



The Australian Industry Group  
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ABN 76 369 958 788

22 February 2017

Ms Sara Mirabella  
Australian Competition and Consumer Commission  
GPO Box 3131  
CANBERRA ACT 2601

By email: [adjudication@accc.gov.au](mailto:adjudication@accc.gov.au)

Dear Ms Mirabella

### **A91567 & A91568 – SACOME & Ors - submission**

We are writing in response to the ACCC's request for comment on the application by the South Australian Chamber of Mines and Energy (SACOME) and others for authorisation to take certain collective and coordinated individual actions to secure electricity supply in the South Australian market for an 11 year period.

The applicants include both members and non-members of the Australian Industry Group and we are closely mindful of the wider interests of energy using businesses in South Australia. Ai Group supports the application and we believe that it offers the potential for wider benefits during a very difficult period for South Australian energy users.

Brief answers follow to several of the questions raised by the ACCC.

### **Likely future without**

- 1. Please identify major developments expected to impact on the wholesale and retail electricity industries in South Australia in the coming decade.**

The electricity sector is undergoing major change across the National Electricity Market and the outcomes are difficult to predict and heavily subject to political, policy, technological and market uncertainty. However, key factors currently are:

- older coal fired generators are retiring, including Northern in South Australia, due to age and the difficulties inflexible generators face given increasingly volatile demand and competition from variable renewables with short run marginal costs of zero;



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- gas fired generators are playing an increasingly important role in meeting demand previously met by coal, filling in when renewables are unavailable, and stabilizing the grid;
- gas prices are rising steeply and supply is very tight, due significantly to the rise of LNG exports, exacerbated by weaker than expected production and the gas bans in New South Wales and Victoria;
- uncertainty is weighing on new investment, as well as the willingness of market participants to sign longer term agreements.

In the immediate term wholesale price futures and retail prices have risen steeply, with many businesses finding the wholesale price component of new contract offers to be double the level of their previous contracts.

In the longer term there is some hope that additional gas supply, falling costs of renewable generation, energy storage and demand response can moderate prices. However, a great deal of reform and investment will be required.

## **2. Without the proposed collective purchasing, are there barriers to the Applicants securing reliable and similarly priced electricity contracts?**

Retailers are clearly cautious about their ability to reliably meet large energy user demand without very large risk premiums. These in turn partly reflect their own difficulty in securing fuel supplies.

## **3. Without the proposed collective purchasing, are any of the Applicants likely to cease operations in South Australia?**

Trade exposed industries, particularly manufacturing, are under severe pressure in South Australia and Ai Group has seen plenty of evidence that head offices are concerned at the increase in energy costs and uncertain supply that has taken place. Without further action, it is plausible that manufacturers will scale back or leave altogether.

## **4. Is the collective purchasing likely to increase competition between suppliers of electricity in South Australia? Why?**

South Australia has a relatively concentrated generation sector and a great deal of uncertainty and short-termism (as well as severe difficulties in the wider gas market). Much of the time South Australia has an abundance of renewable energy with zero short run marginal costs, which suppresses the prices and volumes that other generators can achieve. These factors are



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making it difficult for existing gas-fired capacity to commit to participate, since they are unable to secure gas supplies except on onerous take-or-pay terms that leave them with considerable risk if demand falls short. The same factors also weigh on potential new entrants.

The availability of a long term contract to supply a significant quantity of electricity to industrial customers is likely to be very attractive to existing participants with the ability to bring more of their capacity into the market, as well as to possible new entrants. We believe that there is the potential to draw in new suppliers and increase competition.

## Areas of competition

The Applicants consider that the relevant markets are the market for: (i) the generation and wholesale supply of electricity in the National Electricity Market or in the South Australian region of the NEM, and (ii) the market for the retail supply of electricity in South Australia.

### **5. Please comment on whether the South Australian region of the NEM constitutes a separate market.**

While the NEM involves common rules and institutions for all regions, significant differences emerge in practice in the price and risk profile of supply in different regions. The South Australian region is distinguished by its relatively slim connections to the rest of the market, its greater dependency on gas and wind, and the concentration of ownership of dispatchable generation. Events in other NEM regions do impact South Australia and vice versa, and the most sensible course is to consider the South Australian segment as distinct but closely interrelated.

