



Selling Gas Distribution in a Competitive Market

The VECTOR team

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Focus of this presentation

- The threshold question the Commission must address is:
are gas services supplied or acquired in markets in which competition is limited or likely to be lessened?
- VECTOR's submission and this presentation focus on the threshold question
 - We have other issues with the draft Framework
 - Powerco and NGC have addressed them and we mostly agree with their approach
 - We will address other issues in cross submissions
- The evidence shows that competition is not limited in the Auckland marketplace (differs from Airfields Inquiry)
- The Commission should proceed further only in markets where competition is limited



Overview of presentation

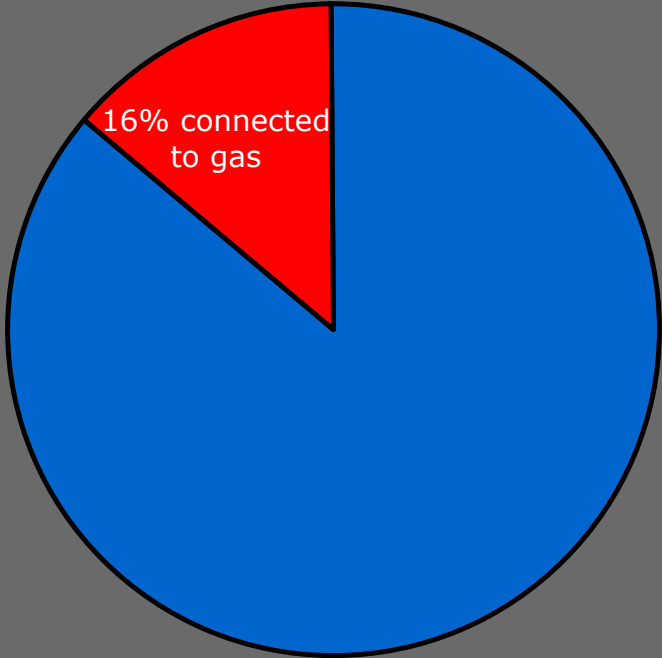
- The realities of our market
- Residential
 - Features
 - Choices
 - Challenges
 - Consumer perceptions
 - How VECTOR competes
- Commercial/industrial
 - Features
 - Choices
 - Challenges
 - How VECTOR competes
 - Examples of competitive activity
- Summary
- Next steps



