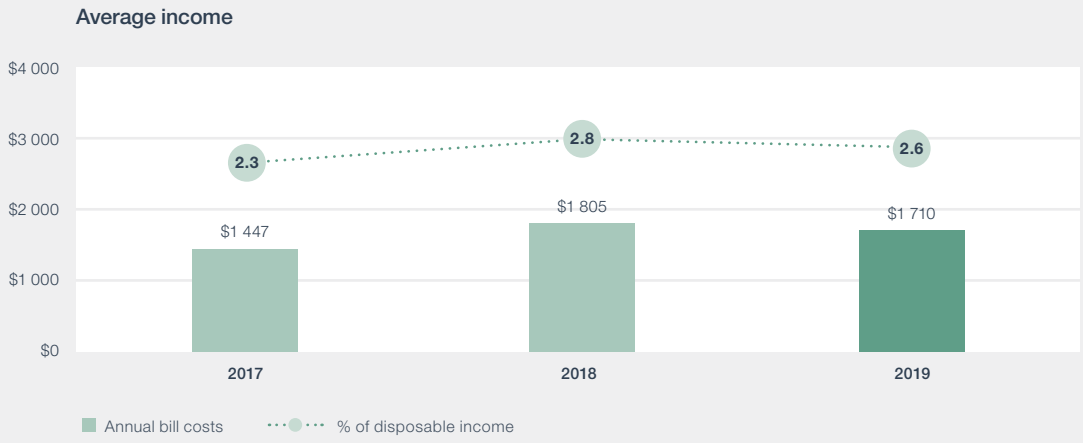
6 545
AVERAGE USAGE KWH

$1 383
ANNUAL BILL LOW INCOME

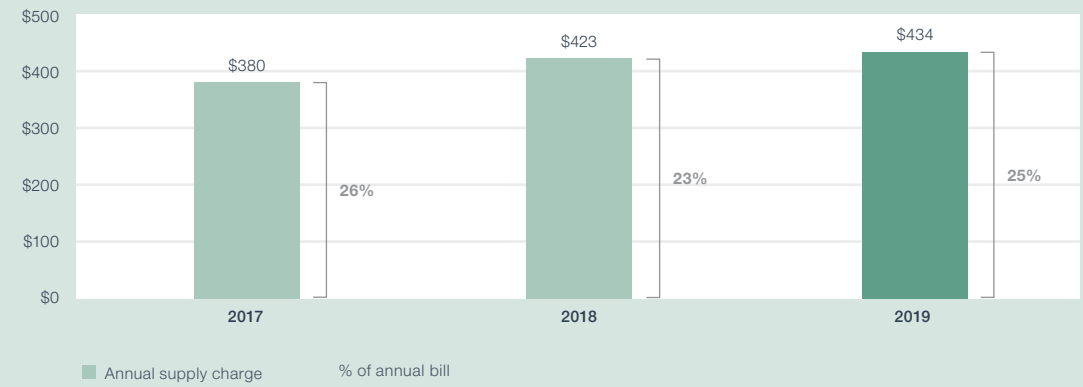
$1 710
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Australian Capital Territory
Gas 2018-19

1
DISTRIBUTOR

3
RETAILERS

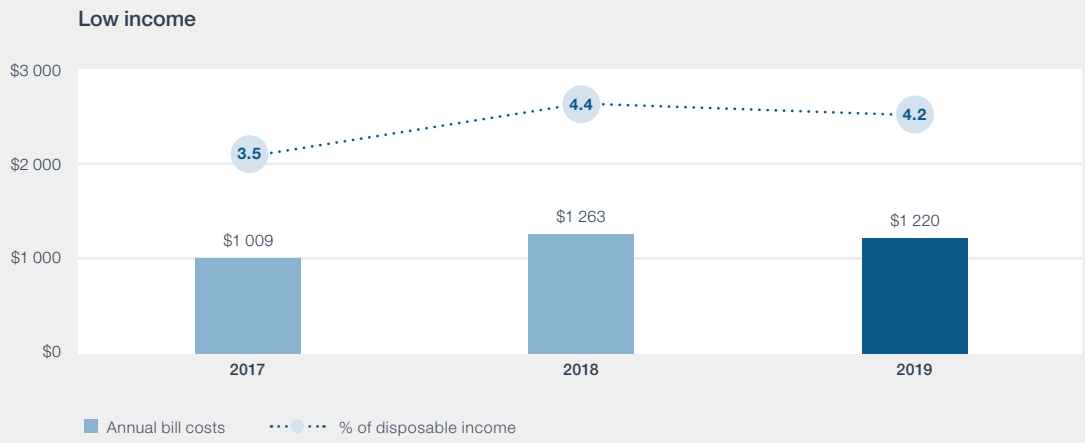
123 592
CUSTOMERS

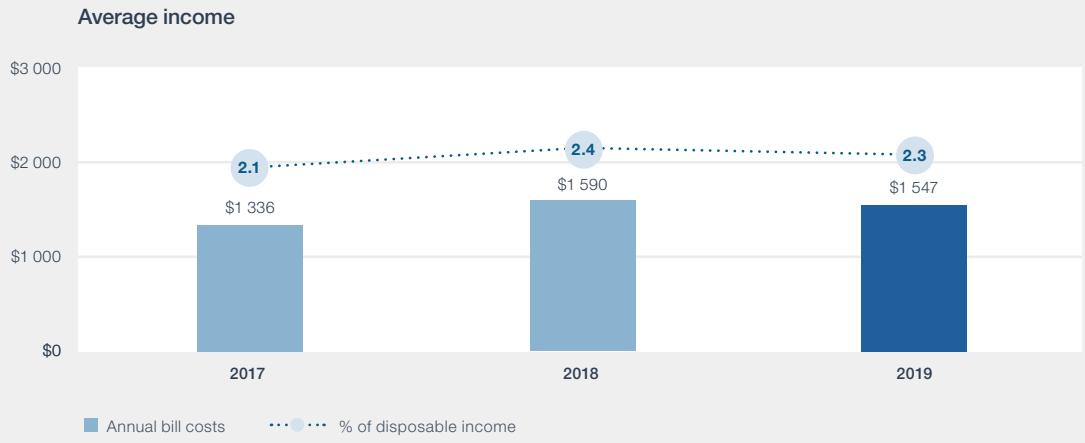
42 078
AVERAGE USAGE MJ

$1 220
ANNUAL BILL LOW INCOME

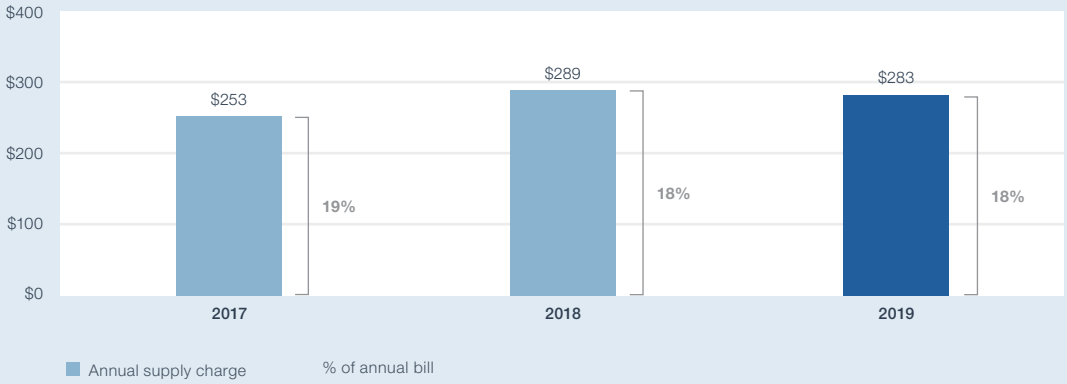
$1 547
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Victoria
Electricity 2018-19

