

Electricity Wholesale Market - facts and figures

Why has the system for trading electricity changed?

1990 - electricity privatisation

1990 - 2001 - arrangements called the Electricity Pool operated for the production, purchasing and trading of wholesale electricity.

These arrangements were complex and flawed in that they operated in favour of generators.

Fact: For the 10 years of the Pool, wholesale prices failed to fall despite generation costs falling by a half - and efficiency of the best generation plant increasing from 35 per cent in 1980 to 48 per cent in 1990.

December 1997 - the incoming Government signalled its intention to reform the electricity market and work began with an energy White Paper in the following year.

March 2001 - the Pool arrangements were reformed.

The new electricity trading arrangements were put in place, creating for the first time a truly competitive market working in the interests of customers rather than of generators.

This means that those who produce, buy or trade wholesale electricity can do so like companies in any other commodity market.

Some 98 per cent of electricity is traded on a bi-lateral basis, business to business. The remaining 2 per cent is traded in the balancing mechanism set up to deal with electricity imbalances.

Fact: The combination of greater competition and oversupply has resulted in a 40 per cent fall in wholesale prices in the last four years. Since March 2001, prices have fallen by 15 per cent.

Why have we got more electricity than we need?

The market under the Electricity Pool encouraged generators to build and commission new plant to take advantage of artificially high wholesale prices.

Fact: Today, according to National Grid Company (NGC), England and Wales has 68 GW of electricity generating capacity available for the 2002-2003 winter.

NGC predicts that peak demand for electricity in this period could reach 55 GW.

There is a margin of 22 per cent spare capacity over maximum demand.

Have customers benefited?

Industry and commerce consume two thirds of all electricity produced in Britain. Wholesale costs make up 75 per cent of their bills.

Fact: Since October 1998, the price industry and commerce pay for electricity has fallen by 20-25 per cent.

These reductions have saved British industry and commerce a total of £1.5 billion.

Contracts agreed in April 2002 saw these prices fall a further 9 per cent - with more reductions predicted in future contract negotiations.

What about domestic customers?

Electricity wholesale costs make up some 40 per cent of domestic customers' bills.

Fact: Since 1998 - when reforms to the electricity trading were first announced - domestic customers who have stayed with their original supplier (the old electricity boards) have seen an 8 per cent cut in their bills.

Those customers who have switched supplier, have seen bills cut by 17 per cent.

Customers switching suppliers today can save up to 22 per cent on their bills.

Supply companies have focused savings on offers to attract customers away from their incumbent suppliers. That is why switchers have seen more savings.

New environmental costs which suppliers are now passing on to customers have also added 1.5 - 2 per cent on to domestic customers bills.

If there is evidence of companies colluding to keep prices high, or abusing a dominant position, Ofgem has powers under competition law to investigate and, where necessary, take action.

What is 'mothballing' and why are generators doing it?

Oversupply, together with falling prices, have led generators to 'mothball' plant. Generators can normally bring plant back on to the system if the economics of the plant reverse.

When there is 22 per cent overcapacity and a 40 per cent fall in prices, no one should be surprised that 'mothballing' takes place.

Generators have known since reforms began in 1998 that competition would intensify, and that with significant overcapacity, prices were likely to fall. They have had ample time to respond with the appropriate commercial decisions.

Fact: To date 6 per cent of total capacity has been 'mothballed'.

If prices rise, generators can - and have - returned 'mothballed' plant back to the system.

Forward prices will help ensure security of supply by signalling the need for 'mothballed' plant to be returned to the system, or for new plant to be built.

Are we facing a California-style crisis?

No.

The crisis in California was caused by:

- lack of generating capacity
- inability to contract ahead for the purchase of electricity which prevented future investment in generation, and inability to pass on increased wholesale electricity costs to customers because of regulatory price caps.

In Great Britain, there is:

- more generation than we need
- ability to contract ahead, which provides price signals for future generation investment, and
- full competition in the retail market.

Britain's generating capacity is expanding, with 3 GW of generation currently being built or being commissioned in England and Wales alone. The Government's renewable obligation is also encouraging an expansion of renewable generators.

What are Ofgem's responsibilities to secure supply?

Ofgem:

- regulates the natural monopoly companies which run the pipes and wires to ensure they have the right incentives to invest and develop their networks
- ensures that the wholesale electricity market remains fully competitive and that there are no barriers to new entrants, and
- monitors the operation of the market to ensure it is acting competitively and in the interests of consumers.