THE NORWEGIAN POWER INDUSTRY'S REPUTATION IN A DEREGULATED MARKET

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ABSTRACT

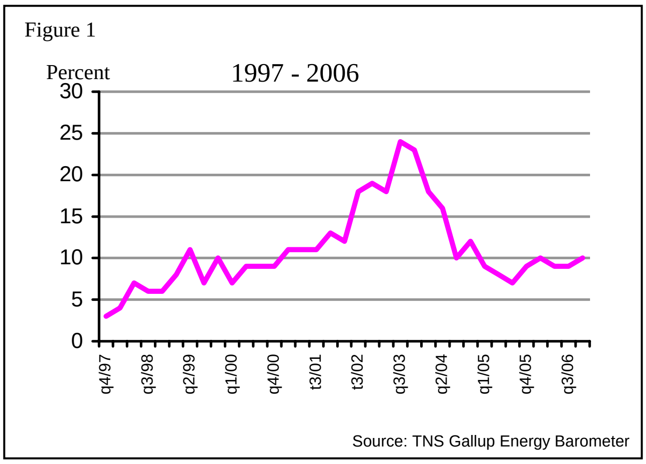
To what extent has the deregulation of the Norwegian power market affected the behaviour of Norwegian electricity customers and their attitudes towards the Norwegian power sector? This article will focus on the switching behaviour of consumers and their confidence in the industry. Experiences from the Norwegian market will provide insight into and an understanding of what challenges deregulation may present in other markets.

INTRODUCTION

The Norwegian power market has been deregulated since the early 1990s. When the amendments to the Energy Act entered into force on 1 January 1991 we had a free market in principle. However, the electricity customers had to pay a fee if they wanted to switch their supplier until as late as 1997. It was not until this fee was eliminated that we could really talk about a genuinely free power market in Norway. This article will take a closer look at what has happened during the period from 1997 to 2007.

BEHAVIOURAL CHANGES AS A RESULT OF MARKETING CAMPAIGNS

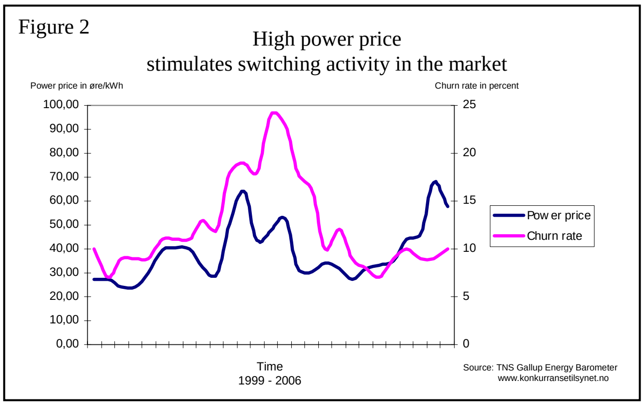
The initial period after deregulation was marked by a lack of knowledge among consumers as to what rights they had to switch from their power supplier. The few customers who did know about their opportunities did not see what advantages changing their supplier would bring. The suppliers were, for their part, not very interested in informing the customers about what opportunities they had to switch. This marked the situation until the spring of 1998 when Statoil wanted to establish itself as a power supplier in the Norwegian market. Statoil already had a strong position as a supplier of heating oil, paraffin, petrol and diesel. Electricity would give Statoil a complete range of products for the consumer market, One Stop Energy Shopping. Statoil had broad experience in marketing, a well-known brand name, and a good distribution organisation. A direct marketing campaign, initially aimed at 900,000 of its own customers, and somewhat later at an additional 1.3 million households, really got the market going. During the first campaign the percentage of households that had switched their power supplier doubled from 3.5% to around 7% (see figure 1). If Statoil had not invested so heavily, it is not very likely that the switching activity in the market would have accelerated the way it did. Statoil emerged as a threat to the established power companies. A handful of power companies accepted Statoil's challenge and launched their own nationwide campaigns, partly to protect their own customers, and partly to compensate for the loss of customers who had chosen another supplier.



Switching activity: Percentage of household customers who have changed their power supplier during last 12 months.