5
DISTRIBUTORS

24
RETAILERS

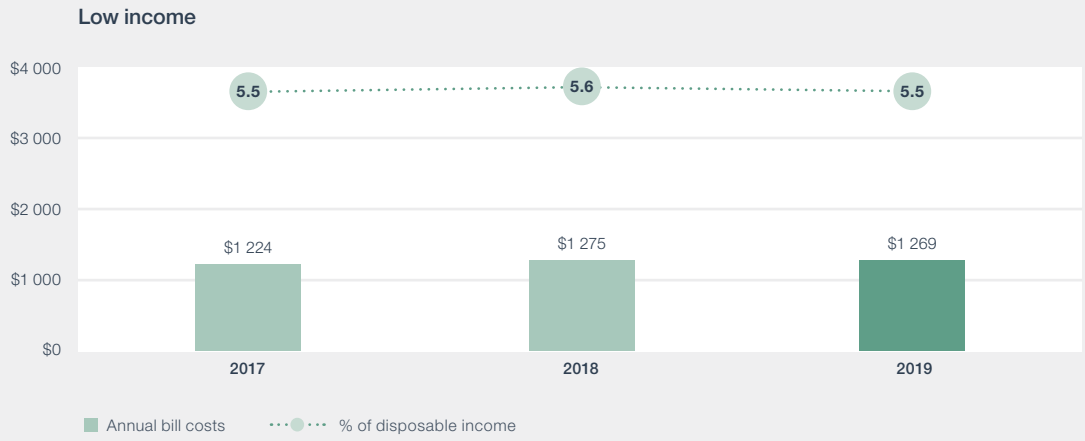
2 520 620
CUSTOMERS

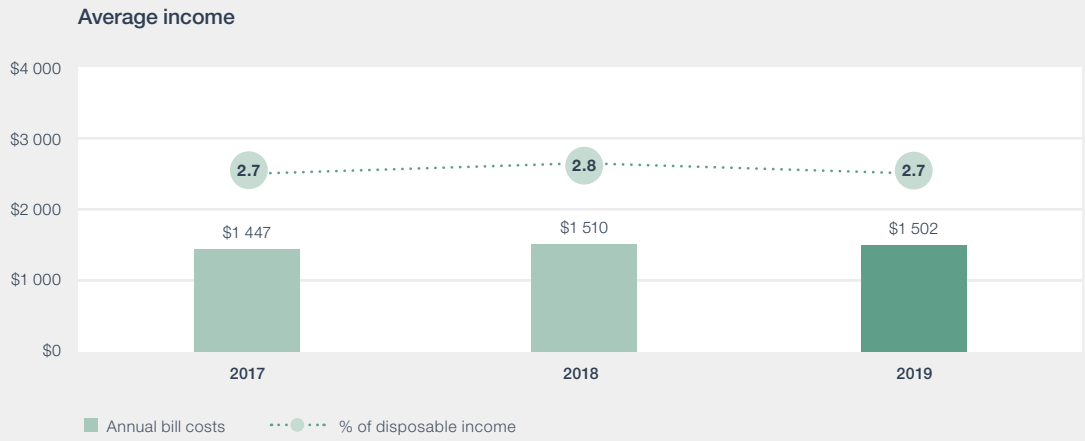
4 589
AVERAGE USAGE KWH

$1 269
ANNUAL BILL LOW INCOME

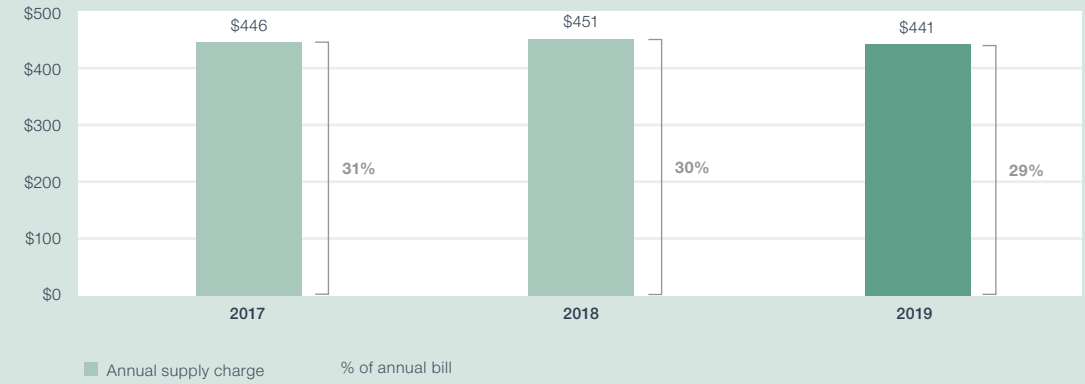
$1 502
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Victoria
Gas 2018-19

