

11 March 2019

SAVES AND WIN-BACKS – RECOMMENDATIONS PAPER

MARKET
DEVELOPMENT
ADVISORY
GROUP

The MDAG has reviewed evidence and submissions regarding potential market failures and regulatory problems relating to customer acquisition and saves and win-backs. A wide range of issues and concerns have been raised about customer acquisition and saves and win-backs having an adverse impact on competition. To investigate these claims, we examine current market structures, firm conduct and regulated switching procedures. We conclude that there is not strong evidence of market failures or regulatory problems that need addressing. Saves and win-backs practices and retail competition do, however, need to continue to be monitored to better understand their effects on consumers.

Note: This paper has been prepared for the purpose of reporting findings from a review of saves and win-backs and providing recommendations and reasons to the Authority on next steps to address concerns about saves and win-back practices. Content should not be interpreted as representing the views or policy of the Electricity Authority.

Market Development Advisory Group members

- Tony Baldwin (Chairperson from December 2018)
- James Flannery
- James Flexman
- Darren Gilchrist
- Stu Innes
- Rebecca Osborne
- Bruce Rogers
- Matt Rowe
- James Tipping

Executive Summary

Objective

This report presents the findings and recommendations of the MDAG following the group's initial review of potential problems with saves and win-backs practices.

The Authority requested the MDAG to conduct a review of saves and win-backs practices, focussing on answering the following question:

Is there a regulatory problem or market failure relating to customer acquisition, including saves and win-backs practices, and the switching process?

In relation to this question the Authority asked the MDAG to consider:

- Are there problems with the customer acquisition process that result in a 'non-level playing field' for acquiring retailers, including new entrant retailers?
- To what extent do perceptions around a potential 'non-level playing field' affect the durability of the retail electricity market?

The underlying objective of our review of saves and win-backs, in line with the Authority's statutory objective, is to ensure that competition is as robust as it can be.

Robust competition exists when retailers live in the knowledge that their customers are at risk of being lost to competitors with lower prices or better services. This creates competitive pressure. When retailers know that their customers are at risk, they are compelled to find ways to reduce their own costs and improve the quality of their own services. Part of this competitive process is competitors trying to both attract customers and retain customers.

Competition will not work as well as it can, for the long-term benefit of consumers, if retailers are competing on a non-level playing-field.

Issues

Submissions and prior research point to a wide range of issues about the functioning of retail competition, customer acquisition and effects of saves and win-backs.

We have divided these issues into matters of market structure, retailer conduct, policy or regulatory rules, and market performance. This framework helps to distinguish causes of potential problems from symptoms of potential problems.

Market structure

We heard two related concerns with market structure that a number of submitters, smaller retailers in particular, have said are creating a non-level playing field and cause competition to be less robust than it could be:

- One is that consumers are disengaged, that they do not switch. Small retailers are confined to competing in a subset of the retail market where consumers switch frequently and fierce price discounting takes place. Long-established retailers have an advantage from also having large dependable and inert customer bases.
- The other issue is that long-established or 'incumbent' retailers – a retailer with majority market share in a distribution network area when retail competition was

introduced in the late 1990s – have competitive advantages that newer ‘entrant’ retailers cannot replicate.

The use of win-backs is most often cited as an example of this competitive advantage. Retailers with large customer bases can maintain high prices on their existing disengaged customers with little concern that these customers will be lost. If customers do decide to switch these retailers can offer highly competitive discounts to win these customers back. This discourages competition for customers.

Three mutually reinforcing factors contribute to the non-level playing field:

- consumer inertia
- a high degree of concentration in the retail market, with the top 5 retailers having an 88% market share
- retailers that lose customers have access to information about customers that enables them to offer departing customers a discount to win them back.

There are also concerns that these structural problems contribute to problems with retailer conduct.

Retailer conduct

Issues of retailer conduct include how retailers set their prices and how they communicate with and represent themselves, or other retailers, to consumers.

We considered concerns relating to:

- unreasonable or anti-competitive conduct such as:
 - discounts or prices that are below costs to deter competitors from competing
 - retailers or their agents making unsubstantiated claims about their own services or those of other retailers
- retailers electing not to publish the discounts they offer to customers so that:
 - consumers are unaware of the full extent of gains from shopping around for a different electricity provider
 - retailers being unable to pre-empt counter-offers.
- consumers making decisions in the heat of the moment, in response to time-limited offers, and
- consumers not necessarily having recourse to a ‘cooling off’ period to change their mind.

Switching processes

Retailers are notified that a customer intends to switch before the process is completed. This provides for retailers to exchange information about the customer who is switching. It also allows the losing retailer to use the information of a customer’s intention to switch as a prompt to contact the customer to discourage them from switching.

The save protection scheme was introduced in 2015 to allow retailers to elect to be protected from other retailers making counter-offers to prevent the switching process from being completed.

Concerns remain about switch notification continuing to provide an undue advantage to retailers making counter-offers to retain customers.

Retailers are free to contact any customer after a switch has been completed, to make a counter offer and to have a switch withdrawn up to 2 months after the switching process has been completed.

Market performance

There are concerns that retail prices are, on average, higher than they should be (would otherwise be) and that this is due to market structure (monopoly pricing) and conduct including, but not limited to, saves and win-backs behaviour.

There are also concerns about distributional consequences from prices being higher than they should be – that prices are highest for those that are least able to afford them.

Scope of evaluation

Terms of reference

Under our terms of reference, our evaluation is limited to identifying

- a) regulatory problems or
- b) market failures

related to customer acquisition and switching processes, including saves and win-backs practices.

The evaluation thus focusses on causes of potential problems with market performance. That is, issues relating to market structure, retailer conduct and switching processes.

Issues out of scope

Given our focus on market failure and regulatory problems, there are some issues that are outside scope for our evaluation.

Customer segmentation and non-uniform pricing, for example, are not market failures or a regulatory problem. Differentiated pricing and services can be an efficient response to differences in consumers' demands and willingness or ability to pay for electricity services. However, segmentation or non-uniform pricing may be factors that could exacerbate more fundamental market failures or regulatory problems.

Asymmetric information is also not a market failure. All retailers can benefit from informational advantages, once they are established in the market. Though asymmetric information can be a regulatory failure.

Key issue

The high-level question guiding our evaluation is whether customer acquisition and switching processes, including saves and win-backs practices, reduce competitive pressure by:

- a) contributing to non-competitive market structures including by
 - i. creating barriers to entry and expansion of competitors
 - ii. reducing consumer engagement (shopping around)

- b) promoting or facilitating undesirable or anti-competitive conduct.

Strong evidence of these conditions would constitute a ‘non-level playing field’ for acquiring retailers, including new entrant retailers, and thus a potential problem for competition in the retail market.

Evaluation

Our evaluation focusses on identifying evidence for issues raised i.e. problem definition. Our sources of evidence include publicly available analyses and surveys of competition issues and consumer switching behaviour, and analysis of detailed data on customer switching and retailers’ customer losses and acquisitions from 2003 to 2017, at the level of individual residential electricity customers.

Our evidence base is likely to differ from, but be complementary to, information available to the Electricity Price Review’s Expert Advisory Panel.

Competitiveness of market structure

Our evaluation considers:

- evidence for market dominance
- whether customer acquisition – namely saves and win-backs – could be contributing to consumer inertia
- whether the switch notification process provides an asymmetric advantage to retailers trying to retain customers, and is thereby increasing market concentration.

The last of these questions is a question about regulatory failures associated with switching processes as well as market structure.

By in large, retail market concentration is too low for firms to be ‘dominant’ in the sense of the term used by competition agencies. Furthermore, incumbent retailers have been consistently losing market shares.

In respect of consumer inertia, and the effects of saves and win-backs, the data is equivocal. There is some correlation between increasing rates of saves and win-backs and reductions in numbers of consumers shopping around – measured by visits to the Powerswitch and What’s My Number? Websites – but this correlation does not appear to be causal.

To investigate whether switching procedures give losing retailers a competitive advantage, we consider whether changes to switching processes would reduce the effectiveness of retailer’s counter-offers. If they did, this could imply that current processes may be giving the losing retailer an advantage by increasing the effectiveness of their counter-offers and thus creating a non-level playing field. We consider counter-offers to be presumptively pro-competitive, but not if the playing field is not level.

We find that reforms could speed up the switching process, at the expense of reducing the scope for timely exchange of information between retailers. Faster switching seems most likely to increase the effectiveness of counter-offers – striking while the iron is hot – if it has any effect at all. As such, existing switching processes are more likely to be impeding than effectiveness of counter-offers, than anything else.

Impacts on undesirable or anti-competitive conduct

Our evaluation considers whether:

- win-back activity is targeted at new entrants, potentially to discourage competition
- there is any clear evidence for loss-leading pricing, for anti-competitive purposes
- win-backs are a conduit for misleading claims
- hidden discounts inhibit competition or consumer engagement

Indications of selective targeting of win-back activity may be suggestive of anti-competitive attempts to dissuade entrants from competing in some parts of the country or even of tacit collusion amongst some retailers.

We find:

- nationally, almost all retailers use saves and win-backs
- win-back rates are highest between retailers with high market shares
 - average win-back rate between the 5 largest retailers is 25%
 - average win-back rate of the 5 largest retailers against the next 5 largest retailers is 15%
- the largest retailers have the highest rates of failed acquisitions (28%) (i.e. acquisitions lost through win-backs)

We considered evidence presented on loss-leading discounts and find that they are not anti-competitive but are consistent with some customers paying a much smaller share of the retailer's fixed costs than the retailer's average customer.

In terms of misleading claims, we do not see any evidence that existing market structures or regulatory settings provide any additional incentive for making misleading claims. On the contrary, switch notification can help to provide a discipline on retailer conduct and switch withdrawal reduces transaction costs associated the switching process. And submissions have suggested that these are one-offs rather than systematic.

Similarly, there is no obvious causal connection between the use of saves and win-backs and a lack of pricing transparency. In the absence of saves and win-backs retailers could, for example, still offer consumers (e.g. via door-to-door marketing) unpublished one-off or time-limited discounts that are not widely observed by other consumers.

It is possible that reduced transparency of prices does reduce the rate at which consumers shop around, but this need not necessarily imply that all prices ought to be public. Retailers may remove discounts rather than have to publicise them. And uncertainty about discounts in the market can be an incentive for retailers to put forward their best offer possible when trying to win customers.

Conclusions

There is no strong evidence of regulatory problems or market failures related to customer acquisition and switching processes, including saves and win-backs practices.

Patterns of win-back activity are consistent with increasing competitive pressure as retailers need to pay attention to costs and to price levels to avoid losing customers to

counter-offers. The fact that win-backs are most prevalent between larger retailers is significant evidence of this.

The Authority previously introduced the saves protection scheme because it observed that there was a potential regulatory failure in existing switching procedures whereby losing retailers were being advantaged with notification of impending switches. There is no similar rationale in relation to win-backs.

Win-back discounts do reduce the transparency of electricity prices and this could be affecting the rates at which consumers shop around – there is some, weak, evidence of an association between increased use of win-backs and less shopping around, measured by visits to price comparison websites. This could be due to consumers not fully understanding the potential benefits they could gain from shopping around.

But there is no strong rationale for regulating customer acquisition processes, particularly saves and win-backs, in order to promote greater transparency of retail pricing. Unpublished discounts are not peculiar to saves and win-backs. Mandatory price disclosure also risks unintended consequences, such as higher average retail prices.

Recommendations

The Authority should continue to monitor saves and win-back practices and the implications they have on prices and on consumers. In particular, the Authority should recommit to ongoing monitoring of consumers' experiences of win-back practices, including the scale and terms of discounts that are offered as part of win-backs, by including questions on these issues in consumer switching surveys.

Impacts on consumers are a central concern. But consumer perspectives on saves and win-backs are not well understood and evidence about impacts on consumers is not clear. Targeted monitoring or research is still needed to clarify these things, otherwise the impact of saves and win-backs will continue to be uncertain.

These issues should be explored by adding questions to the Authority's biennial consumer switching survey to ask consumers if they:

- have been offered a win-back discount(s), the value of the discount(s), and terms and conditions of the discount(s)
- have accepted a win-back discount
- whether they view these discounts favourably
- whether they have felt that retailers have conducted themselves reasonably when offering discounts to win them back.

The biennial survey of consumers has only recently been completed. The Authority should conduct a one-off survey of consumer experiences of win-back behaviour so that information is gathered without significant delay. This one-off survey could be an update of the one used for the Authority's 2014 enquiry into consumer switching experiences

Contents

Market Development Advisory Group members	1
Executive Summary	2
Objective	2
Issues	2
Market structure	2
Retailer conduct	3
Switching processes	3
Market performance	4
Scope of evaluation	4
Terms of reference	4
Issues out of scope	4
Key issue	4
Evaluation	5
Competitiveness of market structure	5
Impacts on undesirable or anti-competitive conduct	6
Conclusions	6
Recommendations	7
1. MDAG has reviewed saves and win-back practices	10
Terminology	10
1.2 Objective of MDAG’s review: promoting competition	11
1.3 Background	11
1.4 MDAG has consulted and considered submissions on its issues paper	14
1.5 Scope	15
2. Issues	16
2.1 Organising framework – structure, conduct, performance	16
2.2 Market performance	16
2.3 Policy	16
2.4 Market structure	17
Large numbers of disengaged consumers	17
Market dominance and incumbency	18
Losing retailers have consumer information that others do not have	19
2.5 Retailer conduct	19
Retailers target lower prices at win-backs and higher prices for other customers	19
Saves and win-backs can be a conduit for anti-competitive conduct	19
Win-back offers involve misleading information and questionable conduct	20
Win-backs discounts are secret	20
2.6 Scope of evaluation	21
Regulatory problems	21
Market failure	23
Issues out of scope in our evaluation	23
Key questions guiding our evaluation	23
3. Evaluation	25
3.1 Competitiveness of retail market structure	25
Is market dominance a problem in the retail market?	25
Is the market trending towards increased occurrence of market dominance?	26
Have saves and win-backs reduced consumer engagement?	28

Do switching procedures increase the effectiveness of counter-offers?	31
3.2 Impacts on undesirable or anti-competitive market conduct	37
Use of saves and win-backs to discourage competition	37
Do saves and win-backs facilitate or promote misleading claims	42
Transparency of win-back discounts and prices	43
4. Conclusion	45
4.1 Findings	45
4.2 Recommendations	46
5. Data appendix	47

1. MDAG has reviewed saves and win-back practices

1.1 The Authority requested a review of saves and win-backs

- 1.1.1 This report presents the findings and recommendations of the MDAG following the group's initial review of potential problems with saves and win-backs practices.
- 1.1.2 The Authority requested the MDAG to conduct a review of saves and win-backs practices and complete consultation on an issues paper by June 30 2018.¹

Terminology

Switch – when a customer moves their account from one electricity retailer to another

Save – a switch that is stopped and withdrawn before the switching process is complete

Win-back – a switch that is withdrawn after the switching process has been completed or when a customer switches back to the previous retailer shortly after the switch has been completed

Losing retailer – the retailer from whom a customer is switching away to a gaining retailer. When a retailer wins a customer back, they are referred to as the “losing retailer”.

Incumbent retailer – a retailer with majority market share in a distribution network area when retail competition was introduced in the late 1990s.

Entrant retailer – a retailer that is not an incumbent retailer.