The realities of our market

The realities of our market

Total Auckland households and businesses

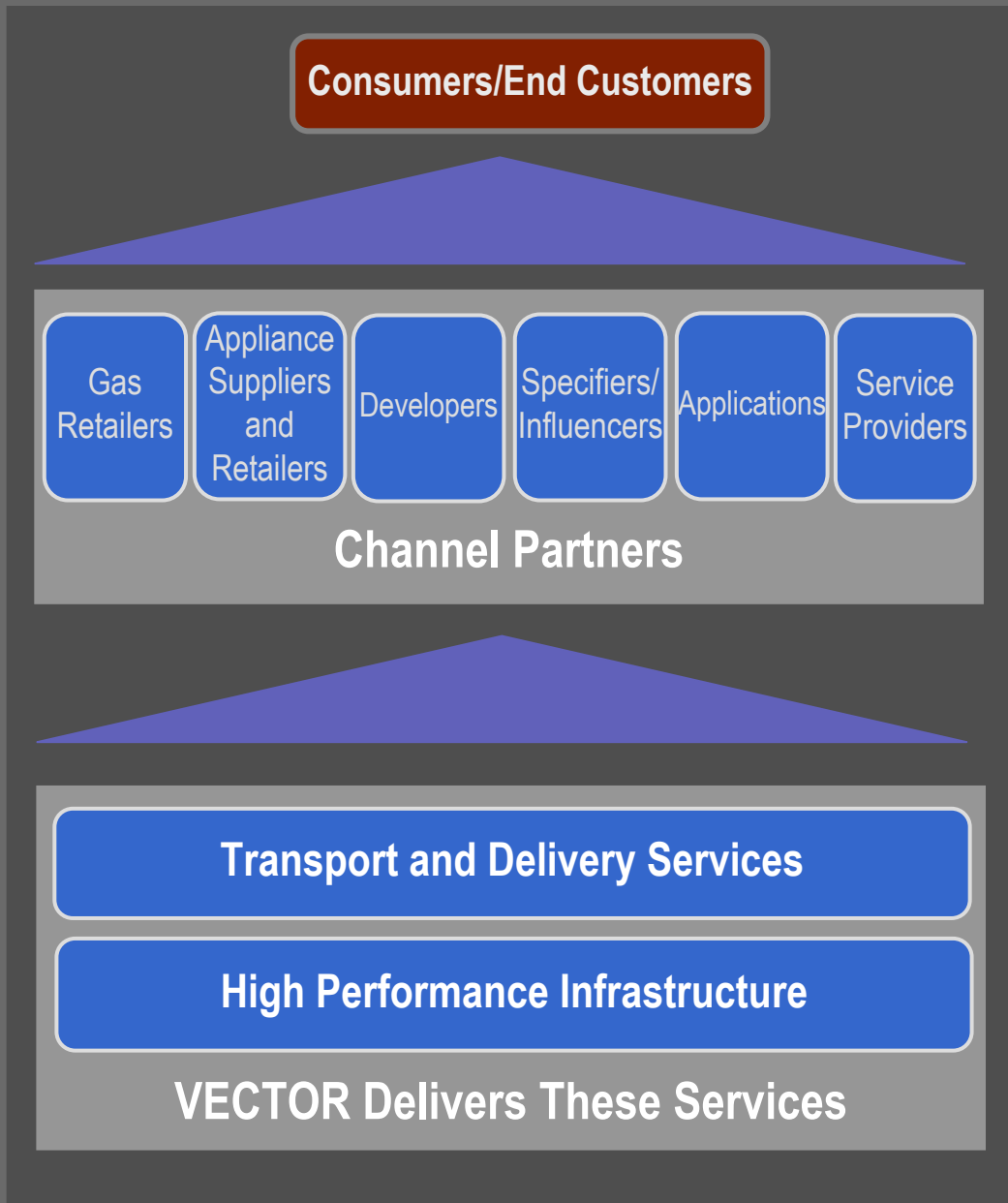


The realities of our market

- Demand for gas distribution is derived from the choices consumers make
- Consumers have a number of choices:
 - Electricity
 - Natural gas
 - LPG
 - Diesel
 - Coal
 - Wood
 - Solar
- The market will tell you that these choices are real

