

Small is Efficient in the Electricity Sector

Just like supermarket chains, [business electricity](#) retail is dominated by a few major players who share some 96% of the total market. However, rather than compete head-on for market share, they appear only compete for a small percentage of customers at the peripherals.

They attract these new customers from each other by offering competitive 'new customer only' introductory rates, quickly reverting to standard rates (and sometimes more), when contracts roll-over after the first year or so. These practices are not dissimilar to the loss-leaders used by supermarkets to attract customers into the store where they are likely to spend much more on non-discounted goods.

Although showing very similar market structures now, these sectors got to this position in very different ways. The grocery sector was originally fragmented with no major players really dominating until the emergence of supermarket chains. Whereas, electricity was monopolised by regional suppliers and de-regulation simply served to reduce the number of suppliers still further, encouraging competition only amongst each other nationwide.

On one hand we have a market which was previously competitive with many suppliers that have been squeezed by ever-increasing concentration. So much so that the top three supermarket chains now have over 50% of the total market, with the market leader alone claiming 30%. On the other hand you have a market where efforts to expand the number of suppliers have been stifled by the barriers to entry and the sheer power of the incumbent suppliers.

The jury is out on the positive or negative effects of supermarket dominance, however, whatever the rights or wrongs of where we are now, no one can deny that those who now dominate have arrived at their position through their own efforts and ingenuity.

But electricity is a different matter. Power has been bestowed upon the 'big six' major suppliers such as British Gas, Powergen and Npower to name a few, irrespective of who actually owns them today. And one might argue that power which has been gained in such a way reduces the drive or even the necessity to compete to win.

Evidence suggests that in the 90% or so of the business that don't switch year on year price patterns for each supplier are extremely similar. One major player makes a marginal price move and the others simply follow over time.

The argument which supports the view that supermarkets actually create competition and push prices down by their huge economies of scale and purchasing power is also one which is somewhat lost in the electricity arena. Many would view the big six as inefficient legacies of the old system who are protected from real competition by the extremely tough barriers of entry.

Indeed, some of those smaller suppliers who have managed to scale these barriers have been able to demonstrate far more efficiencies aided by intelligent investment in technology. Unlike the supermarkets, there are no real efficiencies related to scale as most electricity retailers must turn to the same wholesale market for their supply. Some can cushion any market turmoil by relying on their up-stream activities when the retail market gets tough – a luxury which is simply not an option for the smaller supplier.

But businesses needn't switch to the smaller supplier out of sympathy nor from fear of what might lie around the corner should the major players succeed in driving them out completely. They should switch simply because they are now able to get a much better deal and a deal with longevity. The smaller supplier with a plan to mimic the big six in order to attract new customers would be committing commercial suicide. What would be the point of fighting so hard to win new business and then letting it slip away at renewal?

Businesses can save significant amounts of money by switching to the smaller independent supplier now and can relax in the knowledge that they will continue to save money and receive an exemplary service into the bargain. Only then will the big players be forced to sit up and take note and who knows, we might just see the emergence of a truly competitive electricity sector in the future.

About the Author

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