

The energy supply market probe

Ofgem launched a probe into the energy supply markets in February 2008. The work to develop initial findings is now complete and we will publish these next week (w/c 6 10).



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The probe has sought to establish how far competition is working to deliver value for money for all customers. The probe is being carried out under Ofgem's Enterprise Act powers. These powers enable the regulator to call for detailed information of the kind that Ofgem does not regularly access

in its ongoing market surveillance work. Energy companies are bound under the Act to provide this information.

The probe has also been informed by responses to a wide call for evidence and new consumer research into attitudes to and experience of the energy market today.

What has the probe looked at?

The investigation has examined:

- the customer's perspective and experience of the market including access to information and barriers to switching supplier;
- suppliers' market shares, switching rates for different groups of customers (such as online, dual fuel, single fuel and pre-payment);
- the competitiveness of suppliers' pricing in the different market segments and customer movement between payment types as well as suppliers;
- the relationship between retail and wholesale energy prices; and
- the economics of new entry and the experience of companies trying to enter the energy market.

The investigation looked at markets serving domestic customers and small businesses.

Why did Ofgem launch the Probe?

We had a number of concerns and we had seen new patterns of behaviour by the companies.

For example, the timing and spread of price changes early in 2008 had changed. When the suppliers dropped prices in 2007, there was a period of nearly eight months between the first company's announcement of a price cut and the last company's (following naming and shaming by Ofgem). And the amounts by which they dropped their prices had a range suggesting the consumer was being presented with choice.

When the suppliers announced price increases between late January 2008 and early February they went roughly at the same time. The increases took immediate effect and on a national average there was little differentiation between them. Add to these observations tremendous consumer concern and our statutory duty to protect customers we felt a detailed examination of the supply markets was needed. The retail sector is the energy industry's most important interface with customers and signals their preferences and demands.

What will happen next?

We will announce our initial findings in the first week of October. They will include an appraisal of the market's performance and, if appropriate, our preferred remedies.

There are a range of powers and options available to Ofgem. These extend from doing nothing through to ensuring

increased information is given to customers; seeking new obligations in the suppliers' licences; or making a reference to the Competition Commission. These measures could be applied to different parts of the market.



What impact will the probe have on prices?

The probe aims to ensure that competition in the supply (retail) sector is working effectively for all customers.

The retail end of the market includes the costs of marketing, billing and the profit margins of the supply companies. In total it accounts for about 13 per cent of the household energy bill

Wholesale costs (the cost of electricity and gas) account for more than half the household bill. Increases in costs have

been driven by rising global commodity prices – the price of oil, coal, gas and carbon. Ofgem has no jurisdiction over these.

Moves to address the impact of those costs on levels of fuel poverty, in particular over the long term, will have to tackle issues relating to low incomes and the quality of housing stock. Those responsibilities lie primarily with Government.

What is the supply market?

The **suppliers** are the companies that sell gas and electricity to households and businesses throughout GB. The six main players are the familiar brand names: British Gas, EDF Energy, Eon UK, npower, ScottishPower and Scottish and Southern Energy.

Other parts of the energy market are:

- the **wholesale markets** where the electricity generators, gas producers and shippers trade, selling their outputs to the suppliers and other large energy users such as heavy industry;

- the regional **distribution networks** – the companies running the pipes and wires that carry energy to most domestic and commercial premises;
- the **national transmission pipes and wires** (run by National Grid) that carry gas and electricity nationwide from the generators and gas terminals to feed into the regional networks.

What does Ofgem regulate?

Ofgem sets allowances of revenue and expenditure for the companies that run the gas and electricity networks because, for most of their businesses, they are not in competition with others.

Ofgem does not set the prices that suppliers charge households or businesses. Our role is to ensure that there is adequate competition between players in the market to rein in prices. To do this we draw on powers under the Gas and Electricity, Competition and Enterprise Acts.

Ofgem does not regulate **wholesale** electricity or gas prices which are driven by the market. Ofgem's role in the **wholesale** market is to monitor market behaviour and use powers to ensure competition is working

Gas and oil production is licensed by the Government's Department for Business Enterprise and Regulatory Reform.