

# The power to choose



## National electricity market explained

The National Electricity Market (NEM) allows trading in electricity between generators and wholesale customers, including authorised electricity retailers.

It has a common set of rules under which electricity can be traded within and between states at a wholesale level. Industry participants obtain access to electricity transmission and distribution networks. It also allows for competition at a retail level.

A number of mechanisms have been put into place to regulate the NEM and ensure that it runs efficiently, securely and safely. The wholesale market is operated by the Australian Energy Market Operator (AEMO). Its functions are laid out in the National Electricity Law and its operation is guided by the National Electricity Rules.

## How does the NEM operate?

Electricity cannot be stored and it is impossible to distinguish which generator produced the electricity consumed by an individual customer. As a result, the NEM uses the concept of a wholesale pool in which electricity is centrally dispatched to meet electricity demand.

Electricity retailers purchase the electricity that they sell to customers from AEMO through the wholesale pool, whilst generators sell directly to AEMO through the pool and are dispatched to meet customer demand, using, in general, the lowest priced generator first.

The wholesale price of electricity in the pool varies on a half-hourly basis, depending on the prices of bids submitted by generators and the level of customer demand for electricity in each half-hour period. As demand rises relative to supply, prices tend to increase (sometimes rapidly), and vice versa.

As the wholesale price (spot price) of electricity can be volatile, generators and retailers enter into financial contracts (hedge contracts) outside the pool. These financial contracts allow generators and retailers to manage the risks associated with fluctuations in half-hourly spot prices.

These financial contracts perform an essential function by enabling retailers to manage price fluctuations and thereby offer customers greater price certainty. Therefore, while the spot price fluctuates every half hour, the price offered by a retailer to its customer generally does not.

For more information on the operation of the NEM, go to [www.aemo.com.au](http://www.aemo.com.au).

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