Bad in theory, fine in practice:

an insider account of the Energy Price Cap

Giles Wilkes 9 August 2019

Around midnight one early October I found myself in a Manchester hotel room, facing a furious Chancellor (in black tie) and his aides (more slovenly), waving a draft PM conference speech containing an unexpected retail energy cap.

Perhaps he should not have been surprised — it was a manifesto commitment, after all. But "it's in the Manifesto" was not a popular argument in late 2017. The world thought the majority-less PM had no way of driving this sort of policy any more. Hence the No10 team found it remarkably easy to keep the announcement secret, including from the energy department.

The argument festered overnight and was only squared away with a further confab next morning, featuring a host of even scarier, sleep-deprived Cabinet ministers.* In the end a horrible escalation was avoided when I swore that the price cap would be temporary, while we got "the market" working properly again. So it survived collective responsibility to make it into That Speech, sadly overshadowed by the prankster, the dodgy signs and the sore throat.

This is an odd policy for me to feel any ownership towards. I inherited it — going into the election, there was another team in No10 handling energy, one that had wrestled with all sorts of batty interventions before agreeing with Greg Clark, secretary of state for BEIS, on the case for a cap. The last time I had really thought about an energy price cap, I was writing pieces mildly sneering upon the idea. There are few columns easier to write than one attacking a price intervention. Marks should be given for:

- The government cannot get the price right. Too high, and all the companies get a government-mandated bonus; too low and even the best go bust.
- Regulated prices push company efforts towards lobbying, not innovating for the customer
- Regulated prices drive away competition, which has been so great for the UK consumer — look at the number of companies! Look at the comedy animals!
- Cap the price and the consumer will just stop shopping around, having been told by the government that there is no point to it

Against this, Theresa May was definitely onto something when she railed against the iniquities of "broken markets". When the utilities were first privatised, the optimistic assumption was that the regulators would "wither away" as competition gradually took hold. By the end of Cameron's time, there were some 70 retail energy companies, price comparison sites proliferated, numberless tariffs available — and yet the ordinary punter only felt ripped off and confused. Regulators were under attack for failing at their job. The rational, self-optimising consumer was nowhere to be seen. The competing diagnoses drew on economics old and new — crimped competition, asymmetric information, behavioural biases, unevenly enforced protections — all of which added up to vulnerable customers getting a raw deal. Later work by Citizens' Advice into the "loyalty penalty"added some empirical clout to the charge.

I added my own anecdata to the case. In my first months in No10 I took on the mantle of Consumer Champion Guinea Pig, and went after all my providers. It saved me £000s on Sky, house insurance, energy, broadband and mobile. This might encourage some optimism that the market actually works. For me the experience only reinforced the case for *some* intervention. If customers like me make savings, others have to be taking a hit, and they are likely to be more vulnerable. I am at the high end of financially savvy, and yet found the process hazardous and stressful. My office got used to the tinny sound of Blue Danube as I spent hours on hold, chasing payments. One auto-switching service stuck me with one of those fly-by-night companies that owed me £1200 for months. It was a scam; if this was the market being "competitive", then being competitive is not enough.

After that Conference, we got the policy through, which meant a convoluted process of consultation, challenge, regulatory calculation, and finally the imposition of a "safeguard tariff" at the turn of 2019, calculated every six months by Ofgem. (Politicians have nothing to do with the setting of the cap.)

The obvious question remains: has it been a good idea?

First, there were political costs. There is a certain breed of auto-parodying libertarian for whom the energy cap is proof that the Tory party has lost its mind. That's a cost, though I can think of better examples of how they have gone nuts. Never mind that only 15 US states enjoy competitive retail energy , or that the Competition and Markets Authority found some favour in the idea. Investors in energy and other infrastructure often took the same primary-colours view: "Head office doesn't like the look of this", even though they were seldom directly invested in retail.

Now it's in place, what about warnings of destroying the market? Here the market-liberal whinge has proven well off the mark. Standard variable tariffs *have* dropped compared to what they would have been. Switching numbers have not fallen at all, indeed they have risen. The really innovative entrants — I rate Bulb, Ovo, Octopus, Shell/First Utility — are still strong, innovative and growing, and the loss of many of the tinier ones was probably overdue. I do not know any theory of the market that says the customer need 70 different exotically named start-ups; many were basically a big bet on what Octopus call "tease and squeeze", and too thinly capitalised to play what was a poor game for the consumer.

Much of the £1.7bn excess consumer cost was assumed not to be profit, but inefficiency: this was shown to be true, when companies responded by cutting jobs, too. This is a regrettable but near-inevitable outcome whenever an industry is reformed to be more productive.

Ultimately, both sides of the argument exaggerate. Household energy costs are around 4% of incomes, and this *might* fall 5% for those affected. Perhaps £60 a year for ten million households — worth going for, but hardly enough to transform the fortunes of the 'just about managing'.

But those getting hysterical about a grotesque invasion of the free market need to calm down. The way retail energy worked was bugging the voter. Politicians have every right to step in when things don't work for voters. More broadly, the Conservatives were overdue a big think about how they respond to markets that aren't performing. The question of what *kind* of economy we want is one for politics: Do we want to encourage markets where the greatest rewards go to those who most ruthlessly search out and retain the doziest customers?

The "one last push" free marketeers look horribly naive. Sometimes ideology represents the outcome of positive thought, at others, a symptom of its lazy absence. Expect attacks on the price cap to come from the same thoughtless voices heard calling for bonfires of red tape, without ever saying what they mean. Weirdly, the critics of the free market are far more curious and informed about how they actually perform in the real world. This agenda made more progress under May than is recognised: the Williams Review for Rail, Jason Furman's work on Digital markets, and the CMA's response to Citizens Advice for much else. But with Greg Clark and Theresa May gone, I am not sure who is left to make the intelligent case for reform.

If this one stalls or goes backwards, it would be a pity. Labour had a bad answer (nationalisation) to the wrong question (who *owns* these companies, which does not determine how they are run). The price cap was a bodge; it shouldn't have worked, but it looks like it might.

*In normal times, there is an entire Civil Service to draw upon for the trickier questions. During Conference, all its distilled knowledge is meant to reside in the form of the hapless spad. Did I mention that I hate Conference?