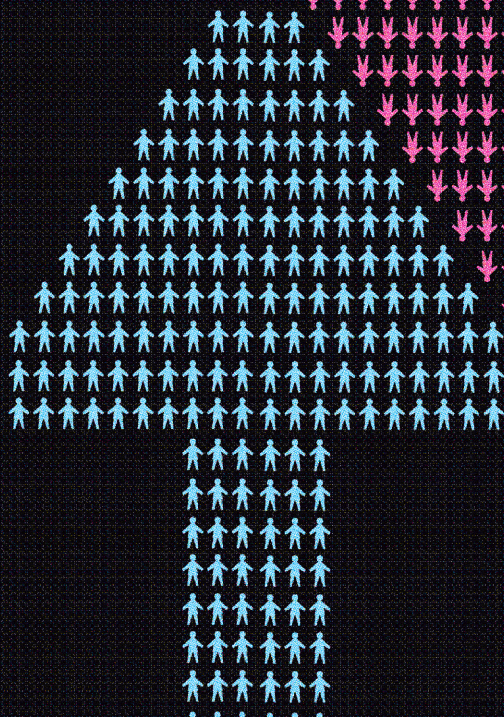


Despite reports of low customer switching levels, the reality is that 75 per cent of gas and power users have embraced competition • By Peter Franklin.

Changing booms



On the move: three out of four households connected to both energy grids have changed supplier for either or both services

Competition in gas since 1996, and in electricity since 1998, has brought with it significant change to both the nature of household purchasing and to the structure of the energy industry.

Customers used to buy their gas and electricity separately. Gas was purchased from British Gas and electricity from a local regional electricity company. From the first day that electricity and gas became available in a single package the dual fuel market came alive, with over 80 per cent of all new contracts signed in the liberalised market being joint contracts for both energy supplies. This continues to be the case today.

Industry structure has followed suit. What used to be separate electricity and gas organisations within the supply companies have become integrated within single corporate structures. The regulatory offices of Ofgas and Offer have combined into Ofgem. And British Gas has become the UK's largest supplier of electricity. We have moved a long way down the path from single product markets to an integrated energy market.

Ofgem has recently published its *Domestic Competitive Market Review (April 2004)*, which examines the changes in detail. This comprehensive and important study represents a wonderful opportunity to take stock and gauge how far we have travelled down the road to a competitive energy market.

The document itself is structured along product lines, first examining the changes that have taken place in the gas market and then analysing the changes in the electricity market. The report concludes that in both markets only 39 per cent of consumers have switched supplier, including switchbacks.

This was recently reported in the *The Times* as 'six out of ten gas and electricity customers have not switched supplier'. But is this a fair reflection of how households have embraced competition? The answer, perhaps surprisingly, is an emphatic 'no'.

EnStra has analysed Ofgem's figures from an energy rather than single product perspective and concludes that only 5.5 million households out of the 21 million who have both a

gas and electricity supply have failed to embrace the competitive market (see chart, below). That is to say that three out of four households have taken the opportunity to switch. Energy competition has penetrated UK society much more than the Ofgem report would suggest.

So how can it be the case that Ofgem reports, quite correctly, that 61 per cent of electricity and gas customers have not switched – and that 74 per cent of dual-energy households have embraced competition. The answer is twofold.

First, it is erroneous, in our opinion, to classify a household that has decided to move its electricity to its gas supplier, or vice versa, as a 'non-switcher'. This is what happens if you look at the market from a single fuel perspective. It is our view that if a household changes the way it buys its energy, be that taking both fuels from one of the ex-incumbents or from a third party, it has embraced the competitive market opportunity.

Second, there are five million households that do not have the opportunity to purchase a dual fuel contract since they are not connected to the gas network. Given that electricity-only deals are much less attractive than dual fuel, and given the remote location of these households and hence lack of door-to-door sales presence, we believe switch rates will be much lower in this segment of the market (we assumed 20 per cent) leading, arithmetically, to higher switch rates in the 21 million households who have the opportunity to purchase a dual fuel contract.

So both sets of numbers are right – and consistent with each other. However, the right view of the extent of competition is that the overwhelming majority (about 75 per cent) of households attached to both energy grids (themselves accounting for more than 80 per cent of UK households) have embraced competition so far. Across the market as a whole (all 26 million households) rather than 60 per cent having missed out on competition, 60 per cent have taken the plunge and taken advantage of the competitive energy market. A truly remarkable transformation. ■

● Peter Franklin is director of EnStra Energy Strategies, a provider of specialist analytical services and consulting support to the retail energy sector. For more information on the analysis, see www.enstra.com/documents.

