

Pile on the **savings**

If you wait till the dying weeks of your energy supply contracts before re-negotiating, you're almost certainly missing a trick. Paddy Baker explains how market changes have increased buyer power

Since the supply market was opened up in the 1990s, energy managers have typically re-negotiated a few weeks before the end of their contract periods – in July or August for a contract beginning in October. "If you work like that, you will get badly stung," says Christopher Lydiard-Wilson, CEO of EnergyQuote, an online energy procurement company. "You'll pay a significantly higher price, with an ever-increasing differential over what you could be paying. It's unavoidable."

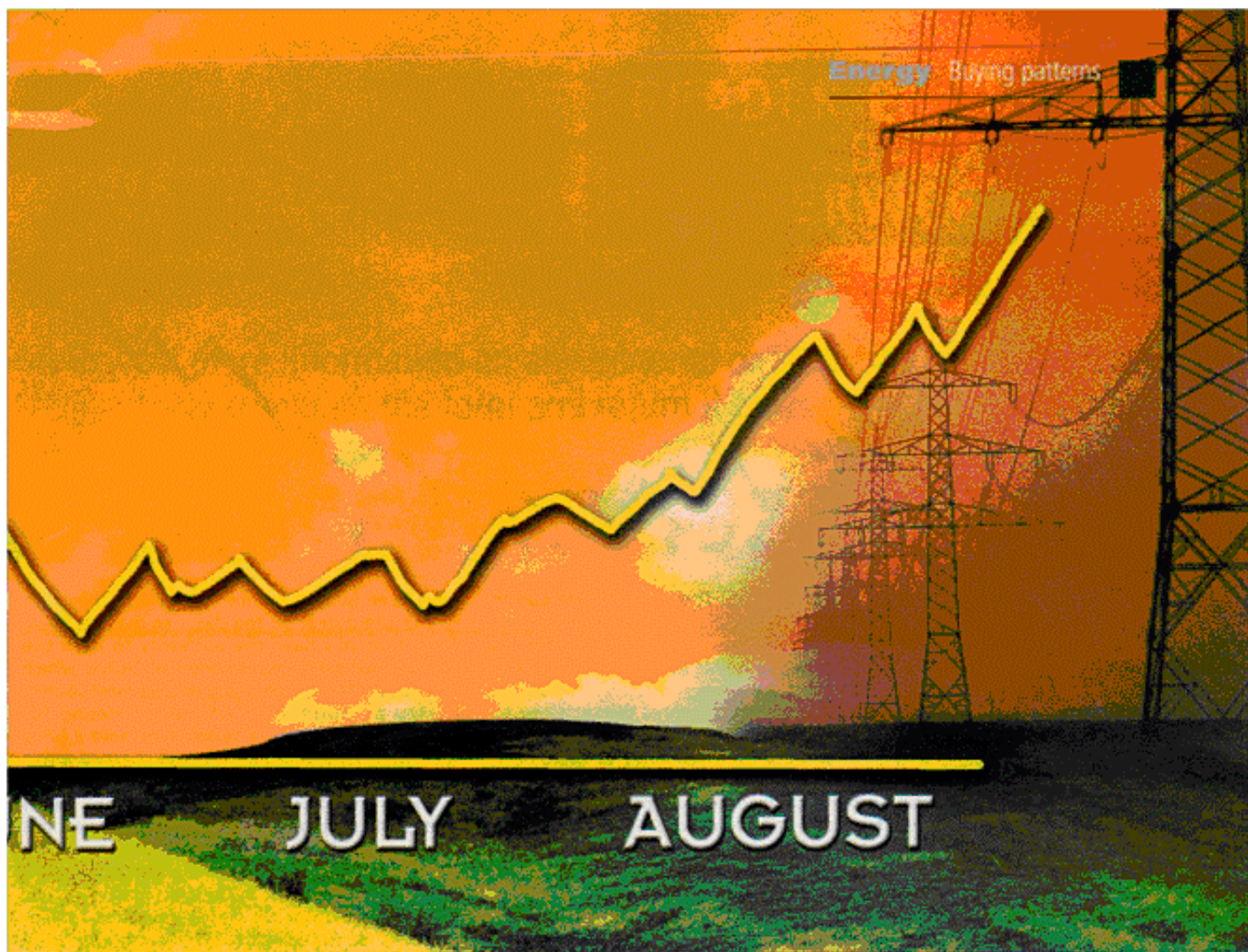
Chris Bowden, CEO of electronic energy trading platform Utiyix offers a similar message. The old way of working is, he says, "like shopping in a department store on Oxford Street on Christmas Eve – you'll get poor service, and you're unlikely to find a bargain."