3
DISTRIBUTORS

14
RETAILERS

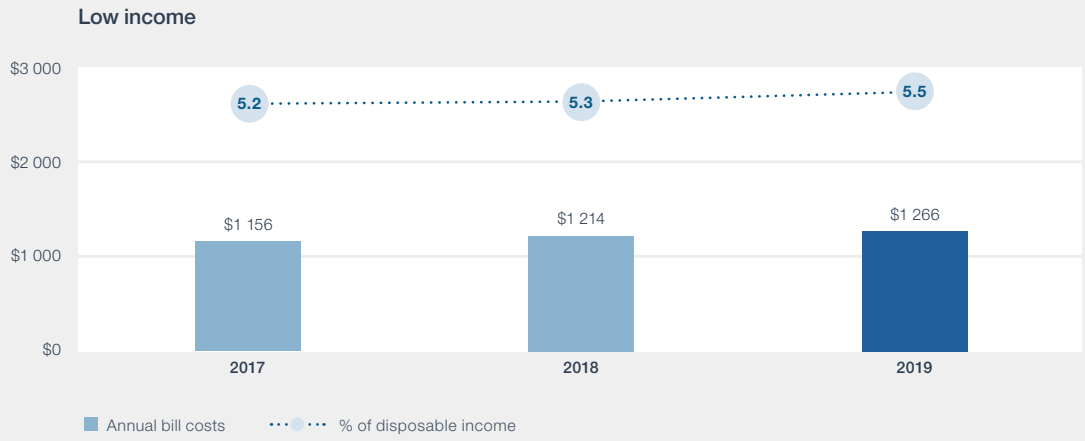
1 952 604
CUSTOMERS

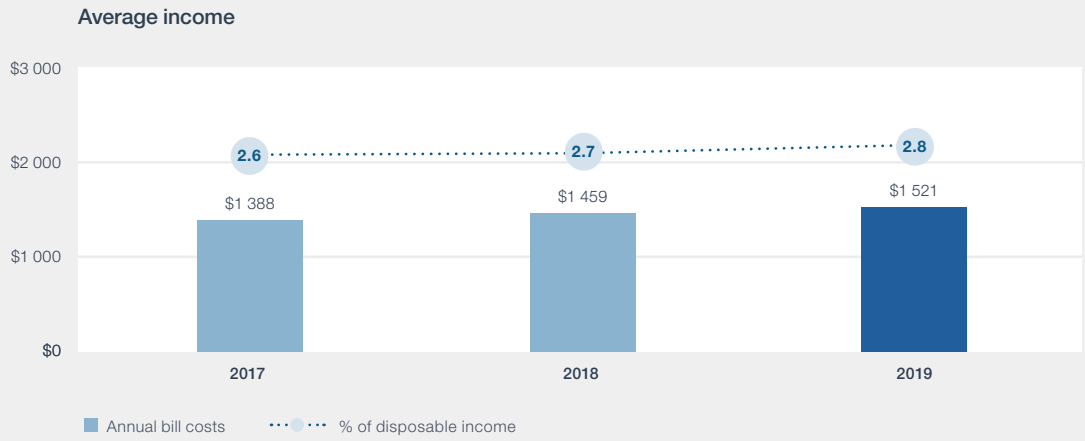
57 064
AVERAGE USAGE MJ

$1 266
ANNUAL BILL LOW INCOME

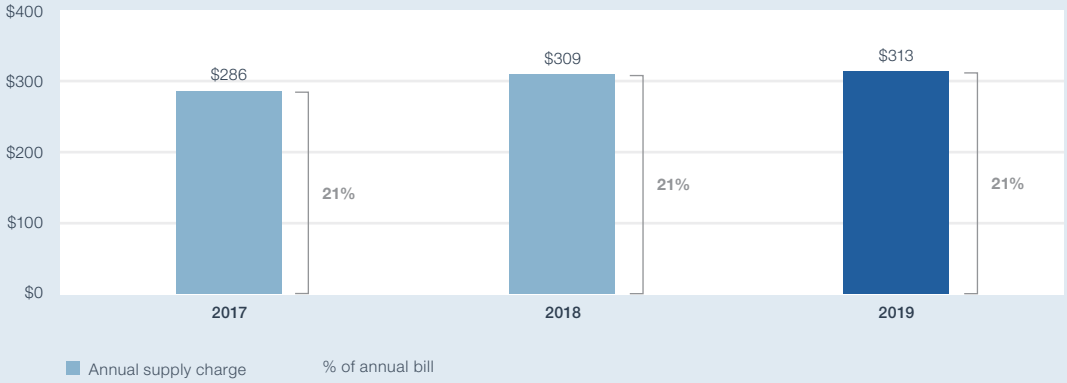
$1 521
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Tasmania
Electricity 2018-19

1
DISTRIBUTOR

2
RETAILERS

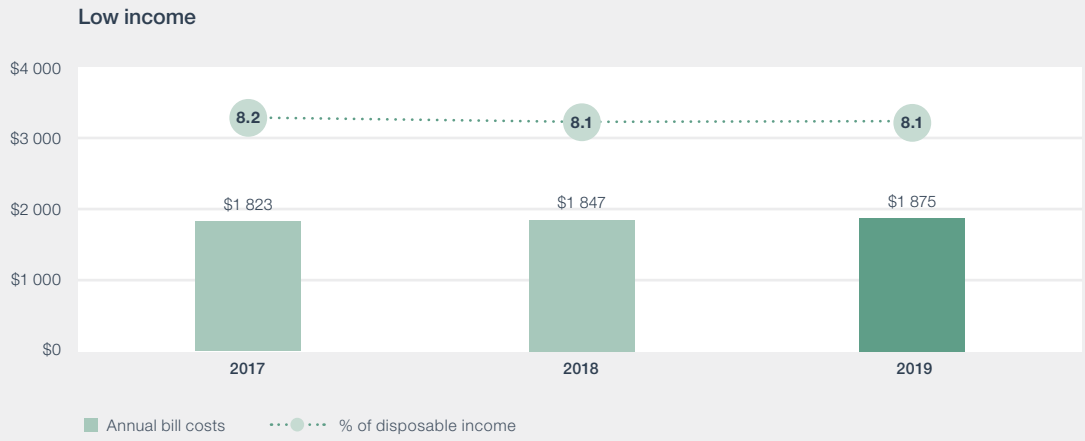
244 007
CUSTOMERS

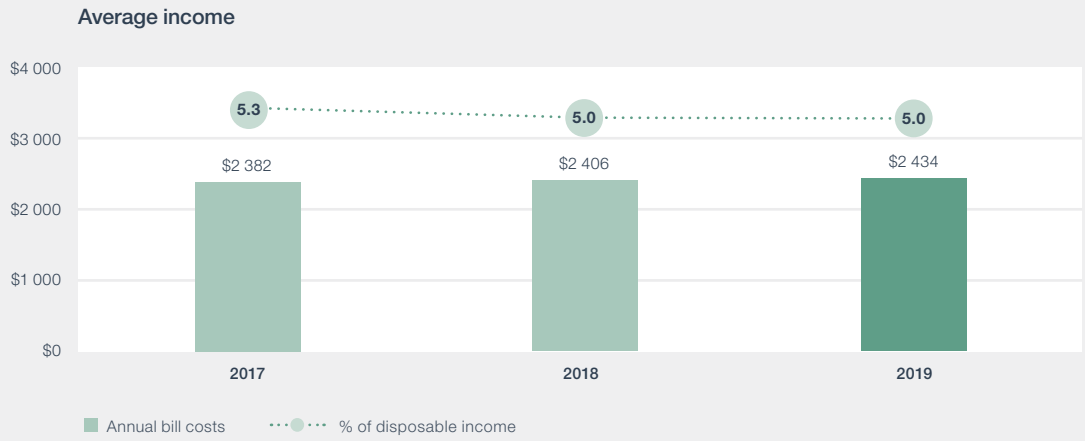
7 976
AVERAGE USAGE KWH

$1 875
ANNUAL BILL LOW INCOME

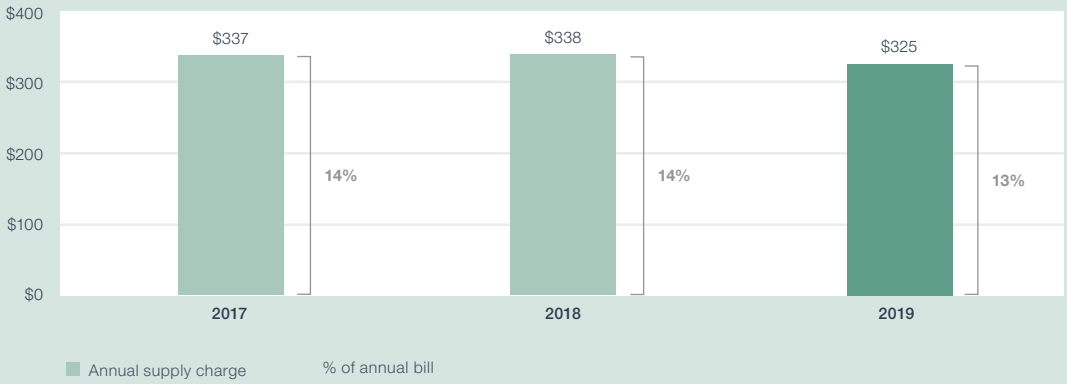
$2 434
ANNUAL BILL AVERAGE INCOME

Annual bills and disposal income





Annual electricity supply charge and proportion of annual bill



Appendix A: Affordability methodology

The key inputs into our analysis include:

- estimates of annual median market and standing offer bill costs for each region, which comprises:
  - average annual household electricity and gas usage in each region
  - retail electricity and gas offers in each distribution or pricing zone

