

AEMC 2014 ELECTRICITY PRICE TRENDS REPORT

THIS REPORT LOOKS AT THE FACTORS DRIVING RESIDENTIAL ELECTRICITY PRICES OVER THE NEXT THREE YEARS TO 30 JUNE 2017

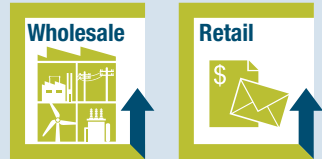
Western Australian electricity prices are set by the State Government and have decreased by 4.1% in 2014/15, but are expected to increase by 7% per year in 2015/16 and 2016/17

WHAT ARE THE COMPONENTS THAT MAKE UP A TYPICAL WESTERN AUSTRALIAN ELECTRICITY BILL?



Wholesale and retail

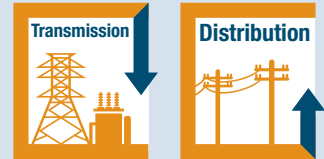
Wholesale and retail costs are increasing at slightly above inflation



- On average, wholesale costs are expected to increase by 2.9% per year and retail costs by 2.8% per year to 2016/17
- These costs may be impacted by reforms resulting from the WA Government's Electricity Market Review
- Residential prices are currently subsidised by the government and would need to increase by around 30% to reflect the cost of supply

Regulated networks

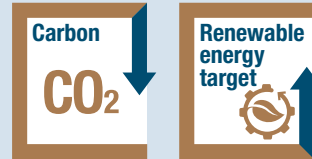
Pressure on the cost of poles and wires is increasing



- Regulated network prices are expected to rise, on average, by 5.8% per year to 2016/17
- Distribution network costs are increasing due to growth in the size of the WA network, greater consumer numbers and increasing labour costs
- Energy sales have recently been lower than expected, meaning that prices are rising in order to recover previously approved network revenue

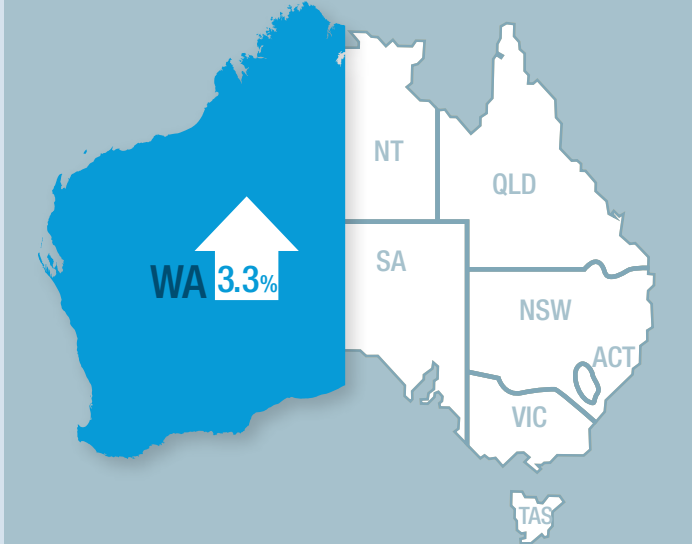
Environmental policies

The cost of the Renewable Energy Target continues to impact prices



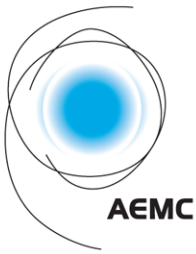
- Prices in Western Australia are lower in 2014/15 due to the removal of the carbon price. However the fall is partially offset by increases in other costs
- Costs associated with the Renewable Energy Target are expected to rise, on average, by 4.8% per year

WHAT WILL EXPECTED AVERAGE ANNUAL PRICE TRENDS BE BETWEEN JULY 2014-17?



EXPECTED PRICE TRENDS IN WA





Report on Western Australian electricity price trends released

The Australian Energy Market Commission (AEMC) today released its 2014 Electricity Price Trends report, which shows residential prices are expected to increase in Western Australia to 2016/17.

The report analyses trends in the wholesale and retail sectors of the electricity industry; the regulated networks sector; and resulting from government environmental policies. The factors driving each of the three are different, so understanding price trends involves looking into each individually.

“The cost of supplying electricity in Western Australia has fallen by 4.1 per cent in 2014/15 following removal of the carbon price, and is expected to increase by 7 per cent each year in 2015/16 and 2016/17,” AEMC Chairman John Mr Pierce said.

Mr Pierce said total electricity costs are mainly being driven by the cost of expanding the electricity network in Western Australia, but prices are ultimately determined by the Western Australian Government.

Residential electricity prices are subsidised by the Western Australian Government, meaning the price paid by residential customers is lower than the cost of supplying them with electricity.