SWITCHING ACTIVITY AS A RESULT OF PRICE

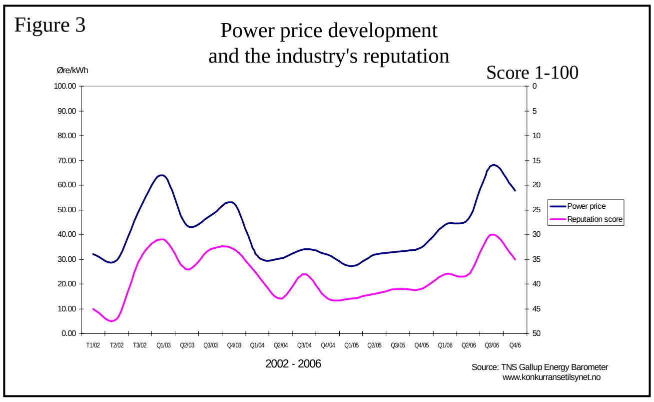
The marketing activities affected awareness of the individual companies and the percentage who switched their power companies. However, the power price levels in the market and the price gaps between the suppliers had a significantly greater impact. Figure 2 illustrates the percentage who switched their power supplier during the last 12 months and the development of the power prices. These curves followed each other all the way until the third quarter of 2005, and they indicate that high power prices stimulate switching activity in the market. When the prices increase, the customers become more aware and concerned about their household budgets. However, it may also be that the switching activity is stimulated by the price gaps between the various suppliers. Our studies show that the price gap between the suppliers is greatest during the period just before and after a price increase. The reason for this is the fact that some companies hold back their prices, either to attract new customers in a market with rising prices or to compensate for bad purchases in a market with declining prices. We also find a clear increase in the switching tendency during such periods, probably because the consumers see that there is a lot to gain by changing their supplier. The results show that large price differences in the market, high power prices, and a heightened switching tendency are three events that often coincide.



Percentage of household customers who have changed their power supplier during the last 12 months and power price development.

RELATIONSHIP BETWEEN THE PRICE OF POWER AND THE REPUTATION OF THE POWER INDUSTRY

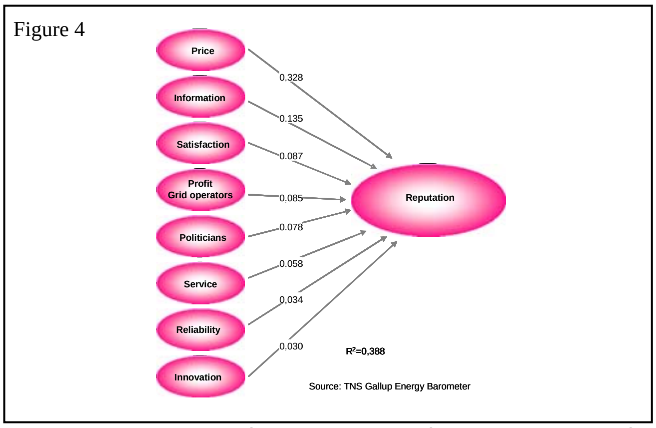
The Norwegian power industry has experienced two critical periods of failing confidence. The first time was in 2002/03, the next time was in 2006. Both of these periods were marked by high power prices as a result of a limited supply and high demand for power. Empirically we know that price is very important with respect to the consumers' impression of the power industry and the level of satisfaction with their own power supply. This is evident in figure 3, which illustrates the development of power prices and the electricity customers' overall impression of the power industry. The scale for the reputation score is reversed and shows that the power industry's reputation is weakened when power prices rise.



High prices weaken the reputation of the power industry.

DRIVERS FOR THE REPUTATION OF THE POWER INDUSTRY

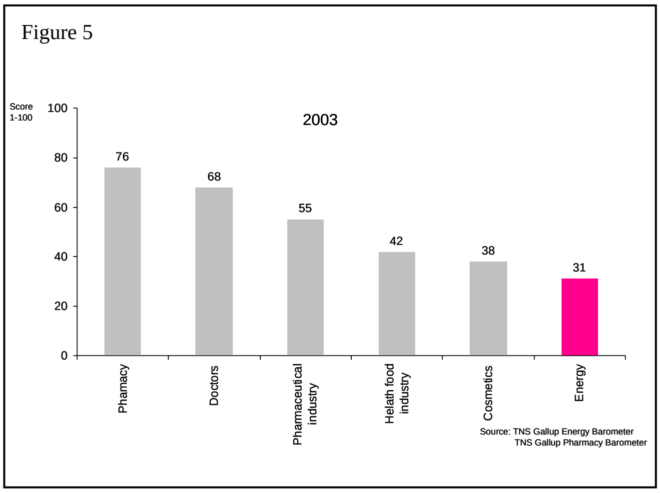
Of the eight reputation elements we have measured and followed over time, *price* is the most influential element for what impression the consumers have of the power industry overall (see figure 4). *Price* has a regression coefficient of 0.382. There is a large gap down to the next, *Information*, which has a regression coefficient of 0.135. The other variables are all below 0.1. This shows that the price the customers pay, as well as what and how the industry communicates, are the factors that primarily determine whether the customers have confidence in the Norwegian power industry or not.