- 1.1.3 The MDAG released an issues paper on 22 May 2018 with submissions received by 29 June 2018. The issues paper was focussed on gathering information to answer the following question, set out by the Authority in its letter to the MDAG:

Is there a regulatory problem or market failure relating to customer acquisition, including saves and win-backs practices, and the switching process?²

- 1.1.4 In relation to this question the Authority asked the MDAG to consider:

¹ 'Letter to MDAG – 2017-18 work plan – saves and win backs + battery storage', available at <https://www.ea.govt.nz/development/advisory-technical-groups/mdag/meeting-papers/2018/8-february-2018/>.

² Ibid, item 1. p.2.

- a) Are there problems with the customer acquisition process that result in a ‘non-level playing field’ for acquiring retailers, including new entrant retailers?
 - b) To what extent do perceptions around a potential ‘non-level playing field’ affect the durability of the retail electricity market?
- 1.1.5 The Authority’s request to the MDAG also asked that the group consider and report back on possible actions to address any problems that are identified, if any:
- a) should the saves protection scheme be amended and, if so, how?
 - b) are there other regulatory mechanisms that should be considered/adopted?
- 1.1.6 This report focusses on the question of potential problems with saves and win-backs, as this has been the focus of the group’s work and consultations to date.

1.2 Objective of MDAG’s review: promoting competition

- 1.2.1 The Authority’s statutory objective is to “promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers.”
- 1.2.2 Robust retail competition helps to ensure that the electricity industry operates for the long-term benefit of consumers.
- 1.2.3 Robust competition exists when retailers live in the knowledge that their customers are at risk of being lost to competitors with lower prices or better services. This creates competitive pressure. When retailers know that their customers are at risk, they are compelled to find ways to reduce their own costs and improve the quality of their own services. Part of this competitive process is competitors trying to both attract customers and retain customers.
- 1.2.4 The Authority tracks retail market concentration to measure market performance and competition and this data shows that concentration has been consistently declining since 2010 across all key national concentration measures and in every network area in the country.³ This implies that retailers have been under increasing amounts of competitive pressure.
- 1.2.5 The objective of our review of saves and win-backs is to ensure that competition is as robust as it can be.

1.3 Background

- 1.3.1 In 2014 the Authority implemented an opt-in ‘saves protection’ scheme. The objective of the scheme was to promote competition.
- 1.3.2 Some retailers had been using notifications that a customer was switching to offer customers better deals to stop a switch from being completed. The

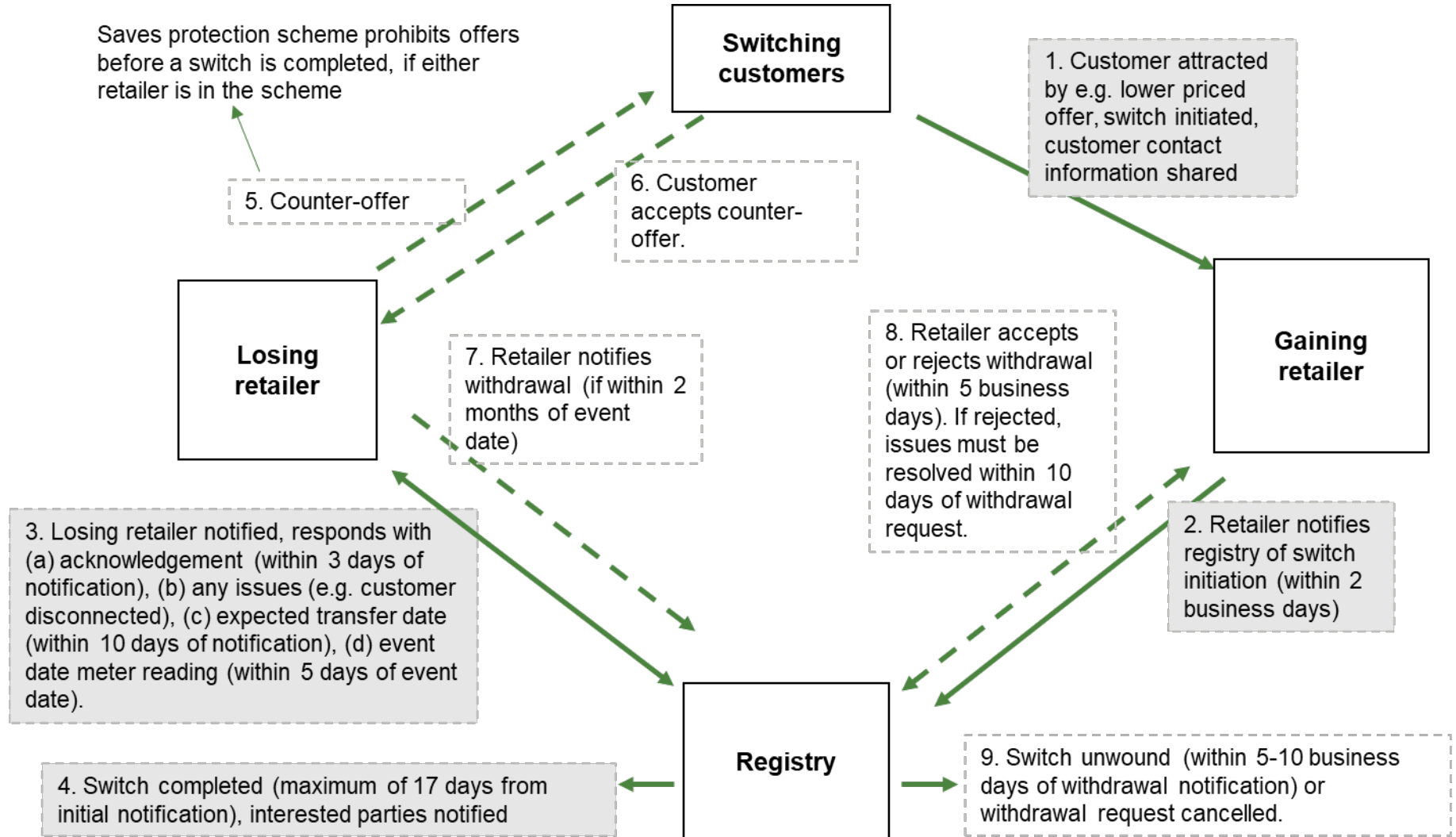
³ These measures include the Herfindahl-Hirschman index and concentration ratios for the top 1, 2, 3, and 4 firms. See the Authority’s market performance metrics at www.emi.ea.govt.nz/r/bo41w and www.emi.ea.govt.nz/r/hlue3. The observation that these measures have been declining is based on growth rates in the HHI and concentration ratio for the top 4 firms. In all network reporting regions these ratios have declined significantly between 2008 and 2018 and between 2015 and 2018. The average rate of decline in the HHI has been 8% per year between 2008 and 2018. The average rate of decline in the concentration ratio for the top 4 firms has been 2% per year between 2008 and 2018.

Authority determined that the switch notification process was enabling this process – by providing the losing retailer with information belonging to the customer and the new retailer – and that this information is not available in most other markets.

- 1.3.3 The Authority expected that giving retailers the option of removing this advantage, by allowing them to opt into the saves protection scheme, would reduce undue barriers to the entry and expansion of independent retailers and the expansion of existing retailers and facilitate retail competition and innovation. The Authority also expected this support for ongoing competition would improve the durability of competitive retail markets.
- 1.3.4 The Authority also considered whether the saves protection scheme should be extended to win-backs – where a switch is withdrawn after it has been completed – but decided not to do this because:
- a) win-backs do not rely on early notification of a switch
 - b) there was no evidence that win-backs had a material negative impact on competition
 - c) retailers could take steps, independently, to guard against win-backs.
- 1.3.5 An evaluation of the saves protection scheme in 2017 found no evidence that the scheme had either improved or harmed competition. It did find retailers had adapted to the limitations on saves by increasing win-backs and completing switches more quickly so they could effect win-backs more quickly. Time taken to complete switches fell from an average of 97 hours (4.04 days) before the scheme to 82 hours (3.42 days) after the scheme was introduced.
- 1.3.6 Figure 1 below provides an outline of steps in the switching process, as set out in the Code (Schedule 11.3). Step 3 in the switching process – when the losing retailer is notified of switch – is the step that was identified as a source of unintended competitive advantage for losing retailers. The saves protection scheme places restrictions on retailers making counter-offers, until after a switch has been completed. Hence counter-offers can only be made at step 5 in the switching process.

Figure 1: Switching processes, win-backs, and maximum timeframes for switching processes specified in the Code

The term “event date” refers to the date at which the switch finally comes into effect. Win-back steps in boxes with dashed grey lines. Switch steps are in boxes with grey backgrounds.



1.4 MDAG has consulted and considered submissions on its issues paper

- 1.4.1 In preparing its issues paper, the MDAG sought input, in person, from retailers that had expressed concerns about negative effects of saves and win-backs⁴ and from Consumer New Zealand. MDAG also considered correspondence from retailers with concerns with the effects of saves and win-backs.
- 1.4.2 MDAG also considered information about the saves protection scheme: the Authority's 2014 consultation paper and decision and reasons paper and the Authority's 2017 post-implementation review of the saves protection scheme.
- 1.4.3 Fourteen submissions were received on the issues paper: 12 from retailers (including the 5 large generator-retailers) and 2 from other interested parties.⁵
- 1.4.4 Cross-submissions were also requested, to give submitters an opportunity to comment on points raised in submissions by other submitters. Six cross-submissions were received.⁶
- 1.4.5 After the submissions process had been completed the MDAG and MDAG secretariat also obtained input from Electric Kiwi to clarify reasons for differences in data sources and data points presented in the issues paper and in submissions.
- 1.4.6 In preparing its issues paper and weighing views and evidence in submissions and cross-submissions the MDAG has also considered:
- a) analyses from the MDAG secretariat about rates of saves and win-backs and treatment of saves and win-backs in other countries and network services industries
 - b) related information in other reviews such as the report of the Electricity Price Review's Expert Advisory Panel (30 August 2018) and the ACCC Retail Electricity Pricing Enquiry (11 July 2018) – the latter to the extent that this was raised in submissions on the issues paper
 - c) submissions made in response to the report of the Electricity Price Review's Expert Advisory Panel, to the extent that these reflected on issues raised in our own issues paper and offered new evidence or insights⁷

⁴ Representatives from Ecotricity, Electric Kiwi, Pulse Energy, and Vocus Group attended the MDAG's meeting on 15 March 2018. These were members of a group of retailers that also sent a letter to the Authority's General Manager Market Performance (4 May 2017) raising concerns about the effects of win-backs on retail competition. Additional correspondence considered by MDAG was: a letter from the CEO of Electric Kiwi to the Chair of the Authority (28 March 2018, copied to the Chair of MDAG), an email from GM Vocus Group to the MDAG Secretariat (29 March 2018). Letters were also received from Pulse Energy (9 July 2018) and Electric Kiwi (dated 17 July 2018).

⁵ Submissions were received from: David Riley, Ecotricity, Electric Kiwi, Entrust, Flick Energy Limited, Future Energy NZ, Genesis Energy, Mercury Energy, Meridian Energy, Nova Energy, Pioneer Energy, Pulse Energy, Trustpower, Vocus Group.

⁶ Cross-submissions were received from: Electric Kiwi, Entrust, Mercury Energy, Meridian Energy (including Powershop), Pioneer Energy, and Vocus Group.

⁷ Many of the submissions to the report of the Electricity Price Review's Expert Advisory Panel did raise matters of relevance to MDAG's review but none of these were, in our view, differed substantially from information provided directly to MDAG.

- d) issues and options raised, with respect to retail competition and saves and win-backs, in the Electricity Price Review's 20 February 2019 options paper.

1.4.7 The Electricity Price Review panel has put forward an option of prohibiting saves and win-backs.⁸ We note, as did the panel, that their assessment takes into account wider fairness considerations and possibly other data sources.

1.5 Scope

1.5.1 This paper and MDAG's review has been guided by the scope of work set out by the Authority and by consideration of issues being dealt with in other parts of the Authority's work programme or outside the Authority's statutory objective or statutory powers. Where issues have been raised by submitters they are considered and addressed, even if outside scope, although consideration may only extend to explaining that such matters are out of scope.

1.5.2 A losing retailer's informational advantage is one issue specifically outside the scope of the terms of reference for the MDAG's review. The Authority notes, in the terms of reference, that

"It has been identified that losing retailers may have an informational advantage over gaining retailers regarding which consumers considering switching should be targeted for consumer retention or acquisition. The losing retailer acquires this information during the course of acquiring the consumer and providing retail services to them.

While this information may influence a losing retailer's decision whether to try and retain a consumer, it is not directly related to the switching process. Accordingly, the informational advantage a losing retailer acquires through providing retailing services to a consumer is outside the project scope.

We note our Multiple trading relationships project is considering this matter in more detail."

1.5.3 Other matters considered outside scope for this review are:

- a) matters relating to affordability and price discrimination
- b) lack of consumer engagement leading to inequitable outcomes
- c) matters regarding price transparency
- d) improvements to the switching process which are already being considered as part of the Market Enhancements Omnibus.

⁸ Electricity Price Review (2019), Options paper for discussion, 18 February, <https://www.mbie.govt.nz/have-your-say/electricity-price-review-options-paper/> pp.15-16.

2. Issues

2.1 Organising framework – structure, conduct, performance

- 2.1.1 Various issues have been raised about the way the retail market functions. These concerns have been categorised here according to the structure-conduct-performance (SCP) framework. This helps to distil the essential nature of these concerns.
- 2.1.2 In the SCP framework a market's performance, including efficiency, follows from the market's structure and the conduct of the market's participants; competitive structures will produce competitive conduct and drive competitive and efficient outcomes. Uncompetitive structures will induce uncompetitive conduct and result in uncompetitive and inefficient outcomes.
- 2.1.3 The SCP framework acknowledges that policy, regulation and rules also influence both market structure and conduct and ultimately market performance.
- 2.1.4 The SCP framework is used here not for its predictions but as an organising framework for grouping issues into those that are fundamental and those that are symptoms of underlying problems. The focus of our investigation is on causes of problems, rather than symptoms.
- 2.1.5 Nonetheless, issues of market performance are mentioned briefly below to reflect concerns raised in submissions and potential consequences of competition problems arising out of market structure, retailer conduct, and potential policy problems.
- 2.1.6 At the end of this section the issues raised below are filtered in terms of matters that in and out of scope for our evaluation.

2.2 Market performance

- 2.2.1 Many of the submissions on our issues paper pointed to indicators of market performance as evidence of a failure of competition and problematic effects of saves and win-backs.
- 2.2.2 Two categories of concern were expressed. One was that prices are, on average, higher than they should be (would otherwise be) and that this is due to market structure ("monopoly" pricing) and conduct including, but not limited to, saves and win-backs behaviour.
- 2.2.3 The other, related, concern was about the distributional consequences of prices being higher than they should be. The concern is that prices are highest for those that are least able to afford those higher prices. While some consumers are benefitting from lower prices submitters say that these benefits are not available to all consumers (Entrust) and are least likely to accrue to poorer households (Ecotricity, Electric Kiwi).
- 2.2.4 Submissions that touched upon these market performance problems did so with reference to specific concerns about how policy and rules are currently functioning and concerns about market structure and market conduct. These are discussed in the following sub-sections.