### **6. Please comment on whether any upstream or downstream markets are likely to be impacted by the proposed conduct.**

While the proposal is technology neutral, it appears most likely that a new supply agreement will be underpinned to some degree by gas-fired generation. That will increase (or at least firm up) demand in the upstream gas market. That market is currently very tight, owing to the tripling of gas demand driven by the Queensland LNG industry and inadequate production growth (exacerbated by limits on unconventional gas production in New South Wales and Victoria). Additional certain demand could have the effect of driving more investment in gas production in friendly jurisdictions, including South Australia.



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The impact on downstream markets is likely to be limited. Heavily trade exposed businesses are typically unable to pass through cost increases to customers unless these are reflected in global market prices, and instead tend to absorb cost increases. However, absorbing sufficiently large and protracted energy costs will see some businesses forced to scale back, relocate or close altogether. That would have wider negative impacts throughout South Australia's supply chains.

## Public benefits and detriments

- 7. Please comment on the relative bargaining power of the Applicants (individually and as a group) and of relevant electricity suppliers. The Applicants argue that the joint tendering arrangement may induce new entrants in the supply of electricity, incentivise existing suppliers to expand operations, or incentivise existing suppliers not to cease or roll back operations.**

Our members' experience has been that larger energy users are generally able to secure longer contracts with better prices and terms more responsive to their unique needs. The applicants represent about 1.4TWh of annual demand; that is about 160MW of load at any given moment. This demand is equivalent to the output of a major generating unit or two at a gas-fired power plant or of a reasonably sized wind farm. It is very plausible that this volume of demand is sufficient to sway decisions about new, expanded or preserved generation.

- 8. Do you consider the proposed arrangements are likely to incentivise new entry or expansion in the relevant electricity supply market? The Applicants also argue that 'the introduction of further synchronous generation into the South Australian market' would increase power system security and reliability, citing two instances of unreliable electrical supply in November 2015 and September 2016 (pp14-15).**

New entrants are possible but not guaranteed. Such entrants would likely help with South Australia's need for system security, though this is already the subject of considerable attention from stakeholders. The Australian Energy Market Operator has begun to require that at least two gas fired generators operate at all times in South Australia, even if at very low levels, in the wake of the 2016 system black event. The COAG Energy Council is moving to fast track projects that could deliver additional inertia and frequency control in the South Australian segment. To the extent that the applicants are able to sustain more gas fired or other synchronous generation in the South



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Australian market than the market would otherwise supply, they will bolster or reduce the costs of these other initiatives.

**9. Please comment on the likelihood and extent that the proposed conduct may increase power system security and reliability and prevent future instances of unreliable electrical supply.**

This is difficult to assess, since as noted considerable changes have been made or are being planned to improve South Australian system security. However, the availability of approximately 160MW of synchronous generation capacity – which is the likely outcome of the applicant’s proposal – would provide valuable inertia and frequency control capabilities to the SA region.

**10. Please provide any other comments regarding the public benefits claimed by the applicants or any other public benefits of the proposed collective purchasing.**

We have no other comments.

**11. Please provide any other comments regarding any public detriments likely to arise from the proposed collective purchasing.**

We do not foresee any public detriment as a result of the proposal. Given the objective and feasibility of securing additional supply (whether from existing underutilized assets or new entrants), it does not seem likely that the proposal will result in any shifting of costs to other consumers.

**Period of authorisation**

**12. Please comment on the appropriateness of the period of authorisation requested, which is a total of 11 years, comprising 6-12 months for the tendering process, a 3-5 year contract term plus the option to extend for a further 3-5 years.**

The proposed term is appropriate, giving flexibility to offer a long contract if that is required to secure supply, as well as shorter terms if counterparties require more flexibility. Given major ongoing reform efforts to energy policy and climate policy, there is great value both in the capacity to offer long term certainty, and the freedom to agree a shorter term to take more account of changing circumstances.



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Should you have any queries in relation to this submission, please contact the undersigned on 0419 818 048 or Tennant Reed, Principal National Advisor Public Policy on 0418 337 930.

Yours sincerely

**Stephen Myatt**  
**Head- South Australia**