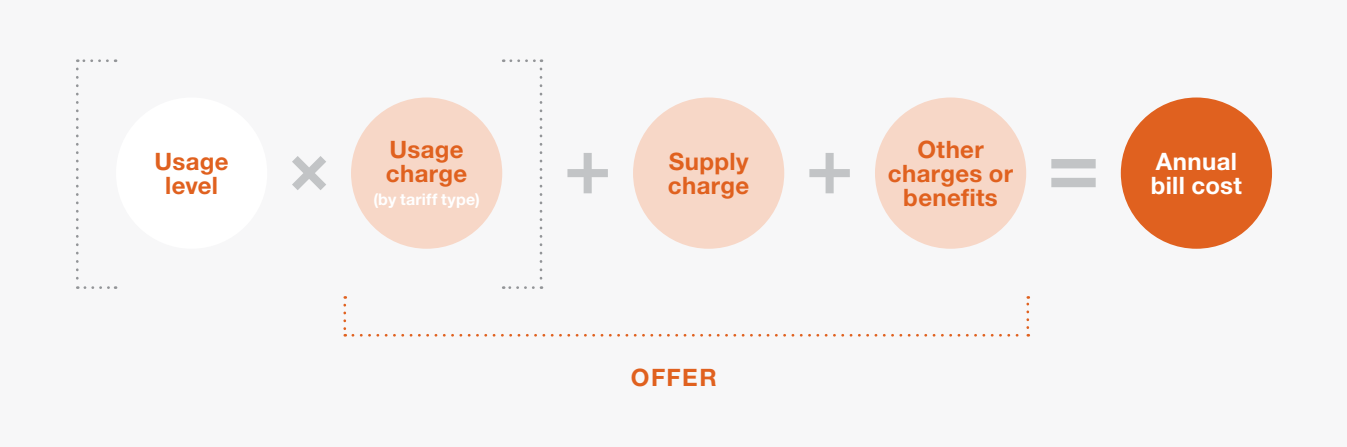
- estimates of affordability for each region, which comprises:
  - annual median market and standing offer bill costs
  - concessions offered to those who may experience financial hardship
  - household disposable income.

These inputs are outlined in more detail below.

Annual bill cost

The calculation of an annual bill cost is comprised of several components including usage levels, usage charges, supply charges, and other fees such as membership or metering fees. Figure 23 disaggregates these, and highlights the components that feed into a retailer's offer.

Figure 23: Components of retail annual bill costs



Usage levels

Our sources for usage vary across electricity and gas, due to the differing availability of public information. The levels of electricity and gas usage applied in our analysis can be found in table 1.

Electricity

We based our analysis on average actual household electricity usage for each region in each year. This is sourced from information provided by distribution network businesses each year in response to Regulatory Information Notices (RIN) issued by the AER. This data includes the total usage for all residential users (including usage through controlled loads), as well as total residential customer numbers, in each distribution zone. This data is collected on a financial year basis for all regions except Victoria, which is collected on a calendar year basis. The timing of businesses providing this data to the AER means the usage levels presented in this report are lagged by one year (i.e. usage levels for the 2018-19 year are sourced from RIN data for the 2017-18 year).

Gas

We source average gas usage estimates for each region from a bill benchmarking survey conducted by ACIL Allen on behalf of the AER. These surveys are completed every three years, with the most recent survey released in 2017.[12] Unlike for our electricity analysis, we do not have access to information on annual changes in gas usage.

Table 1: Annual electricity and gas usage levels, 2016–17 to 2018–19

Region	Annual electricity usage per customer (kWh)			Annual gas usage per customer (MJ)
	2016-17	2017-18	2018-19	2017
NSW	6 104	6 132	5 881	22 855
Queensland	5 939	5 947	5 699	7 873
South Australia	5 153	5 104	4 752	17 501
ACT	6 811	7 009	6 545	42 078
Tasmania	7 860	7 982	7 976	NA
Victoria	4 754	4 811	4 589	57 064

Offers

We collect offer details for both electricity and gas from our energy price comparison website, *EnergyMadeEasy* (www.energymadeeasy.gov.au). For Victoria (the only region in our analysis in which the National Energy Retail Law had not commenced at 30 June 2019), we collect tariff details from the Department of Environment, Land, Water and Planning, based on information submitted by retailers to the Victorian Energy Compare website (https://compare.switchon.vic.gov.au).

Our analysis is based on all unique generally available offers in each distribution or pricing zone at a point in time in June 2017, June 2018 and June 2019. We only consider single rate offers, which represent the most common offer type that energy customers are on. We filter these to remove offers with additional elements above an accessible, energy-only basic offer. For example, we remove offers with a solar/green component and offers that have specific eligibility criteria.

12 ACIL Allen Report to the AER, 'Energy Consumption Benchmarks', October 2017. See www.aer.gov.au/retail-markets/retail-guidelines-reviews/electricity-and-gas-bill-benchmarks-for-residential-customers-2017.

Annual Bill Calculation

We use the energy usage levels in table 1 to calculate an annual bill cost for each single rate offer. We base our analysis on the median market and standing offer in each region, for electricity and gas. We use the median (rather than a simple average) to ensure the analysis is not skewed by a small number of very cheap or very expensive offers.

The annual bill estimates include key conditional discounts offered by energy retailers (such as discounts for paying on time, paying by direct debit) but exclude discounts for bundling or dual fuel offers. One-off credits and non-cash incentives are also excluded. Ongoing fees that are attached to an offer (such as membership or metering fees) are included in the annual bill calculation.

We take seasonal pricing into account when calculating the annual bills, but we assume a consistent level of usage throughout the year.

Electricity

In this report we conduct two types of analysis in electricity.

For our trends in electricity prices analysis, we keep usage constant for the time series by applying the usage figures for the latest year for each region. We then divide the median annual bill by average usage to identify costs on a per unit basis. This analysis isolates the effect of changes in retailer offers on annual bills.

For our cost impacts on households analysis, we vary the usage data across each year of the time series. This gives a better sense of what consumers are actually paying for their annual bills in regions.

We recognise that basing our analysis on total electricity usage (including electricity used by controlled loads) will tend to overestimate the annual cost of electricity when applied to single rate offers. This is because it does not reflect that in practice some usage is charged at a lower controlled load rate.

Gas

As we do not have a data source for the change in gas usage across years, all of our analysis uses a consistent usage estimate across the time series.

Affordability

To get an estimate of affordability we calculate annual bill costs as a proportion of average household disposable income for low income households for each region. Figure 24 illustrates this calculation. We also calculate annual bill costs as a proportion of average household disposable income for all households.

Figure 24: Components of affordability analysis

*Concessions are only applied to annual bill costs for low income households

Concessions for low income households

For our analysis for low income households, we adjust the annual bill calculation to account for the benefit of any relevant energy concessions in each region. State and territory governments administer concessions to provide financial assistance to individuals, including people who are elderly, have a disability, are low income earners, or are experiencing disadvantage. We have included the value of all concessions that are available to households on the basis of low income. These concessions our outlined in table 2.

For simplicity we apply the concessions that apply to the most recent year (in this case 2018–19) to bill costs for the whole time series.

Table 2: Energy concessions in 2018–19

Region	Electricity	Gas
NSW	$313.50	$121
Queensland	$350.40	$72.51
South Australia	$274.86	$274.86
ACT	$327.00	$327.00
Tasmania	$559.63	NA
Victoria	17.5% off bill after the first $171.60	17.5% off bill after the first $62.40

Household disposable income

Household disposable income best represents the remaining income (after income tax, the Medicare levy and the Medicare levy surcharge are deducted) available to households for expenditure on goods and services, including electricity and gas bills. We use equivalised household disposable income data to reflect a household's purchasing power, as it takes into account the household's ability to share resources and enables better comparisons between different size households.[13]

This data is collected every two years by the ABS, and is most recently available for the reference periods 2015–16 and 2017–18.[14] We estimated income levels for 2016-17 as the midpoint between these data sets. We extrapolated 2018-19 income by inflating 2017-18 income based on the consumer price index (see table 3).

Low income households

We represent low income households in each state and territory using an adjusted lowest income quintile. This comprises the average income of the lowest two deciles, excluding the first and second percentiles.