The trends identified in this report indicate a move towards greater cost reflectivity, however it is estimated that residential prices would have to increase by around 30 per cent for the price to reflect the full cost of supply.

Mr Pierce said the main factors affecting the cost of supplying electricity in Western Australia were increases in network prices, as well as wholesale and retail costs.

“The cost of poles and wires is set to increase by an average annual 5.8 per cent in Western Australia to 2016/17, mainly due to growth in the size of the network.”

Wholesale and retail costs are expected to rise at slightly above inflation – around 2.9 per cent – although these costs may be impacted by reforms resulting from the Western Australian Government’s electricity market review.

Mr Pierce said the removal of the carbon price has reduced electricity prices in 2014/15, however other environmental policies like the Renewable Energy Target continue to impact prices.

“Costs associated with the Renewable Energy Target are expected to rise by an annual average 4.8 per cent to 2016/17 in Western Australia.”

The annual Residential Electricity Price Trends report is part of the AEMC's work to strengthen consumer engagement in energy markets.

The full report and further information is available at www.aemc.gov.au.

About the AEMC

We are the independent body responsible since 2005 for providing advice to Australian governments on development of the electricity and gas sector. We make statutory energy market rules which are applied and enforced by the Australian Energy Regulator (AER).

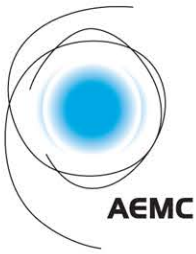
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EMBARGOED 1pm AEDT, 11 December 2014

**The AEMC's
2014 price
trends report
shows Western
Australian
electricity
costs are being
driven mainly
by network
expansion**



Western Australia: Household electricity price trends

Residential electricity prices in Western Australia expected to rise over the next two years

The 2014 Residential Electricity Price Trends report identifies factors driving electricity prices over the three years to 2016/17 in all states and territories. By providing this information at the request of the COAG Energy Council, the AEMC is seeking to strengthen consumer engagement in the market.

The Residential Electricity Price Trends report presents expected movements in prices for a representative consumer in Western Australia, with an annual consumption level that was provided to us by the Western Australian Government.

- The annual consumption of the representative consumer in Western Australia is assumed to be 5,747 kWh.
- The average prices reported are specific to the representative consumer and may not reflect the pricing outcomes for all residential consumers.

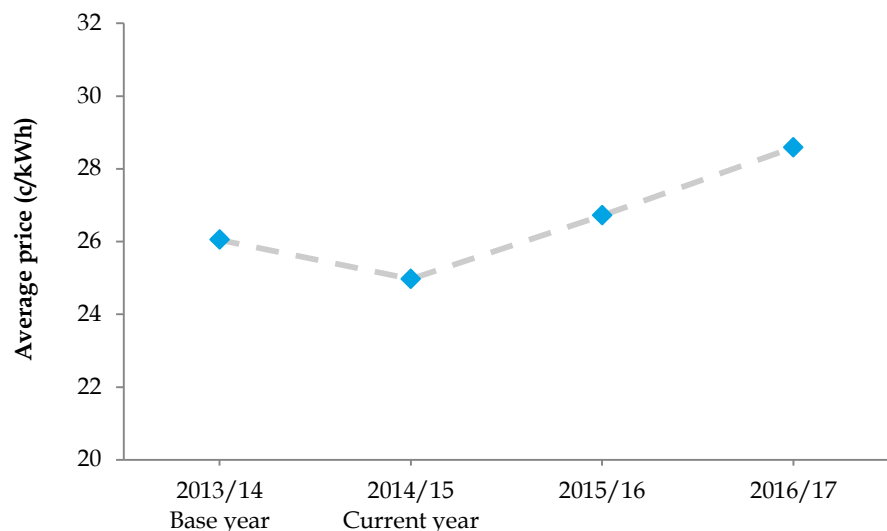
To undertake this work, we analysed trends in the competitive market sector of the industry, the regulated networks sector and the impact of government environmental policies. We report on how these trends affect overall prices paid by residential consumers, in order to identify the relative contribution to the price movements of these drivers.

Key findings for Western Australia

Residential electricity prices for the representative consumer in Western Australia have decreased by 4.1 per cent in 2014/15 and are expected to increase by 7 per cent per year in 2015/16 and 2016/17, as shown below. This is equivalent to an annual average increase of 3.3 per cent over the reporting period.

The 7 per cent increases in 2015/16 and 2016/17 are budget assumptions only and the Western Australian Government will make price decisions closer to when the prices are to apply. As prices are set by the government, the retail prices paid by consumers do not necessarily reflect underlying costs, nor follow expected cost trends.

