



Australia's Energy Sector: The State of the Market

Steve Edwell, AER Chairman
CEDA, 29 August 2007

Overview

- New AER functions
- Electricity and gas prices
- Industry consolidation

AER role

➤ Now:

- electricity transmission
- National Electricity Market monitoring
- National Electricity Law enforcement

➤ Early 2008: **add**

- gas transmission
- electricity and gas distribution

➤ Late 2008: **add retail**

- consumer protection, retailer of last resort etc
- retail price regulation at discretion of each jurisdiction

Regulatory structure post reform

	NSW	Vic	SA	QLD	ACT	Tas	NT	WA
Retail Pricing	IPART	ESC	ESC	Office of Energy	ICRC	OTTER/ GPOC	UC	ERA
Retail	Australian Energy Regulator (AER) (including NEM and Gas Code regulation)						UC	ERA
Distribution								
Transmission								
Wholesale								
Competition Regulation	Australian Competition and Consumer Commission (ACCC)							

Rule Changes	Australian Energy Market Commission (AEMC)	AEMC	AEMC
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Energy prices

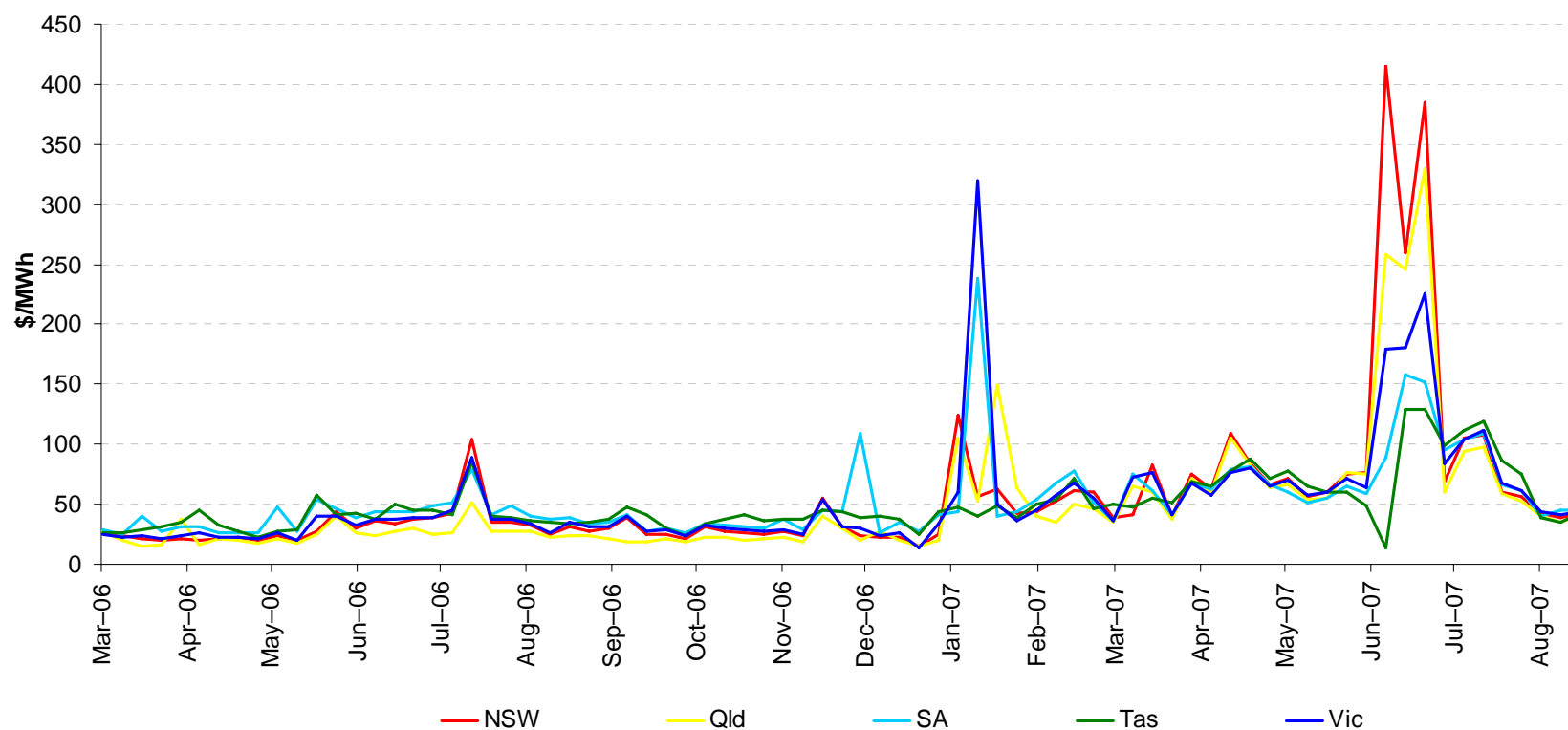
Electricity price update

- Price shocks in 2007
- Impacts
 - Forward market
 - Retail sector
 - Investment
- AER monitoring



