

Major Energy Users' Council response to Ofwat's:

Consultation on the review of non-household retail price controls

30 November 2015

Introduction

- The Major Energy Users' Council (MEUC) is a membership organisation for large energy and water consumers. Our members account for over 25% of industrial and commercial energy demand. Alongside providing regular market intelligence and on-demand support to members, we work to represent their interests to policy makers and other energy and water sector stakeholders.
- The MEUC regularly convenes a Water Competition Action Group, which is open to all our members. The group works to ensure large customers are informed on and engaged in the development of the retail water market. In addition, this year the MEUC established a Water Market Policy Group (WMPG), which brings together business customers, suppliers and expert parties to speak with a united voice on issues of common interest concerning the opening of the non household retail market. Its objective is to influence policy. Members of the WMPG Steering Group include Bernard Matthews, Enterprise Inns, Business Stream, Anglian Water Business, Gemserv and Waterscan.
- In responding to this consultation, the MEUC acknowledges that the precise mechanisms of the retail price controls are not our specialism. However, we are here to represent the customer voice and as such we view this consultation as an opportunity to raise our concerns around non household retail margins.
- **We have serious concerns that unless the margins are widened from the outset, we will not end up with a competitive market that truly benefits customers. Customers have expectations of what the market will deliver – including savings, improved service, more choice and the ability for multi-site customers to switch to one supplier. If the margins remain at an average of only 6%, we don't believe it will be possible for these expectations to be delivered. Consequently, we believe many customers will be deterred from participating in the market and denied the benefits that a competitive water retail market could offer.**
- **We urge that this issue is addressed in the manner set out in our Conclusion below before April 2017 to give the market the best possible chance to succeed.**
- **In the sections that follow, we comment on the following questions raised by Ofwat in its consultation:**

Q1 Should this review focus only on issues relating to the non-household retail price controls and the default tariff price caps?

Q2 In considering non-household retail issues, should this review allow for the reallocation of costs and margins between default tariff price caps, but with the constraint that aggregate levels of non-household retail costs and margins remain the same as in the existing controls, consistent with the expectations set out in our final determinations?

Q4 Do you consider it appropriate to encourage companies to increase the consistency in default tariff cap structures and consider carefully whether the diversity in the present levels of default tariff caps is properly justified?

Customer expectations of the market

Through our ongoing engagement with members (which include a large number of water-intensive users and multi-site businesses across Scotland and England), we know that they have a number of expectations around what the market will deliver. Several have already taken advantage of the benefits available in the Scottish market and consequently expect similar benefits to be on offer in England.

Savings

- One of the key things customers are looking for is price savings and it is our understanding that the margins set will determine the level of savings and discounts available. If the gross margin remains at around 6% on average then we know it will be difficult – if not impossible – for retailers to be able to offer attractive price discounts to customers.
- A recent YouGov survey for Economic Insight suggested 48% of businesses would require a saving of over 5% to switch, and 19% would require a saving of over 10%. This suggests a mis-match between the margins that have been set and customer expectations.

Improved services

- We appreciate that a key feature of the Scottish market for customers has been improved services. Competition has encouraged licensed providers to help customers reduce consumption (and hence cost). It has also galvanised licensed providers to sharpen up their customer service practices, including on billing and account management. Our members in England would like to take advantage of similar opportunities. However we are concerned that thin margins will also retard retailer investment in service improvements and innovation, and hence that our members will not only miss out on price discounts but also on service enhancements.

More choice

- We anticipate that low margins will deter some new entrants from coming into the market. This would mean that in addition to the above, our members will have less choice than they might expect. They tell us that in the energy market, when there has been innovation or service improvement for business customers, it has commonly come from new entrant companies rather than from incumbents. On that basis, we are keen to see new entry actively encouraged in water.

One supplier (for multi-site customers)

- Finally, one of the key benefits multi-site customers anticipate is the ability to switch to a single supplier for all their water and wastewater needs. Our concern is that given the current margins, new entrants will cherry pick the regions they operate in, leaving some areas where the margins are particularly low with very few suppliers to choose from – consequently limiting the ability for multi-site customers to use just one supplier.

- There is an additional concern for multi-site customers around the lack of consistency. Given the degree to which tariffs vary across the different regions, it could be very difficult for multi-site customers to negotiate a good single supplier deal. We would therefore urge that more is done to increase the consistency in default tariff cap structures.

Comparison and lessons learned from the energy market

The MEUC's members are experienced energy purchasers and our organisation has considerable expertise on the energy market. It has been interesting to make comparisons between the energy and water industries as we move towards water market opening.

- We have been made aware (and note that the CMA evidence is also referred to in your consultation document) that margins in the energy market are a great deal higher – around 15% – than those proposed for water. Since our members on average spend 20 times more on energy than on water, this difference is even larger in cash terms.
- Furthermore, until margins were increased in energy, there was very limited switching (this was also evident in the Scottish retail water market). This being the case, we would urge that the English water retail margins are increased from the outset to give the market the best possible chance to succeed.

Conclusion

- **Clearly the MEUC would not support a wider retail margin if it meant costs for customers would rise. But we believe a wider retail margin is essential for customers to achieve the savings, services and supplier choices they desire and expect. For this reason, we urge Ofwat to lower wholesale prices and expand the retail margin next year when it reviews non household retail prices ahead of market opening. Lower wholesale prices would allow the retail margin to be widened without the customer incurring higher costs.**
- **We support increased consistency in default tariff cap structures.**
- **We hope that this consultation provides a real opportunity to reflect and act on the concerns we – and others – have raised around the current margins and that this issue is addressed before the market opens.**
- **Unless the retail margin is widened, there is a real risk that our members' aspirations for the market will not be realised and that some will simply opt not to participate.**

If you have any questions or if we can be of any further assistance please do not hesitate to contact us. Please see details below.

Karma Ockenden, Water Advisor, MEUC 07880 550945 karmao68@gmail.com

Andrew Bainbridge, President, MEUC 0208 997 2561 ab@meuc.co.uk