2.3 Policy

- 2.3.1 As discussed in section 1.3, a key factor in the Authority’s decision to introduce the saves protection scheme was that losing retailers have ‘inside information’ about switching customers⁹ and, through the switching process, are warned of customers’ intention to switch.¹⁰ This notification is provided in accordance with clause 22 of Schedule 11.3 of the Code.
- 2.3.2 The Authority’s post implementation review of the save protection scheme characterised this problem as follows: “In the retail electricity market the incumbent retailer is notified that a customer intends to switch before the process is completed. This notification allows the losing retailer to use the information of a customer’s intention to switch as a prompt to contact the customer to discourage them from switching, rather than use the information for its intended purpose, which was to complete the switch process”.
- 2.3.3 The Authority determined, when deciding to introduce the save protection scheme, that reducing the informational advantage of losing firms might increase retailers’ returns to acquisition activity and increase competitive pressure in the retail market by reducing a potential barrier to entry.¹¹
- 2.3.4 Many of the submitters on our issues paper endorsed the view that switch notification continues to provide an undue advantage (Electric Kiwi, Flick, Pulse, Vocus). This is because, as observed in the Authority’s post implementation review, retailers can speed up their switches and then win customers back, thereby side-stepping protections provided by the saves protection scheme. The view has also been expressed that incumbents are advantaged by the mere knowledge that their customers are leaving, regardless of regulatory processes. That is, knowledge or notification of a switch are matters of market structure rather than policy (Vocus).
- 2.3.5 Others contended that any advantage obtained from switch advantage acquired from switch notification was mitigated by the switch protection scheme (Trustpower) or that any undue advantage from switch notification does not apply to win-backs (Mercury, Meridian, Nova).

2.4 Market structure

Large numbers of disengaged consumers

- 2.4.1 Some submitters considered competition is not as robust as it could be because a large number of consumers do not switch suppliers (Electric Kiwi, Ecotricity). Estimates presented in our issues paper suggest that 42% of ICPs have never switched suppliers. This number is only a rough estimate of the number of consumers that have never switched – being based on ICPs rather than households – but it does suggest relatively high numbers of disengaged consumers.

⁹ We refer to ‘customers’ when discussing commercial strategy and retailers’ relationships with those that they sell services directly to. The term ‘customer’ is distinct from ‘consumers’ which is, in general, a broader category of those people or organisations that use and benefit from electricity services.

¹⁰ Electricity Authority (2014b), paragraph 3.2.3.

¹¹ Ibid, paragraph 3.2.2.

- 2.4.2 Submitters with concerns about the lack of switching considered this raises three different types of concerns. One is that consumers that do not switch are on higher prices than they would otherwise be (i.e. the market is not performing well).
- 2.4.3 A second concern is that large numbers of disengaged consumers limits competitive pressure. Retailers with large customer bases can maintain high prices on their existing disengaged customers with little concern that these customers will be lost. If customers do decide to switch these retailers can offer highly competitive discounts to win these customers back – with limited effect on their profitability: “The incumbent retailers have deep pockets and the advantage of their non-switching customer bases to subsidise offers to switchers. This means that even with a perfect auction the incumbents will always have the upper hand” (Vocus, p.6).
- 2.4.4 Pulse submitted that, in effect, the cost of winning customers back is lower, on average, for losing retailers than for retailers that have invested in attracting these customers. Investment by gaining retailers, to attract customers, provides information that enables retailers with large customer bases to target their customer retention activity, while reducing returns on investment in customer acquisition for entrant retailers without large customer bases. This has a chilling effect on competition.
- 2.4.5 The third type of concern relates to retailer conduct and the potential for retailers with large customer bases to engage in anti-competitive behaviour. This is where retailers offer discounts, to win-back customers, that are unprofitable or barely profitable, at the margin, with the intent of discouraging other retailers from competing (Pulse). Retailers can do this because they are making excessive profits from their disengaged customers.

Market dominance and incumbency

- 2.4.6 Some submitters consider the use of saves and win-backs exacerbates advantages that long-established (incumbent) retailers have in competing in the retail market. Part of this advantage arises from the large number of disengaged customers, as discussed above.
- 2.4.7 These submitters suggested a contributing factor to incumbency advantage is that more recently established (entrant) retailers struggle to establish brand recognition. This limits their ability to compete and to defend against saves and win-backs, such as by offering new customers fixed term contracts to limit the risk that their customers are won-back: “Incumbents have a significant advantage in brand recognition over most new entrant retailers. This means that until a new entrant becomes established and recognized in the market, a customer often perceives they are taking a risk when switching to a new entrant retailer” (Vocus, p.6).
- 2.4.8 More generally, there is a view that the retail market is characterised by a high degree of market concentration which gives incumbent retailers a dominant position “which is only being slowly eroded, with the 5 largest incumbent retailers controlling 89% of the market” (Entrust, p.1). As such, saves and win-backs, are problematic because they facilitate incumbent retailers’ retention strategies and support continuation of high degrees of market concentration

and, potentially, market power that can lead to inefficiently high prices for consumers. There is a view that entrant retailers are growing more slowly than should be expected in a competitive market (Entrust).

Losing retailers have consumer information that others do not have

2.4.9 Submitters have noted that retailers that lose customers have access to information about their customers, such as their contact information, that enables losing retailers to offer departing customers a discount to win them back (Flick). This information gives losing retailers an advantage that is not available to other retailers. This issue, though strictly out of scope for this review, is material to the extent that it aggravates other concerns about negative impacts of saves and win-backs.

2.5 Retailer conduct

Retailers target lower prices at win-backs and higher prices for other customers

2.5.1 Retailers can segment customers – into those worth saving or winning-back and those that are not. They can do this because they have information about their customers that competitors do not (such as timeliness of payments and consumption levels). In and of itself, this is a matter that is outside scope of this review, but it is a material consideration if saves and win-backs increase the extent of market segmentation.

2.5.2 Electric Kiwi has submitted that price discrimination enables retailers to keep some prices high while discounting only where they must – to retain customers via saves and win-back discounts – and that this is evidenced by a widening in the difference between the highest and lowest prices in the market between 2000 and 2013.

2.5.3 Several submitters and cross-submitters noted that there have been increases in estimated gains from switching and say that this is evidence for excessively high prices and a “two-tier” market where customers that do not switch or do not receive win-back discounts are not benefitting from competition (Vocus, Electric Kiwi, Entrust, Future Energy).

Saves and win-backs can be a conduit for anti-competitive conduct

2.5.4 Concerns have been expressed that win-back discounts can be used to chill competition; by offering discounts or prices that are below costs in order to deter competitors from competing for a retailer’s customers.

2.5.5 New retailers who are seeking to grow expend more effort and spend proportionately more than large companies as they do not face reduced costs of retention since they have few to no customers to save or win-back. This results in saves potentially impacting disproportionately on new retailers compared to older retailers.

2.5.6 Win-backs are also viewed as retailers exercising a last right of refusal (Pulse Energy). Some submitters suggested that retailers need not offer their best price to consumers but rather can wait and see what price is offered by a competitor and then match or better it. They consider this is enabled by switch notification processes that alert a losing retailer to the pending departure of a

customer and the losing retailer can then contact the departing customer, ask what terms they have been offered and then better those terms.

- 2.5.7 Last right of refusal (or last look) clauses are considered potentially problematic for competition because they can be a source of tacit collusion amongst retailers. As discussed in the Authority’s 2014 decisions and reasons paper on the ‘Competition effects of saves and win-backs’ (2014, p.27) “They make it harder for retailers to acquire customers, because any acquisition offer can be matched by a retention offer. In consequence, they can discourage new retailers from entering the market, and existing retailers from growing their customer base”.

Win-back offers involve misleading information and questionable conduct

- 2.5.8 Some submitters noted that win-back offers can be aggressive and promote the benefits of staying with a losing retailer while making unsubstantiated claims about the credibility of the retailer the customer has chosen to move to (Flick). Consumers may be pressured into making decisions in the heat of the moment – when presented with take it or leave it time limited discounts.
- 2.5.9 At the same time, some retailers note that acquisition campaigns can also involve misleading claims, by an acquiring retailer, and it is in the customer’s best interests for the losing retailer to be able to scrutinise and clarify such claims (Mercury).
- 2.5.10 Some submitters suggested that questionable conduct and misleading information are most likely to be the result of action by an occasional rogue salesperson rather than systemic fault in the industry (Nova, Vocus).
- 2.5.11 There is also a concern that retailers’ approaches to win-backs may not be adequately adhering to requirements under the Fair Trading Act. The Fair Trading Act mandates a “cooling off period” of 5 days, for direct marketing, within which consumers can change their minds, no questions asked.¹² As discussed in our issues paper, there is some ambiguity around whether the “cooling off period” requirements apply to saves and win-backs. “Cooling off periods” do not apply for renewals of agreements. Whether a save or win-back is a renewal agreement is fact-specific for each individual situation. Since regulation of retailer conduct may apply unevenly as between losing retailers who make a successful save or win back and gaining retailers acquiring a new customer this is a potential source of regulatory problem(s).

Win-backs discounts are secret

- 2.5.12 There is some concern that win-back discounts reduce transparency of retail electricity prices available to consumers. This means that:
- a) consumers are unaware of the extent of savings they can receive by shopping around and, as a result, consumers are less engaged than they might otherwise be and competitive pressure is not as strong as it could be
 - b) it is difficult for entrant retailers to assess the competitive dynamics of a market (Electric Kiwi cross submission).

¹² The Code also requires gaining retailers to notify customers about these cooling off periods where they apply.

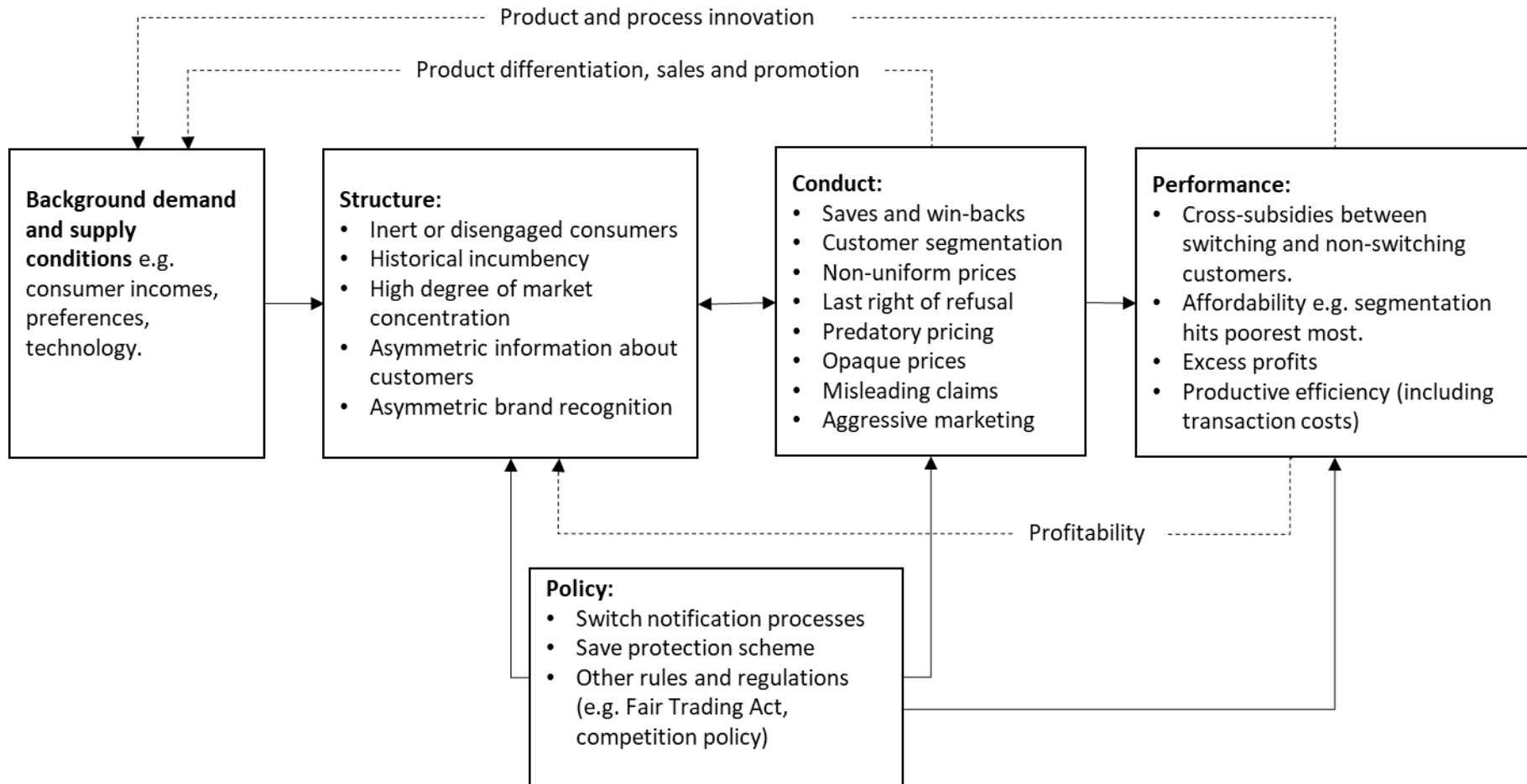
2.6 Scope of evaluation

- 2.6.1 Figure 2 below provides a summary of concerns raised above, within the context of the SCP framework.
- 2.6.2 The issues that we evaluate are the ones that are in the structure, conduct and policy parts of the framework.
- 2.6.3 In addition to focussing on structure, conduct and policy issues, under our terms of reference, our evaluation is limited to identifying
- a) regulatory problems or
 - b) market failures
- related to customer acquisition and switching processes, including saves and win-backs practices.

Regulatory problems

- 2.6.4 'Regulatory failure' is when regulation fails to achieve its objectives or makes matters worse, through faulty design or fundamental impediments such as asymmetric information and an inability to design, prescribe and enforce effective regulation.
- 2.6.5 One example of this is the undue informational advantage obtained by losing retailers during the switching process, i.e. the notification that a customer was intending to switch, which gave rise to the saves protection scheme. The rules which govern switching are very much part of the playing field as opposed to competitive behaviour. To the extent that these rules confer advantages to only some retailers, there is a potential regulatory problem.
- 2.6.6 Our consideration of regulatory problems is largely limited to switching processes, including switch notification, and the performance of the saves protection scheme. Other regulatory and policy matters, such as regulatory prohibitions on firms making misleading claims, are outside the mandate of the Authority.
- 2.6.7 This follows from our terms of reference and from the statutory responsibilities of the Authority. As discussed in our issues paper (para 2.2.12) the Authority is prevented, under the Electricity Industry Act 2010, from making Code amendments that purport to take actions or regulate matters that are the responsibility of the Commerce Commission under certain parts of the Commerce Act 1986 or policy matters.

Figure 2 Issues raised in relation to saves and win-backs, arranged according to the SCP framework



Market failure

- 2.6.8 'Market failure' occurs when non-regulatory impediments exist that prevent markets allocating resources efficiently. Causes of market failure include market power, externalities, asymmetric information or prohibitive transaction costs.¹³
- 2.6.9 An important market failure in this context is barriers to entry or expansion of competitors that can undermine competitive pressure. Barriers to entry are costs necessarily incurred by new entrants that incumbents do not (or have not had to) bear.^{14 15} A cost advantage, for example, is not a barrier to entry if the same advantage can be obtained by others.