Weekly electricity prices

NEM prices March 2006 – August 2007 (weekly volume weighted averages)



Drought

Water shortages:

- Snowy dams
- Tasmanian and Vic hydro
- Queensland coal plant

Impact: tighter supply conditions, higher prices

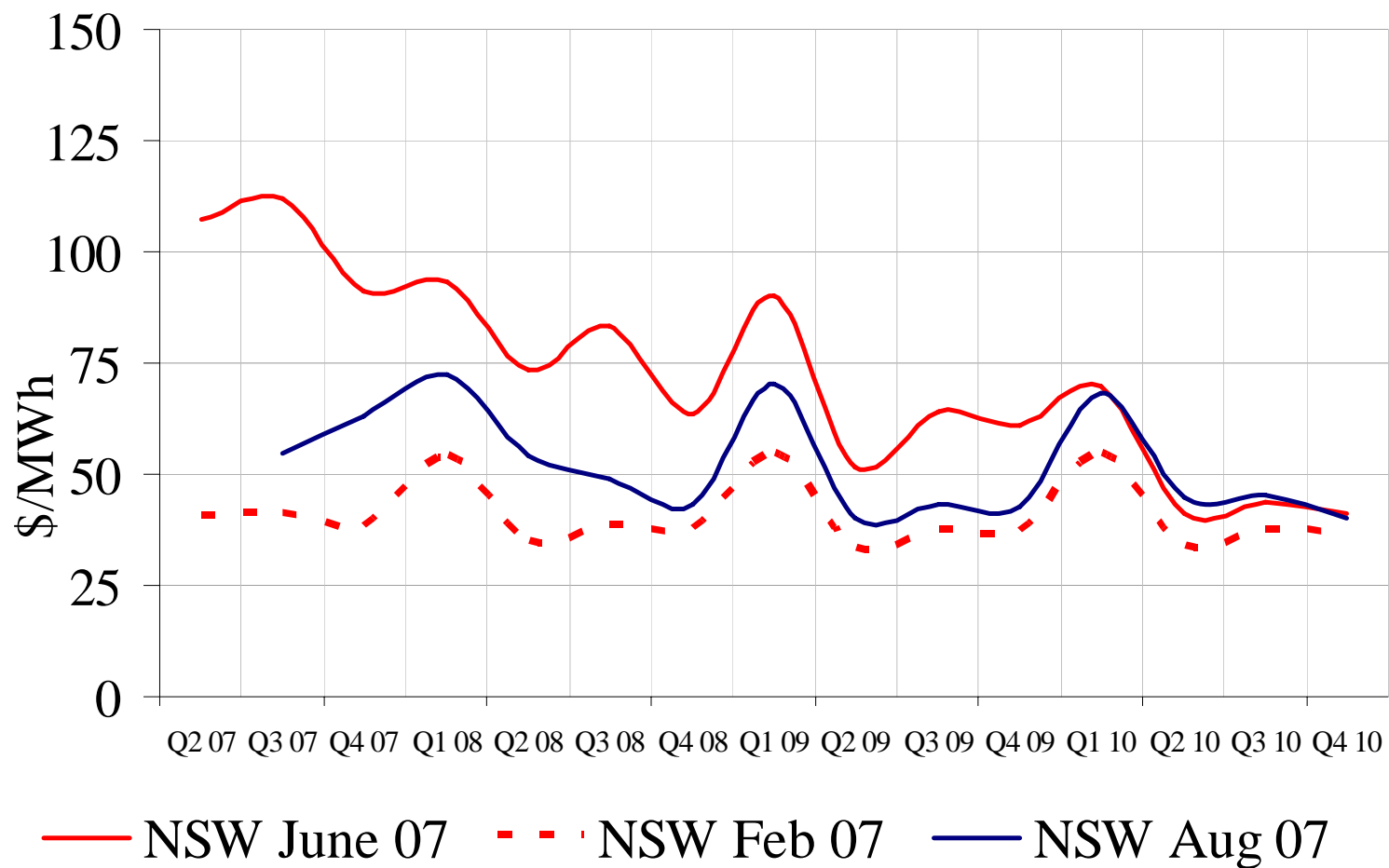
Market under stress in June 2007

- Record prices: 42 price events above \$5000
- Retailers under pressure
 - High prices squeezing margins
 - Energy One withdrew from the market
 - Momentum sold 15,000 customer accounts
- Some major users under pressure

Why the high June prices?