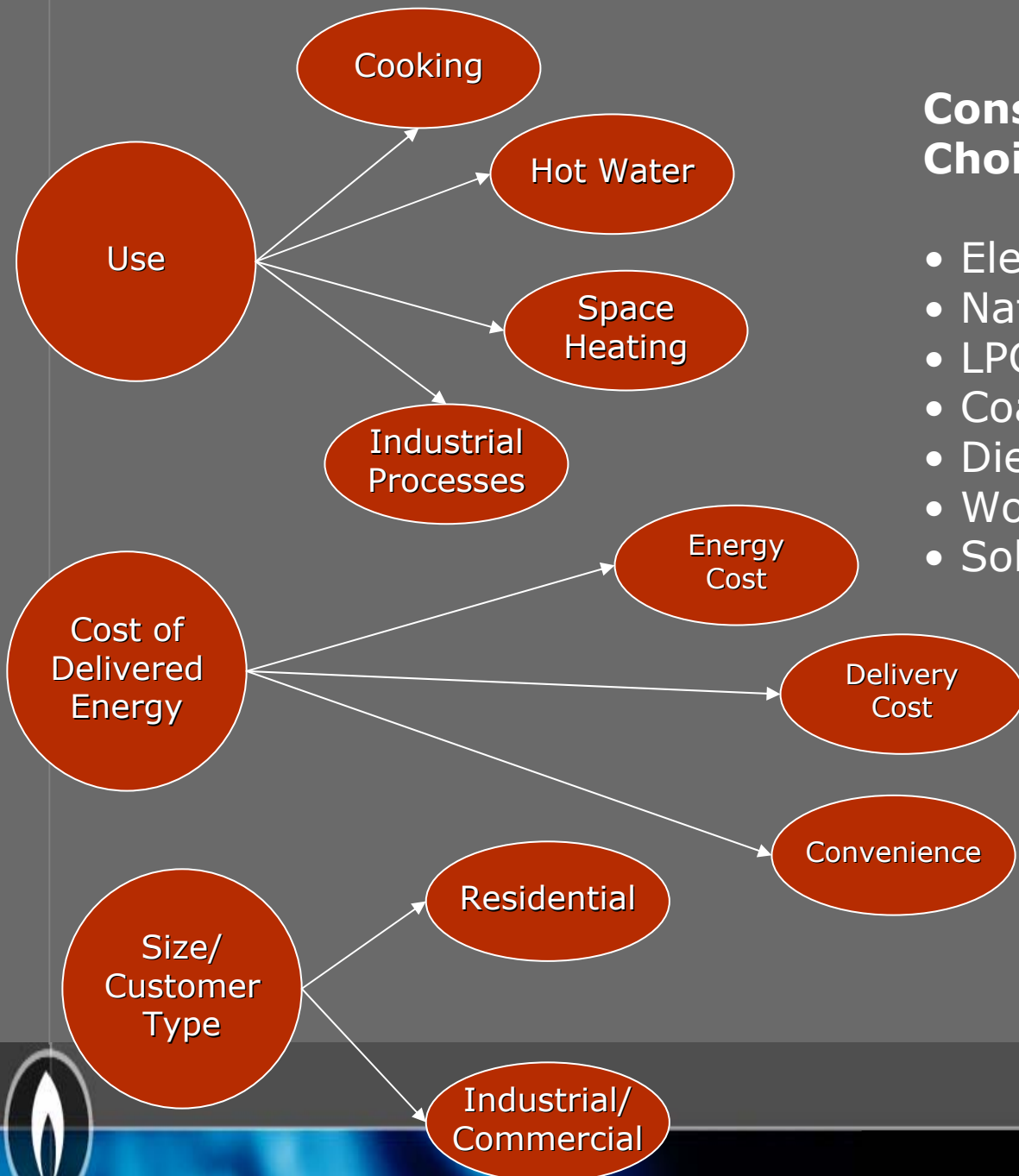


The gas channel



The realities of our market

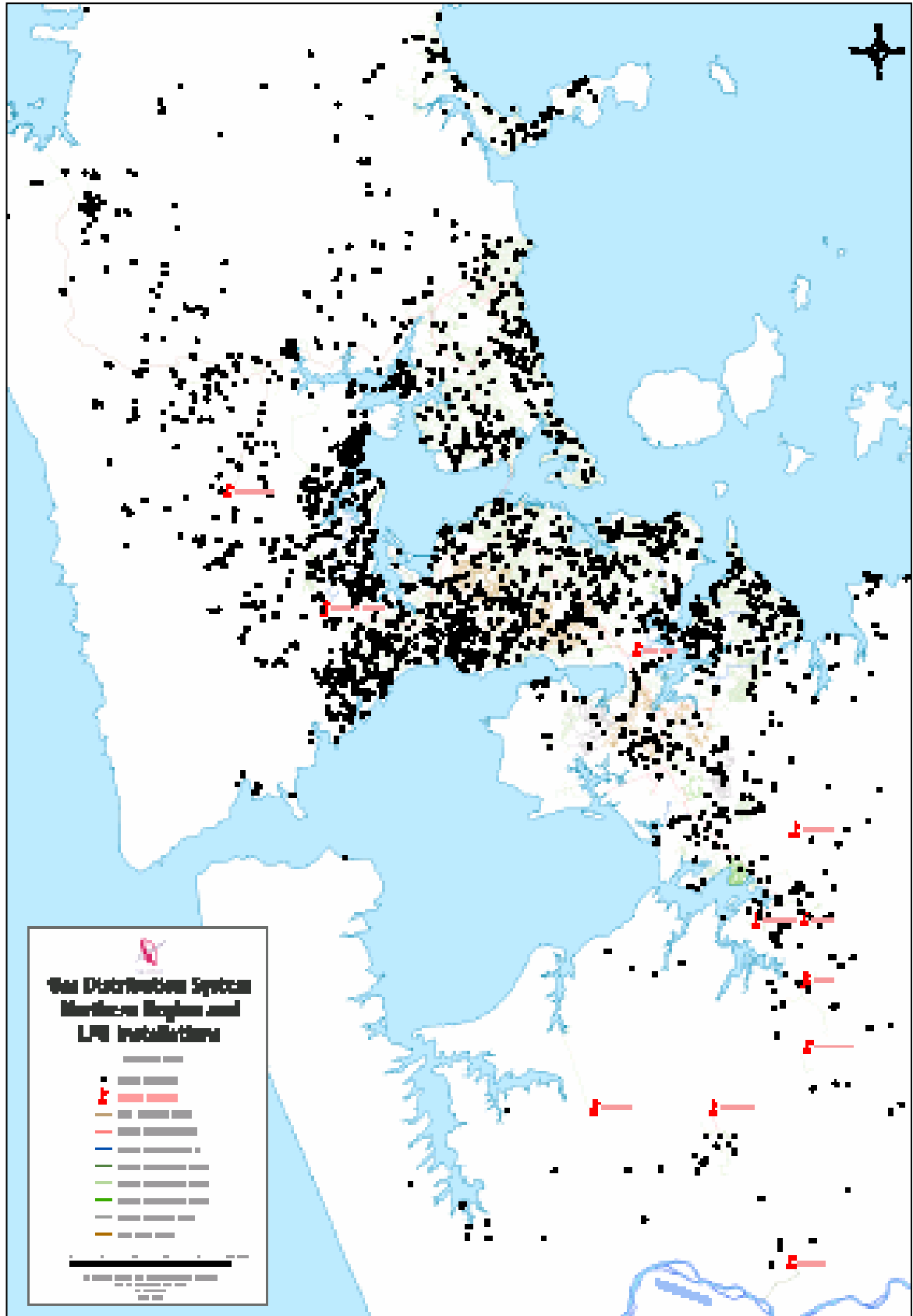
A consumer's choice will vary depending on:



