

Research Brief

Mass Market Energy Services – How Will Markets Develop?

Two potential scenarios and lessons from other industries

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Mass Market Energy Services – How Will Markets Develop?

This paper draws on Delta's research which is being undertaken as part of our multi-client study "Mass Market Energy Services – Strategies for Success".

Energy services provides a potential 'Golden Key' for new entrants into the energy supply market to take swathes of the energy retail market away from conventional utilities. "Never!", cry many incumbents, who believe that energy services growth will only be incremental, and that having 'Me Too' energy services offerings will be sufficient to put a padlock around their positions in the energy supply market.

This paper explores these 'Golden Key' and 'Me Too' energy services scenarios developed by Delta, illustrating them with case studies from the banking and telecoms sectors.

Competition, regulation and technology are combining to enable customers to become more engaged with energy supply into their home. If energy suppliers can capture (or even spark) this engagement, then deep customer relationships can be built based upon provision of services rather than commodities alone.

But the mix of market forces that are shaping the emerging energy services market varies across Europe – some countries are already beginning the journey, while others possibly never will. The pace and trajectory of this journey will shape the role which utilities could, and should, play in each market. Furthermore, utilities will not be alone on this journey, as new entrants eye the massive market potential.

Here, we look at two possible scenarios for how the energy services market will develop, each at opposite ends of the spectrum: 'Me Too' and the 'Golden Key'.

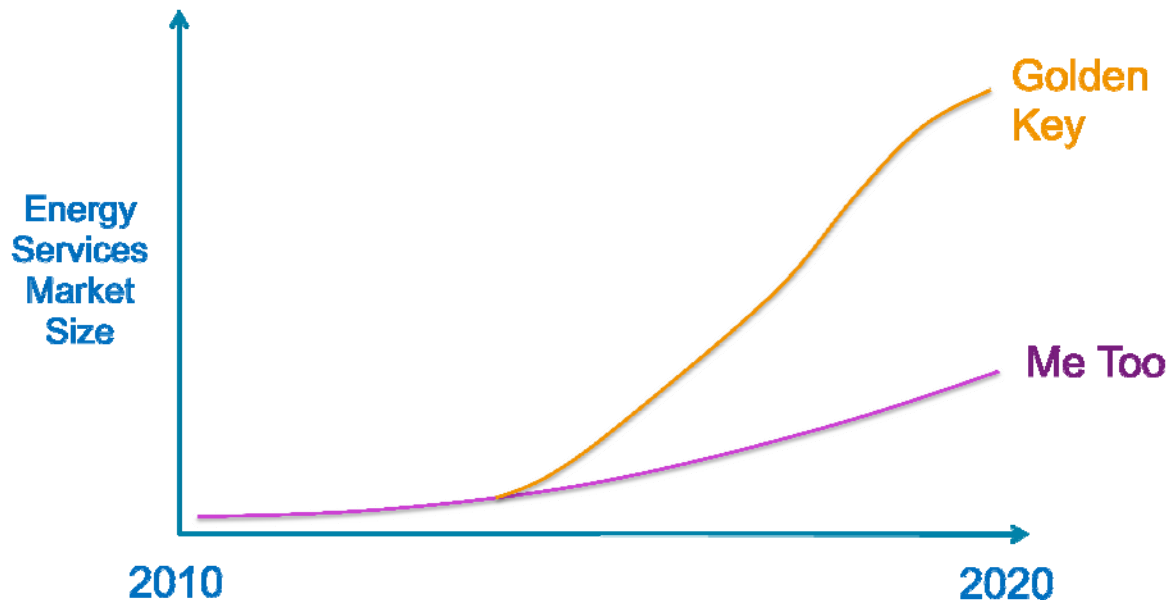
The safe utility world of 'Me Too' versus the new entrant threat of 'Golden Key'

Each market will have its own unique blend of market ingredients; from policy incentives to customer pull, from the level of retail competition to supplier obligations. But just because the policies or technologies exist doesn't mean customers will want, or be prepared to pay for, energy services, especially as the current level of customer engagement with their energy supply remains low and primarily price driven. Hence, the search for the 'killer application' or 'Golden Key' that will transform customers' engagement with their energy supply and management, putting them at the centre of a relationship that is tailored to their specific circumstances or 'wants' (as opposed to 'needs').

Without a 'Golden Key', market development may be evolutionary rather than revolutionary – a process driven by local market competition and regulatory incentives or obligations.

This leads us to two distinct scenarios, which we call:

- ▶ The 'Me Too' Scenario
- ▶ The 'Golden Key' scenario



The 'Me Too' Scenario

There will be a gradual evolution and extension of services provided by utility suppliers. This will be driven by 'Me Too' propositions with the main objective of customer retention rather than acquisition i.e. to maintain competitive positions with other utilities. New entrants may be able to use energy services to establish themselves but will not create significant market disruption.

