NEGative: How the National Energy Guarantee fails Australians

The Federal Government and The Council of Australia Governments will meet on Friday to determine the future of the Turnbull Government's National Energy Guarantee (NEG). Australia's largest industry research company, IBISWorld, expects that the NEG would fail to accomplish its proposed goals and do little to improve the energy sector or reduce carbon emissions beyond what is already expected to occur.

The National Energy Guarantee has been promoted as the most comprehensive change to the National Electricity Market since its creation in 1998. The Turnbull government hopes that the NEG will end the energy and climate policy wars that have raged since the Rudd Government attempted to introduce an emissions trading scheme in 2010.

The first goal of the NEG is to ensure that sufficient dispatchable power is always available to the grid, which will minimise power prices and prevent blackouts in peak periods. The second goal of the NEG is to ensure that Australia meets its climate obligations as set out in the Paris Agreement. Finally, the NEG seeks to restore certainty to the private sector, which has become hesitant to invest in energy infrastructure due to the frequent changes in government policy over the last decade.

By targeting reforms at the National Electricity Market, which includes all of Australia except for WA and NT, the NEG hopes to secure a collaborative policy approach which will be suitable to the state and territory governments. However, IBISWorld analysis suggests that structural flaws in the NEG will prevent it from meeting its objectives.

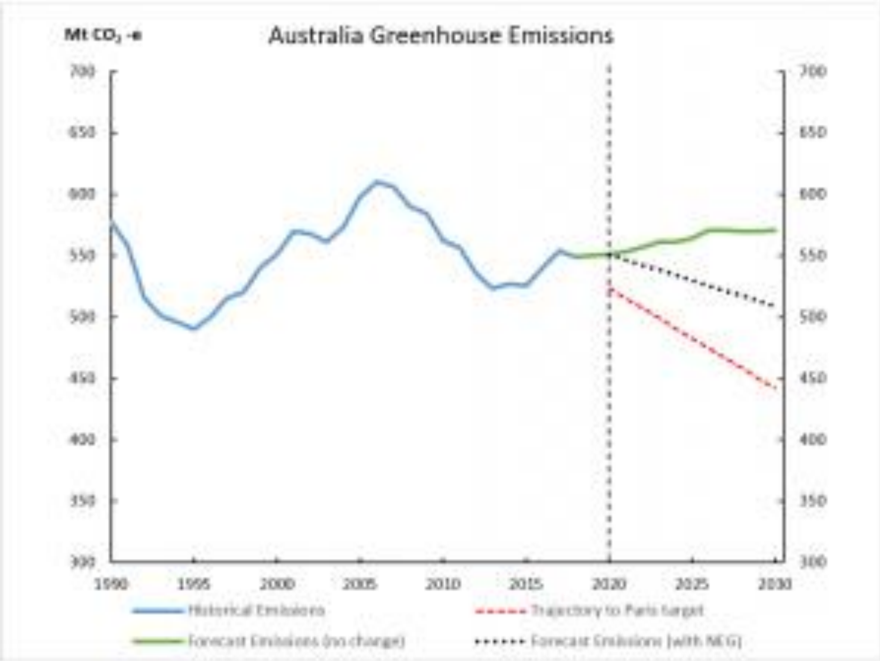
Climate control

To reach the target set out by the Paris Agreement, Australia must produce less than 4,800 million tonnes of greenhouse gas emissions between 2021 and 2030. However, IBISWorld expects that Australia will produce close to 5,650 million tonnes of greenhouse gas emissions during this period. Therefore, Australia needs to implement policies that will reduce expected emissions by at least 850 million tonnes between 2021 and 2030.

According to IBISWorld Senior Industry Analyst Jason Aravanis, "it is surprising within this context that the NEG's own modelling states that it will only reduce emissions by 44 million tonnes, or 5% of the economy-wide requirement. As electricity emissions account for 31% of total emissions from the economy, the Turnbull government's policies implicitly assume that other sectors will cut emissions at a far greater rate than previously required".

"Cutting emissions from other sectors, such as agriculture, mining, or manufacturing is far more expensive and is likely to be both politically and practically difficult. Should this obligation be foisted upon operators in these sectors, it could significantly increase costs in industries such as **beef cattle farming, iron ore mining,** and **iron and steel forging** among many others", said Mr. Aravanis.

"Despite the burden it places on these industries, the NEG will not do much to reduce emissions beyond what is already expected to occur. The pre-exiting Renewable Energy Target (RET) is set to reduce emissions by 24% from 2005 levels by 2021. The NEG target of reducing emissions by 26% by 2030 suggests that the government expects the NEG to cause hardly any additional reduction in emissions from 2021 to 2030", said Mr. Aravanis.