Consumer's Choice

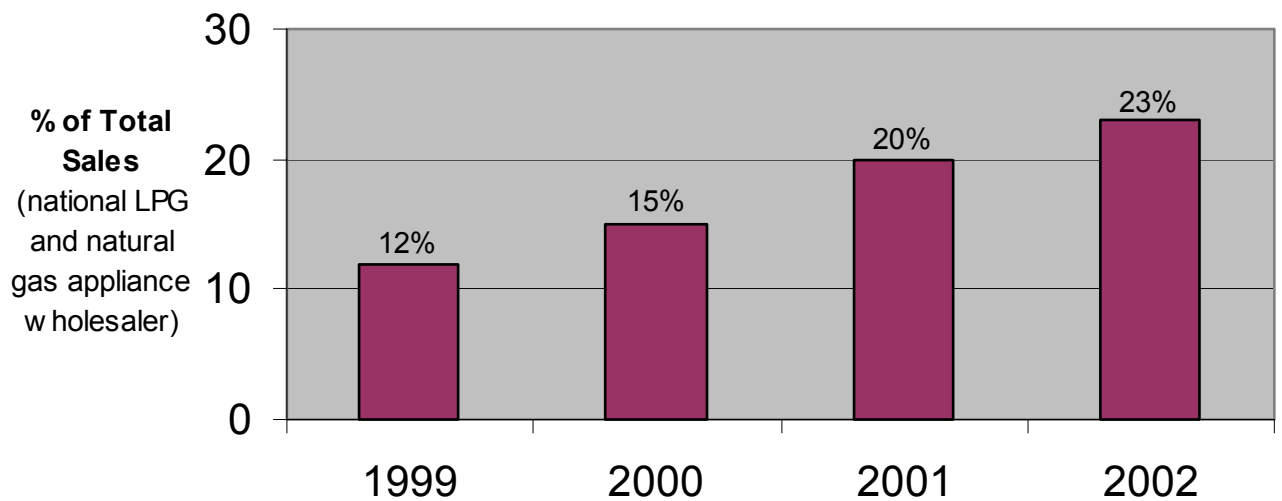
- Electricity
- Natural Gas
- LPG
- Coal
- Diesel
- Wood
- Solar





The realities of our market

Increase in LPG Penetration – relative to natural gas (residential)



The realities of our market

- Consumers are looking for choices – natural gas is just one of them
- Consumers also have a choice of retailer on VECTOR's networks



Residential

Residential - features

- Total Auckland homes 391,000
- Homes fronting gas network 240,000
- Number of connections 63,000
 - 16% of total
 - 26% of fronters
- Electricity connections 100%
- Of homes that are connected to VECTOR's network:
 - 1/3 have one type of usage (cooking, heating, hot water)
 - 1/3 have two types of usage
 - 1/3 have three types of usage