What are the implications of this scenario for utilities from a 'Me Too' scenario? Some might be:

- ▶ Energy services is not a game changer
- ▶ First mover advantages may be limited
- ▶ Likely returns on discretionary investment will be low

Case Study: 'Me Too' - Development of Online Banking

For financial institutions, a primary factor driving the development of online banking was **competition** – banks saw it as a means of **customer retention**, and also a way of **attracting new customers**. Other factors included cost reduction and revenue enhancement through **upsell**. For customers, the attractions of 24/7 access and control are clear. However, internet banking also removed one of the significant barriers to entry for new players, i.e. real estate, and the range of potential competitors and forms of competition have increased.

In many respects, home or internet banking failed to revolutionise the financial services industry in the way many people anticipated. Banks consistently **over-estimated how much consumers really valued the convenience** of the service – and how much they were willing to pay for it. After initial successes with early adopters in the 1990s, many home banking initiatives withered for lack of interest. It was only in the last decade when **the technology caught up with the concept** and reached the point where consumers found it 'easy' (access, software and speed), and had sufficient trust (e.g. security), that online banking has at last become commonplace.

Whether banks have been able to earn an attractive return from their investment in technology platforms is uncertain. The evidence for the impact of online banking on the financial performance of banks appears mixed, although on balance banks with a strong online banking proposition in combination with other traditional channels and brands perform more strongly.

The key characteristics of Delta's 'Me Too' scenario shine through:

- ▶ New entrants (in the 1990s) providing pure online banking struggled to compete with traditional incumbents, and most had to quit the market
- ▶ Incumbents slowly adopted online banking into their business, as customer adoption gently increased
- ▶ Online banking is now a fundamental pillar of all banking business models, essential to maintaining a competitive position, despite having an uncertain return on investment

Insight for Utilities

1. **Be careful not to over-estimate the value consumers place on a service – especially if it is perceived as a 'need' rather than a 'want'**
2. **New customer propositions may give best results when combined with traditional channels and brands, giving utilities an inherent advantage over any potential new entrants**



The 'Golden Key' Scenario

In this scenario, a market player identifies the 'Golden Key', enabling them to really engage consumers by successfully transforming their 'needs' into 'wants'. Customer pull rather than supplier push drives the market. The market opportunity grows very rapidly and energy services demand takes off, with the potential for extensive market penetration.

The implications of a 'Golden Key' scenario for utilities include:

- ▶ Energy services will be a game changer – threatening utilities' position in the retail market
- ▶ First mover advantages will be crucial
- ▶ The right discretionary investment will generate attractive returns

Case Study: 'Golden Key' – Telecoms

The advent of mobile internet was heralded by mobile operators as the future of their business. But **the 'Golden Key' has consistently been developed by other players rather than the incumbent mobile operators themselves.** For example:

- ▶ Internet – firstly via WAP, then using 'walled gardens' such as Vodafone Live where the operator exerted full control over content. These failed, with mobile browsing only taking off with the introduction of smartphones.
- ▶ Email services – initially ignored as users continued to use online providers (e.g. Yahoo!), eventually bypassed by Blackberry who installed software in the handset
- ▶ Picture messaging never took off, but users now upload directly to social networking sites such as Facebook
- ▶ Group calling – hailed as a 'must have' feature by providers, but was wholly ignored in favour of Skype
- ▶ Location-based services mostly failed, but are now hugely successfully provided by Google

The mobile operators have invested hugely in the infrastructure but the real winners are the content providers, such as Apple, Google, Blackberry and Skype.

Insight for Utilities

- 1. Utilities will most likely struggle to develop the kind of applications and services that get customers really excited. Therefore, in this scenario, it is critical to identify and establish the right partnerships early, or run the risk of being bypassed.**
- 2. Customers will get what they need at the lowest available price, but will pay for what they want.**



So does the ‘Golden Key’ exist, and who is likely to find it first? The utility industry itself cannot claim to have a strong track record of customer engagement or innovation so it might appear more likely to come from outside the industry. This is a key focus for Delta’s research as we look across different global utility markets and different industry sectors such as telecoms, retail, finance and technology.

The ‘Me Too’ and ‘Golden Key’ scenarios for an Energy Services market have vastly different implications for the strategic and tactical decisions that market players should make:

- ▶ In a ‘Me Too’ market, energy services provision may be a critical tool for customer retention, but generating a sufficient return from discretionary investment will be challenging. Being the pace setter is not a significant advantage – but staying close to your competitors and anticipating market developments is crucial.
- ▶ In a ‘Golden Key’ market, energy services provision can drive customer acquisition and be profitable as customers are drawn to the offerings. Being the pace setter is a significant advantage. If they are not, utilities risk losing valuable relationships with customers and becoming purely commodity suppliers, while new entrants capture the ongoing and high margin revenues from energy services. Partnership strategies and tactics are crucial.