The average household

We represent the income of all households by the 'all person' value (the average across all quintiles).

13 An explanation of equivalisation is available under 'key concepts' in ABS, 6523.0 – Household income and wealth, Australia, 2015–16, available at https://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/6523.0~2015-16~Main%20Features~Key%20Concepts~3

14 ABS, Household Income and Wealth, Australia, 2017-18. https://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/6523.02017-18?OpenDocument

Table 3: Household disposable income 2016–17 to 2018–19

		2016-17	2017-18	2018-19
NSW	Low income households	$22 386	$22 464	$22 761
	Average household	$56 888	$58 136	$58 904
Queensland	Low income households	$22 152	$22 204	$22 540
	Average household	$50 830	$51 844	$52 628
South Australia	Low income households	$21 632	$22 620	$22 924
	Average household	$49 348	$51 428	$52 119
ACT	Low income households	$28 652	$28 496	$29 009
	Average household	$62 608	$65 312	$66 487
Tasmania	Low income households	$22 152	$22 828	$23 301
	Average household	$45 006	$47 944	$48 937
Victoria	Low income households	$22 204	$22 828	$23 110
	Average household	$52 754	$54 132	$54 801

Conditional Discounts

When customers are on an offer with conditional discounts, they are facing two prices—one in which they meet the conditions of their offer and one without.

For our analysis on conditional discounts we have calculated the average of the difference between annual bill costs when all conditional discounts are applied and annual bill costs without. This is calculated for single-rate, energy-only offers (as specified above) that contain conditional discounts, for each region.

Appendix B: Default Market Offer analysis

Purpose of this section

The Default Market Offer (DMO) is a new regulatory intervention in the Australian energy market that aims to reduce excessive prices paid by electricity customers on standing offer contracts – the default contracts that a customer might be on if they have never switched to a retailer's market offer, or if they were placed on one when their market offer expired.[15]

While the AER is not required to provide ongoing monitoring and reporting on the impact of the DMO on the electricity market, we consider it is appropriate that we do so. This is because the AER has a broad role to monitor markets to identify trends and issues that may be relevant to the efficient operation of markets and the welfare of customers.

More specifically, as the agency responsible for determining DMO prices each year, we consider it is necessary to understand any DMO-related impacts so that they can inform our future DMO price determinations.

In this context, the purpose of this analysis is to provide a snapshot of how the market has moved immediately following the DMO's introduction.

Our analysis looks at prices of retailers' publicly available offers to understand what has happened to standing offers and market offers following the introduction of the DMO prices on 1 July 2019, comparing this to offers available prior to 1 July to provide an very early indication of changes over time.

Price analysis is useful indicator of the market's response to the DMO, highlighting potential trends for us to monitor, as well as evidence of significant market changes – for example, in regard to discounting practices.

We consider it is too early to draw any strong conclusions about the impact of the DMO from this preliminary analysis.

The July 2019 dataset represents a static snapshot of a point in time around three weeks after the introduction of DMO prices. In a dynamic market, we expect electricity retailers will respond to competitors by adapting their offerings and pricing, meaning significant changes would become apparent over a longer period of time.

In the longer term, we will be looking at metrics in addition to observed prices to understand if and how the DMO has influenced the market, such as changes to retailer market share, numbers of customers on standing offers, levels of competition between retailers, retailers entering and leaving the market, and levels of customer engagement.

What is the DMO?

The DMO is a new Commonwealth Government policy measure that limits what retailers can charge electricity customers on standing offer contracts.

In 2018 the ACCC found standing offer contracts:[16]

- were no longer working as a safety net, as originally intended
- were unjustifiably expensive, with retailers having incentives to increase standing offer prices as a basis to advertise artificially high discounts
- penalised customers who had not taken up a market offer, acting as a 'loyalty tax'.

To address these concerns the ACCC recommended the introduction of a default market offer that would be a cap on what retailers could charge residential and small business standing offer customers.

15 Other causes for customers being on standing offers include poor or no credit history or for not engaging with the market for whatever reason.

16 ACCC, *Restoring electricity affordability and Australia's competitive advantage, Retail Electricity Pricing Inquiry—Final Report*, June 2018, p. xi.

The Commonwealth Government accepted the recommendation and made the regulations to give effect to the DMO, which came into effect on 1 July 2019.[17]

The AER's role under the regulations is to determine DMO prices each year for each network distribution area and customer type. In April 2019, we published our first DMO prices determination, covering the period 1 July 2019 to 30 June 2020.

All retailers must apply DMO prices in network distribution areas where there is no other retail price regulation – south-east Queensland (Energex), New South Wales (Endeavour, Essential Energy and Ausgrid) and South Australia (SA Power Networks - SAPN).

While the DMO is a cap on what retailers can charge, it is not a cap on customers' bills. Individuals' bills will depend on how much electricity they use and their retailer's specific charges.

Under the regulations, the DMO price also acts as a reference price that retailers must compare all their plans against when they provide pricing details in advertising, on their websites, or other places. It is designed to make it easier for customers to compare energy plans across different providers.

The ACCC was clear that the purpose of the DMO was to act as a fall-back for those who are not engaged in the market, and should not be a low-priced alternative to a market offer. It was intended to reduce unjustifiably high standing offer prices, while allowing retailers to recover their costs in servicing customers, and providing customers and retailers with incentives to participate in the market.

We have met these objectives by setting the DMO at a price where standing offer customers will see price reductions, but where retailers still have incentives to compete on price, invest and innovate with their market offers. We set the DMO price in each distribution at the mid-point (50th percentile) in the range between the median standing and median market offer.[18]

The DMO and affordability

The introduction of DMO pricing will have an impact on affordability for standing offer customers in the regions where it applies.

Approximately 681 000 residential customers across South Australia, south-east Queensland and NSW are on standing offers (between 9 and 14 per cent of all customers, depending on region). Around 115 000 small business customers (15 to 23 per cent) are on standing offers.

For customers on high-priced standing offers prior to 1 July 2019, the savings from moving onto the DMO price can be significant.

DMO impact on market offers

While the new DMO regulations do not directly affect what retailers can charge for their market offers, it is a significant regulatory intervention and may have positive and negative indirect impacts on market offer affordability in the longer term.

For example, some stakeholders have noted risks the introduction of DMO prices could make market offers less affordable for some engaged customers if retailers responded by withdrawing low-priced offers to cover DMO-related revenue losses.

Conversely, competitive forces may prevent retailers from withdrawing low-price offers, while greater price transparency due to the introduction of the reference price may facilitate competition among retailers by simplifying the task of customers identifying the cheapest deals.

We will be closely monitoring this section of the market to identify possible issues and discuss this further in the next section.

17 Competition and Consumer (Industry Code – Electricity Retail) Regulations 2019.

18 AER. AER *Final Determination – Default Market Offer Prices 2019-20*, April 2019.

DMO methodology and affordability analysis

The DMO regulations require us to determine an annual usage amount for the purposes of developing annual DMO prices.

For residential customers, we determined annual usage using average consumption data provided by the network distribution businesses. These benchmark figures therefore vary between different areas.

For small business customers, we used 20 000kWh as the annual usage. This figure was developed by Energy Consumers Australia.

For consistency and comparability, the charts and pricing analysis in this section use the same annual usage as our DMO determination. We note the DMO usage assumptions are different from those used in the affordability analysis in the main section of this report.

We have added the relevant annual DMO usage figure beneath each chart.

Preliminary observations

Standing offers

The new regulations require that retailers' standing offer prices must not exceed the DMO price for that network distribution area and customer type.

