Are lower prices an illusion or reality in a deregulated market?

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The South African energy market has been solely managed by utility company Eskom, accounting for generating, transmitting and, in other cases, supplying and distributing energy countrywide.

With this in mind, the South African energy market has the prospect of embarking on deregulating the current energy market, allowing for both local and foreign investment, forming a more viable solution to the energy crisis at hand.

In light of this fact, this paper intends to address the issue of a competitive energy market, and the consequent effect thereof.

The current South African energy outlook

“President Zuma’s call for a radical transformation in South Africa’s energy sector in his State of the Nation Address hit at the core of the country’s energy catastrophe. Without energy, the National Development Plan (NDP) and all plans for growth are dead in the water, along with prospects for jobs. South Africa has an immediate and future energy crisis. We need a radical policy to secure affordable and reliable energy to solve the short-term emergency and the long-term supply to power essential GDP growth.” [1]

The National Development Plant (NDP) iterates that the economy urgently needs increased competition in electricity generation, that gas should be explored and new generation capacity should be divided between Eskom and Independent Power Producers (IPP):

“Economic growth and development through adequate investment in energy infrastructure and the provision of quality energy services that are competitively priced, reliable and efficient. Local production of energy technology will support job creation.” [2]

What are the consequences if South Africa continues with a regulated market?

“Eskom Energy Generation Company has been at the heart of the South African energy market, generating approximately 95% of the electricity used in South Africa and a significant 45% of the electricity used in Africa. Eskom generates, transmits and distributes electricity to industrial, mining, commercial, agricultural and residential customers and redistributors.” [3]

Many factors, including ‘load shedding’, pressure authorities to devise more than one energy producer and transmission company. Therefore if no alternative to Eskom is established to enter the market and compete, the track record of Eskom will decline, resulting in South Africa relinquishing foreign trade investment opportunities. The consequences of continuing with a regulated market leads to increased theft, poor revenue collection and increased energy tariffs.

Rapid progress and partnerships must be established with IPPs, ensuring that the demand on the electricity grid is sustained. In the past, one out of every three South Africans had access to electricity. Currently, over 80% of the population has access to power. This rapid growth will impact the state-owned utility, resulting in poor domestic and commercial services, support and infrastructure. This alarming issue is evident in today’s climate of vandalism and destruction of property by end-users experiencing high tariff increases and load shedding.
Are lower prices an illusion or a reality in a de-regulated environment?

In retrospect, telecommunication giant Telkom, being the only communications company for decades, with no competitors, required drastic deregulation as the communication company could not sustain the demands of the market timeously. With the correct market competitors and stimulation, consumers now have a wide range of products and service providers to choose from, resulting in a more conclusive communication network and increased customer satisfaction, to mention a few.

Transparency concerns raised in the de-regulation of telecommunication company Telkom included:

- How can end-users really check what a particular phone call costs?
- How many minutes have they actually used when the statement arrives more than 30 days later?
- What are set-up costs or kick-back rates – and what is breakage?

Similar transparency concerns could relate to Eskom:

- How can Eskom provide key customer service across South Africa in an effective and conclusive manner?
- Transparency relating to costs involved with maintenance call-outs, new installations, if no alternative exists for pricing comparison.

What are the consequences if South Africa moves to a deregulated market?

A reliable energy market, which is competitive in pricing and service delivery, will be one of the major driving factors for the success of the NDP. The average household will be able to choose between competitive energy suppliers, resulting in more manageable tariff increases. The consequent factors of a deregulated market have far reaching beneficial impacting factors, i.e. increased revenue protection, job creation, sustainability and increased productivity.

Some noticeable benefits experienced by other countries positioned similarly to South Africa:

- Regulators will no longer be allowed to determine which firms will be given the privilege to serve consumers via exclusive franchising arrangements and other barriers to entry.
- Lower prices for residential users by empowering them to choose their electricity supplier.
- Direct competition posed by new firms entering the market would also develop higher quality of service and innovation within the industry.
- Competition among firms will lead to organisations being more responsive to user demands.
- Deregulation means empowering the end-user with options and ultimately trust in the service product.
- Collectively, commercial users especially small power users, stand to benefit a large percentage of overall monthly costs allocated to utility bills, in particular electricity. The most cost-effective service provider will be chosen, within these smaller organisations, ensuring sustainability.

Tariffs increases in South Africa

The cost of electricity will most definitely change, based on other use case studies across the world. The impact of deregulating the energy market results in most benefits realised. Tariff increases within a regulated market will always be a challenge, experienced by most countries.

“The 2012/13 tariffs are NERSA approved rates as per the 9 March 2012 NERSA decision on electricity tariff increases averaging 16%, which is lower than the 25.9% originally approved by NERSA. The 2012/13 tariffs are effective as of 1 April 2012 for non-local authorities and 1 July 2012 for local-authorities." [4]

Multi-year price determination (MYPD3)

The lower electricity price increases are the result of a combined effort by government and Eskom to lessen the impact of higher electricity tariffs on consumers and the economy in the short term without compromising Eskom’s ability to keep the lights on and ensure its long-term goal for financial sustainability. If this has not
occurred, the result would be that many South Africans will be faced with the reality of not being able to afford electricity.

In the future, this type of intervention displayed by government might be driven by clients, forcing Eskom or competing firms to lower or decrease tariff increases, largely attributed to competitiveness within a synergised market.

**The New Zealand deregulated case study**

- **1992:** New Zealand officially opened its energy market up to competition – converted local power distributors into individual companies.
  
The driving factor and roots for New Zealand’s deregulation trace back to the mid-1980s when concerns grew over the country’s economy; the proposed way forward was the efficient management of resources and a more transparent market.

  The government’s ministry of energy ran New Zealand’s electricity generation and transmission, pricing and investments driven by politics. Operations were plagued by inefficiencies and lack of end-user choice.

- **1996:** New Zealand opened the wholesale electricity market officially with a state-owned company Contact Energy, being in direct competition with the Electricity Corporation of New Zealand.

  This resulted in a major breakthrough with generators, purchasers and traders being able to set the market electricity prices.

- **1998:** Government demands corporate separation of line and energy businesses, preventing cross-subsidies and monopolies of local distribution networks.

- **2008:** Ten years later, distributor SLAs and transparency in terms of company pricing and profits bought customers a range of options and suppliers to choose from.

Based on the study and timeline in Fig. 3, South Africa might meet the set target of the NDP for 2030, with the introduction of IPPs and alternative energy sources.

**Conclusion**

South Africa as a country requires some rigorous market transformation, ensuring longevity and growth. The introduction of IPPs and alternative energy sources will assist in driving down the cost of energy. The envisioned competitive market will bring about much innovation and initiatives for saving or reducing energy usage. Paramount to reducing South Africa’s carbon footprint is the introduction of alternative renewable energy sources.

The deregulation of the energy market similar to that of New Zealand, where transmission lines or generating power for the same grid are shared, will result in a competitive and resilient market for all parties involved.

This competitiveness, as seen in the New Zealand market, will bring about the much needed makeover, and pricing will decline for previously regulated ‘regular tariff increases’. Therefore, lower prices are not merely an illusion but in fact a true manifestation as experienced by other countries in a deregulated market.

**References**


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