

Strategic Priorities for Energy Market Development

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OVERVIEW

National Electricity and Gas Objectives are overarching

Promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers

Major new challenges



- Tightening of demand supply balance
- Climate change
- Period of price increases
- Development of gas STTM

What are the implications for market design?

Arrive at consensus for priorities



Development of AEMC work program

INVESTMENT REQUIREMENTS

Demand/supply balance is tightening

- Investment of up to \$1.5 billion per year for next 5 years required to meet demand



Increased cost of new generation

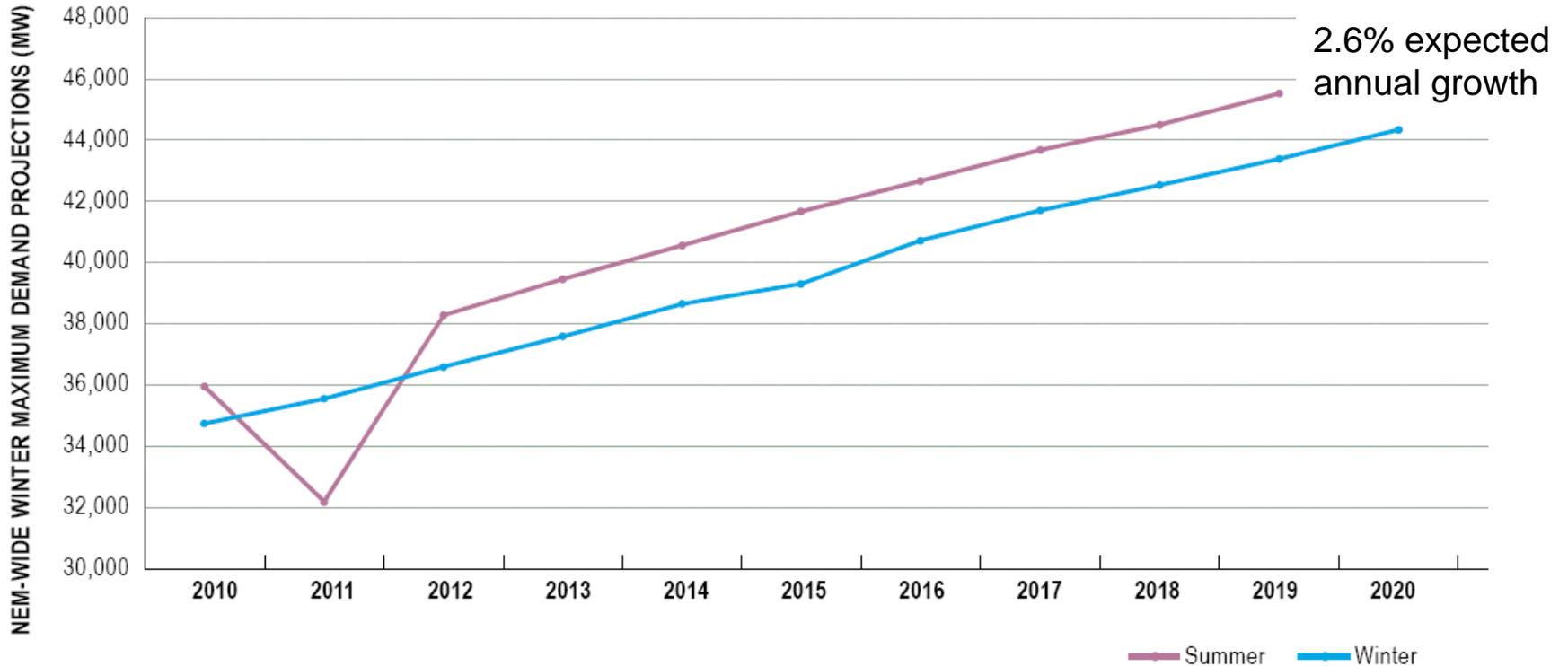
- Carbon policy uncertainty
- Increased costs of finance since GFC
 - Difficulties financing baseload generation plant



Sources of investment changing

- Dominance of the gentailer
- Few projects being undertaken by independent generators
- Reduced role of Government