In practice, this means retailers whose standing offer prices were above the DMO price (more than 90 per cent of retailers in most areas) have reduced these to the DMO price or lower.

For a residential customer using the benchmark consumption level, the annual bill reductions from moving from the median standing offer to the DMO price were approximately:[19]

- In NSW:
  - $129 in Ausgrid's network distribution area
  - $175 in Endeavour Energy's area
  - $181 in Essential Energy's area
- $118 in south-east Queensland (Energex)
- $171 in South Australia (SAPN).

For small business customers on the benchmark consumption level, annual median savings were approximately:

- In NSW:
  - $878 in Ausgrid's network distribution area
  - $579 in Endeavour Energy's area
  - $709 in Essential Energy's area
- $457 for South-Eastern Queensland (Energex)
- $896 for South Australia (SAPN).

Market offers

This section looks at changes to highest, lowest and median market offer prices before and after the introduction of the DMO on 1 July 2019.

It shows these changes over three points in time:[20]

- October 2018 – the same data that informed our DMO *Final determination*. The offers in this dataset preceded the announcement of our DMO
- June 2019 – immediately before the introduction of the DMO
- July 2019 – immediately after the introduction of the DMO.

19 As at October 2018.

20 Specifically: 1-31 October 2018, 1-30 June 2019 and 27 July 2019.

Figures 25 to 36 show these movements in graph form.

Slightly different trends emerge in the comparisons between October 2018 and July 2019, and June 2019 (immediately before the DMO introduction) to July 2019.

This may reflect different pricing strategies by retailers reacting early in June 2019 in anticipation of DMO changes. Our analysis considers trends from October 2018, which pre-dates the publication of our DMO methodology and therefore is not influenced by any DMO-related retailer strategies. We also review the price changes made just before the DMO came into effect.

We also note that from 1 July 2019, network prices increased in some areas (Essential and SAPN) but reduced or remained flat in all other areas. Network charges form a major component of retail pricing (accounting for around 40 per cent of a retail bill), and retail price changes may be explained in part by changes in these costs.

Overall, the trends suggest retailers used the introduction of the DMO to rationalise their range of market offers and, in many cases, simplify their offerings by moving away from conditional discounts. We will continue to monitor these changes over the longer term.

Highest price market offers

The highest residential market offer, of any retailer in July 2019, was lower in all areas in comparison to October 2018, with the exception of Energex's area, where it remained flat.

For residential market offers, these reductions generally occurred before June 2019, meaning the figure remained flat between June 2019 and July 2019. The exception to this trend was in SAPN's area, where the highest offer decreased by 11 per cent between June 2019 and July 2019. These trends varied by retailer size. For example:

- between June 2019 and July 2019, the highest market offer of any of the largest three 'Tier 1' retailers (Origin Energy, AGL and EnergyAustralia) reduced in all areas (between 3 and 10 per cent) to converge on the DMO price of each area
- among Tier 2 retailers, the highest market offer fell by up to 17 per cent (depending on area) between October 2018 and June 2019. It remained flat between June 2019 and July 2019.

For small business offers, between October 2018 and July 2019, the highest small business market offer decreased significantly in Ausgrid, Endeavour and Essential Energy's areas, but increased by 16 per cent in SAPN's area. A similar trend is observed between June and July 2019, where the highest market offers have decreased by 2 and 10 per cent in Ausgrid, Endeavour, Essential and Energex, but increased by 16 per cent in SAPN's area.

Lowest price offers

Across all retailers, the lowest residential offer decreased from October 2018 and July 2019 (by up to 3 per cent) with the exception of Essential Energy's area, where it increased by 2 per cent.

Pricing trends in regard to the lowest available market offer varied between retailer segments and areas.

The lowest offers of Tier 1 retailers:

- reduced or remained flat between October 2018 and June 2019
- increased between June and July 2019 between 3 to 9 per cent (depending on area).

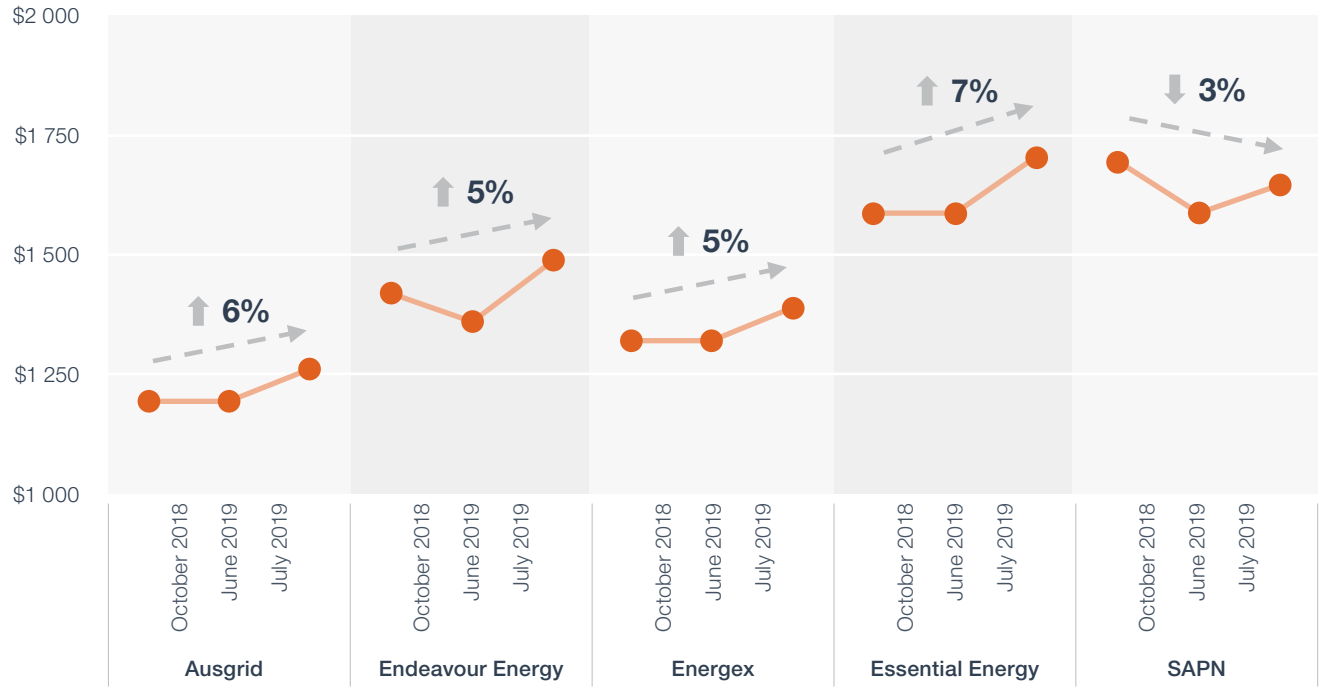
This resulted in an overall increase of Tier 1 retailers lowest market offers by 5 to 7 per cent between October 2018 and July 2019. SAPN's area was the only exception, with the lowest offer reducing by 3 per cent over this period.

Around 70 per cent of residential electricity customers in the DMO areas are with a Tier 1 retailer.[21]

Figure 25 shows changes to Tier 1 retailers' lowest flat rate residential offers.