Delta’s multi-client study analyses country markets and competitive landscapes, mapping markets into scenarios such as those described in this paper. We evaluate how different utilities are positioned to succeed, and the potential impact of new entrants in their markets.

About The Delta Multi-Client Study

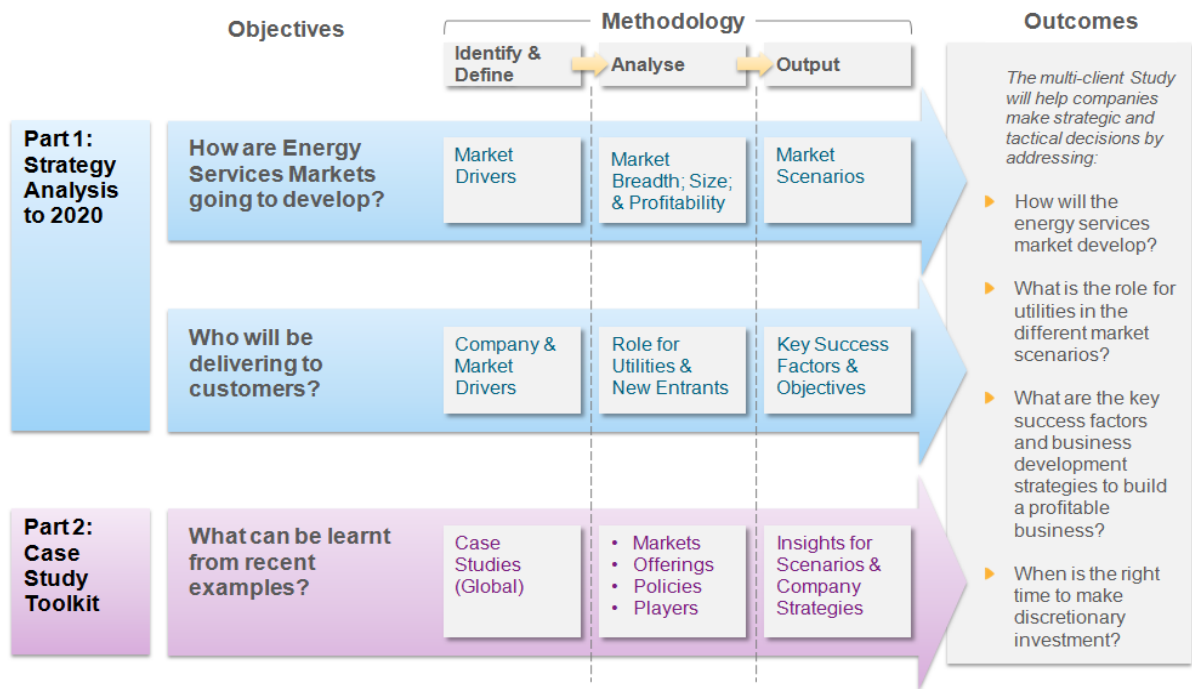
“Mass Market Energy Services – Strategies For Success”

The Study will provide you with detailed, objective information on recent developments and initiatives relevant for your market. Different market scenarios will be identified and developed, with insight into the criteria for winners for each scenario, including how to build a profitable business that matches your local market. Developed for European energy companies, it will analyse competitors, including the threat from new entrants.

The Study will help subscribers answer the following questions:

- ▶ **How will the energy services market develop?**
- ▶ **What is the role for utilities in the different market scenarios?**
- ▶ **What are the key success factors and business development strategies to build a profitable business?**
- ▶ **When is the right time to make discretionary investment?**

The study consists of two discreet parts, which combine to provide subscribers with the necessary insight to help answer these difficult questions, as outlined below.



The direction of travel is clear: mass market energy services are set to become an important business for utilities in the future, whether or not they decide to actively play in them. And for those that decide to participate, the challenge is to identify the blueprint that not only incorporates the key ingredients of success but also creates a profitable business that is flexible enough to respond to uncertainties in policy, technology and customer attitudes.

Study Deliverables

- ▶ **Summary & Conclusions:** a concise and easy-to-share presentation (Powerpoint format)
- ▶ **Part 1 Strategy Analysis to 2020:** a Word format report detailing the analysis and conclusions for markets, companies and strategy development.
- ▶ **Part 2 Case Study Toolkit:** the Case Studies and analysis will be an online resource, in Word and/or Powerpoint format, hosted on a secure part of our website.
- ▶ **Online Resource:** all study deliverables – including data and forecasts in spreadsheet format – will be made available as direct downloads from a secure part of our website.
- ▶ **Webinars:** we will host a webinar to share draft findings with subscribers. Following completion of the report, a second webinar will be organised
- ▶ **Contact the Delta team:** during the course of the study and for 3 months after delivery of the report, subscribers can contact Delta team members for informal discussions, ad hoc questions, queries etc.

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