snowy hydro Limited
renewable energy

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Mr Michael Rawstron
General Manager
Regulatory Affairs – Electricity
Australian Competition and Consumer Commission
PO Box 1199
DICKSON ACT 2602

Delivered by e-mail to: electricity.group@accc.gov.au

Dear Michael

Response to Draft Determination – Bidding and Rebidding Code Changes

Snowy Hydro Limited (SHL) appreciates the opportunity to comment on this draft determination.

SHL believes that, consistent with code objective 1.4, market regulation should be "light-handed". The proposed code changes in this matter are heavy-handed and intrusive in the context of unfettered market operation.

It is unclear in SHL's opinion what precise market failure the proposed code changes are seeking to remedy. This is of genuine concern to SHL, given the interventionist nature of the proposals at hand.

Possibly the proposed code changes seek to address the public and political perception of NEM spot price outcomes. As the discussion to follow will demonstrate, these perceptions are not fully informed and unrepresentative of the true operation of the NEM.

Alternatively, the intention is to curtail the market's response to potential structural deficiencies, in what is essentially, a maturing market. If this is the case, SHL's position is that the operation of market forces over the medium to long term will stimulate the resolution of these potential structural shortcomings. Curtailing the freedom of market participants in the short-term will jeopardise the long-run efficiency of the NEM and run counter to the *modus operandi* of energy market reform.

At the Rebidding Forum convened by the ACCC on the 26 February 2002, the National Retailer Forum (NRF) indicated that the market was virtually fully hedged at a level above 90%. Thus, retailer spot market exposure is less than 10%. Furthermore, suggestions of a direct, and positive linkage between historical, atypical, intra-day spot price volatility and long-term contract pricing ignores the fundamental difference between their respective drivers. In the short-run, market participants, given the immediate market conditions, act to maximise profit. Longer-term contract negotiations however, 'price in' the investment incentives being communicated via current spot market outcomes. To the extent that current spot market outcomes encourage investment in the medium to long-term, the relationship between spot market pricing and contract market pricing is likely to be negative rather than positive.

SHL would emphasise that regulators and user advocacy groups look to contract market indicators such as the AFMA forward curve and Electricity Broker screens for a true indication of the state of the market. This available contract information needs to be incorporated into the analysis of the competitiveness of the NEM. This information in conjunction with spot market information will enable a complete and fair assessment of the NEM.

SHL also espouses that the role and magnitude of demand side management has been diluted and not fully taken into account. Anecdotal evidence suggests that as a percentage of total system demand, demand side response could constitute 5% of this demand. This is a very important point because the bulk of the analysis has been on the supply side. The demand side operates at the very steep knee point of the supply curve and hence has a lot of "leverage" on the resultant spot price outcome.

Analysis of spot market outcomes must also give consideration to the ownership of generation assets by NEM retailers. In the context of spot exposure, these assets undeniably, provide an internal hedge to retail operators. The extent of this hedging mechanism must be considered in addition to the more transparent contractual hedges. To quantify, participants operating in the retail sector own 5% of the NEM's installed generation capacity.

A detailed analysis of the NEM's performance would not view spot price outcomes in isolation. It is essential that account be given to;

i. Demand side responses – potentially 5% of total system demand;
ii. The internal generation capabilities of NEM retailers – 5%;
iii. The extent of hedging undertaken by NEM retailers – greater than 90% hedged, less than 10% spot market exposure; and
iv. The complexity of the relationship between spot market and contract market outcomes.

The debate's focus on high and volatile spot market prices has been over emphasized and is misleading.

The major issue for Australia is future private investment in new generation and its impact on competition and future electricity prices in the longer-term. Regulators need to be aware of the trade-offs in short-term regulatory intervention and its impact on long-term market outcomes.

In conclusion we espouse that until the short term and the long term implications of the proposed code changes are fully understood the code changes as presented should be rejected.

If you have any enquiries in relation to this issue then I can be contacted on (02) 9278 1862.

Yours faithfully,

for Kevin Ly
Manager, Market & Regulatory Strategy