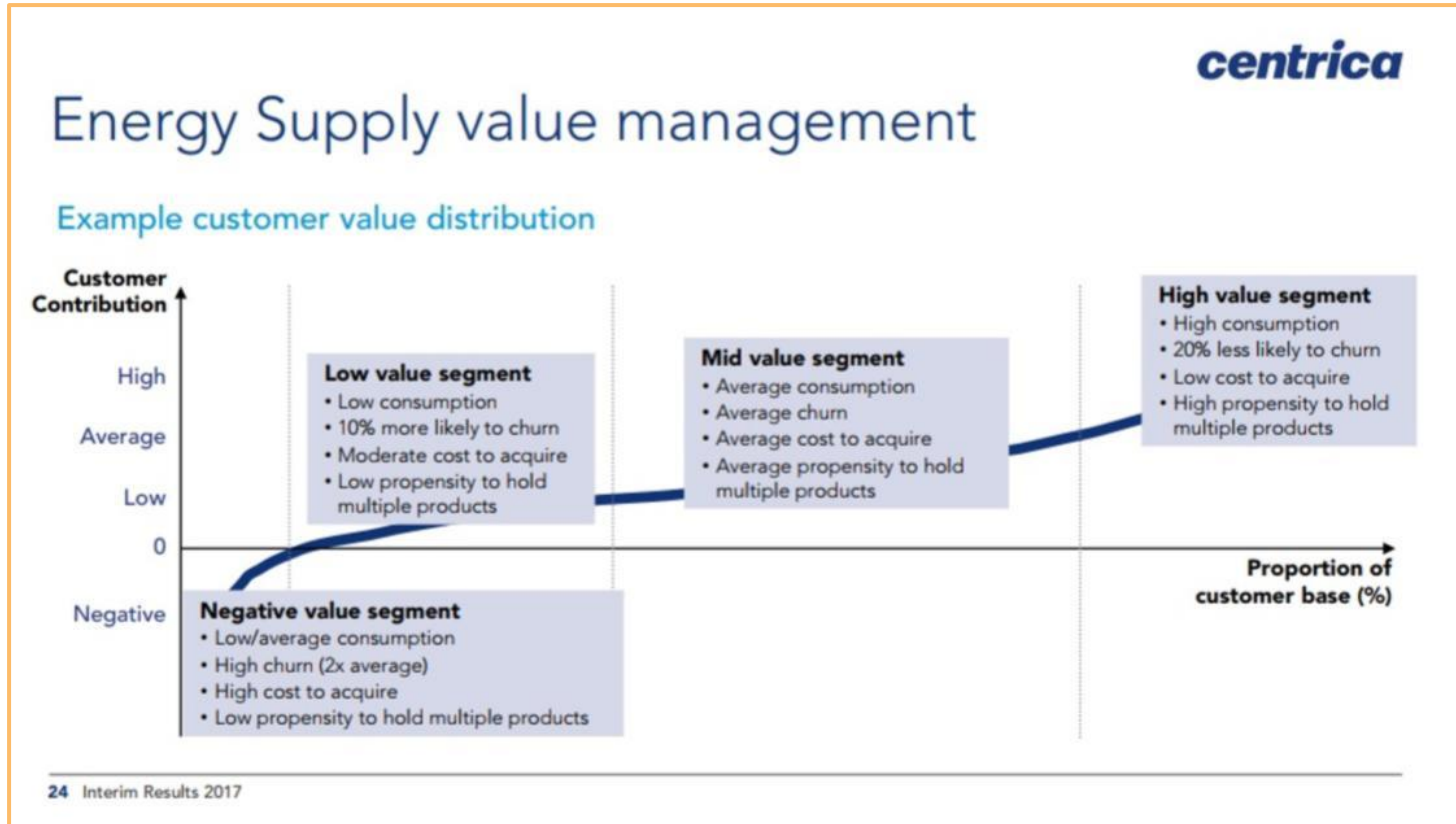


The wrong model? Why energy retail needs to change



Richard Hall
Chief Energy Economist

The model going into the crisis



The wrong incentives

The ideal customer for a supplier is

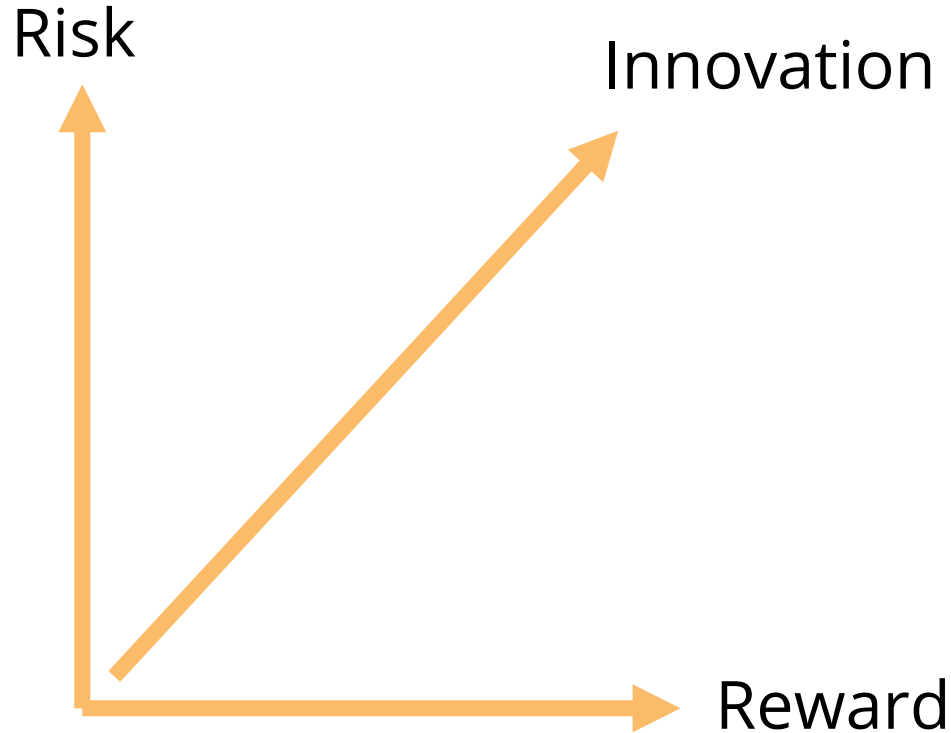
- disengaged
- high consumption

To reach net zero we need consumers to be

- engaged
- lowering or shifting their consumption

We also need to protect vulnerable consumers - who are currently disproportionately likely to be disengaged

Change requires innovation



“So scrap the price cap”

The price cap isn't the problem:

- The sector wasn't any more innovative when we didn't have one
- Ofgem's 2.4% margin isn't far short of the historical fully merchant 4%
- Public and political appetite for large supplier profits has never been there
 - And if it wasn't there in an era of £1,200 bills, it's not going to be there in an era of £2,000 bills.

The real problem is that the public good and the private good are currently badly aligned. The solution is to align them.

Better aligned incentives

The most healthy evolutionary path rests in energy services

- “Hardware”. Eg insulation, heat pumps
- “Software”. Eg demand response, flexibility services

If consumers are profiting from their relationship with suppliers - paying less, getting paid to be flexible, or simply living more comfortably, they are more likely to tolerate supplier profitability. It also boosts the incentives to engage

But these markets will have to be inclusive. The vulnerable have most to gain. And we don't get to net zero if we don't bring everyone with us

How that might look

Dual markets, co-existing:

- A boring, low innovation, low margin plain vanilla supply market selling baseline Kwhs
- A higher margin, higher innovation market selling energy services

Meter splitting may enable this

Suppliers, I have good news & bad news:

- The good: your pre-existing relationships with consumers give you some advantages in serving both markets
- The bad: there's no reason why energy services can't be delivered by someone else. You snooze, you lose

How that might look (2)

A fundamental challenge:

- We need everyone to move on net zero, not just some people
- We need the market to serve everyone, including the most vulnerable

Access to upfront capital, and borrowing costs are major constraints to household investment

- The market will have a role in solving that, but the government needs to play a role too. Likely in upfront financing, regulating to ensure inclusiveness

Affordability is a major problem, and sadly an enduring one

- Better targeted price support for the vulnerable is needed

Thank you

Richard Hall

richard.hall@citizensadvice.org.uk

