14 December 2022

The Electricity Authority

Wellington

Reviewconsultations2022@ea.govt.nz

Re: Submission on Promoting competition in the wholesale electricity market in the transition toward 100% renewable electricity.

Thank you for the opportunity to submit on this paper. We make some opening comments before addressing the specific questions posed in the paper. NZ Steel also commends the MEUG submission and accompany NZIER report for your consideration.

New Zealand needs abundant, reliable, and affordable electricity from renewable sources if we are to be competitive as a nation. These factors are essential to a thriving economic structure and social environment we aspire to.

The electricity industry and country face huge challenges to meet the renewable electricity targets required for powering NZ and decarbonising of our energy supply. However, NZ Steel is not confident the settings for the current market model are going to bring on stream the volume of electricity required at a price and within the timeframe required for accelerating transition to a decarbonised Aotearoa New Zealand.

Large consumers have been under energy-related stress for the past 4+ years (with a lull for the current abundant level of water in the hydro lakes). During this time, we have seen two large electricity users and some small retailers close their operations.

The price levels experienced since 2018 hamper demand side investment decisions and the decarbonisation journey. By investment we include the sustainable capital required to keep large complex plant operating. For those with overseas owners this means competing for capital with overseas jurisdictions with more favourable cost structures. Also noting investment in decarbonising technologies can only be justified with electricity prices at rates substantially lower than currently quoted out to the extent of the ASX futures market.

The current paper from the Authority is useful in that it moves us forward from the question of ‘is the Market broken’? The paper acknowledges a number of areas where the Market has not performed as should be expected. This includes

- Higher than expected spot prices continuing longer than would be expected[1]
- Some evidence that market power has been exercised[2].
- Evidence of windfall gains to generators[3], (backed by MEUG EVA analysis[4]).
- Delayed new investment[5].

The Authority has identified Market power and the need to facilitate new investment as the greatest priorities. We agree with this and reference the appendix to the MEUG submission for comment on the recommendations outlined in table 6 of the paper. The issue is these recommendations are not new and continue the largely passive approach we have seen to date: “monitor”, “investigate”, “conclude”, “clarify”, “explore”. As a package it is continued tinkering around the edges with no certainty we will ever get to a fully functioning market, and certainly not any time soon.

The Authority’s paper places great store on ‘being sure’ before any changes are made. We can understand a conservative approach to minimise the risk of unintended consequences. However, failure to act also brings costs to consumers, risks and consequences.

The report outlines areas where the market has failed to deliver in many respects. Some of the issues MAY have been addressed, but other core issues are now masked by the drive to zero carbon electricity.
More change to the market is required. Some will be structural. This needs to happen with a degree of urgency with the consumer of the day in mind. In the words of Voltaire, “perfect is the enemy of good”.

Chapter 2

1. Do you agree that a key competition issue in the transition toward 100% renewable electricity is that it weakens competition during extended times when intermittent generation cannot run?

2. Do you have any comments on the contents of this chapter?

Paragraphs 2.19 to 2.23 draw attention to “competition is not constant over time”. While in market theory, price cycles and time-lags should be expected as supply re-adjusts to the dynamics of demand, there are economic and social costs that need to be considered. For electricity these cycles extend over a period of years. Also, electricity in most cases is not a discretionary purchase for businesses and households. The long-term benefit for consumers referred to in 2.23 is not acceptable if undue ‘suffering’ is inflicted in the short-term.

[1] Promoting competition in the wholesale electricity market in the transition toward 100% renewable electricity – issues paper, Electricity Authority, 2022, para 1.7
[2] Ibid, para 3.5
[3] Ibid, Box 2 Page 25.
[4] Refer MEUG submission
[5] Ibid 3.18

Chapter 4

3 Do you have any comments on the impediments to generation investment?

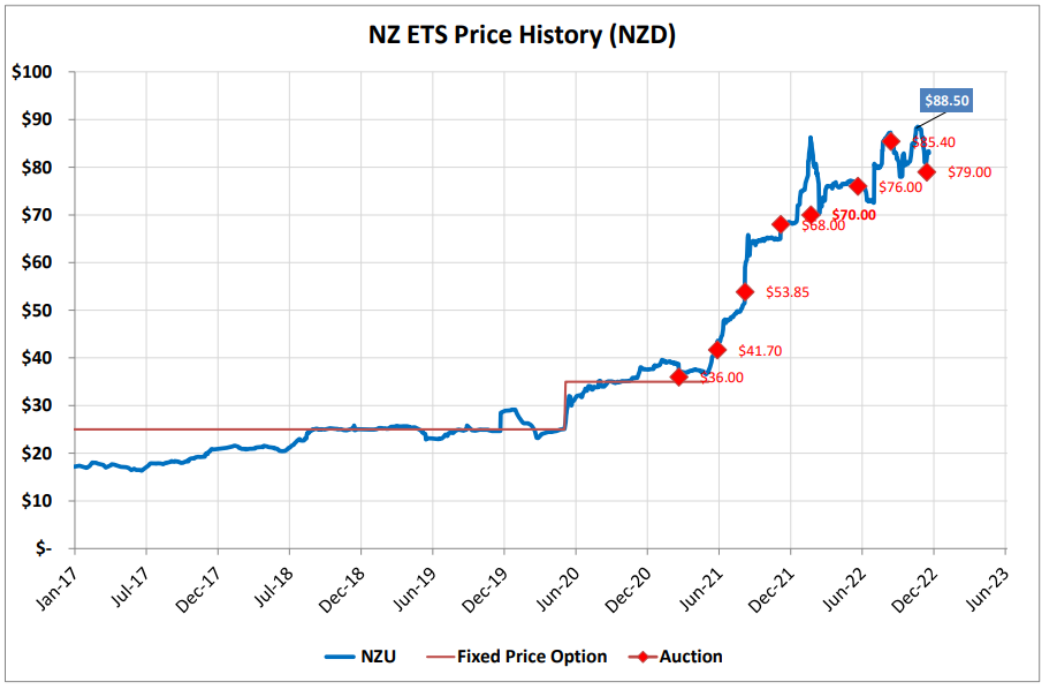
Chapter 4 sets out the issues and challenges well.

