

# **The Treasury**

## **Mixed Ownership Model for Crown Commercial Entities: Electricity Prices Information Release**

### **Release Document**

**8 October 2012**

**[www.treasury.govt.nz/publications/reviews-consultation/mixed-ownership/advice](http://www.treasury.govt.nz/publications/reviews-consultation/mixed-ownership/advice)**

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Information withheld is indicated by **[withheld]**.

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

## Treasury Report: Recent data on electricity prices

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<b>Date:</b>	26 September 2012	<b>Report No:</b>	T2012/2330
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### Action Sought

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	Action Sought	Deadline
Minister of Finance (Hon Bill English)	<b>Agree</b> that Treasury should proactively release this report on the Treasury website	Friday 5 October 2012
Associate Minister of Finance (Hon Steven Joyce)	<b>Note</b> contents	Friday 5 October 2012
Minister for State Owned Enterprises (Hon Tony Ryall)	<b>Agree</b> that Treasury should proactively release this report on the Treasury website	Friday 5 October 2012

### Contact for Telephone Discussion (if required)

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Name	Position	Telephone		1st Contact
Juston Anderson	Senior Analyst, Commercial Transactions Group	[withheld]	[withheld]	✓
Andrew Blazey	Manager, Commercial Transactions Group	04 917 6985	[withheld]	

### Actions for the Minister's Office Staff (if required)

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None.
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**Enclosure: No**

## Treasury Report: Recent data on electricity prices

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### Executive Summary

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On Friday 14 September the Ministry of Business, Innovation and Employment (MBIE) released its latest quarterly survey of electricity prices as at 15 August 2012. Previous releases of this survey have been used to argue that private companies charge more for electricity than SOEs.

Treasury's advice has been that this argument is based on flawed analysis of the MBIE data, which does not prove that private companies charge more than SOEs. The latest MBIE data confirms our earlier advice.

Media commentary on electricity prices using the MBIE data has been based on a national weighted average price of electricity for private companies and SOEs. In our view this is not appropriate, for a number of reasons.

No customer in New Zealand pays a weighted average price of electricity – customers choose between prices offered by the companies in their area. Underlying differences in electricity prices in regions in New Zealand due to factors such as transmission costs which are common to all retailers, along with the fact that electricity companies have their customer bases in different regions from each other, mean a national weighted average price is likely to result in misleading conclusions.

The MBIE data also excludes electronic payment discounts. When comparing prices between private companies and SOEs, a more realistic comparison would be to include all payment discounts that are available to customers, including Contact Energy's 22% "Online, Ontime" discount.

Finally, Trustpower is 33% owned by the Tauranga Energy Consumer Trust (TECT). Income received by TECT, which is primarily from its shareholding in Trustpower, is used to provide benefits to approximately 62,000 Trustpower customers in Tauranga and the Western Bay of Plenty District. This includes an estimated \$25.7 million in "Consumer Distribution Cheques" in the year to March 2013. As a result, Trustpower customers in these areas face an effective electricity price significantly lower than Trustpower's reported rates. These payments are not factored into the MBIE survey.

Given the issues above, we do not believe that a New Zealand weighted average is an appropriate way of comparing the prices of SOEs and private companies. However, given that such an approach has been used by a number of commentators, we have repeated the weighted average analysis using the latest MBIE data, but factoring in Contact Energy's 22% online payment discount.

This analysis, in the body of this report, shows that Contact, the largest privately owned company, has the lowest national weighted average price for electricity of any retailer. This is a change from the last quarterly survey – reinforcing the point that electricity pricing is dynamic and changes over time.

A regional weighted average price is a less misleading approach for comparing prices than a national average. Using the MBIE data and factoring in Contact Energy's online payment discount, the weighted average price for SOEs is higher than the weighted average for private companies in 21 out of 45 regions in the MBIE survey, including Auckland, Hamilton, Christchurch, Northland, Hawke's Bay and the Manawatu.

Collectively the largest 11 regions out of the 45 in the MBIE survey, each with more than 50,000 electricity consumers, account for just over two-thirds of the electricity customers in New Zealand. In 7 of these 11 regions SOEs charge higher prices on a weighted average basis.

It is also notable that in 7 of the 11 regions, including 3 of the 4 regions where private companies prices are higher than SOEs, the difference in weighted average price between SOEs and private companies is less than 2.5%. The other four regions are: Auckland, the largest single region, where SOEs are 6.9% higher on a weighted average basis; Northland where SOEs are 5.4% higher; Christchurch where SOEs are 3.5% higher; and Tauranga, where private companies are 19.6% higher, but which as discussed above is a special case.

A different measure would be to look at whether private companies or SOEs are offering the lowest price in each region. On this basis, using the MBIE data:

- a private company is offering the cheapest price in 29 out of 45 regions (64%), and
- a private company is offering either the cheapest price or the second cheapest price in 35 regions (78%).