- Continuing drought conditions
- Flood impacts on Hunter Valley coal supplies
- High demand
- Macquarie Generation bidding

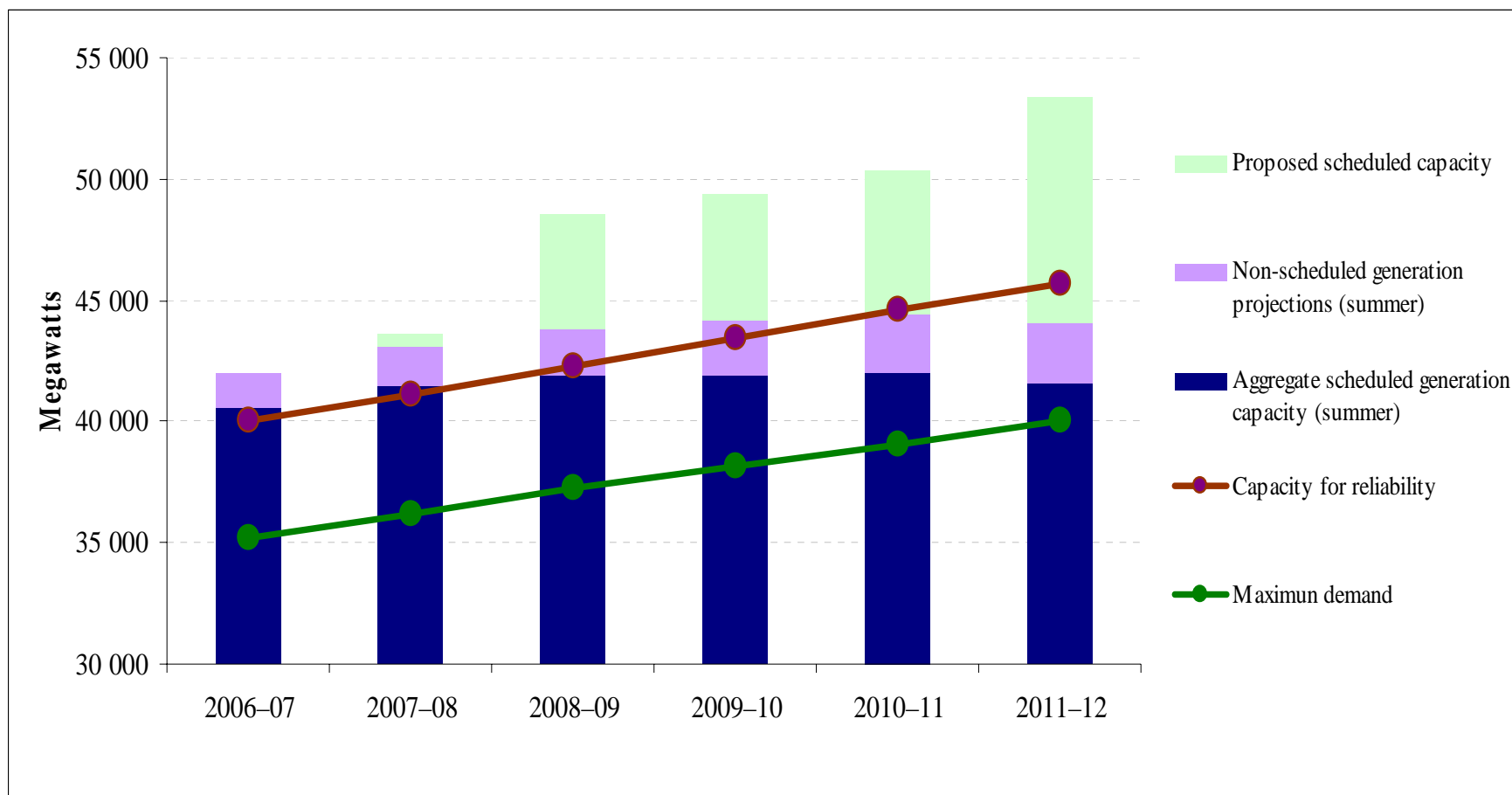
Forward prices



Higher forward prices — why?

- Uncertainty about future supply
 - risk of persistent drought?
 - timing of investment response?
 - uncertain effects of carbon trading on investment and prices?