They would say that, wouldn't they, you

might argue. But there are sound, market-based reasons why energy buyers can increasingly benefit from the services of companies like these.

Here's a recent history lesson. When the energy markets were deregulated, they were set up with a non-vertically integrated structure: the generating companies acted as wholesalers, selling gas or electricity to the regional gas or electricity companies (effectively retailers), who sold it to consumers – businesses and households. This situation has now changed: "There's no generator, apart from British Energy, that doesn't have a retail arm," says Lydiard-Wilson. "So they are all looking at balancing wholesale and retail demand." In the case of gas supply, there's a third leg to the market, as gas can be sold to or bought from mainland Europe through the interconnector.

The other important development has been



the introduction of NETA – the New Electricity Trading Arrangements – in March 2001. When launching NETA, then Energy Minister Peter Hain described the previous arrangement, called the Pool, as “deeply flawed – it was effectively a means of generators setting a wholesale price which suppliers and large consumers had little choice but to accept. It was no better than a generators’ club.”

Incidentally, it was the previous market structure that many observers blame for the well-publicised financial difficulties of energy companies British Energy and TXU. With the market working in favour of electricity generators, “building power stations was a licence to print money,” says Lydiard-Wilson. But too many power stations were built, leading to a massive oversupply in the market, and a fall in prices. “We reached the lowest ever wholesale electricity price last year. There is a chronic oversupply of electricity in this country – 32 per cent supply over use,” he explains. The market price fell below the cost of generation for some power stations – so they were losing money on every kilowatt they generated. He therefore believes that the losses made by certain energy companies were “a natural consequence of any market where there is a chronic oversupply.”

Decommissioning power stations is not a straightforward process, so the legacy of the Pool will remain for some time. But at least the way prices are set has moved on. Under NETA the mar-

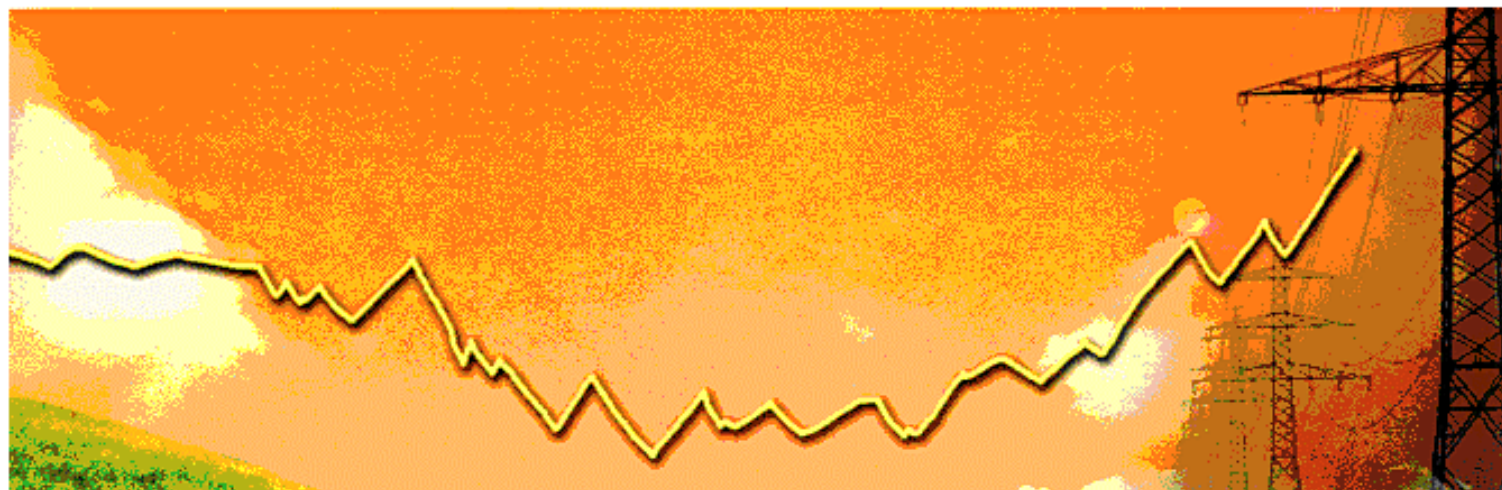
ket operates like most commodity markets, with forward prices that change constantly. This means that, while most energy users have yearly contract periods that run from October (see box overleaf), they can renegotiate these at any time – taking advantage of favourable forward prices. This simply wasn’t possible before. “Pre-NETA, if I tried to get a price early, this was ahead of negotiations between wholesalers and suppliers, so they didn’t have prices to give,” says Lydiard-Wilson.