Residential – choices

Consumer Uses

Choices

Cooking

Natural gas
LPG
Electricity

Space Heating

Natural gas
LPG
Electricity
Wood
Coal

Water Heating

Natural gas
LPG
Electricity
Solar

Clothes Drying

Natural gas
Electricity



Residential – challenges

- Other fuels
- Low natural gas usage rates
- Upfront capital costs to connect
- 43,000 (approx) low socio economic households
- 18,000 (approx) homes not owner occupied
- Perceptions about shortage of natural gas supply
- Consumer perceptions



Residential – how VECTOR competes

- To compete against other fuels, we had to design a programme to rebuild consumer awareness and preference for natural gas
- We wanted to increase connections and load
- We identified the target audience as style/image conscious, mid-upper socio economic - with women as the key influencer
- We embarked on the Pure Energy® campaign
- These are not things that a business facing limited competition needs to do



Channel partner programme

- The programme is typical of programmes used in other competitive industries
- Channel Partners are appliance retailers – not gas exclusive
- Objectives:
 - Re-build confidence in the future of the industry
 - Re-engineer channel processes to lower administration costs and speed up connections
 - Create healthy, growing downstream business partners
 - Ensure market coverage is adequate
 - Reduce conflicting messages about gas as a fuel
- Formal “Channel Partner Agreements”
- Partners allowed to use Pure Energy® brand
- Financial incentives for new connections and new load
- Partner Development Fund
- Separate residential and commercial partners



Commercial / Industrial

Commercial/Industrial - features

- Total Auckland businesses 42,000
- Commercial/Industrial connections 4,700
- Market share 11%
- Electricity connections 100%



Commercial/industrial – choices

<u>Examples of Consumer Type</u>	<u>Uses</u>	<u>Choices</u>
Hospitals	Cooking, Space Heating, Hot Water, Incineration	Electricity LPG Coal
Horticultural	Heating	Diesel
Manufacturing	Process Heating	Natural Gas
Hospitality	Cooking, Hot Water, Space Heating	
Hotels	Cooking, Hot Water, Space Heating	
Prisons	Cooking, Hot Water, Space Heating	
Schools	Space and Water Heating	
Leisure (eg. swimming pools)	Space and Water Heating	
Commercial & Drycleaning	Water Heating, Steam Raising	



Commercial/industrial – challenges

- Upfront capital costs
- Consumers driven by costs
- Other fuels (including new technologies)
- Larger consumers have more options (eg coal, diesel)
- By-pass networks – actual and threatened
- Perceptions about shortage of gas supply
- Sustainability of businesses



Commercial/industrial – how VECTOR competes

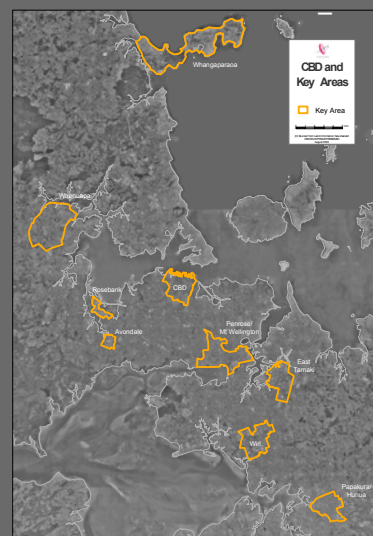
- VECTOR has to influence consumer choice
- VECTOR deals directly with small number of larger customers:
 - to improve transparency of pricing
 - to strengthen our competitive position relative to retailers that also compete in distribution
- VECTOR has developed a commercial Channel Partner Programme



Commercial/industrial - examples of competitive activity

Whangaparaoa

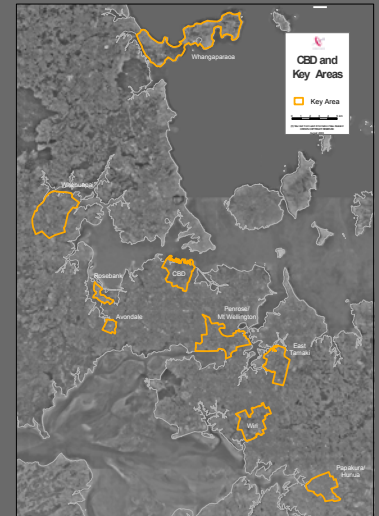
- High growth commercial and residential
- VECTOR and NGC operate pipelines side by side
- NGC's network linked to transmission line at Waitoki
- VECTOR's network is islanded, supplied with CNG tankers
- Many consumers in Whangaparaoa have a choice of gas networks – as well as fuel choices