Given that there are 5 privately owned brands and 7 SOE and SOE subsidiary brands listed in the MBIE survey, this means that privately owned companies are over-represented in terms of retailers offering the lowest price in specific regions.

The Consumer NZ's "Powerswitch" website provides an alternative source of data that can be used to compare the prices of SOEs and privately owned companies:

- privately owned companies were offering the lowest prices in 16 out of the 21 regions reported on the Powerswitch website (76% of regions), and
- in the other 5 regions, where an SOE was offering the lowest price, a private company was offering the second-lowest price, and in most cases the private company's price was only slightly higher than the SOE's.

In our view the assertion that SOEs offer cheaper prices than private companies is not supported by the evidence. In any case in our view what matters is not ownership – it is regulation of the electricity market, and the level of competition between retailers. Analysis of the MBIE and Powerswitch data, along with data on consumer switching, both suggest a high degree of price competition between the privately owned electricity companies and the SOEs.

## **Communications**

We recommend that you refer this report to your media staff, given the ongoing interest in and commentary on electricity prices and the supposed impacts of the Government share offers.

It is possible that the release of the latest MBIE survey will result in you (or the Minister of Energy and Resources) being asked questions in Parliament again, as you were on 19 and 20 June after the last MBIE survey was released.

## Recommended Action

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We recommend that you:

- a **note** the contents of this report, and
- b **agree** that Treasury should proactively release this report on the Treasury website, given the ongoing interest in this topic in the context of the Government share offers.

Minister of Finance  
*Agree/disagree*

Minister for State Owned Enterprises  
*Agree/disagree*

Andrew Blazey  
**Manager, Commercial Transactions Group**

Hon Bill English  
**Minister of Finance**

Hon Steven Joyce  
**Associate Minister of Finance**

Hon Tony Ryall  
**Minister for State Owned Enterprises**

## Treasury Report: Recent data on electricity prices

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1. On Friday 14 September the Ministry of Business, Innovation and Employment (MBIE) released its latest quarterly survey of electricity prices, as at 15 August 2012.
2. As you will be aware, previous releases of this survey have been used to argue that private companies charge more for electricity than SOEs. Treasury's advice has been, and continues to be, that this argument is based on flawed analysis of the MBIE data, which does not prove that private companies charge more than SOEs.
3. The latest MBIE data confirms our earlier advice.
4. The MBIE survey has also been used to argue that the Government Share Offers will result in SOEs increasing their prices, to the detriment of consumers.
5. If SOEs were genuinely pricing below privately owned companies (there is no evidence from the MBIE data that they are) and if this was because of their 100% government ownership, then the MBIE data is not actually capable of proving this – at best it could show a correlation between price and ownership. We also note that the Government will retain majority ownership of the three state-owned electricity companies following the Government share offers.
6. In our view, any statements that the Government share offers will result in electricity price increases cannot be supported by the MBIE data.
7. Those using the MBIE data to assert that private companies charge more than SOEs make a number of errors in their analysis, including:

### **Calculating a national average weighted price of electricity for private companies and SOEs is not an appropriate way of comparing their prices**

8. No customer in New Zealand pays a weighted average price of electricity – neither the national weighted average, nor the weighted average in their area. Customers choose between prices offered by the companies in their area.
9. Different regions in New Zealand have different electricity prices, due to underlying factors such as transmission charges which apply equally to all electricity retailers. For example, electricity prices in rural areas and provincial towns and cities are typically higher than in the major centres (regardless of retailer) because of transmission costs.
10. Electricity companies have their customer bases in different regions from each other, and therefore are subject to different levels of transmission charges. Therefore, a weighted average comparison between privately owned companies and SOEs can easily result in misleading conclusions.
11. Trustpower, one of the two major privately owned electricity companies, has the bulk of its customer base in provincial towns and cities. Therefore its prices, on a weighted average basis, will appear higher than the prices for companies whose customer base is in the major cities.
12. This may be because Trustpower's prices are genuinely higher (which in the MBIE data they do appear to be – as discussed further below), it may just be the result of power prices naturally being higher in these areas because of factors such as transmission charges, or, as it appears to be, some combination of both factors. This means a national weighted average price will result in misleading conclusions.

13. The same applies for Tiny Mighty Power (TMP), a subsidiary of Mighty River Power – on a weighted average basis, TMP misleadingly appears to be one of the highest price retailers, even though its prices are competitive in the areas in which it operates (provincial towns and cities). Just to pick one example, in Waipa TMP serves 14% of electricity customers. TMP's prices are 10% lower than the dominant (privately owned) retailer in the region, and lower than the prices offered by SOEs Meridian and Mercury. Contact Energy offers the lowest prices in Waipa (lower than TMP). On a national weighted average basis, the fact that TMP's prices are competitive is not apparent.
14. A more meaningful comparison is to look at the prices actually charged by electricity companies within each area. Below, we carry out this analysis, using both the MBIE quarterly survey and the Consumer Institute's "Powerswitch" website.

