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Mr Will Fletcher,
Project Manager
Energy market investigation
Competition and Markets Authority
Victoria House
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By email at EnergyMarket@cma.gsi.gov.uk

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Dear Will,

Submission on Updated Issues Statement from Ceres Energy

Ceres Energy has been a licensed shipper since 2008 and operates at all points in the supply chain from off-take at the injection point through to trading at the NBP and delivery to end users. We particularly specialise in managing supply and shipping processes for smaller participants in the market, such as biomethane producers and new entrants to the retail market.

Ceres welcomes the breadth of investigation which has been undertaken and the clarification which the update has made on the issues currently under investigation. Ceres sees the maintenance of effective competition as critical in the future of the domestic and SME retail gas markets and is concerned that the following are addressed in CMA's conclusions:

- increased consumer trust in the energy market as a whole based on effective competition between incumbents and new entrants offering a diversity of supply options;
- reduction in the extent of regulatory intervention, especially in managing the relationship between the supplier and its customer;
- the development of a more responsive approach to industry process change;
- security that the Big Six have not used market power and that they do not have the potential to do so if the market share of new entrants rises.

Increasing trust in the market

Ceres believe that retail energy can be an effective competitive market, offering choice to consumers. We are concerned about the level of distrust in the market shown by the GFK NOP research; customers have a relatively positive view of their current supplier but a poor one of suppliers in general. We see the level of criticism from the media, politicians and regulators is driving groups of people away from the competitive market and increasing the risks for new entrants. The basis of choice should be price, good products and quality of service, and a vibrant

market will bring out the best offers. This negative image necessarily creates the need to make the alternative proposition more attractive through price which in turn makes it much harder for new entrants to build a viable business. With so much of the customer experience provided through industry processes (in particular switching processes) which seldom have the end customer at the centre of its thinking, it is impossible for suppliers to differentiate in a sufficiently material way to overcome this level of negative perception.

Problems of over-regulation

Ceres welcomes the CMA's review of the regulatory interventions over the last few years. The extent of regulatory requirements has several impacts for the new supplier – the need to comply with each rule, the uncertainty about what may come next and the extent to which proscribed regulatory requirements determine relationships with customers, leaving little flexibility to operate effectively in the market. In terms of the extension of regulatory interventions into microbusinesses we believe there is insufficient regulatory understanding of the market – this is typified by the operationally complex definition of the protected groups which would require the supplier to collect extraneous information on the customer. Without clear and substantial benefits, regulation simply hinders the effectiveness of competition.

Of most concern is the extent of price control already in place with the restriction on numbers of tariffs. Ceres believes that pricing should be a product of market conditions and that suppliers should be able to respond flexibly. Adaptability is one of the keys to competing successfully. We note the concern about margins amongst the Big Six; however price regulation cannot be a feature of effective competition. Regulators second guessing the appropriate returns will create excessive regulatory uncertainty and will discourage the new entrants which are needed for effective competition.

The role of industry processes

We note the level of concern about the unresponsiveness of industry processes and the evidence of the resource requirements from suppliers to make changes. While the CMA focusses on the potential for innovation through smart metering in the longer term, we believe the quality of the switching processes provides a better example of how the end customer is not central to industry processes. The industry participants most interested in enhancing the customer experience – new entrants – have the fewest resources to drive for change and are often at a commercial distance from the codes which affect their customers. Unreliable or customer-unfriendly processes contribute to the low levels of engagement and lack of trust in the market.

Dual fuel

We are very concerned about the electricity bias and the presumption of dual fuel supply which is prevalent in the documents. The costs savings and convenience of dual fuel are unlikely to outweigh the benefits of shopping around for the best deal. There is sufficient difference between the gas and power markets that one should expect greater diversity in the magnitude and timing of price changes in the different fuels. Historically dual fuel discounts have been much higher than cost savings; the incumbent suppliers initially saw the conversion of monopoly customers as protective and the pricing strategies for standard variable tariffs have tended to maintain margins in the legacy fuel by lower margins in the fuel in which the supplier did not have a monopoly. We believe that the CMA should have considered this issue in the domestic market. In the SME market there is very little dual fuel supply suggesting some distortion in the

residential market. We consider this dual fuel bias may affect the appetite for innovation amongst the Big Six; unless something can be implemented in both markets it is unlikely to be promoted. Where this is dependent on industry rule changes innovation goes at the speed of the slower fuel.

The role of the Big Six

The issues papers are tentatively suggesting that the Big Six are not exerting nor likely to be able to exert market power in the retail market through vertical integration. This remains a concern amongst smaller suppliers, given the asymmetry between the new entrants and long-term incumbents and there must be confidence that there are no residual possibilities for them to re-establish their dominance. The share of new competitors is at an all-time high but is by no means secure yet. Further flow of new entrants is a necessary sign of confidence in the market. The issue of vertical integration really relates to the electricity market, underlining the importance of recognising unnecessary linkages between the markets.

Helen Edwards
Managing Director