Issues out of scope in our evaluation

- 2.6.10 Given this focus on market failure and regulatory problems, there are some issues that are outside scope for our evaluation. Customer segmentation and non-uniform pricing, for example, are not market failures or regulatory problems and thus not considered directly in our evaluation. Although they may be factors that could exacerbate more fundamental market failures or regulatory problems (as discussed in our issues paper, paragraph 4.3.11).
- 2.6.11 Asymmetric information or asymmetric brand recognition are not market failures – though asymmetric information can be a regulatory failure. This was discussed at some length in our issues paper where it was noted that all retailers can benefit from informational advantages, once they are established in the market (see paragraphs 2.2.6 to 2.2.8). Similarly brand recognition is something that can be obtained by new retailers, over time. Thus, as far as market failures or market structure and market conduct are concerned, the issues of asymmetric information and asymmetric brand recognition are not directly considered in our evaluation.

Key questions guiding our evaluation

- 2.6.12 In our evaluation, we are concerned primarily with evidence of problems with market structure or competitive conduct and the causal role that customer acquisition, including saves and win-backs, plays in creating these market conditions.
- 2.6.13 Our evaluation is not concerned with direct examination or diagnosis of problems relating to market performance – such as high average prices or distributional concerns. Our principal concern is with identifying market structures and conduct that are consistent with poor market performance and uncovering causes (market failures and regulatory problems).

¹³ These examples are cited in the Authority's Consultation Charter (2012) para 2.5.

¹⁴ There are numerous definitions of barriers to entry but this one usefully distinguishes the source of problem from outcomes, which some definitions fail to do. It also accounts for the dynamic nature of competition by not considering sunk costs or capital requirements to necessarily be barriers to entry.

¹⁵ Barriers to expansion would include costs that have to be borne by some firms, in order to expand, but not other firms that are expanding. Such barriers would also be barriers to entry, but they could be distinguished as barriers to expansion by the fact that they emerge over time and affect both new entrants and firms that are already in the market. An example is the introduction of non-tradable licences to one or a few firms, which would also be a regulatory problem if licences were issued by a regulator.

- 2.6.14 The high level question guiding our evaluation is whether customer acquisition and switching processes, including saves and win-backs practices, reduce competitive pressure by:
- a) contributing to non-competitive market structures including by
 - i. creating barriers to entry and expansion of competitors
 - ii. reducing consumer engagement (shopping around)
 - b) promoting or facilitating undesirable or anti-competitive conduct.
- 2.6.15 Strong evidence of these conditions would constitute a ‘non-level playing field’ for acquiring retailers, including new entrant retailers, and thus a potential problem for competition in the retail market.

3. Evaluation

3.1 Competitiveness of retail market structure

3.1.1 Issues concerning market structure are examined using the following four questions:

- a) is there evidence of market dominance, using the sorts of criteria used for conventional competition and merger and acquisition analyses?
- b) is there evidence of an increase in market dominance?
- c) is there evidence that rates of saves and win-backs have reduced consumer engagement?
- d) does the switch notification process provide an asymmetric advantage to retailers trying to retain customers, and thereby increase market concentration?

3.1.2 The last of these questions is a question about regulatory failures associated with switching processes as well as market structure.

Is market dominance a problem in the retail market?

3.1.3 Decisions made by competition authorities are a guide to levels of market shares that have been found to be problematic for competition.¹⁶ There are a range of views, across different jurisdictions, on the size of market shares that are sufficient to raise suspicions of market dominance. Benchmarks range from 40% in the European Union, to a minimum of 50% in the United States¹⁷ and up to 70% based on somewhat outdated research into competition decisions in New Zealand.¹⁸

3.1.4 In this evaluation we consider market shares of less than 50% as insufficient for market dominance. Market shares above 50% are considered to imply some evidence of potential dominance.

3.1.5 Based on our benchmark for market shares that indicate dominance, there are only two regions in which the incumbent retailer has a market share that could indicate dominance. These are Tauranga, where the incumbent had a market share of 67% and Waitaki where the incumbent held a market share of 57%, in 2018. These two regions account for 4.6% of ICPs in New Zealand.

3.1.6 By comparison, a majority of ICPs (54%) in New Zealand are in regions where the incumbent retailer holds less than 40% market share.

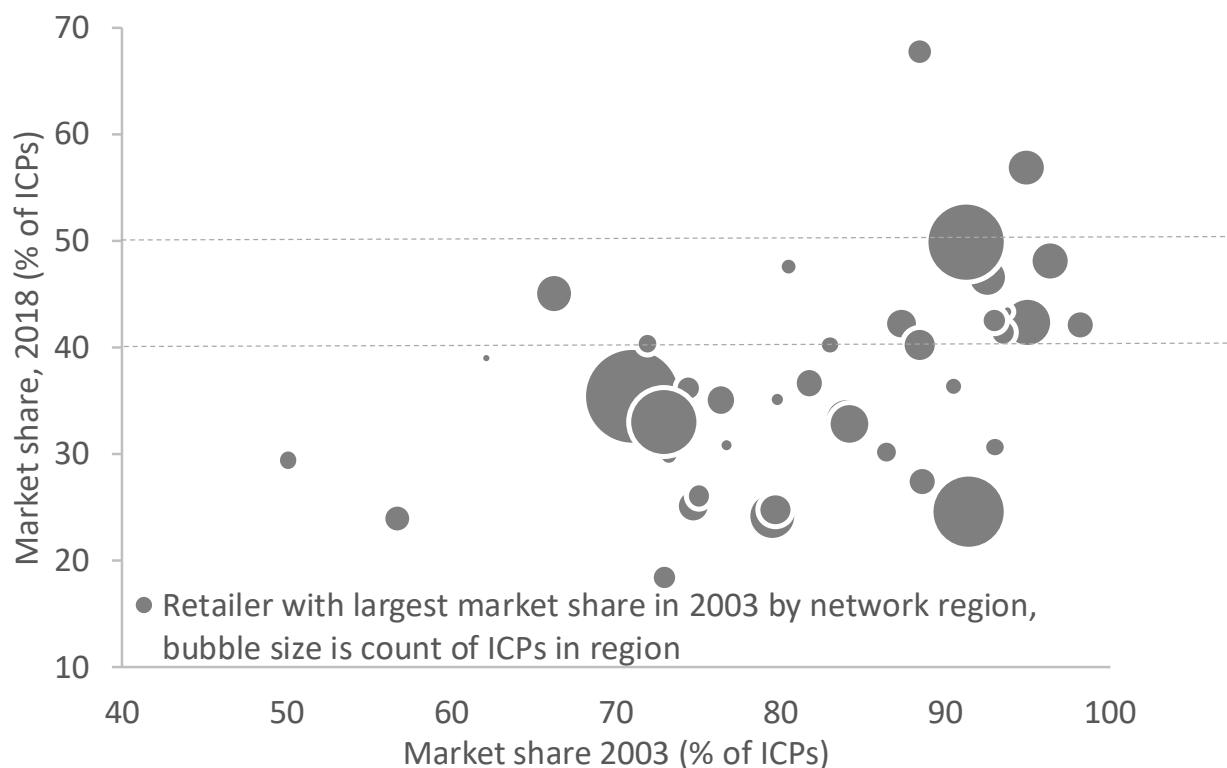
¹⁶ Competition authorities do not have predefined levels of market shares that are regarded as indicating market dominance. The effects of market shares on competition need to be assessed against other factors such as the extent of barriers to entry. However their decisions are a reasonable guide as to levels of dominance that are considered problematic.

¹⁷ Bartalevich, D. (2017). EU competition policy and U.S. antitrust: a comparative analysis. *European Journal of Law and Economics*, 44(1), 91–112.

¹⁸ Research on this issue, in New Zealand, is now quite dated. The most recent robust study was published in 2000 and found that a market share of at least 70% was necessary for a finding of market dominance. See Strong, N., Bollard, A., & Pickford, M. (2000). *Defining Market Dominance: A Study of Antitrust Decisions on Business Acquisitions in New Zealand*. *Review of Industrial Organization*, 17(2), 209–227.

- 3.1.7 Figure 3 summarises this evidence related to market dominance. On the left axis is current market shares of incumbent retailers, by region (network reporting region). The bottom axis shows market shares of incumbents in 2003.

Figure 3 Market shares of incumbents in 2003 and 2018



- 3.1.8 In 2018 the national market share of the largest retailer, Genesis, was 23.75% market share (by count of ICPs at 31 December 2018).¹⁹ The top 4 retailers make up 75% of the market and the top 5 make up 88% of the market.²⁰

Is the market trending towards increased occurrence of market dominance?

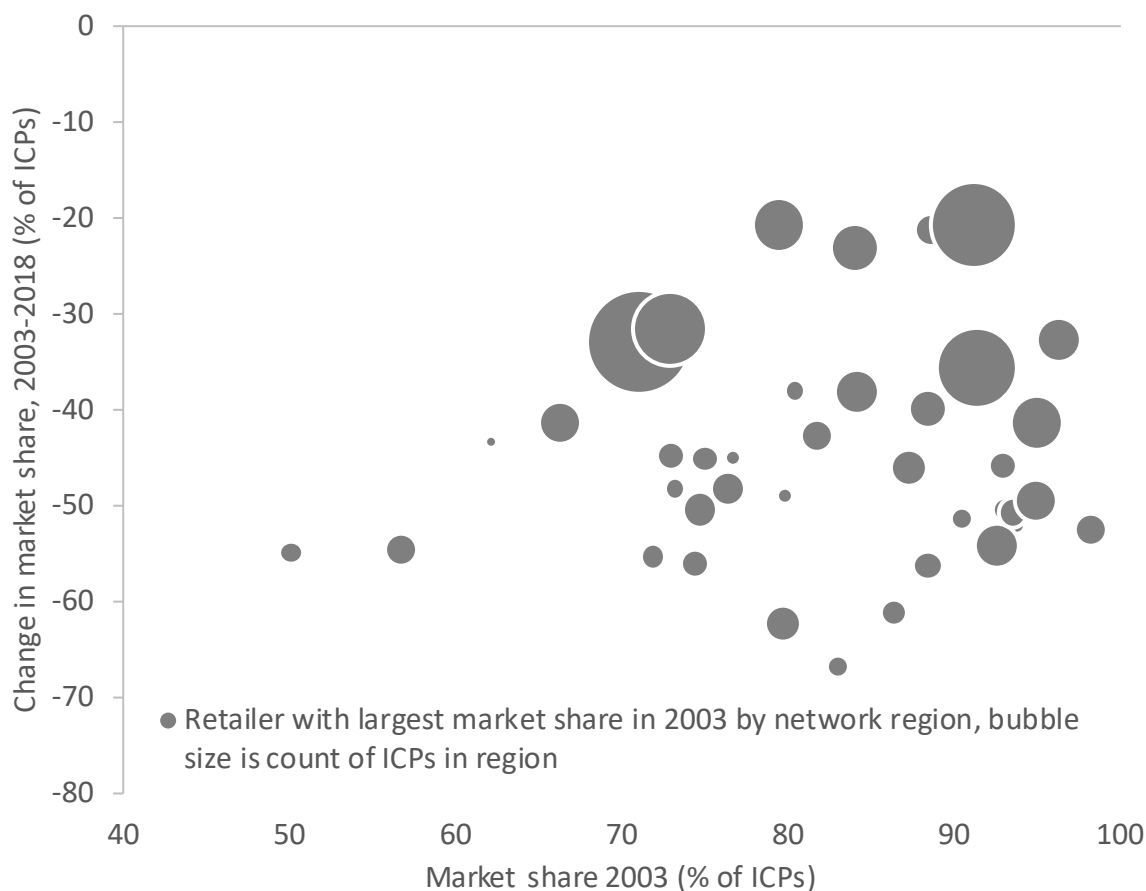
- 3.1.9 To assess whether market dominance has been increasing, we considered changes in market shares over time, focussing on changes in market shares for retailers that are the incumbent retailer in distribution network area.
- 3.1.10 The data show market concentration has been declining. Incumbent retailers have consistently lost market share in the past decade and a half while entrant retailers have been gaining market share. Reductions in incumbent market shares are depicted in Figure 4, showing that all incumbent retailers have experienced a substantial loss of market share in the past 15 years. As can be seen in Figure 3, almost all incumbent retailers held market shares in excess of

¹⁹ www.emi.ea.govt.nz/r/zv0il

²⁰ National market shares in the electricity industry are substantially less concentrated than, for example, market shares in New Zealand's telecommunications markets. By way of example, the top two providers had 73% of the mobile market and 69% of the fixed broadband market in 2018 (<https://comcom.govt.nz/regulated-industries/telecommunications/monitoring-the-telecommunications-market/annual-telecommunications-market-monitoring-report>). The top two electricity retailers had a combined 43% market share at December 2018. This comparison has been made in light of the view that a ban on win-backs in the telecommunications industry is an example of a pro-competitive initiative that could be adopted in the electricity industry.

50% 15 years ago. Now all but a few have market shares in excess of 50% and the average market share is 37% (weighted by market size).

Figure 4: Change in market share of incumbents 2003-2018



- 3.1.11 We have also considered patterns of saves and win-backs and customer acquisition between retailers, ranked by market shares by network area, to determine if retailers with the largest market shares tend to rely heavily on saves and win-backs to maintain or grow market share. This analysis is compared against changes in market share to determine the extent to which saves and win-backs are allowing retailers to maintain or grow market share.
- 3.1.12 We find there are several regions where retailers with high market shares rely heavily on win-backs to try and maintain or assist in growing market share.²¹
- 3.1.13 Figure 5 plots dependence on win-backs relative to market share. Dependence on win-backs is shown on the vertical axis and is measured using win-backs as share of observed customer acquisition (incoming switches) and retention (win-backs) activity.
- 3.1.14 In half (23) of New Zealand's network reporting regions, the incumbent wins back more customers than they attract (53% of regions). That is win-backs make up 50% or more of their customer acquisition and retention activity.²² This

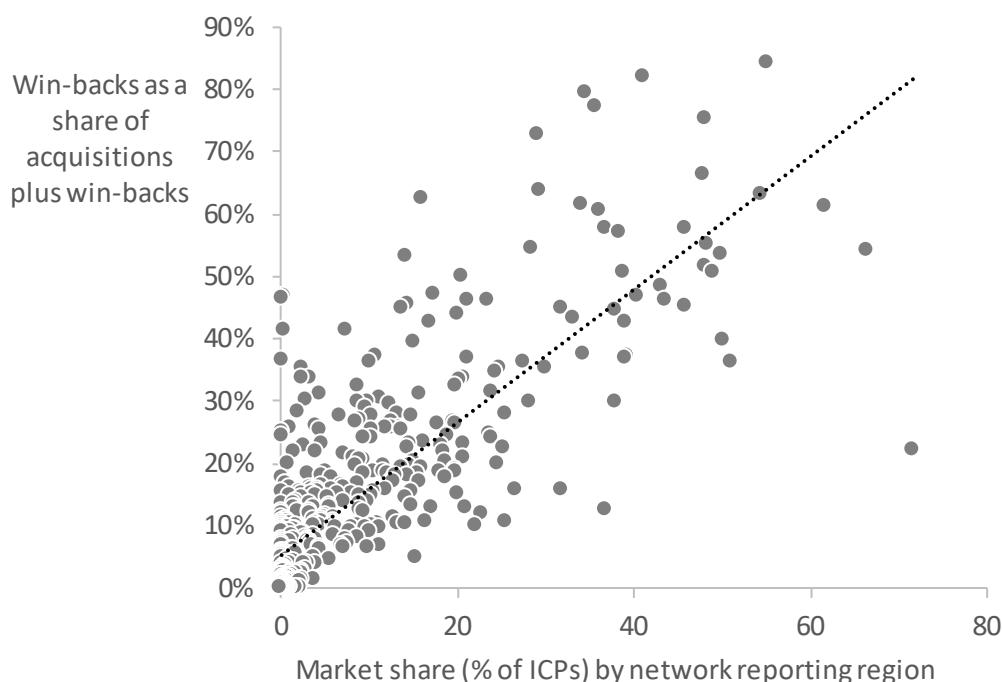
²¹ Notably it is impossible to rely solely on win-backs to grow market share. Market share can only increase if a retailer is acquiring customers as well as retaining customers.