Commercial/industrial - examples of competitive activity

Auckland CBD

- Intensive commercial and some industrial activity
- Example of competitive activity
 - converted Greenlane and Auckland Hospitals from coal to gas
 - Auckland Hospital included a co-generation scheme
 - VECTOR won the contract



Commercial/industrial - a cogeneration opportunity

North Shore

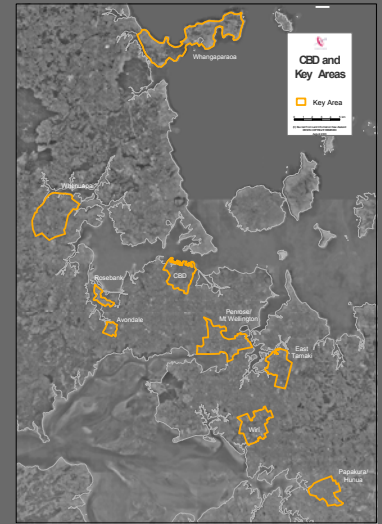
- U S based firm with satellite production agency in Auckland
- Replacement of a boiler gave rise to cogen opportunity, 600 – 800 kW
- Package needed to be internationally competitive for firm to stay



Commercial/industrial - examples of competitive activity

Penrose Industrial Hub

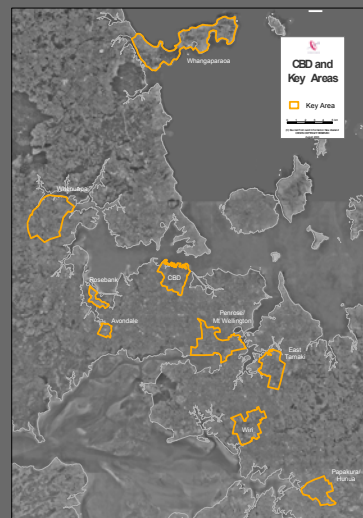
- Largely industrial and commercial
- Example of competitive activity:
 - large industrial “Customer A” expanding
 - supply agreement terminated in March 2003
 - line charge agreement offered and accepted
 - threat of by-pass due to proximity to the gate station



Commercial/industrial - examples of competitive activity

South Auckland Industrial Sectors

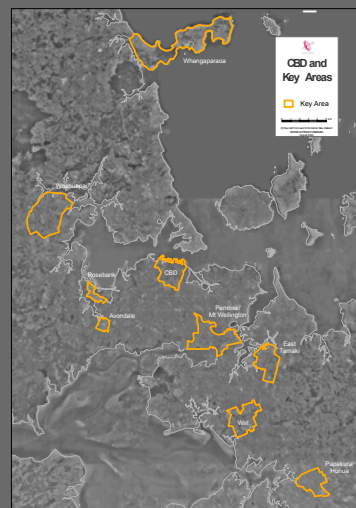
- Largely industrial and commercial
- Example of competitive activity:
 - industrial "Customer B" line charge contract expired May 2003
 - Contact Energy "sold" customer to Nova Gas
 - Nova Gas successful, based on delivered price
 - customer disconnected from network July 2003



Commercial/industrial - examples of competitive activity

Hunua/Pukekohe

- Horticulture, agriculture and industrial area
- An example of competitive activity:
 - glasshouse operator in South Auckland
 - VECTOR competed with NGC distribution
 - NGC retail asked for prices from both businesses
 - NGC distribution was successful
 - three new sites with total load of over 300 TJ involved



Conclusion

- Demand for VECTOR's gas distribution service is derived from consumer choices of energy type and mode of delivery.
- Residential and commercial/industrial consumers have a number of energy choices for uses that involve natural gas.
- Within gas energy types, most appliances can be readily switched between LPG and natural gas.
- VECTOR competes with other gas distributors in most areas.
- VECTOR's gas business is small, underdeveloped and immature – only 16% of Auckland households and businesses use the service.
- VECTOR concludes competition is not limited for gas distribution services in the Auckland region.



Next steps

- The first stage of the Inquiry must focus on whether competition is limited.
- The Inquiry should proceed further only in relation to markets where competition is found to be limited.
- The Commission needs to establish a robust process to undertake this competition test, including engagement with the industry.