Trend in Western Australian residential price



Residential electricity prices are set by the government and do not reflect underlying costs

Residential electricity prices are currently subsidised by the Western Australian Government, meaning that the price paid by residential consumers is lower than the cost of supplying them with electricity. For 2013/14, we calculate that the residential price would need to increase by 30 per cent to reflect the total estimated cost of supply in Western Australia.

Drivers of cost trends

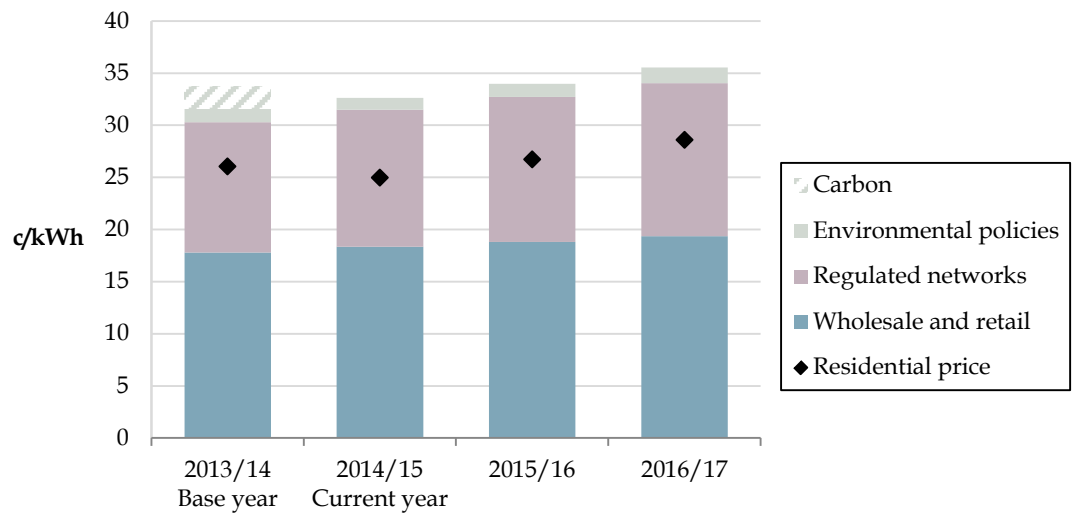
Residential electricity prices in Western Australia are forecast to increase during the period to 30 June 2017.

The drivers for cost movements during this period are the repeal of the carbon pricing mechanism, and expected increases in distribution network prices and wholesale energy purchase costs.

Although the carbon price made up 8.3 per cent of the total residential price in 2013/14, the saving in 2014/15 from the repeal of this policy is partially offset by a legislated increase of 4.5 per cent in the regulated price.

In 2014/15, it is expected that the total cost of supply in Western Australia will consist of around 40 per cent regulated network costs, 56 per cent wholesale and retail costs and 4 per cent environmental policy costs, as shown below.

Trend in Western Australian supply chain components



Regulated network prices

Regulated network prices consist of the costs of the transmission and distribution networks.

- In 2014/15, it is expected that transmission network prices will make up around 6 per cent of the total cost of supply and distribution network prices will make up 34 per cent.
- Regulated network prices are expected to increase at an average annual rate of 5.8 per cent between 2013/14 and 2016/17.

These price movements are based on the current regulatory determination, which covers the entire duration of our reporting period.

In recent years, energy sales have been lower than forecast at the time of the regulatory decision. As the network business is regulated under a revenue cap, when energy sales are lower than forecast, the amount of revenue that is recovered per unit of energy must increase for the total amount of approved revenue to be recovered.

Transmission network

Transmission network costs are expected to decrease at an average annual rate of 6.1 per cent between 2013/14 and 2016/17.

- Transmission costs in the current regulatory period (2012-17) are much lower than in the previous regulatory period, primarily due to a reduction in the rate of return on capital.

Distribution network

Distribution network costs are expected to increase at an average annual rate of 8 per cent between 2013/14 and 2016/17.

- Operational expenditure is increasing due to growth in the size of the network, greater consumer numbers and increasing labour costs.

Wholesale and retail costs

Wholesale and retail costs consist of the wholesale energy component and the costs associated with retailing electricity to residential consumers.

- Over the period to 2016/17, wholesale energy costs are expected to increase, on average, by 2.9 per cent per year.
- Retail costs increase at an average annual rate of 2.8 per cent per year, based on information published by the Western Australian Economic Regulation Authority.

The trend in wholesale energy costs is an output of long-run marginal cost modelling and is not based on how existing market participants may operate in the future. In practice, these costs will be influenced by the market design, industry structure and fuel costs.