Being able to renegotiate contracts when they wish represents both a challenge and an opportunity to manufacturers that use energy in any quantity. With energy buying typically just one of any number of responsibilities for the relevant person within the company (regardless of whether he or she is a dedicated energy manager), it would be a massive challenge for a busy manufacturer to keep tabs constantly on how the

You can take advantage of falls in energy prices by renegotiating your supply contracts early

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market is performing. The opportunity comes from the fact that specialist companies exist to do this, and offer their assistance to their customers in renegotiating contracts at the right time and the right price.

These companies offer three things: access to suppliers and their price information; IT systems that can handle the complexities of customers' consumption profiles, suppliers' tariff structures and, in some cases, online auctions; and people with the skills and knowledge to deal with risk management, energy buying and negotiation. One of EnergyQuote's offerings is access to its systems but not its skillset, so that energy managers can benefit from its data and IT infrastructure without worrying that they are making their own skills redundant.

Obviously, these specialist energy brokers need to make enough of a saving for their own fees to be covered. EnergyQuote has carried out a study of deals it has struck over the past six years, and found that it saved its customers an average of six per cent compared with prices they were able to negotiate themselves. "That shows we're adding value – if you spend £2m a year on energy, that's a saving of £120,000 annually," says Lydiard-Wilson.

Because the market is so fluid, buyers have to be able to make quick decisions once they

have been quoted a price. "You need to be able to execute a deal on the day – so make sure up front that you have the authority to push the 'accept' button," says Bowden of Utilyx, which claims to offer the UK's largest and most sophisticated platform for electronic tendering for energy. "If you want a supplier to hold a price for five days, you're likely to get charged a five per cent premium."

The British Ceramic Confederation, which represents around 250 ceramics companies, has recommended Utilyx to its members, which comprise around 18 per cent of the UK gas market. David Beardsworth, BCC's technical director, explains that Utilyx has mostly benefited companies that did not want to deal directly with utility suppliers. "For those companies who approach their annual negotiations with trepidation and fear, it's been very useful," he says.

Utilyx can host online reverse auctions for its customers' contracts. One of these was building products company Marley, which carried out an online auction covering 21 UK sites in a single day. A purchasing team assembled at a single site monitored the auction, using PC spreadsheets from Utilyx that enabled them to compare bids with the current energy costs for their locations. The 11 electricity suppliers that took part made a total of over 200 bid responses between 9:30 and 5:00. As the bids came in, they were analysed in seconds and presented with like-for-like rankings. The end result was contracts that cut a six-figure sum off Marley's total electricity costs.

A final thought: even if your existing supplier offers you a good deal to sign up again, it's still worth looking around for a better deal. Bowden explains: "If the incumbent supplier says to you, 'you're currently paying 4p per unit for electricity, I'll drop it to 3.5p', he knows it sounds impressive. But this is easy to do in a falling market. Many companies have been suckered into extending their contracts in this way. Energy suppliers are making huge margins on captive clients because they're not going out to tender." ■

Why October?

The various market deregulations all began in April of different years, so contracts tended to begin from this month. Then, says Christopher Lydiard-Wilson of EnergyQuote, "someone looking for a competitive edge worked out that if they gave a price for 18 months, this would have two summer periods" – so they could give a lower average price than before. Next time around, though, the trick doesn't work: "Once you get to October, there's the reverse effect – two winter periods, making the price highly unattractive. So people who had taken on an 18-month contract switched back to yearly – so there's no way out of October," he adds.

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