### **The MBIE survey makes a number of assumptions**

15. The most important assumption in the MBIE survey is that it excludes electronic payment discounts. When comparing prices between private companies and SOEs, a more realistic comparison would be to include all payment discounts that are available to customers. For example, Contact Energy offers a 22% discount for customers who pay their bills on time and electronically (compared to a 10% discount for prompt payment by non-electronic means). Because the MBIE survey excludes this discount, Contact's prices appear to be around 12% higher than the prices that are actually available to consumers.
16. The Consumer Institute "Powerswitch" website does take account of all electronic payment discounts available to customers, including Contact Energy's.

### **Trustpower**

17. Trustpower is 33% owned by the Tauranga Energy Consumer Trust (TECT). Income received by TECT, which is primarily from its shareholding in Trustpower, is used to provide benefits to approximately 62,000 Trustpower customers in Tauranga and the Western Bay of Plenty District. These benefits included an estimated \$25.7 million in "Consumer Distribution Cheques" in the year to March 2013, with the TECT website reporting<sup>1</sup> a minimum payment to customers of \$385 in 2012.
18. As a result of these payments, Trustpower customers in these areas face an effective electricity price significantly lower than Trustpower's reported rates (since they lose the TECT payments if they switch to another electricity retailer). Because the amount of these TECT payments to individuals is not transparent, they are not factored into the MBIE survey or the "Powerswitch" website.
19. The MBIE survey reports Trustpower as charging an average electricity consumer in Tauranga a rate of \$2,499 a year. This appears to be significantly higher than the lowest price available in the region from other retailers of \$2,031 a year. However once the minimum TECT rebate is factored in, the Trustpower price in Tauranga becomes significantly more competitive.

### **Taking account of the Contact online discount**

20. As discussed above, we do not believe that a New Zealand weighted average is an appropriate way of comparing the prices of SOEs and private companies. However, given that such an approach has been used by a number of commentators, we have repeated the analysis using the latest MBIE data.

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<sup>1</sup> [http://www.tect.org.nz/what\\_does\\_tect\\_do](http://www.tect.org.nz/what_does_tect_do)

21. If a weighted average is calculated, then it should include the impact of Contact's online payment discount. Once Contact's discount is factored in, the weighted average prices for each of the retailers are:

<b>Retailer</b>	<b>Weighted average price (\$/year)</b>	<b>Number of customers</b>	<b>Ownership</b>
Trustpower	2,412.81	208,109	Private
Pulse	2,349.25	19,797	Private
Mercury	2,178.67	368,074	SOE
Nova (including Bay of Plenty Energy)	2,177.25	56,650	Private
Tiny Mighty Power	2,175.76	10,529	SOE
King Country Energy	2,160.32	17,460	Private
Genesis	2,097.09	467,780	SOE
Meridian	2,057.10	242,391	SOE
Powershop	2,045.59	48,539	SOE
Energy Online	2,041.03	64,292	SOE
Contact	2,040.15	459,067	Private

22. The table shows:

- Contact, the largest privately owned company, has the lowest weighted average price of any electricity retailer,
- Trustpower, Pulse, Nova and Tiny Mighty Power, who target primarily rural and provincial centres, have some of the higher national weighted average prices – which at least to some extent is due to underlying factors such as higher lines charges, and
- Trustpower is clearly an outlier, with weighted average prices significantly higher than any of the other large retailers.

23. As discussed above, Trustpower's supposedly higher prices in the MBIE survey are potentially misleading, because of TECT distributions available to Trustpower customers in Tauranga and the Western Bay of Plenty.

### **A more meaningful analysis – region by region**

24. We do not believe a weighted average price is an appropriate way of comparing the prices of SOEs and private companies. What matters for customers is the actual prices on offer, not weighted averages.
25. However, if a weighted average is used, a less misleading approach (but still not ideal) is to calculate an average in specific regions, not across New Zealand as a whole. This approach deals with the fact that lines company charges are different in each region.
26. The MBIE quarterly survey examines power prices in 45 lines company regions across New Zealand, and records 12 different electricity retail brands: 5 privately owned (42%) and 7 SOEs and SOE subsidiaries (58%)
27. In 21 out of the 45 regions in the MBIE survey (47%), the weighted average price for private companies is cheaper than the weighted average price for SOEs:
- Auckland (Vector),
  - Hamilton (WEL Networks),
  - Christchurch (Orion),
  - Top Energy (Northland),
  - Northpower (Northland),
  - Waitemata,
  - Waitomo,

- King Country,
- Eastland,
- Hawke's Bay,
- Centralines (Central Hawke's Bay),
- Scanpower (Northern Tararua / Southern Hawkes Bay),
- Wairarapa,
- New Plymouth,
- Hawera,
- Manawatu,
- Electralines (Kapiti and Horowhenua),
- Mainpower (North Canterbury and Kaikoura),
- Kaiapoi,
- Timaru (Alpine Energy), and
- Network Waitaki.