Western Australia's retail sector is not competitive because the government-owned utility, Synergy, is the only retailer for residential consumers. However, Synergy provides several different offers and consumers may find that one of the other offers is better suited to their individual circumstances.

Environmental policy costs

Environmental policies that apply in Western Australia during our reporting period are the:

- carbon pricing mechanism; and
- Renewable Energy Target.

Costs associated with the carbon pricing mechanism apply only in the base year of our reporting period (2013/14) as the policy has been repealed with effect from 1 July 2014.

- In 2013/14, these costs made up around 8.3 per cent of the total bill of a representative consumer.

In 2013/14, Renewable Energy Target costs made up around 3.9 per cent of the total cost of supply, of which 2 per cent was associated with the Small-scale Renewable Energy Scheme (SRES) and 1.9 per cent with the Large-scale Renewable Energy Target (LRET).

- Based on the current Renewable Energy Target legislation, there is expected to be an average annual decrease of 11 per cent in the Small-scale costs, and an average annual increase of 21 per cent in the Large-scale costs.

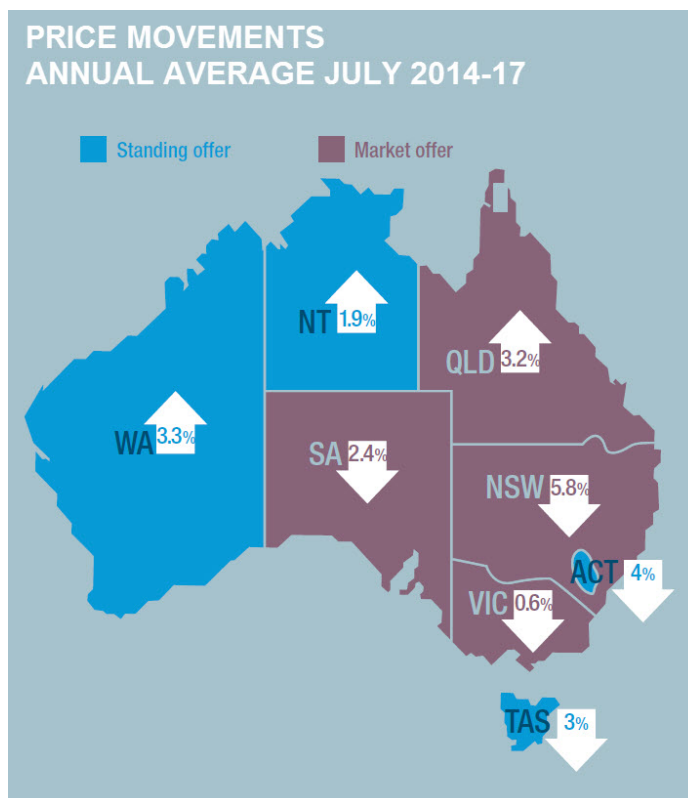
Jurisdictional price trends

Trends in residential electricity prices differ between Australian states and territories. In most jurisdictions, prices are expected to have fallen in 2014/15 following the removal of the carbon pricing mechanism. The extent of this decrease varies between jurisdictions, as the savings are offset by other factors. In 2015/16 to 2016/17, price movements are mixed, reflecting different jurisdictional drivers.

On average across the three year period from 2013/14 to 2016/17, prices are relatively stable or decreasing in most jurisdictions. The exceptions to this trend are Western Australia, Queensland and the Northern Territory, where prices are expected to increase, on average, during the period.

Our analysis of trends in *market offers* covers Queensland, New South Wales, Victoria and South Australia. In other jurisdictions, our analysis is based on trends in the regulated *standing offer* price. In jurisdictions where both *standing* and *market offers* are available, residential consumers are able to shop around for the best offer from retailers.

Price drivers vary between states and territories, although there are some common underlying trends



Information sources

Information for this report has been sourced from jurisdictional governments and regulators. We sourced information from regulators in relation to transmission and distribution network costs and from retailers operating in the relevant states for our analysis of *market offer* prices.

The AEMC also commissioned independent modelling of wholesale energy purchase costs, carbon pricing mechanism costs and Renewable Energy Target costs. Our modelling was undertaken based on current knowledge and assumptions as well as existing legislation and is available on our website.

About the AEMC

The Australian Energy Market Commission is the independent body responsible for providing policy advice to Australian governments on the electricity and gas sector. It makes energy market rules that are applied and enforced by the Australian Energy Regulator.

The Residential Electricity Price Trends report is part of the AEMC's work to empower families, businesses and industry to participate confidently in all parts of the energy supply chain, where they desire to do so. It provides annual information to help consumers better understand the factors which drive residential electricity prices.

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