Power price is most influential element for the reputation of the power industry

NORWEGIAN POWER INDUSTRY'S REPUTATION COMPARED TO OTHER INDUSTRIES

Confidence in the Norwegian power industry is low, lower than all the other industries we have measured. Figure 5 illustrates a comparison made in 2003. The power industry had a reputation score of 31 out of 100 possible points. The greatest confidence was in pharmacies, which scored 76. The study's most sensational finding, however, was the fact that the population had significantly greater confidence in the cosmetics industry than the nation's power supply.



There is little confidence in the Norwegian power industry compared to the other industries TNS Gallup has measured.

In September 2006 we compared the consumers' confidence in the Norwegian oil sector to the Norwegian power industry. At this point in time the reputation index for the two industries differed by 26 points. (Oil sector 56, power industry 30). The survey also revealed that consumers had significantly greater acceptance for the oil industry making a profit. This reinforces our earlier surveys showing that good results have a negative effect on the reputation of the Norwegian power industry. Comments from the Norwegian electricity customers, such as: *"Hydropower is a gift to the people", "We have worked hard for this for ages", "Hydropower belongs to the people", "This is our heritage"*, (Source: TNS Gallup Energy Barometer), indicate that Norwegian consumers have very special expectations to power suppliers and what households should pay for energy. While hydropower is a *gift*, oil emerges as a *source of wealth* for the Norwegian people.

ANALYSIS OF THE SITUATION

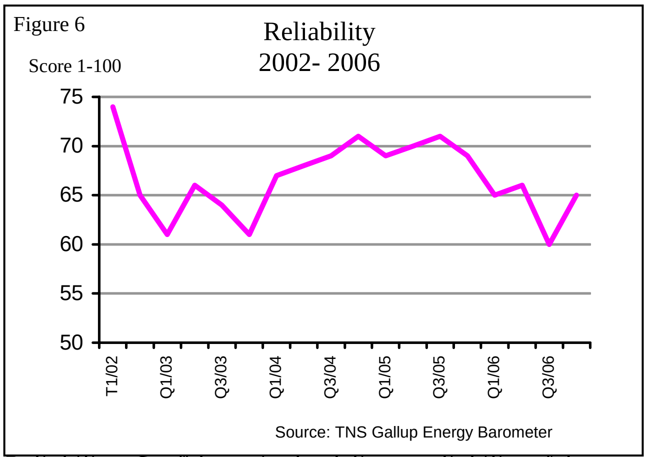
To understand the crisis of confidence in the Norwegian power sector, one must know that hydropower is Norwegians' only source of electricity, it has been key to the country's industrialisation and the growth of its prosperity and hydropower has been cheap – almost free compared with other countries. These are some of the reasons why there has been massive resistance to allowing foreign investors in on the ownership side for ages.

Traditions

In Norway the local power supplier is regarded as an important social institution. Over 40% feel strong loyalty towards their local power supplier. For many people, loyalty is a barrier to investigating and changing to another supplier. This strong loyalty is based on attitudes that the supplier contributes to maintaining and assuring the supply, at the same time as it provides tax-based welfare. Tradition and inherited customer relationships also strengthened this loyalty. It is important to bear in mind that this loyalty is based primarily on tradition and not satisfaction.

A price-sensitive industry

The production of electricity in Norway is based almost exclusively on hydropower. Periods of little precipitation result in high power prices. This was the direct cause of the crisis of confidence that occurred in the winter of 2002/03. The amount of precipitation in the second half of 2002 was lower than in more than 70 years. The power prices rose more than 200% during a six-month period. Due to the low inflow into Norway's water reservoirs, the industry's delivery reliability was questioned. The industry, the authorities and the consumers in particular were uncomfortable with the situation. This had an immediate impact on the consumers' confidence in the industry's delivery reliability. Figure 6 shows a significant decline in confidence in the industry's reliability from the winter of 2002 to the winter of 2003. The power industry was under hard pressure, from the politicians and consumers, and not to mention the media.



Reliability: Confidence in the delivery reliability of the power industry.

The reputation of the power industry and the consumers' confidence in the nation's politicians was at a minimum. The winter of 2002/03 went down in the history of the Norwegian power industry and gave us an important lesson. The industry's reputation index dropped nevertheless to a record low in September 2006 after a sharp increase in power prices (see figure 3, score of 30 out of 100 points). The electricity customers explained the failing confidence by unpredictability and unclear argumentation from the industry. *"The power prices fluctuate, and the reasons given by the industry vary from time to time and are adapted to the situation the companies find themselves in"*, were typical comments from the consumers. There are still many electricity customers who experience that the offers they receive from the companies change over time and that the power prices are not as favourable after some time has passed. Honesty, sincerity and the ability to be humble are some of the things the customers stated they wanted to see more of in a survey that was conducted in September 2006. It is often pointed out that it is the media and not the industry who set the agenda for debates and control the flow of information.