21 AER, 'Annual report on compliance and performance of the retail energy market 2017–18, November 2018. https://www.aer.gov.au/system/files/Annual%20Report%20on%20Compliance%20and%20Performance%20of%20the%20Retail%20Energy%20Market%202017-18_0.pdf

Figure 25: Changes to annual bill for lowest residential market offer of any Tier 1 retailer, October 2018–July 2019



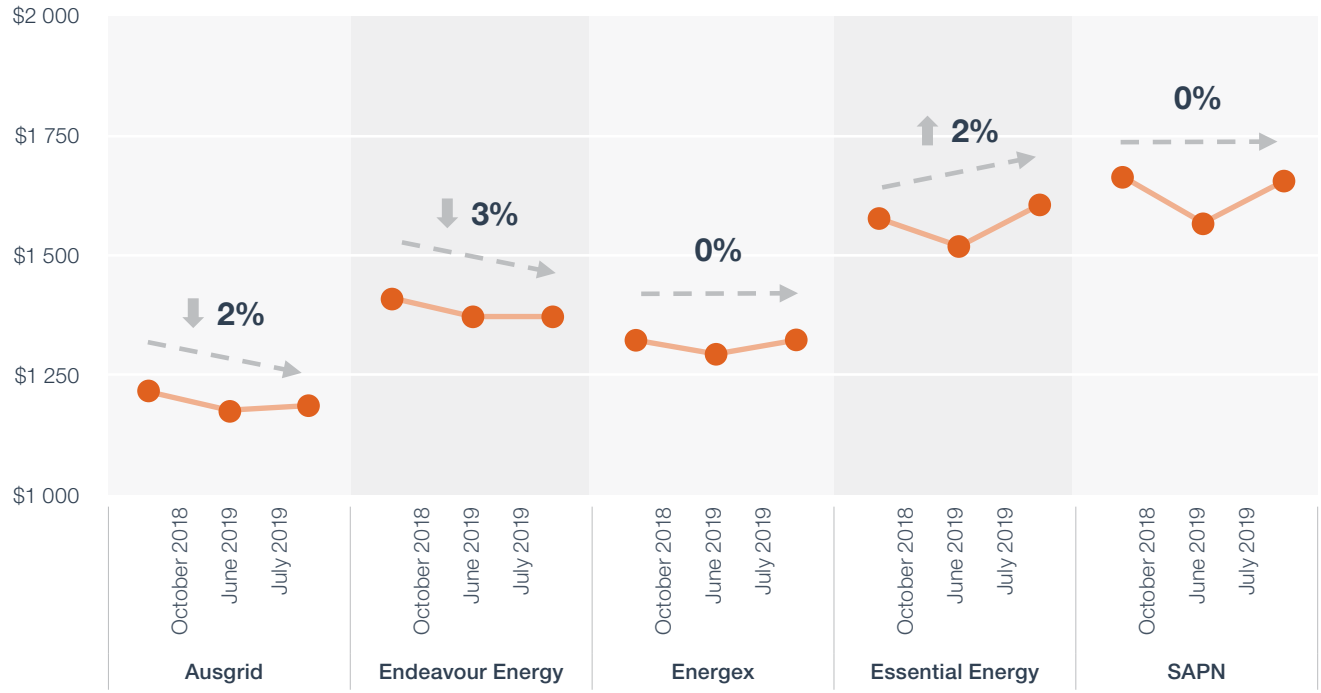
Among Tier 2 retailers the lowest priced offers generally decreased between October 2018 and June 2019. The changes between June 2019 and July 2019 were mixed. Tier 2 market offers increased in Energex's, Essential Energy's and SAPN's areas over this period but did not change in the remaining areas.

Between October 2018 and July 2019, for Tier 2 retailers, this resulted in:

- an overall increase of 2 per cent in Essential Energy's area
- no overall change to the lowest offer in Energex and SAPN's areas
- overall decreases of 2 and 3 per cent in Ausgrid's and Endeavour Energy's areas respectively.

Figure 26 shows changes to Tier 2 retailers' lowest flat rate residential offers.

Figure 26: Changes to annual bill for lowest residential market offer of any Tier 2 retailer, October 2018–July 2019



For small business offers, the lowest price offer also varied between October 2018 and July 2019. The lowest offer of any retailer in Ausgrid, Endeavour Energy, SAPN and Energex's areas decreased over this period, ranging from 6 to 17 per cent depending on the area. The exception was in Essential Energy's area, where the cheapest business offer did not change. When compared to June 2019, the lowest market offer showed mixed trends — it reduced in Endeavour, Energex and Essential Energy's areas (between 2 and 10 per cent), did not change in Ausgrid's area and increased in SAPN's area by 5 per cent.

Median market offer price

Across all retailers and areas, the median market offer price did not change significantly between October 2018 and July 2019.

Over this period the changes ranged from a reduction of 3 per cent to an increase of 3 per cent for residential offers. During the same period, Tier 1 retailers' median market offers reduced by 2 to 5 per cent.

For small business offers, the median reduced by 3 per cent between October 2018 and July 2019.

Market offer numbers

The total number of unique market offers for residential customers fell in July 2019 by 17 to 26 per cent (depending on the area) compared to October 2018.[22] This suggests retailers are rationalising the number of market offers available in July 2019. The trend was similar for small business offers.

The proportion of market offers below the DMO price in each area increased. In October 2018, 76 to 89 per cent of offers were below the DMO price compared to 88 to 97 per cent below in July 2019.

Table 4 shows the change in the number of market offers between October 2018 and July 2019.

Table 4: Total number of market offers, October 2018–July 2019

Distribution Area	Residential flat rate			Small business		
	Total MOs Jul 2019	Total MOs Oct 2018	% difference	Total MOs Jul 2019	Total MOs Oct 2018	% difference
Ausgrid	41	50	-18%	31	49	-37%
Endeavour Energy	42	53	-21%	33	51	-35%
Energex	35	45	-22%	30	36	-17%
Essential Energy	44	53	-17%	34	51	-33%
SAPN	31	42	-26%	28	39	-28%
Total	**193**	**243**	**-21%**	**156**	**226**	**-31%**

Discounting

Retailer discounting practices are an area where significant shifts in retailer behaviour have clearly occurred from 1 July 2019.

There are likely to be a number of reasons for this, directly and indirectly related to the new DMO regulations, including:

- the prohibition on retailers promoting conditional discounts as their most prominent discount
- the requirement to show the annual cost of market offers as a percentage in relation to the DMO price, and a reluctance to show offers as higher than the DMO price.

22 Unique market offers means offers with identical usage and fixed charges.

Other regulatory developments are also likely to have influenced retailers' approach to discounting, including:

- the recent *Preventing discounts on inflated energy rates* rule change that prohibits retailers from offering discounts where customers would definitely be worse off under the undiscounted market offer than under the standing offer.[23]
- the recently commenced *Regulating conditional discounting* rule change consultation, proposing that the level of conditional discounts restricted to the 'reasonable cost savings' that a retailer expects to make if a customer satisfies the conditions of the discount.[24]

Across the board there was a significant reduction in the prevalence of offers with conditional discounts (those where a customer must take some action to receive the discount – such as paying on time), for residential and small business offers.

The number of retailers who had at least one residential offer with a conditional discount fell between 23 to 33 per cent (depending on the zone) following the introduction of the DMO compared to October 2018. Business offers showed similar trends.

The proportion of market offers with conditional discounts reduced from around 47 to 56 per cent of total offers (depending on area) to around 13 to 25 per cent between October 2018 and July 2019. Corresponding to this marked decrease, guaranteed discounts (those where a customer does not need to take any action) increased in prevalence, from the 11 to 15 per cent range in October to the 23 to 29 per cent range in July for residential offers.

This increase was not reflected in business offers, where the prevalence of both conditional and guaranteed discounts decreased.

