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Giant machine powering east coast degrading

After debating about how to run it for more than a decade, the giant machine that provides electricity to the east coast of Australia continues to slowly degrade. Higher prices are a market signalling supply shortages. The threat of blackouts is the next logical warning of what happens when we manage to argue about a problem for so long without doing anything.

Remarkably, while one of the fundamental systems needed to run the economy falters, we remain trapped in an ideological debate about how to fix it; the merits of different fuel types, the nature of policy risk, climate change and even how much life is left in old power stations.

You can now bet on what will happen to Liddell power station and which state is likely to go black first. If we haven't hit peak-stupid on national energy policy, we must be awfully close by now.

The solution to energy policy in Australia hasn't changed in a decade and, at a strategic level, it isn't complicated. We need two things: adequate investment and access to energy resources. The nature of this investment and these resources will then be guided by what investors can and will back, framed by the usual suspects of commercial decision making: risk versus return.

There are multiple risks. New technologies threaten to strand or undermine the value of incumbents. Solar and wind are now the cheapest form of new electricity generation. Battery developers are promising similar disruption.

Electricity demand is no longer certain or predictable. Setting aside LNG processing, industrial demand for electricity is already in decline. Household demand is also falling.

Fuel prices can and will vary, as will the cost risk of greenhouse emissions. This is not something that governments get to choose anymore. Ignoring climate policy only increases the cost of managing this risk to investors. Better to monetise it so that this investment risk is reduced.

These risks are offset by higher wholesale prices, at least in the short run, and the relatively predictable cycle of further generator closures in the future. Efficient national energy policy doesn't want, or need, to pick the solutions. It needs to enable investment to pick what gets the best returns. This ends up being the cheapest solution too.

The cost of energy to consumers will be cheaper if all energy sources are more abundant. This applies to both conventional fuels like gas and coal and new energy sources like wind and sun. Bans and moratoria on energy development in regional Australia have helped push up energy bills.

Planning around energy resources requires a more considered approach, that reflects local conditions and the importance of the assets rather than political ideology. Banning wind farms, gas development or new coal mines pushes up prices for consumers.

Investment in these resources depends on their ability to get returns. We export the majority of our coal and gas, which is crucial to sustaining the health of the Australian economy. Better planning and resource access enables these markets to adjust to shifts in demand in a timely fashion.

Some coal-fired generators in NSW are struggling to source enough extra coal to meet the extra demand imposed following the closure of Hazelwood Power Station in Victoria.

The coal supply system in NSW is constrained and finely balanced. It cannot suddenly produce a few extra hundred thousand tonnes of coal each year without warning or planning.

Through all of this, the National Electricity Market is working as designed. It is signalling scarcity and dispatching generation efficiently. It can and does run a major grid in South Australia every day where half the power comes from wind and solar.

The chronic blackouts in that state were caused by a combination of extraordinary weather and inexperience in handling that scale of intermittent generation in a critical situation.

Despite all the political blame shifting on energy prices, there is little to suggest either the retail or wholesale markets are at fault.

Competitive retail energy markets are evolving but will be a crucial part of the 21st-century grid. There are now more competitors in both markets than ever before.

Earlier this year Professor Alan Finkel proposed a set of recommendations to fix the energy crisis. They remain an effective blueprint for reform. Whatever we do, a workable solution will need to do two things: remove risk to enable investment and enable access to more and cheaper energy resources.

Matthew Warren is the CEO of the Australian Energy Council.

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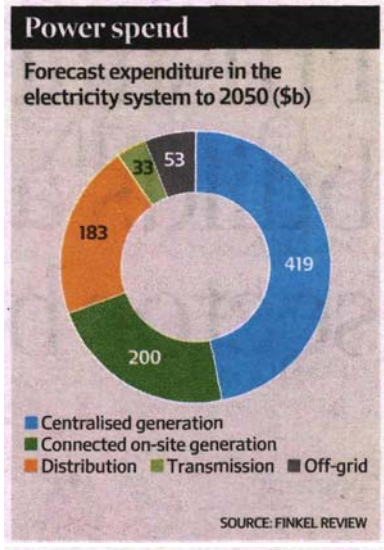

Renewables such as wind and solar are now among the cheaper forms of new electricity generation. Battery developers are promising similar disruption.