



EnergyAustralia

LIGHT THE WAY

2 February 2018

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Dear Mr Adams

2018 – AER - Approach to electricity wholesale market performance monitoring – Draft Statement of Approach

EnergyAustralia is one of Australia's largest energy companies with over 2.6 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion dollar energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market (NEM).

We welcome the opportunity to comment on the AER's draft approach to its new wholesale electricity market performance monitoring function. We have provided feedback on the draft approach to: suggest sources of primary financial market data as requested by the AER; reinforce the risks of relying on single analytical tools; seek clarification on how these tools will be applied to the NEM; and to recommend that the AER's examination of regulatory risks should be broader than energy policy uncertainty. EnergyAustralia recognise that the AER's approach to this new function will evolve and we encourage the AER to continue to engage with stakeholders throughout this process.

Use and interpretation of analytical metrics

The AER have proposed a wide range of analytical metrics to assess the structure and performance of the market. EnergyAustralia urge caution in the application of these metrics and their interpretation. The AER have highlighted that a combination of metrics will be used to draw conclusions as each approach has its own merits and limitations. EnergyAustralia support this approach and request the AER ensure that the limitations and merits are clearly articulated in the final reporting, along with guidance on how results should be interpreted.

The AER should also identify the appropriate dataset to be used for each metric and clarify these in the final approach paper. Care should be taken to identify whether it is most appropriate to assess energy generation, capacity, or capacity utilisation, and whether analysis will be conducted on annual, monthly or hourly data. When assessing the efficiency of investment in reserve capacity, the AER should consider the types of

capacity separately; while there may be sufficient headline capacity in the market, there may be insufficient firm capacity or peaking capacity to meet the reliability settings. Identifying the correct dataset is critical to ensuring that accurate conclusions can be drawn about the performance of the market.

Assessing regulatory impacts

The AER have identified that policy uncertainty could be detrimental to the efficiency of the market by obfuscating market signals for investment. In addition to Federal and State energy policy, we suggest the AER considers a broader range of government actions that could contribute to market uncertainty and higher barriers to entry.

Some examples of government activities that could detrimentally affect efficient market signals include:

- Increased volume of direct market intervention by AEMO and government including directions for synchronous generation to operate, use of Reliability and Emergency Reserve Trader, or market suspension.¹ Interventions may be necessary to manage short term system security issues but a sustained increase in the frequency of events may impact on market investment signals.
- Market subsidies for particular technologies rather than efficient capacity investment (e.g. renewable energy targets, solar feed-in tariffs).
- Increased government participation in wholesale markets risks crowding out private sector investment. Recent developments include proposals for government owned generation (Snowy 2.0, new gas capacity in South Australia, diesel capacity in South Australia and Victoria).
- The uncertainty generated by the high volume of inter-related reviews of wholesale market structures and operations and their potential recommendations for change.
- Delayed action on emerging issues such as the impact of high levels of wind and solar penetration and closure of firm thermal generation on system security in South Australia, addressing AEMO's visibility of increasing volumes of non-scheduled generation in central dispatch, or establishing a stable carbon policy.

While regulatory changes are expected, rapid and high volumes of unanticipated changes can generate market uncertainty, reducing investor confidence. For example, the increased use of RERT could impede investment for new peaking capacity, despite an increase in Lack of Reserve notices to the market. The risk could be heightened if rule change processes are unnecessarily expedited or circumvented altogether by Ministerial direction. The AER should consider a broad range of government activities to assess whether these decisions, independently or in aggregate, have impacted on market efficiency.

¹ <https://www.aemo.com.au/Electricity/National-Electricity-Market-NEM/Market-notice-and-events/Market-event-reports>

Obtaining information to assess financial markets

AER have indicated that poor visibility of the financial market will affect their ability to assess the wholesale market and have requested guidance from stakeholders on how they can obtain this information. EnergyAustralia is of the view that data available through the Australian Securities Exchange (ASX) and the Australian Financial Markets Association (AFMA) will be sufficient for the AER to assess the impact of contracting on the NEM.

The majority of financial trading information will be available through the ASX as participants have steadily increased use of derivatives and reduced use of over-the-counter (OTC) products. This is evident in data provided by AFMA showing an annual average growth in futures contract volume of 9.0% between financial years 2011 and 2017.² There would be limited additional pricing information obtained by examining OTC contracts as these are usually priced relative to the derivatives market, with adjustments made to reflect the bespoke elements of the contract. To assess OTC contracting, EnergyAustralia suggest the AER utilise the AFMA surveys published annual in the Australian Financial Markets Report.³ These surveys were completed annually until 2015 and provided information on market turnover by implement and region. While the survey has been discontinued for the past few years, industry intends to re-establish the survey. Work has commenced and the first report is expected to be published in 2018 and may include updates to capture historical data between 2016 and 2017.

Continuing consultation

In the consultation paper, the AER have indicated their intent to continue to engage with stakeholders during 2018. We support this proposition and request more information regarding how this consultation will proceed; including the proposed frequency and purpose of future engagement.

This is the first time this assessment has been conducted by the AER and we recognise that the approach taken will change as the AER develops its processes and analytical tools. We see that it is imperative for the AER to continue to engage with stakeholders during 2018 as the report is developed to ensure that the AER's analysis remains relevant and appropriate. Between publication of the final statement of approach in March and the final monitoring report in December 2018, we would like to be informed on any changes to the approach including additional or retracted areas of work, further details on areas of analysis that are not fully described in the approach paper, and interpretations of preliminary results. This will allow stakeholders to support the AER by providing feedback on the approach and accuracy of the conclusions.

In particular, we request that the AER undertake further engagement prior to compelling confidential data under section 28 of the NEL. We understand that the AER intend to only use these powers if a potential issue is identified. We request that the AER first engage with stakeholders to discuss their concerns and the data they may be seeking. This will ensure that participants and assist the AER in understanding the results and provide

² 2017 Australian Financial Markets Report, AFMA, <https://afma.com.au/data/afmr/2017%20AUSTRALIAN%20FINANCIAL%20MARKETS%20REPORT.pdf>, Page 18

³ <https://afma.com.au/data/AFMR>

guidance on further sources of public information they can utilise to complete their analysis.

The AER have also identified that they will seek to engage with stakeholders to obtain primary information on the market via voluntary surveys and bilateral discussion. EnergyAustralia is supportive of this approach and will provide assistance as requested.

If you would like to discuss this submission, please contact Georgina Snelling on 03 8628 1126 or Georgina.Snelling@energyaustralia.com.au.

Regards

Melinda Green

Industry Regulation Leader