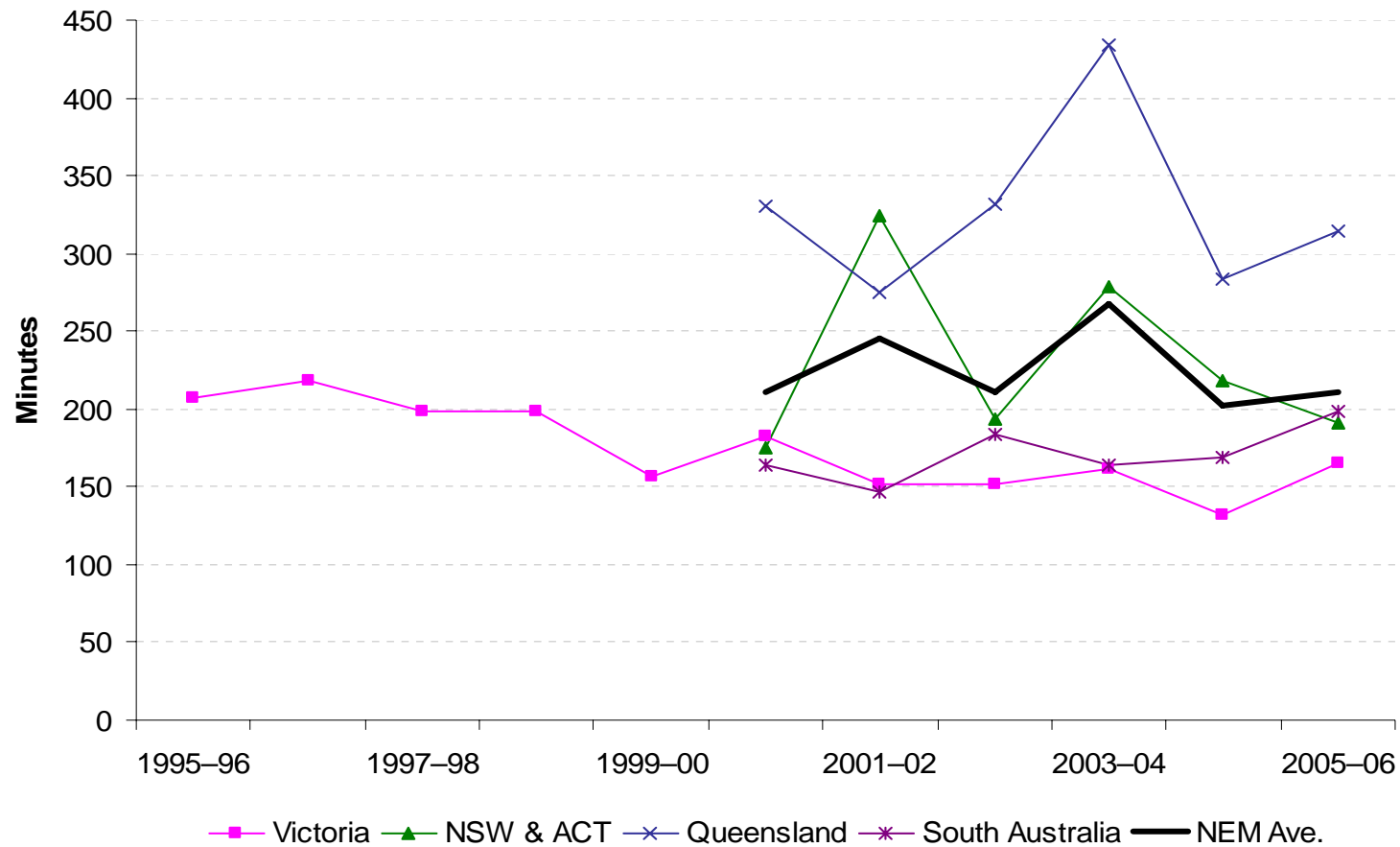
Reliability outlook to 2012



Electricity networks – real investment



Reliability – distribution



Gas prices

Natural gas prices



Historical prices around \$2.25–\$4.00/GJ

WA prices rising sharply since 2006

Victorian spot prices creeping higher

Western Australia

- Prices up from \$2.50 to \$7.50/Gj since 2006
- Tight supply
- Competition from LNG exports
- High prices attracting new entry, but tight supply may persist for some time