²² Data for this analysis is 2015 to 2017.

does not, however, tell us how much effort these retailers have put into either acquiring customers or retaining customers.

- 3.1.15 Observed dependence on win-backs appears to reflect a failure to successfully acquire customers as much as a reliance on win-backs. All the incumbent retailers that have relied primarily on win-backs have lost market share in the past 3 years, with an average decline in market share of 9 percentage points.
- 3.1.16 The regions where retailers rely on win-backs make up 33% of residential ICPs and span rural areas and smaller urban areas (such as Hamilton, Dunedin, and Invercargill).
- 3.1.17 It is difficult to know how retailers would fare in the absence of this reliance on win-backs. It is possible that small retailers may have expanded market shares by more than they have. But this is not certain.
- 3.1.18 Further, robust competition does not require ongoing expansion of smaller retailers. Indeed, by way of comparison, in a theoretically perfectly competitive market all retailers would be offering the same service and charging the same price and small retailers would not be able to expand their market shares because consumers would have no incentive to switch retailers.

Figure 5 Reliance on win-backs compared against market share²³



Have saves and win-backs reduced consumer engagement?

- 3.1.19 To assess whether win-backs are affecting customer engagement we consider whether rates of saves and win-backs have a statistically causal effect on

²³ This data is for residential ICPs in 2017. It is from a data set used to analyse rates of switching and saves and win-backs at the level of individual ICPs. One important change in retail market shares between 2017 and 2018 was the significant acquisition of King Country Energy customers by Trustpower (~25% of ICPs in the King Country area). This caused measured market concentration of retailer market shares to fall significantly in 2018 in an area that, historically had a highly concentrated market share.

indicators of consumer engagement: consumer switch initiation rates and visits to the Power switch and What's My Number websites.

- 3.1.20 This draws on results of an evaluation of the What's My Number campaign by Sense Partners (forthcoming) and an evaluation of the impacts of the Consumer Switching Fund by Covec (2013).
- 3.1.21 The findings from these reviews are supplemented by simple statistical analyses that explore correlations between indicators of consumer engagement and rates of saves and win-backs to determine if they are positively or negatively related and whether there is evidence for statistically causal relationships using so-called "Granger causality" tests, which check if movements in a data series are statistically important predictors of movements in another series (and vice versa).
- 3.1.22 Covec's (2013) review of the Consumer Switching Fund, for MBIE, found no relationship between rates of website visits and saves and win-backs. This was also the finding of Sense Partner's 2018 update of the Covec review.
- 3.1.23 Further descriptive analyses of statistical relationships between save and win-back rates²⁴ and switch initiation rates²⁵ and Power switch and What's My Number website visits does find some but only very weak evidence of a negative relationship between saves and win-backs and consumer engagement. At least in the case of website visits as a measure of consumer engagement.
- 3.1.24 Increases in rates of win-backs are associated with increases in rates of switch initiation²⁶ (see Figure 6) and reductions in Power switch and What's My number website visits²⁷ (see Figure 7).

²⁴ Specifically win-backs as a share of the sum of trader switches (ignoring switches associated with moving house) plus winbacks (i.e. as a share of estimated initiated switches).

²⁵ Specifically, the sum of switches between traders and win-backs as a share of ICPs.

²⁶ From national level estimation of a common statistical ("cointegrating") trend relationship between these two series.

²⁷ From national level estimation of a common statistical ("cointegrating") trend relationship between these two series.

Figure 6: Relationship between win-backs and switch initiation

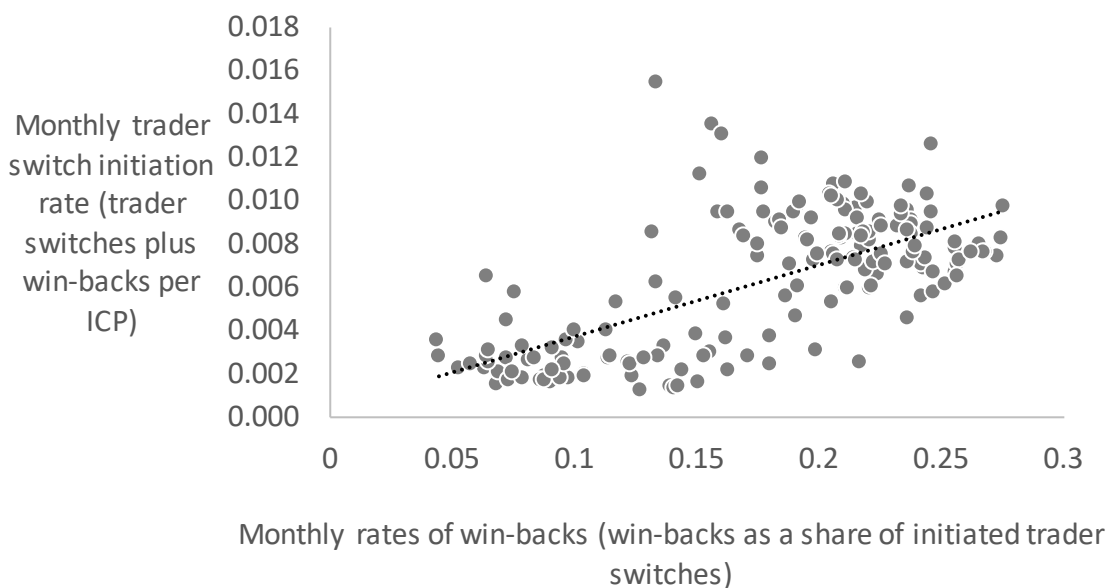
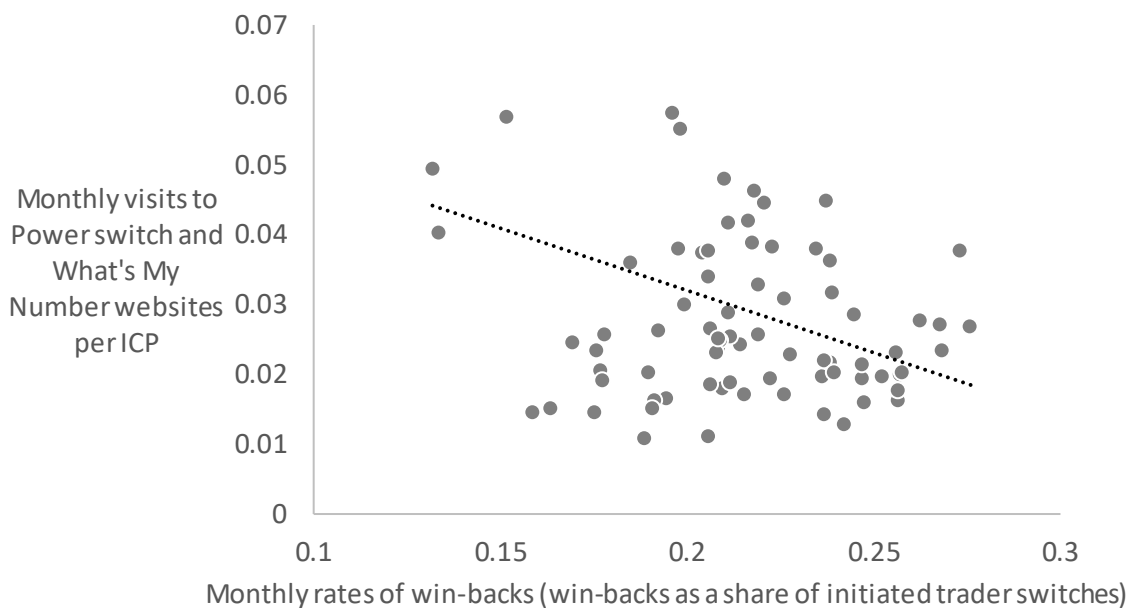


Figure 7 Relationship between win-backs and website visits



3.1.25 The direction of causation, whether from saves and win-backs to indicators of consumer engagement (rates of switch initiation and website visits) or vice versa, is ambiguous.²⁸ Reductions in website traffic may be causing reductions in win-back rates rather than the other way around. We would also expect win-

²⁸ A granger causality test on the levels of the series, with 3 or fewer lags, suggests rates of win-backs do cause changes in rates of switch initiation but not website visits. However, a granger causality test on the levels of the series with larger numbers of lags rejects a hypothesis of a causal relationship. Furthermore, granger causality tests on the differences of the series – to account for non-stationarity of the data – rejects a hypothesis of a causal relationship at any number of lags.

back activity to be positively correlated with people shopping around and hence correlated with switch initiation. The competitive threat from increased switch initiation should be expected to drive retailers to respond with higher rates of win-back offers to stem losses.

- 3.1.26 This analysis is also quite simplistic in the sense that there is no strong reason to believe that consumer engagement or inertia is a cause or consequence of saves and win-backs. Customers that are saved or won-back are not inert.
- 3.1.27 It is also unclear consumer inertia is a problem that is entirely avoidable in a workably competitive market. Consumer inertia is a result of numerous factors. Attempts to resolve this failure need to be weighed carefully against the possibility of unintended consequences (regulatory failures), including potential negative effects on competition. It is difficult to distinguish between a pure market failure – such as when there is insufficient information to support consumer choice – and situations where consumers accurately judge that it not worth their while searching for a better price or higher quality (so-called rational inattention).²⁹ This is also an issue that is being addressed by other initiatives such as the What's My Number advertising campaign and the current Electricity Price Review.

Do switching procedures increase the effectiveness of counter-offers?

- 3.1.28 To investigate whether switching procedures give losing retailers or incumbent retailers a competitive advantage, we consider a counterfactual thought experiment of whether competition and efficiency would be improved if there was
- a) no notification of a switch before switches are completed
 - b) no option for cancelling switches via switch withdrawal.
- 3.1.29 Efficiency is considered alongside potential competition effects because, with administrative procedures, there can be trade-offs between promoting competition and promoting efficiency. Such trade-offs need to be consistent with promoting long term benefits to consumers, in accordance with the Authority's statutory objective.
- 3.1.30 The counterfactual thought experiment considers:
- a) if current procedures favour losing retailers by raising the likelihood that their counter-offers will be successful in retaining customers
 - b) the efficiency of existing switching procedures – in terms of cost, speed and integrity of information – and whether these procedures are efficient, relative to our counterfactual.
- 3.1.31 When considering whether retailers are advantaged by regulated switching procedures, we compare the status quo against a counterfactual where switch notification is governed only by bilateral contractual arrangements between retailers and their customers. We would expect that, in the absence of regulated

²⁹ Technically, rational inattention causes market outcomes to deviate from ideal outcomes and raises the hypothetical possibility that improvements are possible. But finding a way to obtain these improvements, without making matters worse, is incredibly challenging.

switching processes and notifications, retailers would require some form of notification from their customers that they are leaving (that the customer is, in effect, cancelling their contract). Retailers have ongoing obligations to their customers and a counterpart to that is that retailers will want to know, as part of their service agreement, when they no longer have those obligations. Retailers would need to know whether to invoice a customer and whether they are responsible for covering the costs of energy used by the customer.

3.1.32 We assume that faster switching procedures imply higher consumer benefits from switching and a higher likelihood of success of counter offers. The reasoning behind these assumptions is that:

- a) consumers are switching to a preferred product or price and the sooner they can start receiving that product or price the better for them
- b) the probability of a successful counter-offer reduces with the amount of time elapsed between a consumer's decision to switch and the time when a counter-offer is made.

3.1.33 Impacts of speed on the overall efficiency of switching procedures is more ambiguous. Faster processes could imply less effective information verification and more scope for errors and costs associated with rectifying errors.

Impact of notification before switches are completed

3.1.34 Figure 8 outlines a switching process where retailers are no longer notified of a switch before it is completed. Compared to the switching process shown earlier in Figure 1, the third step in the switching process, the point at which the retailer is notified and provides information, is removed and a new step (4) is added where switch information verification takes place after the switch has been completed. All other steps remain unchanged.

3.1.35 In our assessment, the most substantive change, in terms of competition effects, is that switches would be completed more quickly. This is because a gaining retailer has a financial incentive to bring customers on board as quickly as possible and a typical switch would therefore be completed more quickly (or at least as quickly) than it is under existing procedures.

3.1.36 This suggests that removing switch notification, prior to switch completion, would, if anything, increase the effectiveness of counter-offers and increase benefits to consumers from faster switching processes – because of a reduction in the amount of time between switch initiation and counter-offers being made.

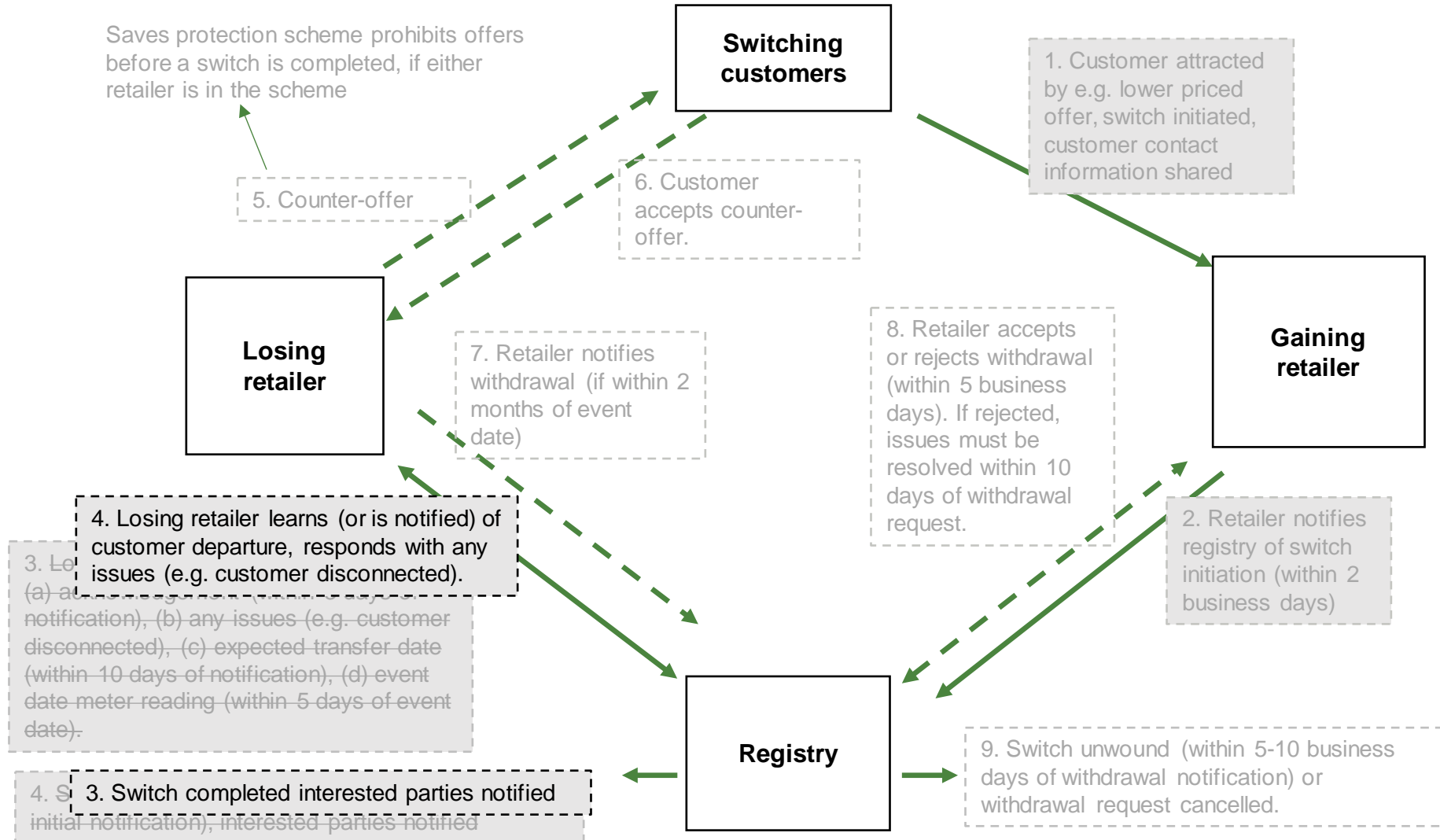
3.1.37 This suggests that the existing switch notification process inhibits the retention (win-back) strategies of losing retailers, to the extent that it increases the time between switch initiation and counter-offers and if the effectiveness of counter-offers declines with time elapsed between initiation and counter-offer. If there is no relationship between the effectiveness of a counter-offer and the time elapsed between switch initiation and counter-offer, then the effect of existing notification processes on retention strategies of losing retailers is ambiguous.