28. Looking at weighted average prices in regions with greater than 50,000 customers:

Region	Number of customers	Weighted average comparison
Northland (Top Energy, Northpower)	84,600	SOEs 5.4% higher
Waitemata	209,700	SOEs 2.0% higher
Auckland (Vector)	321,700	SOEs 6.9% higher
Thames Valley	61,300	Private companies 0.3% higher
Hamilton (WEL networks)	84,900	SOEs 4.7% higher
Tauranga	82,200	Private companies 19.6% higher
Hawke's Bay	61,400	SOEs 1.8% higher
Manawatu	52,100	SOEs 0.1% higher
Wellington (North and South)	165,500	Private companies 1.1% higher
Christchurch (Orion)	184,900	SOEs 3.5% higher
Dunedin	53,900	Private companies 0.1% higher

29. Collectively, these 11 regions account for just over two-thirds of the electricity customers in New Zealand. In 7 of the 11, SOEs charge higher prices on a weighted average basis; in 4 regions, private companies weighted average price is higher (in two of the four, by less than 0.3%, and three of the four by less than 1.1%).
30. The fourth region where private companies are higher, Tauranga, demonstrates the points made earlier. Trustpower has 71% of the customers in Tauranga, and (according to the MBIE data) charges by far the highest electricity prices of any company in the region – meaning the weighted average price for private companies is 19.6% higher than the weighted average for SOEs. However the impact of TECT rebates only available to Trustpower customers means that their incentive to switch to a different retailer is significantly reduced.

### Lowest and second-lowest prices in a region

31. In our view, if the concern was that private companies might be charging more than SOEs, a better measure would be to look at whether private companies or SOEs are offering the lowest price in each region. If there is a private company offering the lowest price in a region, then the fact that the weighted average price for private companies is higher than the weighted average for SOEs should not be a concern – customers are able to switch to the cheaper private company if they wish to do so.
32. Of the 45 regions in the MBIE survey:
- a private company is offering the cheapest price in 29 regions (64%) and an SOE in 21 regions (36%). Given the number of privately owned retail brands, this means that privately owned companies are over-represented, and

- a private company is offering either the cheapest price or the second cheapest price in 35 regions (78%).
33. It is also notable that despite its high national weighted average price, Trustpower is offering the lowest prices of any retailer in Waitomo, King Country and Network Waitaki – regions where Trustpower customers do not receive TECT distributions.

### **Powerswitch**

34. The independent “Powerswitch” website provides an alternative source of data that can be used to compare the prices of SOEs and privately owned companies. Powerswitch is run by Consumer NZ with support from the Ministry of Consumer Affairs.
35. Powerswitch is updated more regularly than MBIE’s quarterly survey, and it uses slightly different assumptions (including taking account of online payment discounts). It is not possible to calculate national or regional weighted average prices using the Powerswitch data. As at Monday 17 September Powerswitch shows that:
- privately owned companies were offering the lowest prices in 16 out of the 21 regions reported on the Powerswitch website
  - in the other 5 regions, where an SOE was offering the lowest price, a private company was offering the second-lowest price, and in most cases the private company’s price was only slightly higher than the lowest priced SOE’s.

### **Consumer switching**

36. The Electricity Authority’s (EA’s) data on consumer switching shows further evidence that the electricity market in New Zealand is competitive. Over the last 12 months, around 33,000 electricity customers switched electricity retailers each month.
37. A recent global study ranked New Zealand number two in the world when it comes to customer switching in the electricity market<sup>2</sup>.
38. It is also notable that despite having the third highest national average price in the MBIE survey, Mercury Energy has gained customers in each of the last 5 months, according to Electricity Authority data, and had the largest gain in customer numbers of any electricity retailer over that period. Meridian Energy, despite having the fourth lowest national average price, has lost customers for each of the last 6 months. This further indicates that national weighted average prices are not a robust measure of the competitiveness of electricity retailers.

### **Conclusion**

39. In our view the assertion that SOEs offer cheaper prices than private companies is not supported by the evidence. In any case what matters is not ownership – it is regulation of the electricity market, and the level of competition between retailers. Analysis of the MBIE and Powerswitch data, along with data on consumer switching, both suggest a high degree of price competition between electricity retailers (both privately owned and the SOEs).

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<sup>2</sup> <http://www.ea.govt.nz/document/17218/download/consumer/csf/>