The situation in the autumn of 2006 resembles 2002/03 a great deal, but it is nevertheless not quite the same. When we experienced the last price peak in 2003, every fourth household switched their power supplier. In September 2006 there were no more than 9% who did the same thing (see figure 1). This may indicate that the electricity customers have become more indifferent and that it will take more than high electricity prices for them to take the trouble to switch their supplier. More information from the authorities, industry, individual companies, and through the media, should have given the electricity customers better knowledge of the market and how the prices are set. This means that more people should probably have understood that there is relatively little that distinguishes one supplier from the other over time. There must thus be factors other than price that trigger the desire to switch suppliers.

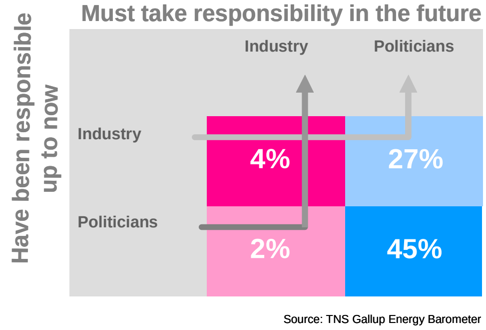
IS DEREGULATION SOLELY A BENEFIT TO CONSUMERS?

The aim of the amendment to the Energy Act that was adopted by the Storting (Norway's parliament) on 29 June 1990 was, for example, to ensure an efficient utilisation of resources, reduce costs, equalise prices, and to provide a reliable and adequate supply for our nation. For the consumers the greatest change was that they could purchase power freely from whatever supplier they desired.

We could see the effect of this legislative amendment in 2002/03. There was a limited supply of power, a marked increase in price, uncertainty about the delivery of power, and every fourth household switched their supplier. At that time 45% of the electricity customers believed that the politicians and authorities were responsible for the high power prices, and 35% believed it was the power industry, while 15% blamed others. The consumers did thus not place all the responsibility with the power industry. The politicians and authorities were blamed just as much for the extraordinary situation. When asked who would be responsible for ensuring that such a situation with high prices would not recur in the future, 75% responded the politicians and authorities. Only 13% believed that the industry itself was responsible. This could be interpreted as a desire for more government regulation of the power market. The majority believed at least that the politicians had to be clearer.

The assumptions from 2003 appear to be correct. When we asked the same questions in December 2006, there was a clear increase, from 75% to 85%, in the number of respondents who believed that the politicians and authorities had to take greater responsibility for the supply of power in Norway. Only 8% believed that the responsibility lay with the power industry. If we look at both these questions together, we find that 45% of all the consumers believe that the politicians are primarily to blame for the high prices, and that the politicians must take responsibility in the future. On the other hand, only 4% believe that the industry is primarily to blame for the high prices and that the industry must also take responsibility in the future. What is interesting, however, is the fact that 27% of all the electricity customers believe that the industry is responsible for the high prices that have occurred, but it is the politicians who must take responsibility in the future. Almost 3 out of every 10 electricity customers shift thus the responsibility from the industry to the politicians. Three years ago this number was 23%. We can thus ascertain that there has been a shift towards a desire for stronger political regulation of the market from 2003 to 2006. See figure 7. Power is a necessity, and many consumers believe that the power supply infrastructure is an infrastructure that the market should not own.

Figure 7



Almost three out of 10 electricity customers shift responsibility for the high power prices from the industry to the politicians. This can be interpreted as a desire for more government regulation of the power market.

The results may also indicate that the average Norwegian would like the state to take responsibility when things get tough. This confirms the thesis of the "state-friendliness" of the Norwegian society. Most Norwegians are used to turning to the government to solve their problems, and the government, for its part, has provided its citizens with welfare and security.

CONCLUSION

The electricity prices have risen during the period after the deregulation of the Norwegian power market, the power balance has worsened, and the reputation of the industry has declined. After the winter of 2002/03 half of the electricity customers were positive towards a liberalised market. In December 2006 this percentage had declined to 35%, and three out of five electricity customers believe that liberalisation of the power market has been of little practical relevance to them as consumers. In the words of an electricity customer: *"I do not have to choose between electricity suppliers. I am sure they will understand. There are so many other choices in life that seem more important."*

REFERENCES

[1] TNS Gallup Energy Barometer, Norway, 1997 - 2006

[2] Norwegian Competition Authority