3.1.38 The existing switch notification process may also be creating costs for consumers, by delaying the presentation and acquisition of a counter-offer – to the extent that the counter-offer is attractive to the consumer and they have to wait longer to receive the benefits of that offer. However, this additional cost

needs to be balanced against the usefulness of the information exchange and verification process that currently takes place in response to switch notification prior to switch completion.

Figure 8 Switching process with notification after a switch is completed

Compared with switching process outlined in Figure 1 New processes in black dashed boxes. Unchanged switching events are in grey text. Revoked switching events are struck out.



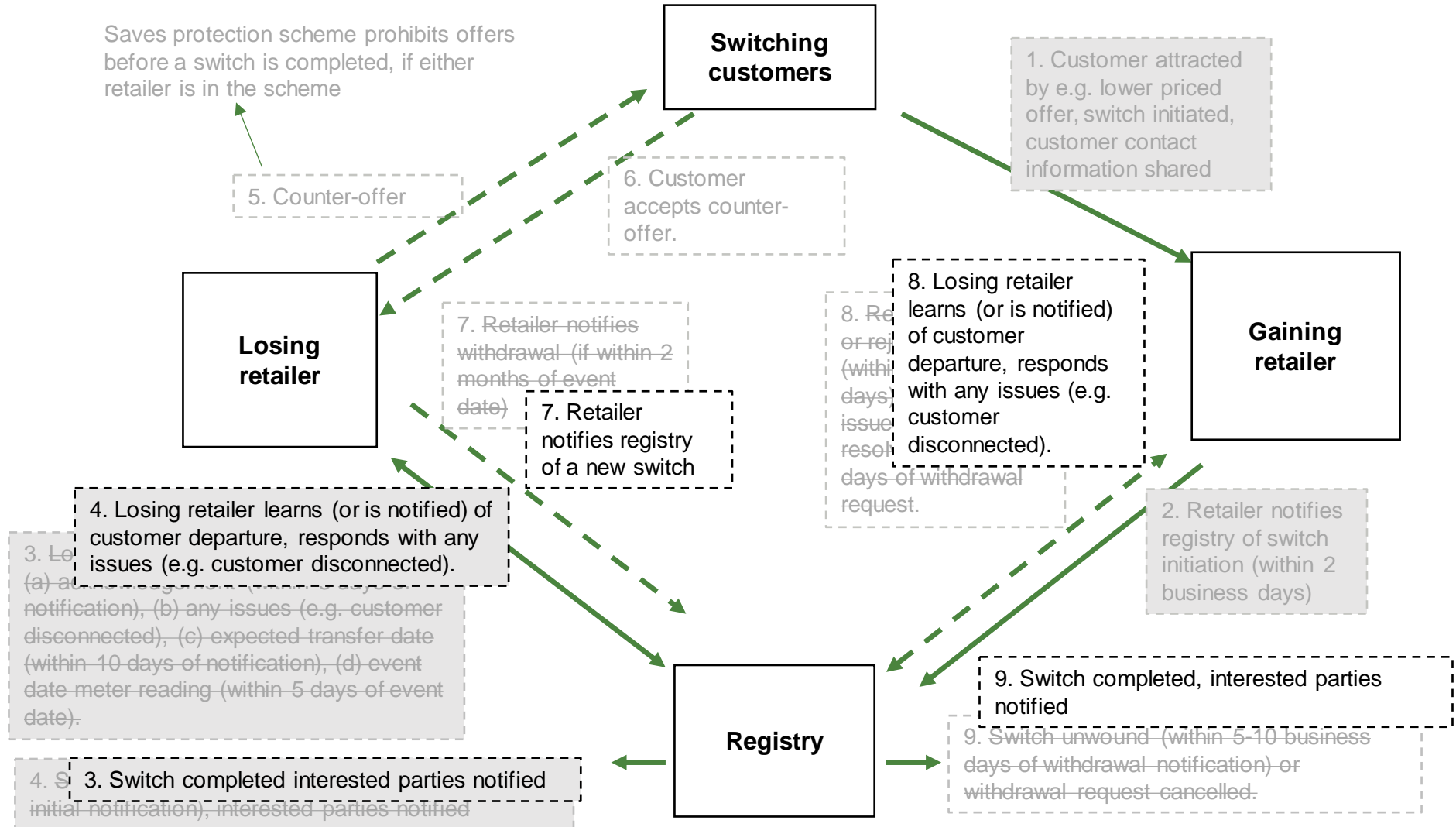
- 3.1.39 There is also some doubt over the accuracy of an assumption that the effectiveness of counter-offers declines with the time elapsed between consumers' decisions to switch and the time when counter-offers are made. The Authority's post-implementation review of the saves protection scheme found that additional time to switch withdrawal had no effect on the probability of switch survival. This is not strong evidence against our assumption – time between switch initiation and switch withdrawal is not the same as time between decision to switch and counter-offer – but it does raise questions over the veracity of our assumption.
- 3.1.40 Regardless, there is no reason to believe that the removal of switch notification prior to switch completion would reduce the effectiveness of losing retailers' counter-offers.

Impact of switch withdrawal

- 3.1.41 Switch withdrawal is a process that may smooth the way for retailers to make counter-offers to try and win customers back. If withdrawal was not an option – or was only an option in limited circumstances, such as to rectify errors – retailers would have to engage in the full switching process to win a customer back.
- 3.1.42 An alternative switching process is depicted in Figure 9. The option to withdraw a switch has been removed. Switch notification, prior to switch completion, has also been removed.
- 3.1.43 Removing the option for switch withdrawal – effectively cancelling a switch – would slow the speed at which losing retailers could regain customers following counter-offers. It would not reduce the speed with which losing retailers could make counter-offers to regain customers. As such, the effects on success of counter-offers is ambiguous.

Figure 9 Switching process notification after switch completion and option for withdrawal removed

Compared with switching process outlined in Figure 1. New processes in black dashed boxes. Unchanged switching events are in grey text. Revoked switching events are struck out.



- 3.1.44 This alternative switching process would increase transaction costs associated with switching because additional information gathering would be required (e.g. meter reads). Retailers that won customers for only a short time, such as a few days or weeks, would also need to issue bills to those customers where currently they do not. This is because the current switch withdrawal process is designed to avoid these costs by nullifying a switch rather than requiring a repeat of the switching process, as long as switch withdrawal occurs within 2 months of the switch being completed.
- 3.1.45 Consumers would have to wait longer before they could receive the price or product counter-offered by the losing retailer. As such, there would be a reduction in consumer benefits.

3.2 Impacts on undesirable or anti-competitive market conduct

- 3.2.1 Issues concerning undesirable or anti-competitive conduct are examined using the following three questions:
- a) are saves being pursued aggressively and targeted at new entrants for the purposes of discouraging competition?
 - b) do win-back discounts obscure the range of retail prices available to consumers and inhibit consumer engagement or competition?
 - c) do saves and win-backs facilitate or promote the use of misleading claims by retailers seeking to acquire, retain or regain customers because of flaws in:
 - i. switch notification procedures or
 - ii. consumer protection legislation?
- 3.2.2 This evaluation is a high-level assessment focussing on the possible role of saves and win-backs in facilitating undesirable or anti-competitive conduct and relying on information to hand from secretariat analyses and submissions on our issues paper. It is not within the scope of this review to conduct a thorough inquiry into anti-competitive practices such as predatory pricing.

Use of saves and win-backs to discourage competition

- 3.2.3 Our approach to assessing the use of saves and win-backs for anti-competitive purposes focusses first on high level trends in saves and win-back practices and relationships between saves and win-backs and retail prices.
- 3.2.4 There is a fine line between discouraging competitors by competing, with lower prices or higher quality, and acting to discourage competition.
- 3.2.5 We reflect upon three indicators to consider whether saves and win-backs may be a conduit for anti-competitive practices that are being used to discourage competition.
- 3.2.6 We also weigh evidence we have been given regarding the use of “loss-leading” or predatory pricing to discourage competition.

Trends in rates of use of saves and win-backs

- 3.2.7 The first indicator is whether trends in rates of save and win-back activity have increased in recent years, following an increase in rates of new entrants.

- 3.2.8 We assess trends in monthly rates of win-back activity, measured by the number of win-backs in a month as a percentage of the number of switches initiated in a month, and also trends in peak win-back rates, measured by maximum monthly rates of win-backs in a year. Peak win-back rates are generally much higher than average annual win-back rates because win-back rates spike when retailers engage in concerted counter-offer campaigns.
- 3.2.9 An increase in win-back rates could be either an indicator of anti-competitive or a competitive response to increased competition. As such, this is a partial indicator of competitive impacts of saves and win-backs activity – to be considered alongside other indicators.
- 3.2.10 Concerns were raised in submissions about larger firms' and incumbents' increasing rates of saves and win-backs in recent years. Electric Kiwi presented data showing that Mercury's save and win-back rates in Auckland in April 2018 were twice their average rate between 2004 and 2018.³⁰
- 3.2.11 There is evidence of rising trends in rates of saves and win-backs in parts of the country. This is a continuation of a long-term trend (see Figure 12 in the Data appendix).
- 3.2.12 "Peak" annual win-back rates have not been increasing (data on peak win-back rates by network area is presented in Figure 13 in the Data appendix).
- 3.2.13 There is no significant variation in these trends between firms with the highest market shares and other firms (see Figure 14 and Figure 15 in the Data appendix). Indeed, trend growth in win-back rates for firms with the highest market shares has been lower than for firms with smaller market shares.

Rates of saves and win-backs between incumbent and entrant retailers

- 3.2.14 The second indicator is whether win-backs are concentrated on entrant retailers and potentially having a disproportionate impact on entrant retailers and creating barriers to entry or expansion for entrant retailers.
- 3.2.15 Indications of selective targeting of win-back activity may be suggestive of anti-competitive attempts to dissuade entrants from competing in some parts of the country.
- 3.2.16 Furthermore, if win-back activity is strongest between incumbents and entrants and weakest between incumbents then this would indicate the potential presence of tacit collusion – such as might occur if retailers were using win-backs as a "last right of refusal" (as discussed in paragraphs 2.5.5 and 2.5.7).
- 3.2.17 Incumbent retailers have some of the highest rates of win-backs, although not the highest. On average, the third highest ranked firms, in terms of market shares, have the highest rates of win-backs³¹

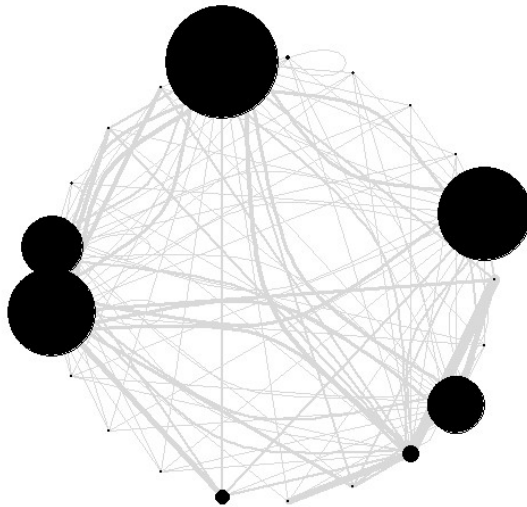
³⁰ Mercury's data was subsequently revised and the way the win-back rates were calculated (win-backs as a share of losses) is not as easily interpreted as the method used in this report (win-back rates = win-backs as a share of initiated switches). Nonetheless it is the case that Mercury's rates of win-backs in Auckland have increased long term and do spike from time to time.

³¹ Table 5 in the Data appendix shows average rates of win-backs between retailers based on market shares by network area. This shows an average win-back rate of 0.29 (29% of initiated switches) for firms with the highest market share. This compares to a win-back rate of 0.25 for firms with the second highest market share and a rate of

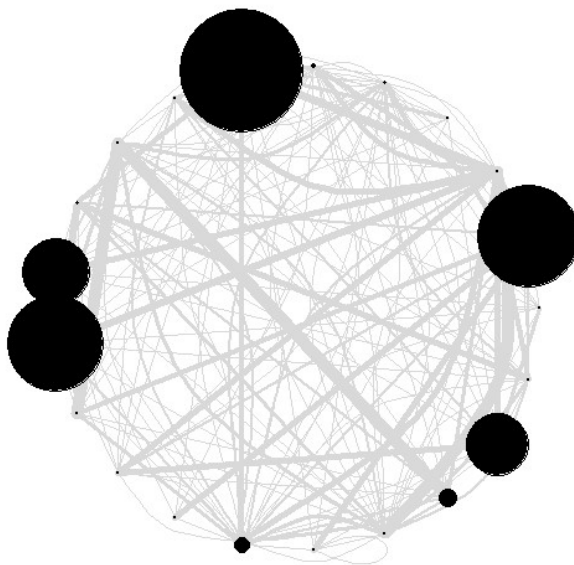
- 3.2.18 Win-back rates are highest between retailers with high market shares. This is partly a consequence of the fact that larger firms are initiating switches against one another at rates that are generally higher than or equal to rates at which smaller firms initiate switches against larger firms.
- 3.2.19 At the same time, larger firms experience the highest rates of win-backs executed successfully against them. On average, across the 26 network pricing regions in New Zealand, the largest retailers have the highest rates of failed acquisitions (28%), due to saves and win-backs, and the third largest retailers have the second highest (27%) (see Table 1 in the Data appendix).
- 3.2.20 Larger retailers also win customers back from smaller retailers at lower rates than they win customers back from other larger retailers. The average win-back rate between the 5 largest retailers is 25%. The average win-back rate of the 5 largest retailers against the next 5 largest retailers is 15%.³²
- 3.2.21 It is possible that larger firms – firms that are incumbents in at least some regional markets – may favour use of saves and win-backs because this increases their ability to retain customers (i.e. is more cost-effective) and reduces incentives for other firms to devote resources to customer acquisition.
- 3.2.22 Further, retention is invariably more important for firms with large customer bases.
- 3.2.23 Companies with low market shares also execute saves and win-backs – amongst each other and with firms that have much larger market shares.
- 3.2.24 Nationally, almost all retailers use saves and win-backs. This is illustrated in Figure 10 which depicts win-backs between retailers. Several other empirical analyses were presented in the MDAG's issues paper to support this conclusion.

