

## Expert conclave meeting summary

Date and time: Thursday, 27 January 2022 - 2 to 4pm (AEDT)

### Expert attendees:

James Hancock (JH)  
Toby Brown (TB)  
Dinesh Kumareswaran (DK)  
Glenn Boyle (GB)  
Graham Partington (GP)  
Martin Lally (ML)  
Tom Hird (TH)  
Jonathan Mirrlees-Black (JM)

### Facilitator:

Anna Brakey (AB)

### AER attendees:

Eric Groom (EG)  
Esmond Smith (ES)  
Warwick Anderson (WA)  
Zhen Wang (ZW)  
Jonathan Seymour (JS)  
Richard Liu (RL)

## Summary

The purpose of the expert conclave meeting was to:

1. Discuss/agree on the scope, agenda, and format of the Concurrent Evidence Sessions (CES).
2. Obtain additional topics and questions the experts thought should be discussed at the CES.
3. Initial discussion on the question “Should the AER’s return on debt reflect the instruments and strategies available to the benchmark business?”
4. Initial discussion on the question “What does the NPV=0 principle mean for the term of the rate of return and our estimate of expected inflation?”

## Scope, agenda, and format

Facilitator noted at the meeting that the purpose of the CES is to allow the Board to obtain views and opinions from the experts on topics and parameters critical to the AER’s determination of the Rate of Return (RoR). It is a platform to engage, both between the Board and the experts, and amongst the experts themselves. It was noted that finance and economic matters often comprise a range of views that are evolving, with no inherent right or wrong answer. The discussions and debates during the CES will inform the AER Board on the spectrum of opinions at this point in time and form part of the Board’s consideration in their regulatory decision making.

While the Board had identified a list of around 35 questions in the Information paper, it was concerned that there would be insufficient time at the expert sessions to meaningfully discuss all the questions. To focus the discussion at the conclave on the issues that the Board most wanted to engage with the experts, the Board prioritised the questions within a proposed agenda circulated.

During the conclave, the experts agreed to the proposed agenda, including the topics selected for discussion and the format of the sessions. Experts noted that some topics may require less time to discuss while others more. During the CES, experts would focus on the questions and topics identified in the agenda.

It was agreed that during the CES, most topics would start off with two selected experts presenting. The presentations are intended to outline the main alternative perspectives. The Board and experts will then discuss the topic after the initial presentations.

### **Additional topics**

During the conclave, experts identified additional topics of interest for potential discussion during CES. These included:

- Weighting of geometric and arithmetic mean when determining the Market Risk Premium (MRP).
- Beta determination considerations – what weight should be given to delisted companies, use of international or domestic infrastructure firms, what should be done with the declining comparator set.
- At a high level - consideration of implications of the NEO/NGO for setting an efficient rate of return.
- The connection of the rate of return and stranding risk.
- The CAPM model used by AER assumes closed equity markets (country segregated). At some point this needs to be reviewed.

The AER will consider these additional suggestions.

The conclave considered two initial questions put forward by the Board prior to the expert sessions.

### **Should the AER's return on debt reflect the instruments and strategies available to the benchmark business?**

On this question, experts interpreted "available" to mean "feasible" or "efficient". Experts' views on this question generally reflected two points:

1. The cost of debt for the benchmark business should be informed by observed business practices. Noting that setting a benchmark from diverse approaches is difficult, and an average may not reflect an efficient benchmark.
2. The AER should not match benchmark to actual cost of debt directly. The experts generally considered that AER should think about what an efficient debt management approach for a business that we regulate should be. Then set the benchmark per that approach.

### **What does the NPV=0 principle mean for the term of the rate of return and our estimate of expected inflation?**

It was agreed by all experts that the NPV=0 is the right principle to adopt. Further discussion on the right term to adopt when considering NPV=0 may be raised at the CES. The difficulty in considering the term is due to differences in principle and investor practice.

Experts voiced divergent views on the right term to adopt, and how the NPV=0 principle could be applied.

Experts on this question also noted any changes should be reflected in other RoR parameters, such as MRP, beta etc.