4. Do you agree that the lag in investment is not due to anticompetitive behaviour to slow down investment and discourage entry, or can you provide instances or other evidence to the contrary?

Any suggestion of anticompetitive actions is a matter for the Commerce Commission.
The basis of any market is the seller is inherently incentivised to drive/maintain the price higher either by increasing demand or restricting supply.

5. Do you have any comments on the role and impact of carbon pricing on investment and wholesale market competition or the other contents of this chapter?

The cost of carbon in NZ has increased significantly in the last 2-3 years[6]. This adds significantly to input costs for natural gas and coal sourced generation. While this is incentivising investment in renewable generation, there will be a transition period where thermal support will be critical to maintain supply.
The marginal cost gap now between hydro or wind compared with coal or gas has increased significantly. For the transition period to 100% renewable, we suggest a re-examination of the marginal price for the last MW setting the price for the market.



6

Chapter 5

6. Do you agree with the Authority's overall conclusion that it currently considers that continued reliance on the current conduct-based measures to mitigate the exercise of market power remains broadly appropriate in the transition toward 100% renewable electricity?

Short answer is no.

The WEM continues to be dominated by four large vertically integrated generators and this looks to continue to be the case for many years ahead[7].

In an ideal world generation and retail would have been separated at the set-stage, however, the risks for the financial viability of retail separated from generation continue today.

It should also be recognised the core of our WEM continues to be four large generators owning assets that were designed and built mid last century to complement each other, have been placed in a structure that requires them to compete. This has increased risk, especially as generation relative to demand has reduced. Increased risk raises prices.

Until we transition to a new 100% renewable generation model, further intervention is required to overcome issues with our current market, the fundamentals of which go back circa 30 years. Some of these issues can only be dealt with through structural changes or administrative intervention.

7. Do you agree with the objective and evaluation criteria set out in this chapter?

We support the objective set out in 5.13. However, as stated above an operating market that provides for the long-term benefits for consumers also needs to provide for an acceptable situation for the consumers of the day. 5.14 should be reworded to capture the 'cost' to today's consumers of a market not delivering what should be expected, impacts the long-term benefit equation.

8. Do you have any comments on the contents of this chapter?

5.11 states "…more fundamental structural options are currently not justified…". To the contrary, the report confirms there are a number of issues with the current operation of the Market. We suggest the costs of not acting more decisively than what is proposed, is greater than the risks associated with the passive measures proposed in Table 6. We are not in a perfect world with the luxury of time for structural option to be "…extensively tested…". The industry has recognised the move to more renewables will result in greater price volatility. This will further complicate the analysis of market power.

Chapter 6

9. Are there any other options that would promote wholesale electricity market competition in the transition that you consider would be more effective and efficient?

[7] Ibid, paras 2.12-2.16

10. Do you have any comments on the contents of this chapter?
This section again captures underlying issues with the current market and identifies potential ways of lessening market power. However, we perceive the Authority to be caught in the paralysis by analysis syndrome.

Chapter 7
11. Are there any other options that would better facilitate efficient investment in renewable generation to promote wholesale electricity market competition in the transition?

12. Do you have any comments on the contents of this chapter?
7.24 mentions PPAs and that they are bespoke agreements. For generation physically remote from load it is a virtual PPA, in effect a long-term CFD. If these become widespread, we will be interested in the Authority's view as to whether this in fact may be counter-productive to the proper functioning of the WEM.

We will be pleased to have an opportunity to expand on or clarify any of the points made.

Yours sincerely

New Zealand Steel

Alan Eyes | Energy Manager
New Zealand Steel

T +64 9 375 8393 | **M** +64 21 870 629
E Alan.Eyes@bluescopesteel.com | **W** www.nzsteel.co.nz
A 131 Mission Bush Road, Glenbrook, Private Bag 92121, Auckland 1142