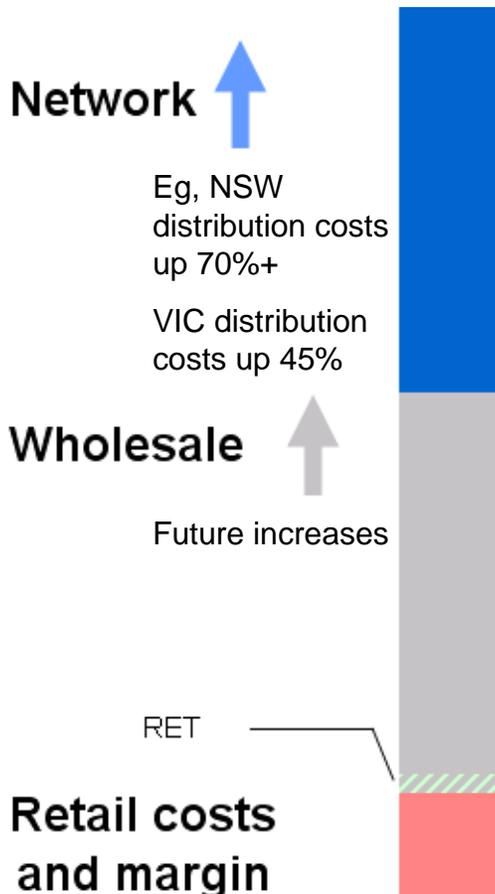
GROWTH IN PEAK DEMAND



- 70% of consumption from commercial sector
 - Driven by strong economic growth

RISING PRICES

30% price increases over past 3 years



CURRENT NETWORK DETERMINATIONS

- Replacement of aging assets
- Increased peak demand (strong economy, air conditioning)
- Higher reliability standards (determined by States)
- Higher return on capital following the GFC

FUTURE INCREASES EXPECTED

- Impact of carbon price (80% of generation capacity from coal fired generation)
- LNG exports may cause movement in gas prices towards export price parity
- Long term coal contracts coming to an end
- Impact of generation mix
- Expanded RET

MARKET RESILIENCE

NEM has proven to be resilient since its introduction

- Relatively few participant failures, minimal impact on customers

Resilience of **physical market** as generation mix changes

- Expanded RET will increase intermittent generation
 - Wind accounts for 20% of generation capacity in SA

Resilience of the **financial markets**

- Potential for increased price volatility
 - Increased intermittent generation
 - Peakier demand
- Higher cost of capital post GFC
- Level of transparency in OTC & exchange traded markets creates risk for market participants and policy makers

STRATEGIC PRIORITY 1

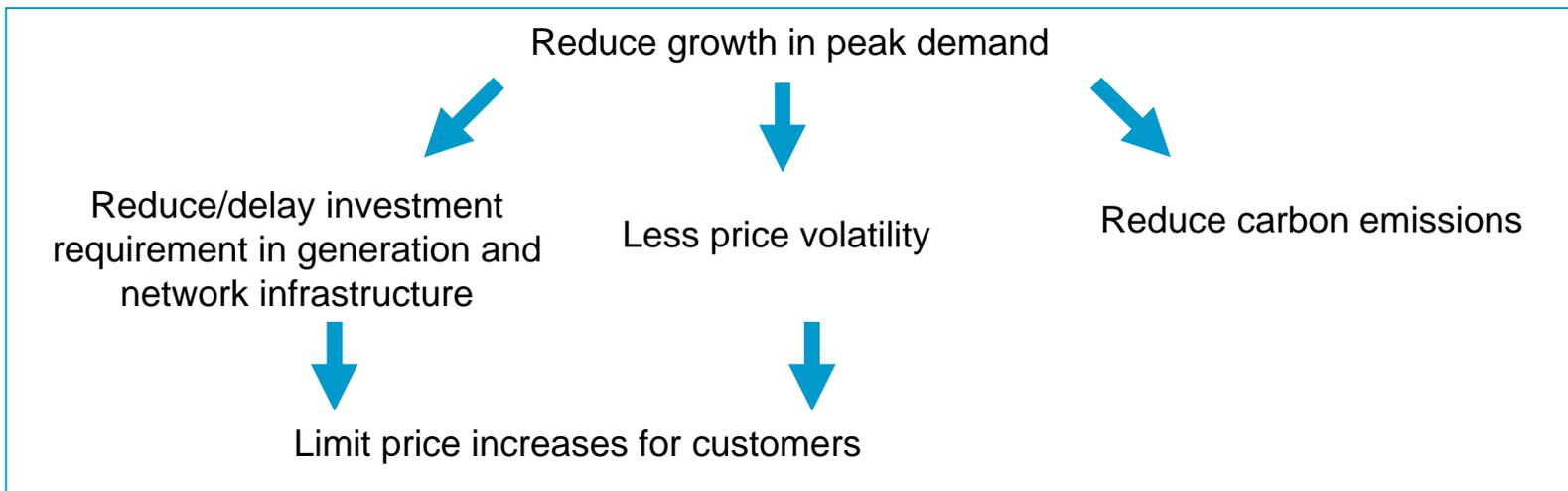
A predictable regulatory and market environment for rewarding economically efficient investment

