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11 July 2012

Electricity Standing Contract – Wholesale Electricity Cost Investigation
Essential Services Commission of South Australia
GPO Box 2605
Adelaide SA 5001

Dear Sir/Madam,



I write to you in relation to the Essential Services Commission of South Australia (ESCOSA) *Electricity Standing Contract – Wholesale Cost Investigation Discussion Paper*.

Business SA is South Australia's leading business membership organisation, representing thousands of businesses through direct membership and affiliated industry associations. We represent businesses across all industry sectors, ranging in size from micro-business to multi-national companies. Business SA advocates on behalf of business to propose legislative, regulatory and policy reforms and programs for sustainable economic growth in South Australia.

The reliable availability of low cost energy has underpinned the competitiveness of many Australian industries. Electricity prices are rising rapidly for a number of reasons, including significant investments in distribution networks, strong peak demand growth and climate change related policies. It is therefore important that if wholesale electricity costs fall or go below what was anticipated, then these cost reductions are passed on to consumers.

Business SA believes that ESCOSA was justified in using a long run marginal cost (LRMC) approach to determining wholesale electricity costs when liquidity in the forward contract market was constrained. But given the preliminary evidence as highlighted in the discussion paper, it appears that the market's liquidity has improved to a point where forward wholesale electricity prices can be estimated with sufficient reliability from the market.

Such an evidence-based approach is likely to provide more accurate estimates of forward prices than a theoretical LRMC approach. Business SA therefore supports ESCOSA in carrying out further investigations regarding estimates of market-based forward wholesale electricity prices and whether or not they differ substantially from wholesale electricity costs as estimated using the LRMC approach.

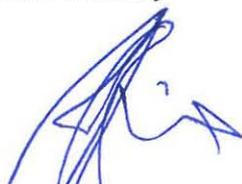
If the difference is material, Business SA supports changing the wholesale electricity cost component of the electricity standing contract price to better reflect actual costs faced by retailers. This will provide better price signals to market participants and in the event that the change results in lower electricity prices for consumers, both businesses and households will benefit.

While Business SA agrees with ESCOSA that the pool price in the National Electricity Market (NEM) should not be relied upon as the only indicator of wholesale electricity costs, sustained periods of low or high prices on the NEM will flow through to forward market contracts.

The average annual electricity price for South Australia on the NEM has been at seven year lows for the last two financial years, in the low \$30s per MWh. This is just one third of the LRMC estimated by ESCOSA. Given the high likelihood that at least part of this significant differential will also appear in the forward contract market, it should be taken into account when estimating the wholesale electricity cost component of the electricity standing contract price.

Should you require any further information or have any questions, please contact Rick Cairney, Director of Policy, Business SA on (08) 8300 0060 or rickc@business-sa.com.

Yours sincerely



Nigel McBride

Chief Executive Officer