19 June 2023

Anna Collyer
Chair
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Submitted online at: www.aemc.gov.au

Dear Ms Collyer

Amendment of the Market Price Cap, Cumulative Price Threshold and Administered Price Cap – Consultation Paper

Origin Energy Limited (Origin) welcomes the opportunity to provide comments on the Amendment of the Market Price Cap (MPC), Cumulative Price Threshold (CPT) and Administered Price Cap (APC) Consultation paper. Our views on the merits of the proposed changes are provided below.

1. Market price cap and cumulative price threshold

Origin considers there is a need to improve investment signals for the flexible dispatchable resources required to support growth in Variable Renewable Energy (VRE), consistent with the intent of the Reliability Panel's (the Panel's) proposed changes.

We agree it is prudent to consider the interaction of the changes to market settings with other mechanisms that are being progressed to support reliability, like the Commonwealth's Capacity Investment Scheme (CIS), noting the Panel was not able to explore this matter due to its overarching terms of reference. However, we do not consider the implementation of these schemes obviates the need for the Panel's proposed change, as the market settings should continue to play a prominent role in supporting investment and incentivising the availability of energy and reserves in operational timeframes.

The MPC and CPT continue to play an important role in promoting market efficiency

The MPC and CPT typically inform the maximum exposure that a retailer or market customer could face under extreme market conditions, with higher market settings inherently incentivising a more prudent approach to hedging. These parameters have therefore been crucial in facilitating the development of a robust financial contracts market that assists retailers with efficiently managing price risk on behalf of customers.

The combination of scarcity price signals and contracting also provides strong incentives for generators (and demand side participants) to be available when they are most needed, including in response to both ramping and high demand events. Specifically, generators and demand response are incentivised to operate / reduce load respectively to support their contracted position when prices are high, with uncontracted plant also motivated to supply into the market at these periods. As storage begins to play a greater role in the National Electricity Market (NEM) in the future, these parameters may also become increasingly more important in signalling the need for energy-limited resources to reserve capacity for low-probability events.

Further, energy-only price signals are crucial in signalling / valuing the type and level of capacity required by the system, with changes in the MPC and CPT impacting the revenue potential of new resources. A key objective of moving to five minute settlement was to provide more granular and efficient energy price signals to improve incentives for investment in flexible resources as the penetration of VRE increases over time. If growth in VRE changes the frequency and / or magnitude of pricing events in the NEM as expected, spot and contract market signals should increasingly value the ability of plant to respond to such events.

Mechanisms like the Capacity Investment Scheme should act to complement the energy only market design, but not subsume it

A key consideration for the AEMC will be how the market price settings interact with reliability mechanisms like the New South Wales Electricity Infrastructure Roadmap and CIS. Ideally, these mechanisms should act to supplement the NEM's current design to help facilitate timely levels of new entry; and potentially preclude the need for substantial increases in the MPC that may materially increase the risk profile for retailers / market customers and be unacceptable for governments / policy makers, noting the MPC has historically been held well below the Australian Energy Regulator's estimated value of customer reliability (VCR).

Where this is achieved, the key attributes of the existing framework (described above) will be retained, whereby market participants continue to primarily rely on energy-only market signals to drive investment in new capacity, and bear any associated risks of doing so.

Implementing the panel's recommendations regarding the MPC and CPT is consistent with such an approach and generally prudent when considering the below factors.

- The NEM will face considerable challenges and uncertainty as the market transitions to higher levels of VRE. Ensuring market frameworks can facilitate the required level of investment will therefore be crucial to supporting an efficient and least cost transition. Given there is still uncertainty around the overall design, scope and development of the CIS, it would generally seem prudent to adopt the Panel's proposed recommendations, which it considers are the minimum changes required to support investment needs and by extension reliability of supply, while also limiting end-user bill impacts.[1]

- As currently proposed, gas-fired generation does not meet the eligibility requirements under the CIS. Gas-fired generation is expected to play an important role in supporting the generation mix out to 2050, as evidenced in the Australian Energy Market Operator's (AEMO) 2022 Integrated System Plan[2]. Ensuring market settings can facilitate investment in that type of plant will therefore be important. In this respect, we note the settings proposed were set at the minimum level necessary to support marginal new entrant Open Cycle Gas Turbines (OCGT) in NSW.

- The proposed settings may be lower than theoretically optimal for most jurisdictions and technologies, with the Panel's modelling indicating an MPC in the order of $35,000/MWh would be required to support investment in 4-hour storage in Victoria. Limiting the proposed increase in the MPC to $21,500/MWh appropriately balances the need to maintain strong scarcity pricing signals while minimising market participant / customer risk, with the balance of any remaining revenue gap for new plant to be resolved by other mechanisms like the CIS.

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[1] AEMC Reliability Panel, '2022 Review of the Reliability Standard and Settings – Final Report', 1 September 2022, pg. 61.

[2] 10GW of gas-fired generation for peak loads and firming will be required in the NEM by 2050. AEMO, '2022 Integrated System Plan', pg. 11.

Importantly, such an approach is not expected to provide dispatchable resources with additional revenue over and above what they would expect to earn in the absence of the proposed changes to the market settings. Rather, revenue provided through the energy market should theoretically reduce the reliance on revenue from those schemes.

2. Administered price cap

We recommend retaining the current APC value of $600/MWh. There is an asymmetric risk profile where a higher APC does not materially increase participant risk but could be important in ensuring the market clears. Retaining the current setting would likely better meet the objective of incentivising sufficient supply during an Administered Pricing Period and by extension, minimising the need for AEMO to direct participants, while also helping to insulate market customers from extreme and prolonged periods of volatility. Noting the market dynamics of the NEM with significant penetration of storage capacity are uncertain, especially in a stressed system where the APC might apply, the current setting would provide greater opportunity for arbitrage during APP periods.

If you wish to discuss any aspect of this submission further, please contact Ben Hayward on 03 9067 3403.

Yours Sincerely,

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