East Coast gas

Downward pressure on prices

- Coal seam methane increases supply

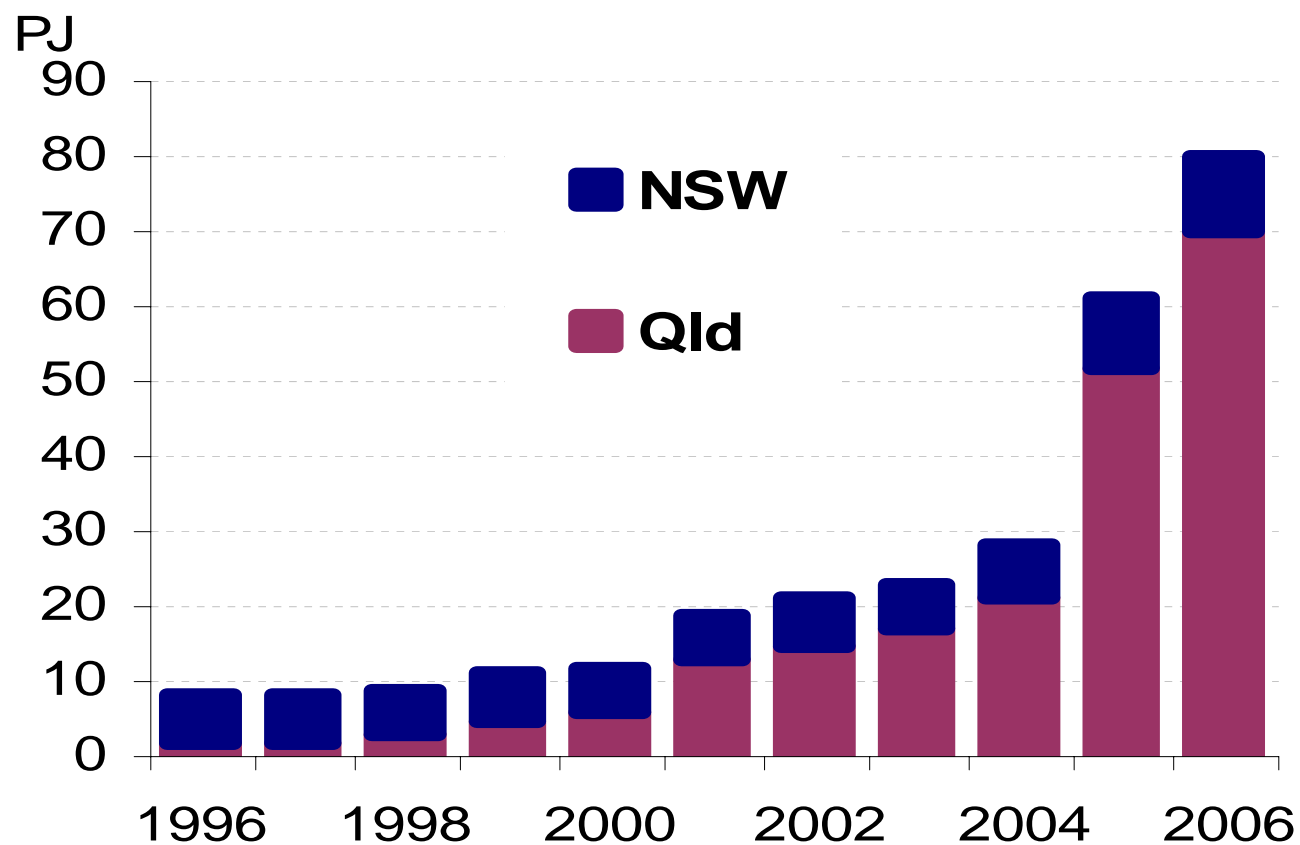
Upward pressure on prices

- Increasing demand – electricity generation
- Santos LNG proposal for export capability ?

Net impact?

- Price rises contained for now – \$3.00 to \$4.00 range
- Victoria prices reached \$5 this winter
- Longer term risks