The size of conditional discounts also decreased in all areas once the DMO was in effect:

- In October 2018, the highest residential conditional discount (of any retailer) in each zone ranged from 25 to 40 per cent depending on zone, while the median conditional discount ranged from 15 to 18 per cent
- In contrast, in July 2019, the highest discount range was 15 to 25 per cent. The median conditional discount reduced marginally, ranging from 10 to 15 per cent.

Of note, the maximum conditional discount peaked in June 2019 at 42 per cent (in Ausgrid, Endeavour Energy, and Essential Energy), which could suggest a push from some retailers to attract new customers with big discounts before the new reference price advertising rules commenced.

While there has been a reduction in the size of the discounts from 1 July 2019, both standing offers and market offers prices have reduced to the DMO level. Therefore, this may reflect a rebalancing in how retailers structure tariffs. This can be observed from the fact that despite the reduction in size of conditional discounts, average bill amounts with conditional discounts have reduced by up to 4 per cent in July 2019.

Another significant change in retailer discounting practices was the application of discounts. In October, over half of conditional offers (residential and business) featured discounts off usage only. In July, this type of discounting had decreased to the 6 to 23 per cent range.

Highest, lowest and median market offer changes, Oct 2018-Jul 2019 – by distribution area

We note the charts in this section and the annual price analysis are based on different assumptions than those in the preceding affordability analysis.

Usage assumptions for residential flat rate are derived from network data, and are different for each distribution area. These are included under each chart.

A flat figure of 20 000kWh is assumed for small business customers.

Appendix C provides a full account of the assumptions behind the DMO annual bill calculations. All bills include GST.

23 AEMC. 'Preventing discounts on inflated energy rates' rule change. 2018. www.aemc.gov.au/rule-changes/preventing-discounts-on-inflated-energy-rates.

24 AEMC. 'Regulating conditional discounting' rule change, 2019. www.aemc.gov.au/rule-changes/regulating-conditional-discounting.

Figure 27: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Ausgrid residential flat rate

Annual bill based on annual usage of 3 900kWh per year

Figure 28: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Ausgrid small business flat rate

Annual bill based on annual usage of 20 000kWh per year

Figure 29: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Endeavour Energy residential flat rate

Annual bill based on usage of 4 900kWh per year

Figure 30: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Endeavour Energy small business flat rate

Annual bill based on usage of 20 000kWh per year

Figure 31: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Energex residential flat rate

Annual bill based on 4 600kWh usage per year

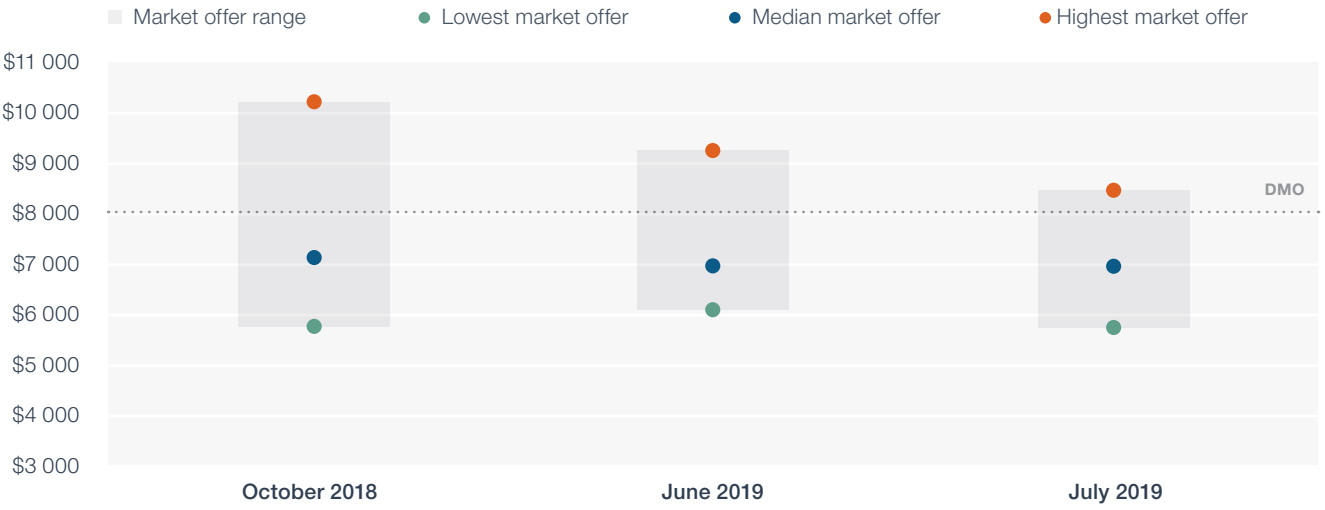
Figure 32: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Energex small business flat rate

Annual bill based on usage of 20 000kWh per year

Figure 33: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Essential Energy residential flat rate

Annual bill based on usage of 4 600kWh per year

Figure 34: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), Essential Energy small business flat rate



Annual bill based on usage of 20 000kWh per year

Figure 35: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), SAPN residential flat rate

Annual bill based on usage of 4,000kWh per year

Figure 36: Changes to highest, lowest and median annual bill of all retailers (inc. all discounts), SAPN small business flat rate

Annual bill based on usage of 20,000kWh per year

Appendix C: Default Market Offer bill calculation methodology

This section sets out the DMO annual bill calculation assumptions and the usage information for the DMO analysis.

This methodology is consistent the same as used in our DMO prices final determination.

We note these assumptions are not the same as those used for the affordability analysis (as set out in appendix B) due to the different purposes and background of each project.

Annual bill calculation assumptions

Table 5: Annual bill calculation assumptions

Subject	Specifications
Unique data set	For offers to be considered unique, the following criteria are used: • Contract type (standing, market) • Retailer • Total annual bill (unconditional, conditional) • Fixed component (unconditional, conditional) • Usage component (unconditional, conditional)
GST	Annual bill includes GST.
Demand charges	Any offers with a demand charge are removed from the data.
Usage profile	Daily consumption is assumed to be the same across the year with no adjustments for seasonality.
Days per year	365 days per year. No further adjustment made for leap years.
Discounts	Discounts on unconditional and conditional offers are applied to usage and supply as per each offer (percentage or dollar amount) as applied in *EnergyMadeEasy*.
Fees	Incidental fees, such as connection fees, disconnection fees, late payment fees, direct debit dishonour payment fee, credit card processing fee, credit card merchant service fee, direct debit payments fee, establishment fees, are excluded for the calculation of the annual bill.
Membership fees	This annual fee is effectively a supply charge, hence is included in the calculation of the annual bill.
Metering charges	Ongoing metering charges are included in the calculation of the annual bill. Up-front metering charges are excluded, as there is no set scenario that would apply to most customers.
Bundling	No bundling included, such as gas, phone, internet, mobile, pool services.
Green charges	Assumption of no additional payment for green schemes to calculate the annual bill. Offers including green supply are removed from the data.
PV / Solar feed in tariffs	Assumption of zero PV solar exported. Offers with 'solar', 'FiT' and 'FI' are removed from data.

Model annual usages

The annual bills are calculated based on the consumption profiles consistent with our *Final determination*.[25] These are set out in table 6.

Table 6: Model annual usage by distribution area

Distribution Zone	Residential - flat rate#	Small business^
Ausgrid	3 900 kWh	20 000 kWh
Endeavour	4 900 kWh	20 000 kWh
Energex	4 600 kWh	20 000 kWh
Essential Energy	4 600 kWh	20 000 kWh
SAPN	4 000 kWh	20 000 kWh

Source: Network distribution businesses' annual pricing proposals

^ **Source:** Energy Consumers Australia, SME Retail tariff tracker

25 AER. AER *Final Determination – Default Market Offer Prices 2019-20*, April 2019.