

Ongoing efficiencies

An overview of our approach from RIIO-1



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For RIIO-GD1 we proposed and decided on common ongoing efficiency assumptions across companies

For RIIO-GD1 (and T1) we set the following ongoing efficiency assumptions:

- **1% for opex** informed by industry averages of partial factor productivity measures (labour, and labour and intermediate outputs) from 1970 to 2007
- **0.7% for capex and repex** informed by total factor productivity measures in construction and industry averages

Average annual changes in productivity measures over the period 1970 to 2007 using the EU KLEMS dataset

Sector	TFP (VA)	Labour productivity (VA) at constant capital	TFP (GO)	Labour & intermediate input productivity (GO) at constant capital	Labour & intermediate input productivity (GO)
Unweighted ave. selected industries	2.3%	2.8%	0.9%	0.9%	1.1%
Unweighted ave. selected industries (exc. manufacturing)	1.1%	1.2%	0.5%	0.6%	0.8%
Unweighted ave. all industries	1.3%	1.5%	0.5%	0.5%	0.8%
Weighted average all industries	1.1%	1.1%	0.5%	0.5%	0.8%
Construction	0.7%	0.7%	0.3%	0.3%	0.4%

- In our Strategy Decision for ED1, we stated our intention to set an ongoing efficiency assumption common across DNOs, drawing on our RIIO-GD1 and T1 approach and data
- We requested DNOs to state and provide evidence of the ongoing efficiencies embedded in their business plans
 - The ongoing efficiencies represented “frontier shift”, and did not include “catch-up” (smart grid savings were also separate)
- DNOs included ongoing efficiencies of between 0.8% and 1.1% p.a. - we accepted these as efficient

Our core purpose is to ensure that all consumers can get good value and service from the energy market. In support of this we favour market solutions where practical, incentive regulation for monopolies and an approach that seeks to enable innovation and beneficial change whilst protecting consumers.

We will ensure that Ofgem will operate as an efficient organisation, driven by skilled and empowered staff, that will act quickly, predictably and effectively in the consumer interest, based on independent and transparent insight into consumers' experiences and the operation of energy systems and markets.

- Selected industries (as set out in IP) were: chemicals and chemical products; electrical and optical equipment; transport equipment; construction; sale, maintenance & repair of motor vehicles, retail sale of fuel; transport & storage; and financial intermediation.
- All industries *exclude*: real estate; public administration; education; health; and social services.

Definitions:

- TFP – Total Factor Productivity
- VA – Value Added (a measure of the value of gross output minus the value of intermediate inputs (energy, materials and services))
- GO – Gross Output (a measure of the value of the output of an industry, ie the combined turnover of the companies within that industry)