AMPC

SNAPSHOT

REVIEW OF ACCC REPORT ON ELECTRICITY AFFORDABILITY AND AUSTRALIA'S COMPETITIVE ADVANTAGE

Project Report Reference: 2019-1005 **Date: 1 August 2018**

Project Description

This Project provides a timely assessment of the implications for the red meat industry of the findings of the ACCC's report on electricity affordability and Australia's competitive advantage.

Project Content

The Project entailed reading the ACCC's report and addressing the following requirements:

- Potential impact on red meat processors.
- Sub-sectors most significantly affected.
- Potential scale of the implications.
- Actionable conclusions and recommendations.

Project Outcome

Some of the key findings of the ACCC report of relevance to red meat processors are:

- The ACCC claims that achievable savings for commercial and industrial (C&I) customers are estimated to be 26 per cent by 2020-21. The Commission does not provide a breakdown of this figure by State. The savings for C&I customers is larger than for residential customers because wholesale costs make up a proportionately larger share of their prices so the significant savings to the wholesale component have a bigger impact for these customers.

- Over the period from 2007–08 to 2017–18, the average cost of electricity for C&I customers increased noticeably across the NEM. On a c/kWh basis, the price increase was around 58 per cent in real terms. The ACCC breaks the components of prices into wholesale costs, network costs (transmission and distribution), environmental (green) scheme costs, and retail costs and margins. Network, and more recently, wholesale costs have made up the majority of the price increases over the period, contributing 35 and 45 per cent respectively. Retailer cost information provided to the ACCC shows that on a NEM-wide basis, wholesale costs accounted for 34 per cent of the retailer cost stack in 2017–18.

- The ACCC has learnt from consultations with medium-sized businesses that engaging with the wholesale market is generally unattractive due to the complexity of managing energy procurement and the difficulty around procuring competitively priced hedging contracts, particularly in markets with limited liquidity.

- The ACCC report notes that Australian electricity prices, gross margins and net margins are among the highest in the world.[1] According to the ACCC, South Australia has amongst the highest electricity prices in the world. It is comparable to Denmark and Germany which have substantial green taxes. NSW, Victorian and Queensland prices are also high compared to prices overseas. The averaged NEM price is higher than the average across the EU. This underscores the electricity affordability issues facing Australian energy users. Retail margins in Victoria and NSW as a percentage of total electricity bill are higher than all the international regions sampled. The NEM-wide average, which is dominated by these states, is also very high.

The ACCC report contains little that is directly aimed at addressing the electricity cost disadvantage being faced by the red meat processing industry. Its recommendations could serve to address them indirectly to some extent, though actions aimed at increasing competition in the supply of electricity.

There are some key recommendations which relate indirectly to C&I customers such as the red meat processing industry because they would reduce overall costs and hence large business would benefit as well as other electricity users. These are identified below in the discussion of the relevant rea of the market to which the recommendations relate. They include:

- The Australian Government should operate a program under which it will enter into low fixed-price (for example, \$45–\$50/MWh) energy offtake agreements for the later years (6–15) of appropriate new generation projects which meet certain criteria

- There should be a prohibition on acquisitions and other arrangements (other than investment in new capacity) that would limit market shares to 20 per cent in any NEM region and across the NEM as a whole to prevent further harmful concentration.

- The Queensland Government should divide its generation assets into three generation portfolios to reduce market concentration in Queensland, with each portfolio separately owned and operated to drive competition in generation markets.

- Governments of Queensland, NSW and Tasmania should take immediate steps to remedy the over-investment of their network businesses in order to improve affordability for consumers. With appropriate assistance from the Australian government, this can be done: in Queensland, Tasmania and for Essential Energy in NSW, through a voluntary government write-down of the regulatory asset base (RAB)

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- In NSW, where the assets have since been fully or partially privatised, through the use of rebates on network charges (paid to the distribution company to be passed on to consumers) that offset the impact of over-investment.

- Any costs remaining from premium solar feed-in schemes should be borne by state governments through their budgets, as Queensland has done, rather than being recovered through charges to electricity users. Further, the ACCC is recommending that the Small Scale Renewable Energy Scheme (SRES) should be wound down and abolished by 2021 to reduce its impact on retail prices paid by consumers.

How do the ACCC's recommendations translate into lower costs?

- Wholesale prices reduction – The ACCC has assumed an effect of $5/MWh for government assistance for new entry in generation/ self-supply.

- Network costs reduction – The ACCC has assumed a reduction in bills by the amount of its recommended Regulatory Asset Base write down. These total an estimated $10.3 billion.

- Environmental costs - The main saving here is bringing premium solar FiT schemes onto state budgets.

- Retail prices - For market offer customers, the ACCC has assumed it is achievable to get 20 per cent of customers on market offers with discounts between zero and 10 per cent to move to market offers with discounts of at least 30 per cent.

The impact of the ACCC's recommendations on red meat processors could be expected to vary among processors. The ACCC claims achievable savings for commercial and industrial customers of 26 per cent by 2020-21 but the Commission does not provide a breakdown of this figure by State.

These cost savings are likely to be more beneficial to the more intensive users of electricity i.e. those with a higher usage per unit of output. This may not necessarily be the bigger volume users, since they may actually be more inclined to adopt technologies which save on energy usage per unit of output. Similarly, those processors with a more modern plant setup that uses up-to-date energy measurement and control systems may have already generated reductions in energy usage and hence will benefit relatively less from reduced prices than older and less energy-efficient plants.

However, the relatively modest cost savings envisaged by the ACCC report in the context of the huge increase in prices experienced in recent years suggests the lowering in prices will not serve as a disincentive for older and less energy- efficient plants to improve their energy efficiency.

Most of its actions directly aimed at reducing costs for business users are targeted at small and medium business. Should the ACCC's recommendations achieve their objectives, the cost of electricity is forecast to fall by 26% for commercial and industrial users. Whilst this would be most welcome, there are a number of reasons to be cautious about this projected outcome.

Taken together these considerations suggest the possibility that the solutions being proposed by the ACCC may not be sufficient in terms of impact or timeliness to address the major international costs disadvantage faced by the Australian red meat processing industry.

Actionable recommendations for the industry are:

1. The industry should undertake research with a view to ensuring that government policies reflect the need for the industry to have access to energy costs that are competitive with those of its key international competitors.
2. The industry should continue to monitor, review and evaluate from the perspective of the industry the progress and outcomes of the ACCC report and the NEG given the significance of energy costs to the economic sustainability of the industry in making progress towards achieving the primary test of international competitiveness.
3. The industry should investigate the potential of the various inceptives offered under the NEG in terms of their potential for use by the industry. In this regard, the industry should investigate the potential for processors to access the Emissions Reduction Fund on a preferred basis, given the energy intensity and trade-exposed nature of the industry.
4. The industry should undertake research that supports industry in its energy policy-related initiatives, including gathering of data on energy usage by volume and type for plants with different characteristics e.g. of different size, in different locations, and with different plant configurations, to augment data on energy costs.
5. The industry should undertake research that assists development of an industry policy on the moratoria currently inhibiting the development of new gas supply.

Benefit for Industry

The overall benefit to the industry is the provision of a timely assessment of the implications for the red meat industry of the findings of the ACCC's report on electricity affordability and Australia's competitive advantage

The benefit of this work will be that AMPC and its members have a better understanding of the ACCC report and its implications in the context of the red meat processing industry.

This analysis flows on naturally from the research undertaken in Project 2017-1062 Milestone 12 report (the 'Cost to Operate report') and will have value in the process of research developing detailed policy recommendations for the industry as suggested by that Report.