Coal seam methane production



Ownership consolidation

Energy sector mergers

- Networks
- Retailers
- Vertical integration

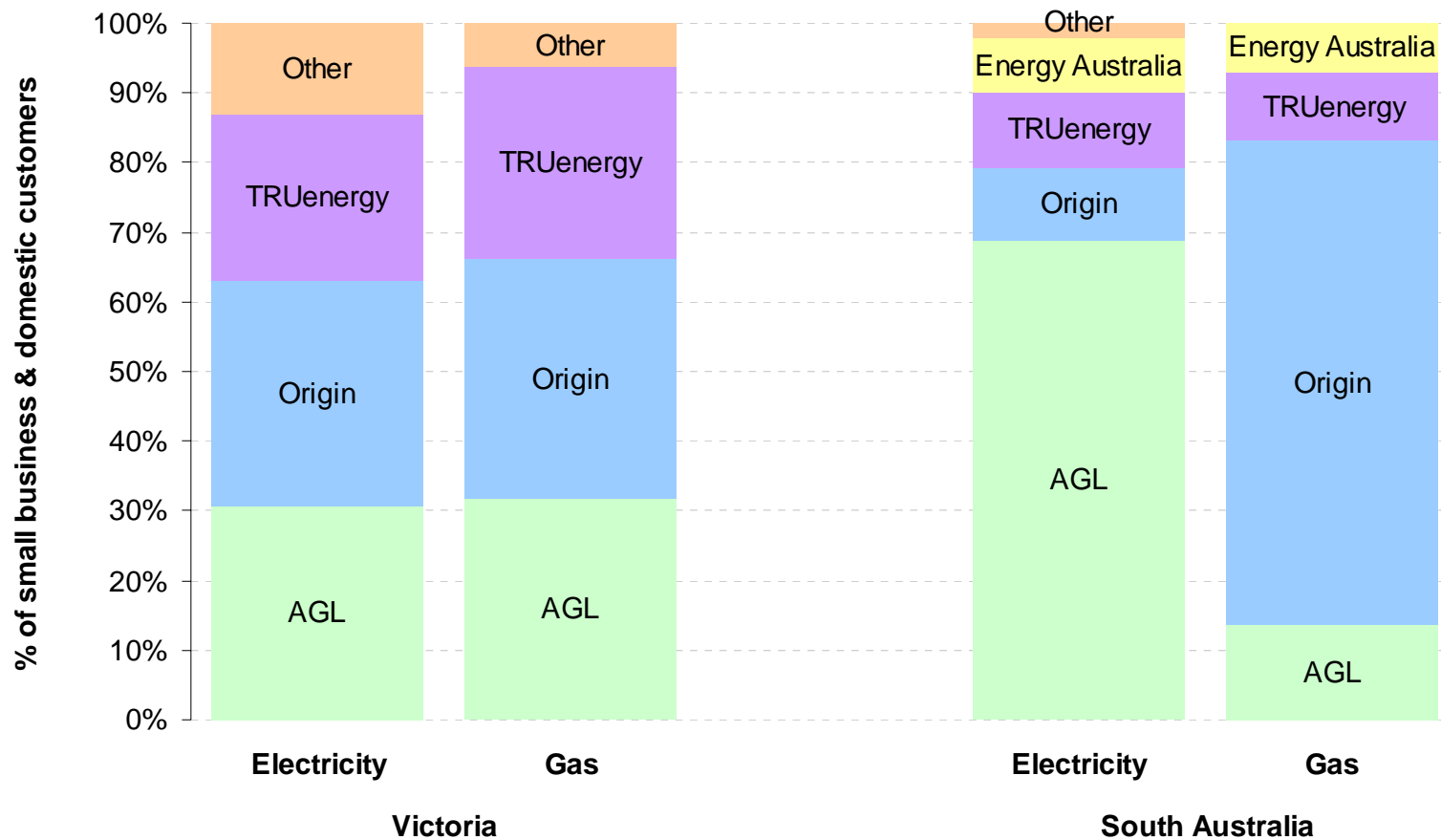
Recent merger activity

- AGL and TRUenergy swap generation assets in SA — AGL acquires Torrens Island (1260MW)
- Sale of Origin Energy's gas assets to APA group
- Sale of Alinta to Babcock & Brown / Singapore Power
- International Power to buy EnergyAustralia–IP retail partnership
- Basslink sale

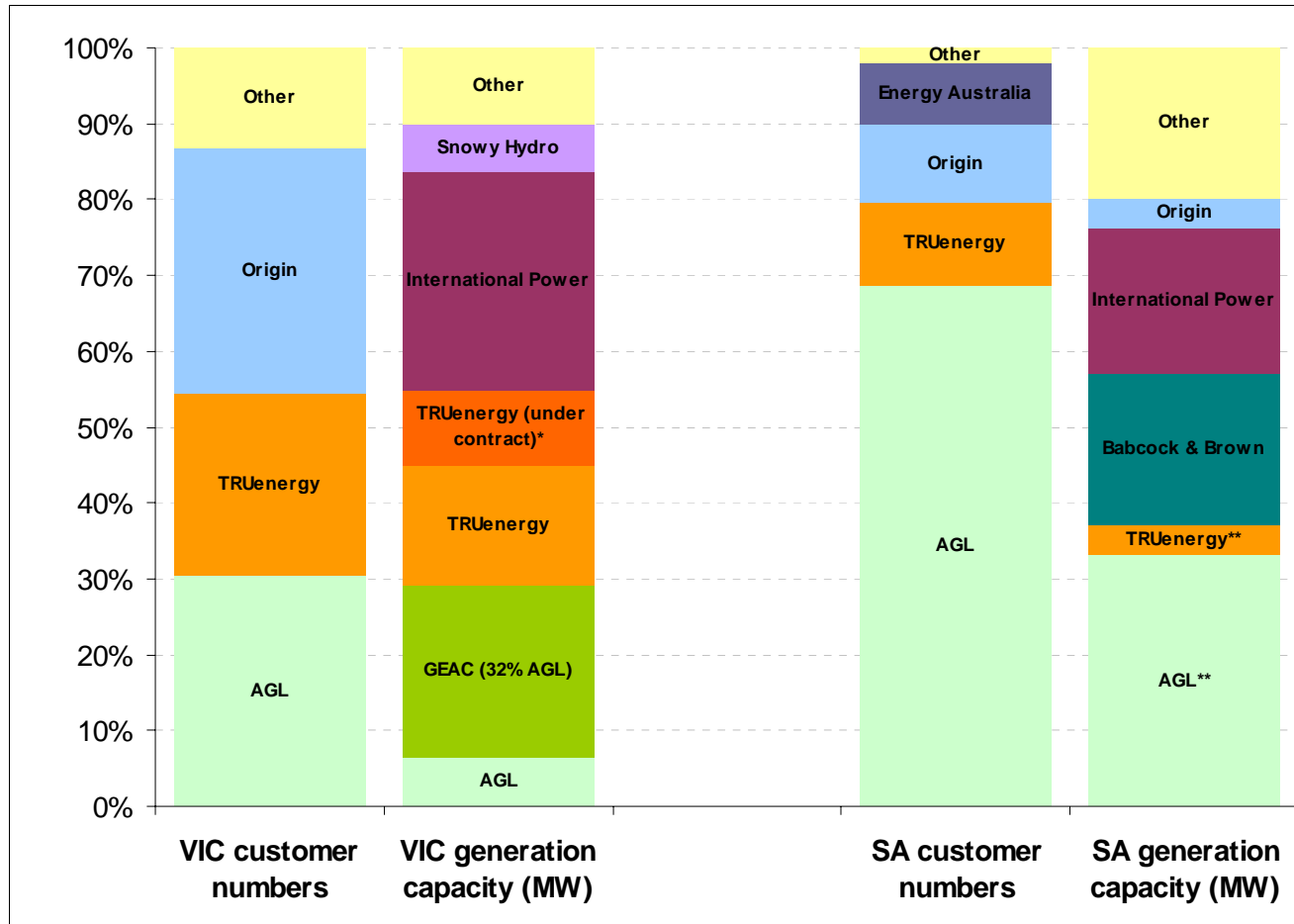
Ownership integration— networks (after Alinta sale)