0.30 for firms with the third highest market share. Note that firms with the highest market share are not always incumbents. Some firms that were incumbents in some areas no longer have the highest market share.

³² These figures represent a combined average of win-back rates across network reporting regions nationally with retailer size defined according to rank of market share by network reporting region.

Figure 10: Rates of saves and win-initiated by incumbent retailers

Spots are retailers, sized by national share of residential ICPs. Lines depict win-backs between retailers (from and to). Line thickness varies by rate of win-backs relative to initiated switches. Data is 2017.

Figure 11 Rates of saves and win-backs initiated by non-incumbent retailers

Non-incumbent win-back rates (win-backs/initiated switches) are frequently high, between non-incumbent retailers, due to small numbers of switches being initiated between these retailers.

Relationship between saves and win-backs and prices posted by retailers

- 3.2.25 Our third indicator is the relationship between saves and win-back activity and retail prices posted by retailers.
- 3.2.26 If win-backs have caused a lessening of competition, an important consideration for a finding of anti-competitive behaviour, we would expect prices to be higher (or at least not lower) where rates of win-backs are higher. If competition is working we would expect retailers to reduce their published prices (inclusive of new customer discounts) to guard against successful counter-offers.

- 3.2.27 The relationship between saves and win-backs and electricity prices is ambiguous. A recent evaluation of the effects of the What's My Number campaign, shows that win-backs are associated with reductions in retailers' prices, consistent with win-backs being pro-competitive, but not in markets with low rates of switching or below average numbers of competitors in the market – that is where competitive activity is relatively low.³³
- 3.2.28 The analysis considered the effects of consumer switching rates – rates of completed switches and rates of initiated switches – on retail prices posted by retailers on Powerswitch taking account of a range of market conditions including: (i) levels of household electricity consumption, (ii) the number of competitors present in a network area and (iii) rates of saves and win-backs.

Use of predatory pricing

- 3.2.29 Charging some customers less than incremental cost can be an indicator of anti-competitive practices. Necessary conditions for loss-leading prices to be predatory prices include that a firm
- a) has priced below marginal (avoidable) costs
 - b) has market power
 - c) intended to lessen competition.
- 3.2.30 Gathering the necessary information to investigate the last of these three conditions is very difficult and seeing as we are primarily interested in systemic market failures and regulatory problems, rather than the conduct of individual retailers, we ignore the requirement related to intent.
- 3.2.31 We do, however, consider the extent to which retailers are likely to have enough market power to engage in predatory pricing.
- 3.2.32 We assume that, on their own, loss-leading prices are not necessarily inefficient or anti-competitive. For example, new firms may charge customers less than the marginal cost of service because they are trying to establish a market presence and scale. Thus, we weigh evidence that we have seen regarding loss-leading prices alongside evidence for whether firms have enough market power to engage in predatory pricing.
- 3.2.33 The use of loss-leading prices to lessen competition is a matter that falls within the mandate of the Commerce Commission. However it is also of interest to the Authority to the extent that market structure or policy could contribute to conditions that enable such behaviour.
- 3.2.34 A submission on our issues paper, from Future Energy New Zealand, provided an example of a win-back offer that was highlighted as being potentially loss-leading and therefore potentially anti-competitive.
- 3.2.35 In Future Energy's example the losing retailer made a counter-offer which amounted to a monthly bill, excluding GST, of \$198.7 inclusive of a prompt payment discount of 20% and based on a monthly consumption of 977 kWh. This represented a 17.7% reduction on the consumers bill before they initiated a switch.

³³ Sense Partners (Forthcoming).

- 3.2.36 Energy costs and lines charges for this customer, assuming the customer lives in Vector's network area, are estimated to be \$165.90. This leaves a \$32.80 difference between revenue and avoidable costs. This example certainly does suggest a very small margin, however it may not be loss leading.
- 3.2.37 The basis for this calculation is that, as Future Energy noted, the losing retailer (Genesis) had published a benchmark transfer price for wholesale energy of \$79.11 per MWh. In addition, we assume that the customer lives in Vector's network area and is on a standard residential tariff, implying distribution and transmission charges of \$88.90.³⁴
- 3.2.38 The losing retailer would have very little margin remaining to cover metering costs, retail billing costs or retail overheads and cost of capital. But this may only imply that the customer will pay a much smaller share of the retailer's fixed costs than the retailer's average customer. This is not necessarily anti-competitive. Rather this is something that is observed in many workably competitive markets.
- 3.2.39 Based on the analysis outlined in subsection 3.1.8, it is also unclear whether the losing retailer would have sufficient market dominance (market power) for these prices to be able to have an anti-competitive effect.

Do saves and win-backs facilitate or promote misleading claims

- 3.2.40 Other things equal, we would expect that a retailer or retailers' agents have the same incentive, if any, to mislead a customer during customer acquisition of all kinds, whether a win-back or an acquisition or a delayed counter-offer to regain a customer.
- 3.2.41 However, it may be that there is something distinctive about the process of retaining a customer, with a win-back offer and a switch withdrawal, that lends itself to misleading claims. Thus we consider the same counterfactual thought experiment, regarding alternative switching procedures, discussed in paragraph 3.1.28, to determine if there is a potential regulatory failure associated with switching procedures that increases the pay-off to making misleading claims and does so in a way that favours losing retailers and gives a competitive advantage to retailers that are attempting to retain customers.
- 3.2.42 In this context, we assume that incentives to make misleading claims are a function of time pressure. That is, we assume that incentives to mislead customers increase where retailers perceive that they need to convince consumers to make quick decisions.
- 3.2.43 We also consider the strengths or weaknesses of existing switching procedures, for self-monitoring of misleading claims, between retailers.
- 3.2.44 As discussed earlier, current switching procedures tend to slow down the rate at which switches are completed – relative to a counterfactual in which a notification of a switch is governed only by private contractual arrangements – and, under the saves protection scheme, tend to prolong the time until losing

³⁴ Vector's price schedule for the year starting 1 April 2018 listed a \$1.01 per day fixed charge, a 6.27 c/kWh uncontrolled charge and a 5.51 c/kWh controlled charge. Future Energy's example was for a customer with 586 kWh of anytime consumption and 391 kWh of controlled consumption.

retailers can provide customers with counter-offers. It is possible that this could increase a losing retailer's sense of urgency in trying to secure a win-back – if consumers' willingness to accept a counter-offer declines with the time since they initiated a switch.

- 3.2.45 The effect of increased urgency, on incentives to make misleading claims, is ambiguous though. The pay-off to making misleading claims declines as the probability of successful retention also declines but commercial risks, to reputations or from regulatory sanctions, do not decline. Thus, the risk adjusted net benefit of making misleading claims would, if anything, tend to decrease when switching procedures are slowed down.
- 3.2.46 Furthermore, existing procedures provide opportunities for retailers to correct information and for consumers to withdraw their switch if they discover that they have been misled. As such, advance notification of an impending switch and the ability to withdraw a switch can be effective mechanisms for disciplining undesirable retailer conduct such as retailers misleading customers or switching customers without agreement.
- 3.2.47 There is some, albeit limited, evidence that poor conduct is a practical problem in terms of misleading claims being made. A survey conducted for the Authority's 2014 consultation on saves and win-backs found that one fifth of consumers that were won back chose to do so because the retailer they had switched to did not turn out to be cheaper as they expected.
- 3.2.48 The option to withdraw switches, rather than complete a new switch when winning a customer back does raise questions about the applicability of "cooling off period" protections that consumers have under the Fair Trading Act. "Cooling off periods" do not apply for renewals of agreements and whether a save or win-back activity is considered to be a renewal agreement is fact-specific for each individual situation. However, no evidence has been found that that this is a problem in practice.

Transparency of win-back discounts and prices

- 3.2.49 We take it as given that more information is always better, other things being equal. This is based on the idea that competition works best when consumers are engaged and that consumers can better engage when they are aware of prices and of the benefits of shopping around.
- 3.2.50 Our evaluation of the impact of win-back discounts on transparency of retail prices focusses on:
- a) whether there are causal relationships between the use of saves and win-backs and reduced transparency and consumer awareness of retail prices and discounts available in the market
 - b) potential implications, for competition, of regulating price disclosure, based on experiences in the United Kingdom.
- 3.2.51 There is no obvious causal connection between the use of saves and win-backs and a lack of pricing transparency. In the absence of saves and win-backs retailers could, for example, still offer consumers (e.g. via door-to-door marketing) unpublished one-off or time-limited discounts that are not widely observed by other consumers.

- 3.2.52 This does not mean that there are no benefits to be gained for consumers from greater transparency (e.g. publication) of discounts that are currently only revealed to customers via saves and win-backs or other offers. This is just to note the issue is relevant to all forms of customer acquisition or retention.
- 3.2.53 There may also be offsetting costs from disclosure of one-off price offers if disclosure is required rather than voluntary. In the UK Ofgem introduced a requirement for retailers to notify customers of their cheapest tariffs. In a subsequent review the Competition and Markets Authority raised concerns that this led to retailers withdrawing their lowest priced offers – with an overall increase in average prices.³⁵
- 3.2.54 One reason that retailers may remove discounts, if forced to publish them or make them freely available to all customers, is that offering those prices to all customers may be unsustainable (unprofitable). For example, a price may include an implicit discount for a high-volume customer that would be unprofitable for a customer with low levels of consumption.
- 3.2.55 A lack of knowledge about competitors' prices can also have pro-competitive effect. Currently, retailers have limited knowledge about the size of the discounts that are being offered. This creates an incentive to put forward the best offer possible. Once retailers know all other retailers' offers they may be able to increase their prices (at least for those retailers with low costs).

³⁵ <https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf> Ofgem's policy is still in place.

4. Conclusion

4.1 Findings

- 4.1.1 There is no strong evidence of regulatory problems or market failures related to customer acquisition and switching processes, including saves and win-backs practices.
- 4.1.2 There are recurring concerns that the retail market is highly concentrated and that saves and win-backs perpetuate this, particularly by giving undue advantage to incumbent retailers. However incumbent retailers do not appear to have dominant market shares.
- 4.1.3 Incumbent retailers do tend to engage in win-backs at a slightly higher rate than the average but mostly against other large retailers and these incumbent retailers have consistently lost market share.
- 4.1.4 There does appear to be an upward trend in the use of saves and win-backs. But evidence that there are problems arising from the use of saves and win-backs, or not, are relatively thin such that no robust conclusions can be drawn one way or the other.
- 4.1.5 Patterns of win-back activity are consistent with increasing competitive pressure as retailers need to pay attention to costs and to price levels to avoid losing customers to counter-offers. The fact that win-backs are most prevalent between larger retailers is compelling evidence of this. Furthermore, there is empirical evidence that win-backs are associated with lower prices.
- 4.1.6 The Authority previously introduced the saves protection scheme because it observed that there was a potential regulatory failure in existing switching procedures whereby losing retailers were being advantaged with notification of impending switches. There is no similar rationale in relation to win-backs. Though retailers are notified of an impending switch they cannot act on this until after the switch is completed, if the winning retailer is part of the save protection scheme. Switch completion takes time, and this reduces the ability of retailers to strike, with a counter-offer, while the iron is hot (so to speak).
- 4.1.7 We also find that switch notification and switch withdrawal procedures do not alter any incentives that may exist for retailers to use misleading claims to attract customers. On the contrary, switch notification can help to provide a discipline on retailer conduct. Allowing for switch withdrawal also reduces transaction costs associated the switching process.
- 4.1.8 Win-back discounts do reduce the transparency of electricity prices and this could be affecting the rates at which consumers shop around – there is some, weak, evidence of an association between increased use of win-backs and less shopping around, measured by visits to price comparison websites. This could be due to consumers not fully understanding the potential benefits they could gain from shopping around.
- 4.1.9 But there is no strong rationale for regulating customer acquisition processes, particularly saves and win-backs, in order to promote greater transparency of retail pricing. Unpublished discounts are not peculiar to saves and win-backs.

Mandatory price disclosure also risks unintended consequences, such as higher average retail prices.

4.2 Recommendations

- 4.2.1 While the evidence does not indicate material market failures or regulatory problems in relation to saves and win-backs, the Authority should continue to monitor saves and win-back practices and the implications they have on prices and on consumers.
- 4.2.2 Impacts on consumers are a paramount concern. But consumer perspectives on saves and win-backs are not well understood and evidence about impacts on consumers is still unfolding. Targeted monitoring or research is still needed to clarify these things, otherwise the impact of saves and win-backs will continue to be uncertain.
- 4.2.3 In particular, the Authority should recommit to ongoing monitoring of consumers' experiences of win-back practices, including the scale and terms of discounts that are offered as part of win-backs, by including questions on these issues in consumer switching surveys.
- 4.2.4 These issues should be explored by adding questions to the Authority's biennial consumer switching survey to ask consumers if they:
- a) have been offered a win-back discount(s), the value of the discount(s), and terms and conditions of the discount(s)
 - b) have accepted a win-back discount
 - c) whether they view these discounts favourably
 - d) whether they have felt that retailers have conducted themselves reasonably when offering discounts to win them back.
- 4.2.5 The biennial survey of consumers has only recently been completed. The Authority should conduct a one-off survey of consumer experiences of win-back behaviour so that information is gathered without significant delay. This one-off survey could be an update of the one used for the Authority's 2014 enquiry into consumer switching experiences.³⁶

³⁶ <https://www.ea.govt.nz/monitoring/enquiries-reviews-and-investigations/2014/consumer-switching-experiences/>

5. Data appendix

- 5.1.1 This appendix provides results of analyses of switching data related to saves and win-backs. The data consists of customer (ICP) level consumer switching between retailers for the period 2003 to 2017.
- 5.1.2 Table 1 presents analysis of switching gains, losses and save and win-back rates by rank of market shares. The data is 2017 averages by parent company. Market shares are based on regional market share ranks (by network reporting region). For example, the second row in the table (labelled 1) shows average win-back rates for retailers that had the highest market share in a region in 2017. That is, the rate at which these retailers are winning back customers. Rates of win-backs are measured as number of switch withdrawals divided by number of initiated switches. Rows are labelled 'Losing' because the convention is that retailers that are losing customers are the ones that engage in win-backs. The row labelled "New" is the average for firms that entered a market during the year.
- 5.1.3 The columns in Table 1 represent the retailers that are losing from win-backs – those that are in the process of winning customers but fail to do so when there is a win-back. The column labelled with 2 is the average of losses due to win-backs for retailers that are ranked second in regional markets.
- 5.1.4 The data in Table 1, being based on parent company activity and market shares, includes win-backs between subsidiaries of parent companies. This can be seen in, for example, the observation that the highest ranked firms in regional markets, on average, effect win-backs on 17% (0.17) of switches initiated by their subsidiaries. These self win-back rates, in the diagonal cells, rates are only imperfect estimates of within company win-backs because they include shifts in market share rank during a year. This is why there are non-zero self win-back rates for lower ranked retailers because there are substantial changes in market shares between these retailers each year. This is not the case for the retailers with the highest rankings in terms of market share.
- 5.1.5 Count values at the bottom and right of the table are rounded to the nearest 100 and represent total number of switches initiated (the right hand column of counts) and gains, losses and net gains of customers by retailer market share rank and across the country after taking account of win-backs.
- 5.1.6 The highest ranked firms in regional markets have the second highest rates of win-backs, on average, at 0.29 or 29% of initiated switches being won-back. Win-backs by the highest ranked retailers are highest with the 2nd and 3rd ranked retailers (0.35 and 0.36, respectively, as shown in the cells in the columns labelled 2 and 3 coinciding with the row labelled 1 in the 'Losing' column).