- Generation focus
- Design of the NEM is for investment to be delivered commercially, rather than through central planning
- Barriers to investment must be minimised
 - Ensuring processes for regulatory change (Market Rules) are transparent, objective, well understood
 - Regulatory risk that cannot be bounded – typified by carbon and energy efficiency policy challenges
- The AEMC can work with Government to advise on policy settings that will minimise market distortions and costs for customers
 - Reviews on retail competition for recommendations on the removal of price caps

STRATEGIC PRIORITY 2

Building the capability of and capturing the value of flexible demand

- **Cost effective** demand shifts/reduction as an alternative to additional network infrastructure development and peaking generation
 - DSP3 Review
 - Energy efficiency
 - Role of Smart Meters



STRATEGIC PRIORITY 3

Ensuring the transmission framework delivers efficient and timely objectives

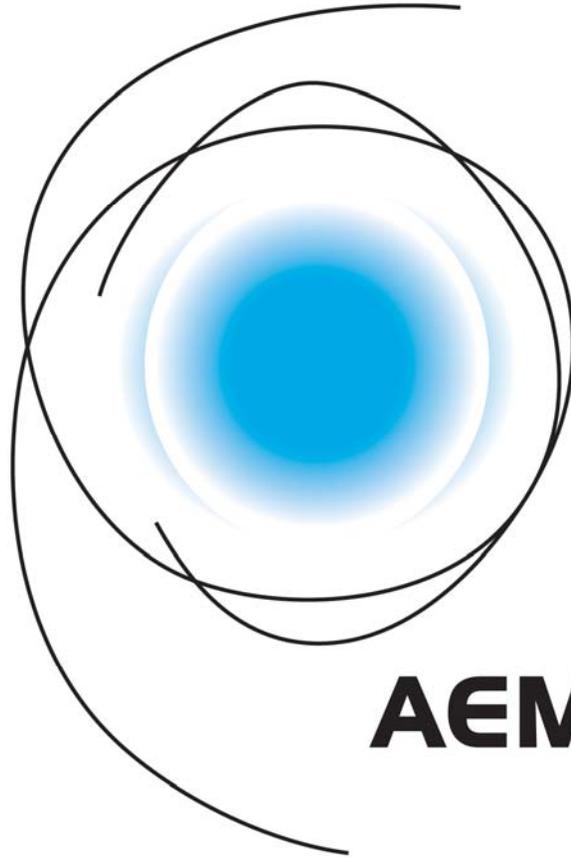
- To meet the 20% RET target by 2020 and other carbon policies, substantial quantities of new generation plant will need to be connected to the transmission network
 - Changes in the mix of generation
 - Maintaining supply demand balance with substantial increase in intermittent generation
- Monopoly network businesses need the right incentives to meet the needs of users and generators and minimise costs
 - Economic regulation
 - AEMC review of transmission frameworks
 - Scale Efficient Network Extensions (SENES) Rule change

NEXT STEPS

- **Development of priorities needs to be a collaborative process**
 - **Government**
 - **MCE**
 - **AER**
 - **AEMO**
 - **Market participants**
- Stakeholder feedback on proposed priorities
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- Views on robustness of the NEM?
- AEMC to finalise and feed into priorities for our work programme
- MCE and State Governments play an important role in setting the policy framework and part of the work program of the AEMC
 - Regular review of priorities to continue

Finalising our strategic priorities

- Comments on our paper due by Friday 13 May
- We will review our proposed strategic priorities in the light of the comments
- Publish a further document summarising the comments and our final strategic priorities
- This paper will also be submitted to the MCE as a basis for continuing discussions about the focus of our future work programme
- We will review and update the strategic priorities next year



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