	Electricity Transmission	Electricity Distribution	Gas Transmission	Gas Distribution
Singapore Power / SP AusNet				
APA Group				
Cheung Kong Infrastructure				
Babcock & Brown				

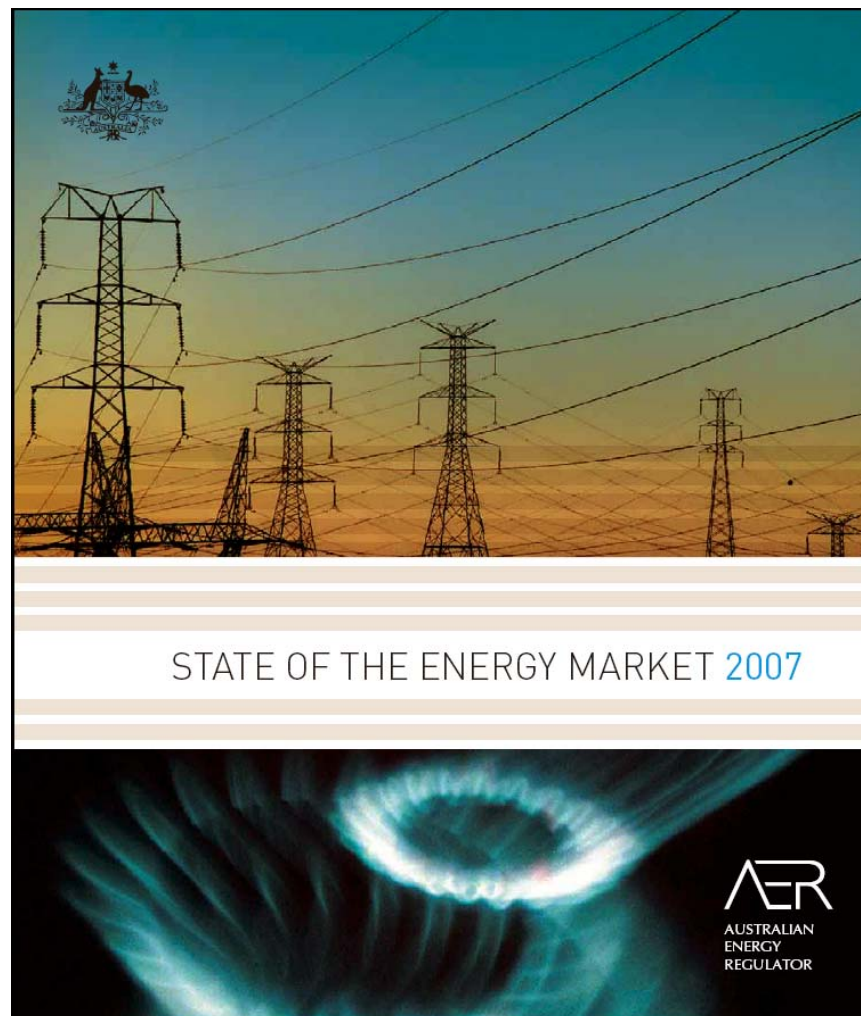
Retail market share – Vic/SA



Vertical integration



State of the Energy Market

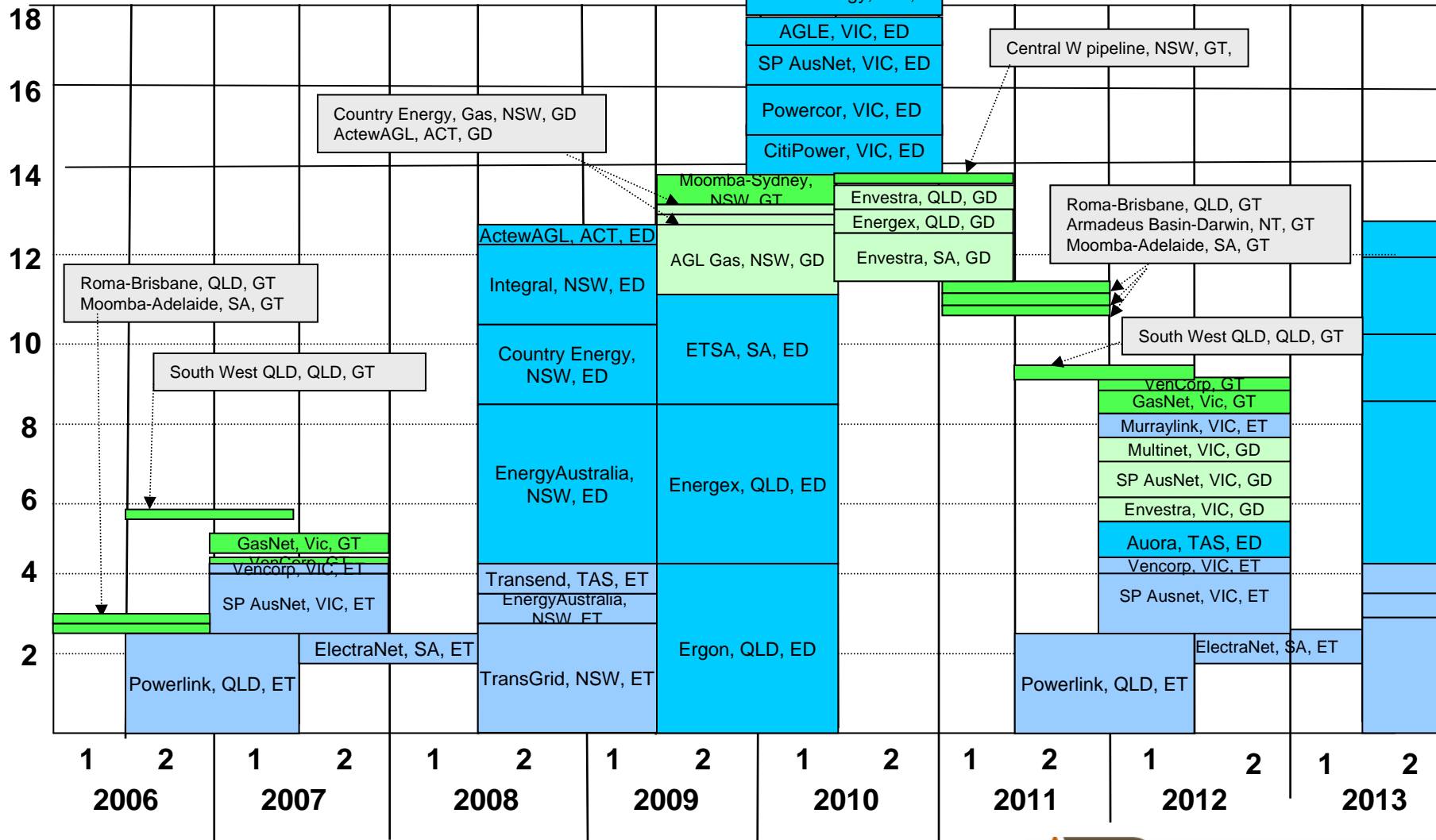


AER's new functions

Indicative timeframe for AER transfers

		2005		2006		2007		2008		2009
		1-Jul	1-Jan	1-Jul	1-Jan	1-Jul	1-Jan	1-Jul	1-Jan	1-Jul
Electricity functions	Regulation of electricity transmission									
	NEM monitoring									
	Regulation of electricity distribution									
Gas functions	Regulation of electricity transmission									
	Regulation of electricity transmission									
Non-price distribution and retail functions										

Resets



AER regulatory portfolio

Sector	Number of regulated businesses / pipelines	Combined regulated asset base
Electricity transmission	9	\$11 billion
Electricity distribution	13	\$28 billion
Gas transmission	14	\$3 billion
Gas distribution	11	\$6 billion
	47	\$48 billion

New regulatory framework

- More prescriptive framework – certainty
- Electricity & gas more aligned
- Merit review extended to electricity
- Light regulation option in gas
- Tighter timeframes
- Information powers stronger – and more accountable

Preparation for new functions

- Internal capacity
 - Budget secured
 - Increase in staff numbers
 - Transfer of staff from the state regulators
- Regulatory guidelines – transmission and distribution
- Preparation for NSW resets
- Industry consultation

Objectives

- Committed to smooth transition to national framework
- Keen to pursue ways to improve the quality of regulation. Looking at:
 - consistent and timely processes established well up front
 - streamlining implementation requirements through standard information templates
 - ways to make regulation less intrusive but still robust
 - ways to effectively engage stakeholders

Conclusions

- AER is well prepared for transition to national regulation
- Electricity price shocks in 2007, but market has eased since July
- Gas prices rising in WA; price pressure in the east cushioned by CSM
- Extensive ownership consolidation
- Strong investment and steady reliability in regulated networks

Questions?