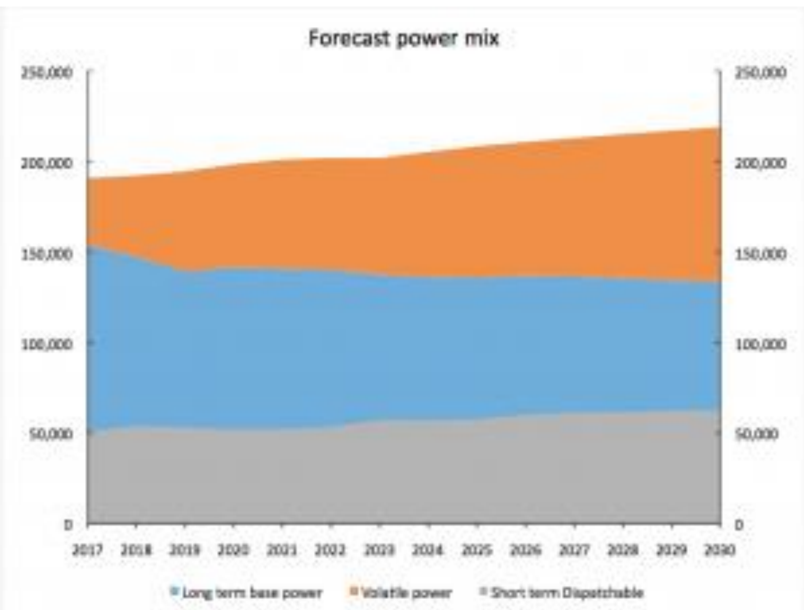
Source: IBISWORLD and Department of Environment and Energy

Energy reliability and price reduction

Base power from coal plants currently dominates The National Energy Market, and gas and hydro sources contribute a smaller share of quickly dispatchable power. Other sources, such as wind and solar infrastructure, are producing a growing share of Australia's energy.

"Renewable energy is typically intermittent, as the wind isn't always blowing and the sun isn't always shining. This means that as the uptake of renewables continues, more dispatchable power is required to prevent blackouts and keep the grid stable", said Mr. Aravanis.

To ensure the stability of the grid, the NEG will force operators in the **Electricity Retailing** industry to make a proportion of electricity from dispatchable sources available, in accordance with the Australian Energy Market Operator (AEMO).

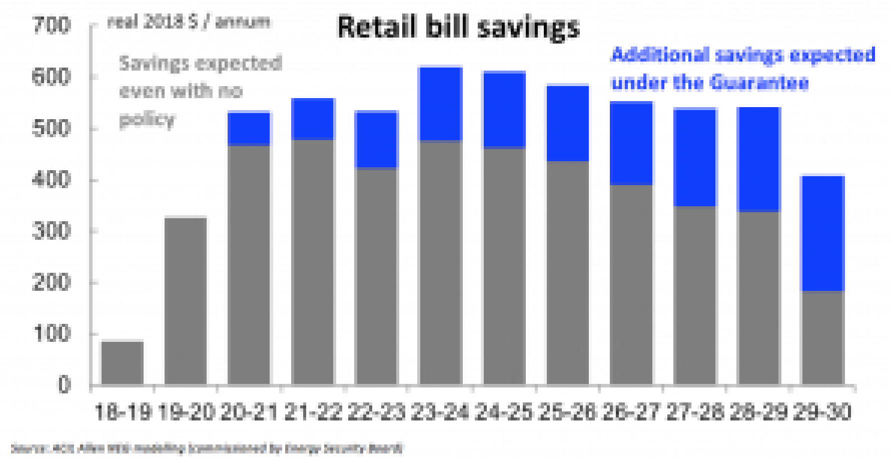


Mr. Aravanis explains that this approach has several critical flaws. “First, according to AEMO forecasts, the entire National Energy Market will easily avoid energy shortages over the next decade, meaning that the NEG reliability guarantee is unnecessary. The reliability guarantee is only likely to increase overhead costs for electricity retailers, and increase energy prices for consumers.

Second, imposing this reliability obligation on retailers, rather than generators, is similar to making car dealerships responsible for the emissions of the cars they sell, rather than car manufacturers. Most similar economies regulate generators as this makes regulation easier to implement, monitor, and adjust. Only France has a similar system to the NEG, and this system took over seven years to implement correctly.

Third, the NEG itself is highly unlikely to reduce power prices. The implicit assumption of the NEG is that spot market prices will fall as electricity retailers increasingly use contracted electricity, eventually reducing consumer prices. However, NEG modelling presents very little evidence that this will occur.

It is difficult to imagine how a reliability guarantee, which the AEMO suggests won’t even be activated, would incentivise retailers to lower prices. The activation of 5,300 megawatts of new power generation assets over the next two years is likely to more directly influence pricing but this would not be as a result of the NEG”.



Making amends with the private sector

The NEG will lock in energy and climate policy mechanisms. The government hopes that this will remove uncertainty for private investors who may be afraid that a new government could significantly change energy policy.

“As private sector confidence is restored, private investment in energy infrastructure may increase and the associated risk premiums associated with these projects may fall. This could support the **wind and other electricity generation, hydro-electricity generation,** and **electricity transmission** industries”, said Mr. Aravanis.

IBISWorld expects that the NEG will do very little to improve investor confidence. The ongoing fight over energy and climate policy reflects deep-seated disagreement on the aim, emissions reduction, rather than the methods by which it is achieved.

"The universal panning of the NEG by both coal supporters and environmental activists shows that the NEG does nothing to resolve this conflict. In addition, attempts to make the NEG immune to future amendments by a Labour federal government are likely to smother any chance of the NEG passing through both the COAG meeting this week, and through the federal senate later this year", said Mr. Aravanis.

IBISWorld Conclusion

According to IBISWorld, The National Energy Guarantee fails on all of the three main goals it aims to achieve, and does little to help the energy sector or the environment.

"Although household electricity prices are expected to fall, this is not as a result of the NEG. Ongoing failure to address the imminent and critical changes to the energy landscape in Australia will result in greater pain for the entire economy", said Mr. Aravanis.

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