Table 1: Rates of win-backs between retailers in 2017, ranked by market shares

Winning																Initiated	
Losing	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15		Ave
1	0.17	0.35	0.36	0.29	0.23	0.30	0.24	0.12	0.08	0.10	0.10	0.40	1.00	0.50		0.29	28,100
2	0.29	0.19	0.30	0.27	0.20	0.26	0.17	0.11	0.15	0.07	0.15	0.29	0.77	0.39	0.50	0.25	40,400
3	0.34	0.33	0.15	0.30	0.24	0.25	0.16	0.08	0.12	0.12	0.16	0.25	0.50	0.58	0.33	0.30	25,900
4	0.29	0.28	0.28	0.10	0.26	0.25	0.23	0.05	0.08	0.07	0.12	0.08	1.00	0.26		0.26	20,500
5	0.24	0.20	0.22	0.19	0.11	0.22	0.18	0.07	0.09	0.10	0.27	0.33	0.50	0.25		0.21	24,700
6	0.34	0.26	0.31	0.24	0.21	0.17	0.17	0.15	0.04	0.18	0.28	0.31	0.38	0.83		0.28	20,600
7	0.18	0.22	0.19	0.15	0.18	0.22	0.16	0.04		0.20	0.17	0.25	1.00			0.19	7,600
8	0.22	0.15	0.15	0.12	0.11	0.22	0.04	0.06	0.09	0.02	0.21	0.25				0.16	12,900
9	0.20	0.18	0.22	0.19	0.13	0.16	0.12	0.05		0.08	0.29					0.18	3,300
10	0.22	0.30	0.20	0.18	0.17	0.30	0.10	0.05	0.04	0.14	0.25		0.40	0.29		0.21	5,900
11	0.24	0.27	0.27	0.13	0.18	0.26	0.13	0.07	0.20	0.18						0.22	1,600
12	0.06	0.17	0.08	0.04	0.10	0.07	0.13				1.00					0.08	300
13	0.09	0.18		0.08	0.11											0.09	100
14	0.13	0.04	0.05	0.05												0.06	100
15	0.13	0.14	0.29	0.11		0.50		1.00								0.19	0
20				0.50												0.04	0
New	0.14	0.17	0.15	0.18	0.03	0.11	0.17									0.14	400
Average	0.28	0.26	0.27	0.24	0.20	0.25	0.16	0.08	0.08	0.09	0.16	0.23	0.50	0.40	0.13		
Gains	19,800	30,300	18,100	15,100	19,500	14,800	6,200	10,800	2,700	4,600	1,200	300	100	100	0		
Losses	-44,400	-35,900	-18,800	-16,000	-13,900	-5,600	-3,400	-3,100	-1,200	-1,200	-400	-100	0	-100	0		
Net gain	-24,600	-5,700	-800	-900	5,600	9,200	2,700	7,800	1,500	3,400	800	200	100	0	0		

- 5.1.7 Figure 12 presents monthly save and win-back rates and trends (blue lines) grouped by network areas. Each grey dot in the figure represents the monthly rate of saves and win-backs (saves and winbacks divided by initiated switches) for a retailer in that area.
- 5.1.8 Figure 13 presents the highest monthly win-back rates per year, per retailer with customers in network area. Trends are shown with blue lines and each grey dot represents the peak monthly rate of saves and win-backs (saves and winbacks divided by initiated switches) for a retailer in that area. Some retailers have 100% win-back rates, but in all cases these involve very small numbers of initiated switches.
- 5.1.9 Figure 14 and Figure 15 show the same analysis of win-back rates that is presented in Figure 12 and Figure 13 but from a different perspective. Rather than present the data by network area, these show results for retailers by rank of market share across the 46 network pricing areas (network reporting regions) in New Zealand.

Figure 12: Monthly save and win-back rates and trends grouped by network areas

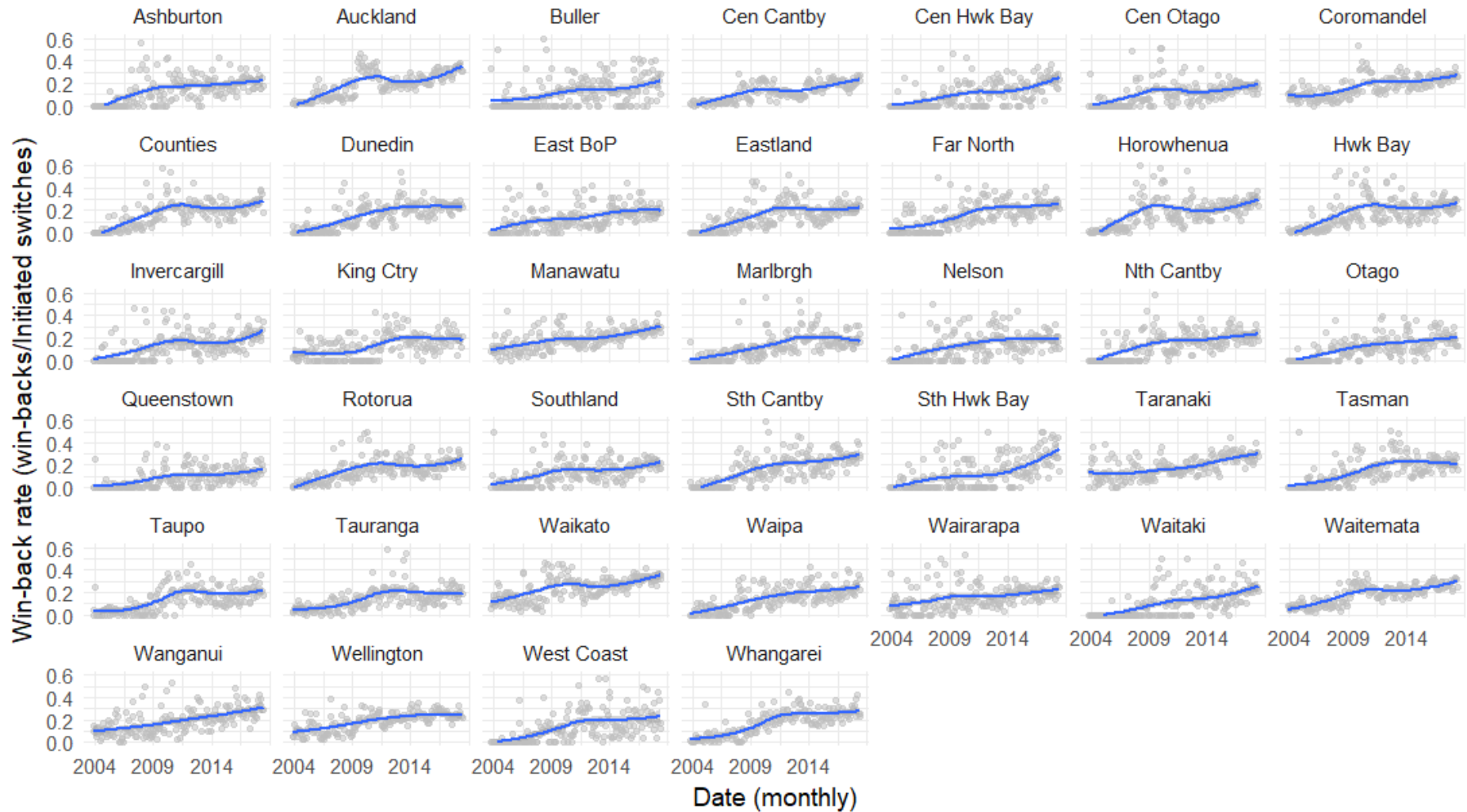


Figure 13: “Peak” save and win-back rates grouped by network areas

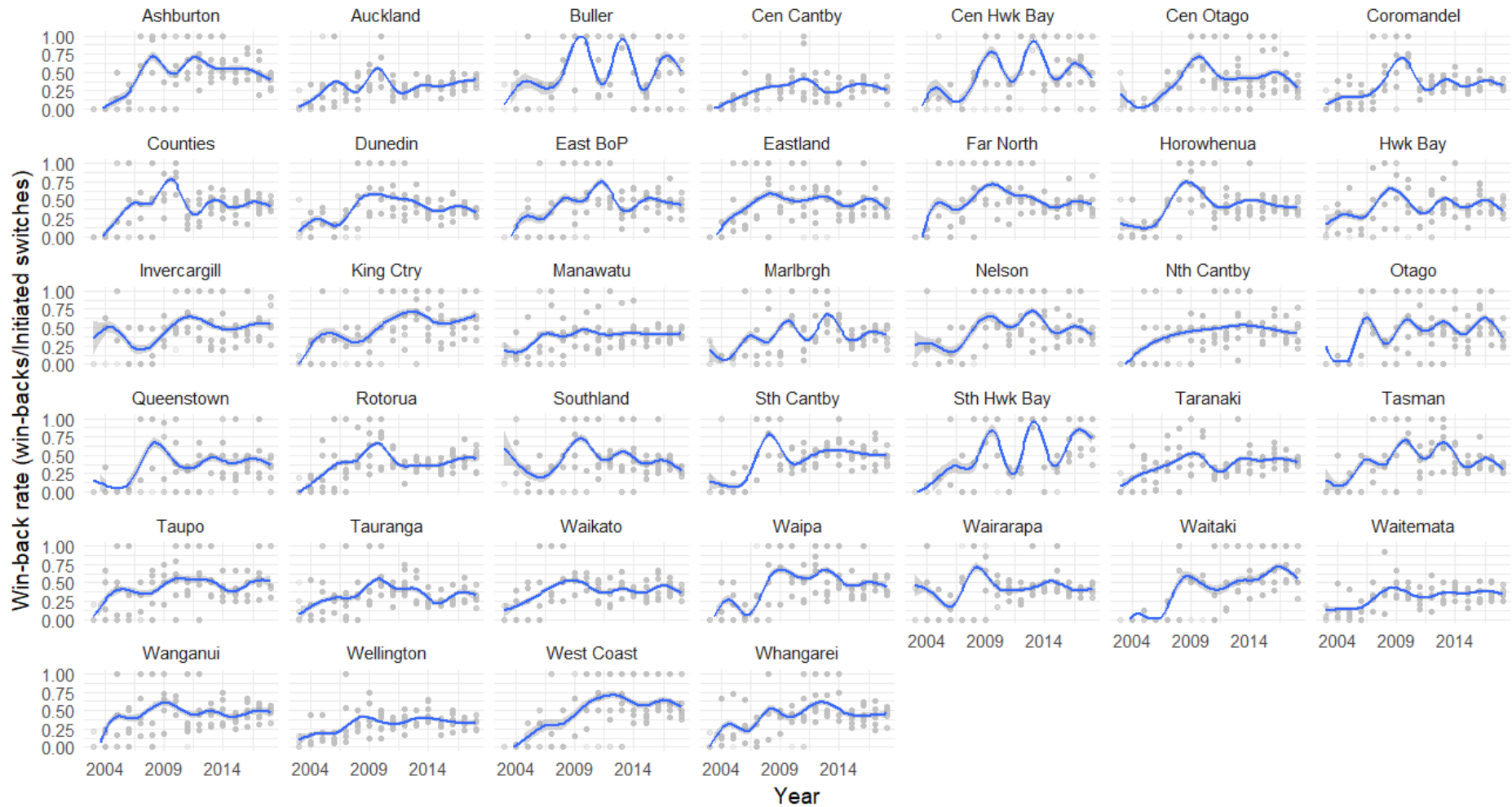


Figure 14: Monthly win-back rates and trends grouped by rank of market share

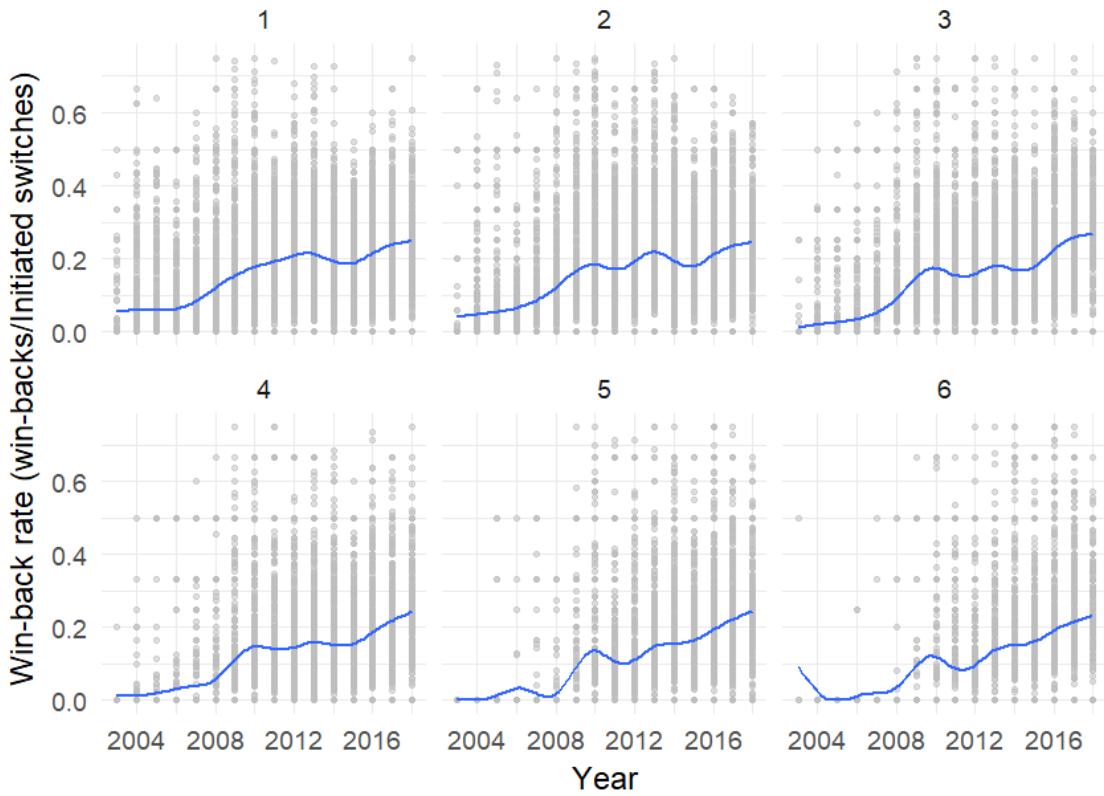


Figure 15 “Peak” win-back rates grouped by rank of market share

