

‘State of the market 2018-19: Review of the second year of the business retail water market’ and the ‘Future protections for business retail customers: Decisions on Retail Exit Code’

Foreword

Today we are publishing our assessment of the second year of the business retail market in England¹. We are also publishing our decisions regarding the protections for business customers who are not engaged in this market that will apply from April 2020.

Our assessment of the second year of the market shows that customer awareness of - and engagement in - the business retail market is largely unchanged compared to the first year. We conservatively estimate that customers who have switched or renegotiated since the market opened saved around £10 million on their bills in year two. This compares to around £8m in the first year.

Value added and innovative services (such as those to help businesses save water) are still slow to emerge. However self-supply has continued to interest large users of water in year 2 of the market, with 3 licensees saving ~150 Ml of water between them in 2018. Our customer research suggests up to 8% of switchers (~21% for large customers, consolidating across multiple premises) have benefitted from some form of bill consolidation.

Smaller customers are still much less likely to engage in and benefit from the market than larger customers. Our research suggests that around 15% of larger customers (250+ employees) switched supplier in the second year compared to around 3% of customers overall.

Our assessment also shows that despite positive action from some market participants in some areas, market frictions persist as the market enters its third year. The main frictions include:

1. poor quality data, including customer and consumption data, which can lead to inaccurate bills;
2. poor levels of wholesaler performance - for example in aggregate wholesalers only completed 63% of operating performance standard (OPS) tasks on time, which can lead to higher costs for retailers; and
3. some inefficient wholesaler-retailer interactions, which means that in some cases customers may be unable to rely on their retailer to resolve issues that

¹ The second year of the market covers the period 1 April 2018 to 31 March 2019.

are the wholesaler's responsibility (such as replacing a faulty meter) in a timely and effective way.

These frictions are getting in the way of the market functioning effectively and mean business customers are not yet enjoying the benefits anticipated at market opening. They are imposing costs on retailers and brokers, and creating barriers to entry and operation. Some frictions (for example poor quality consumption data) could also deter customers from engaging in the market as they can reduce the perceived benefits associated with switching (or renegotiating).

In making our decision regarding protections for business customers not engaged in the business retail market, we have carefully considered our duty to protect the interests of customers, wherever appropriate by promoting effective competition. On balance we believe it is appropriate at this point in time - while the market frictions are being resolved and the effectiveness of the market continues to develop - to retain protections for lower usage customers who have not engaged in the market.

So for customers on deemed contracts who use less than 0.5MI per year we are retaining price protections at a similar level to the current protections. For higher usage customers, who are more likely to engage in and benefit from the market, we believe it is possible to put a greater focus on the promotion of effective competition to protect customers' interests. So from April 2020 for customers on deemed contracts who use more than 0.5MI per year we are retaining but relaxing price protections. We intend to revisit the price protections in two to three years.

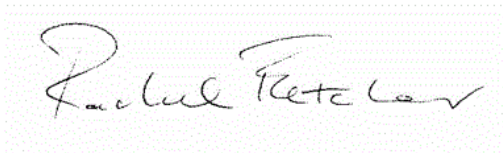
We are also strengthening protections for customers who have not engaged in the market in relation to their non-price contract terms. We are introducing an explicit 'no worse off' principle to apply to deemed contracts from April 2020 onwards. Where retailers wish to make changes to their non-price terms relative to those at market opening, they will need to be able to demonstrate that their customers will be no worse off as a result. This approach strikes a balance between ensuring that customers who have not engaged in the market are protected but in a way which allows retailers some flexibility to improve their service, offering or operations.

It's crucial that industry steps up efforts to address market frictions so the market can function more effectively and deliver improved outcomes for customers. We are seeing some examples of good practice – for example the guidance on unplanned events and leak allowance delivered by wholesalers and retailers working collaboratively through the Retailer Wholesaler Group (RWG). However there are also examples where industry participants need to do more.

I recently [wrote](#) to incumbent water companies challenging them to provide more support to the development of effective functioning markets and to give greater consideration to how their actions impact the development of the market. We expect to see significant improvements in the coming months and Ofwat will review progress in the autumn. There are also some circumstances where retailers need to

do more to support the market. For example, the Consumer Council for Water (CCWater) has recently published data making it clear that complaints - mainly driven by billing and customer service issues - remain worryingly high. Retailers need to respond to this and look to see how they can improve their complaints handling processes.

Resolving market frictions so the business retail market can function effectively and deliver improved outcomes for customers will require all stakeholders - wholesalers, retailers, customer representatives, the market operator (MOSL) and us as the regulator - to work collaboratively and each play our part. MOSL has set out a [programme of work](#) focused on delivering: improved customer outcomes; and improved trading party performance and accountability. We support this and would like to see trading parties play an active role to support and facilitate delivery of this work. For our part we are committed to working with the sector and using our powers and influence wherever appropriate to drive better outcomes for customers in the business retail market.

A handwritten signature in black ink, reading "Rachel Fletcher", is centered within a rectangular area with a light gray dotted background.

Rachel Fletcher
Chief Executive

11 July 2019