

# Queensland Draft Decision Conference

12 May 2015, Brisbane.

# Outline

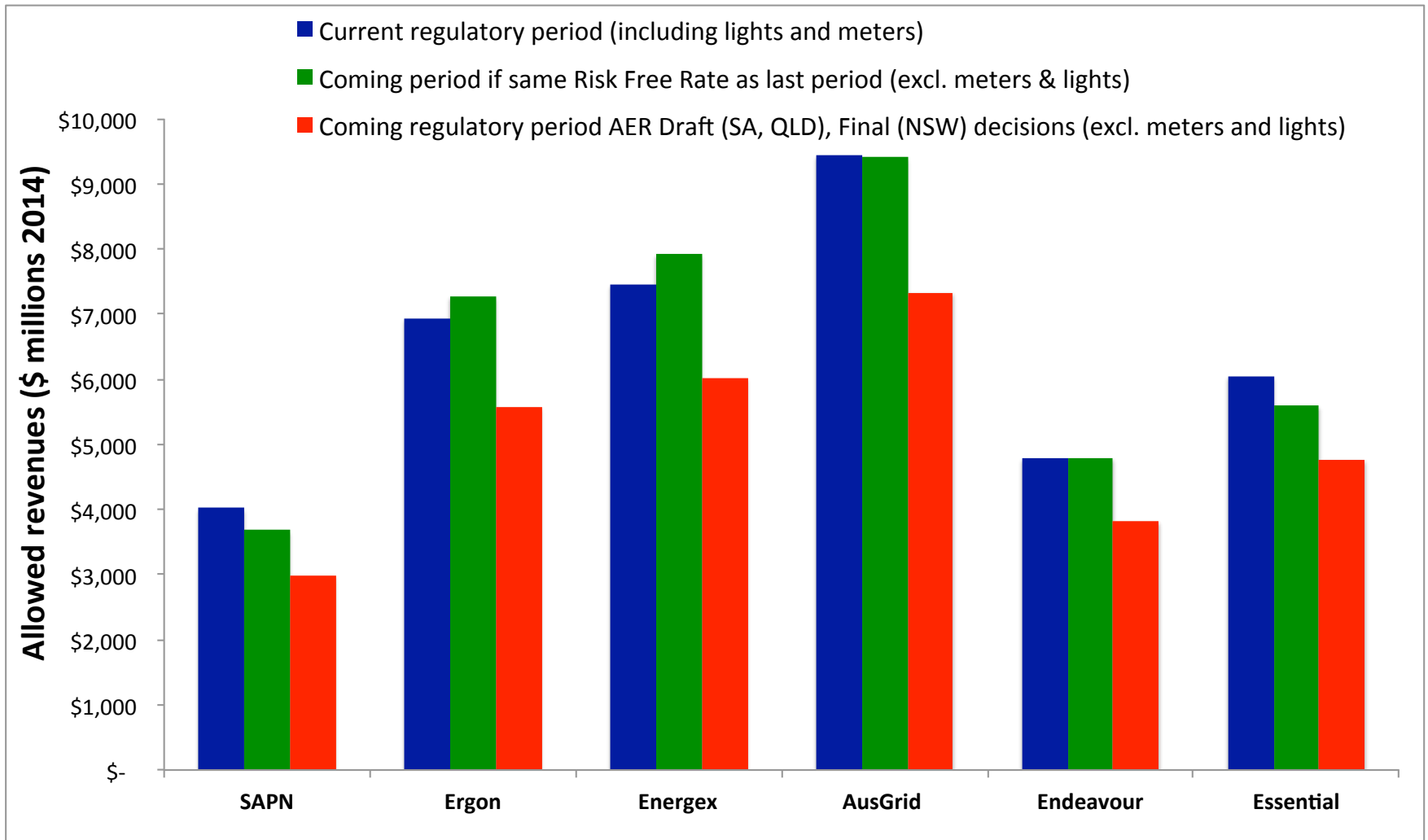
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- Opening remarks
- Overview of revenues, capex, opex
- RAB and WACC comparisons
- Opex comment and benchmark v. allowance
- So, why no progress on opex ?
- Concluding remarks

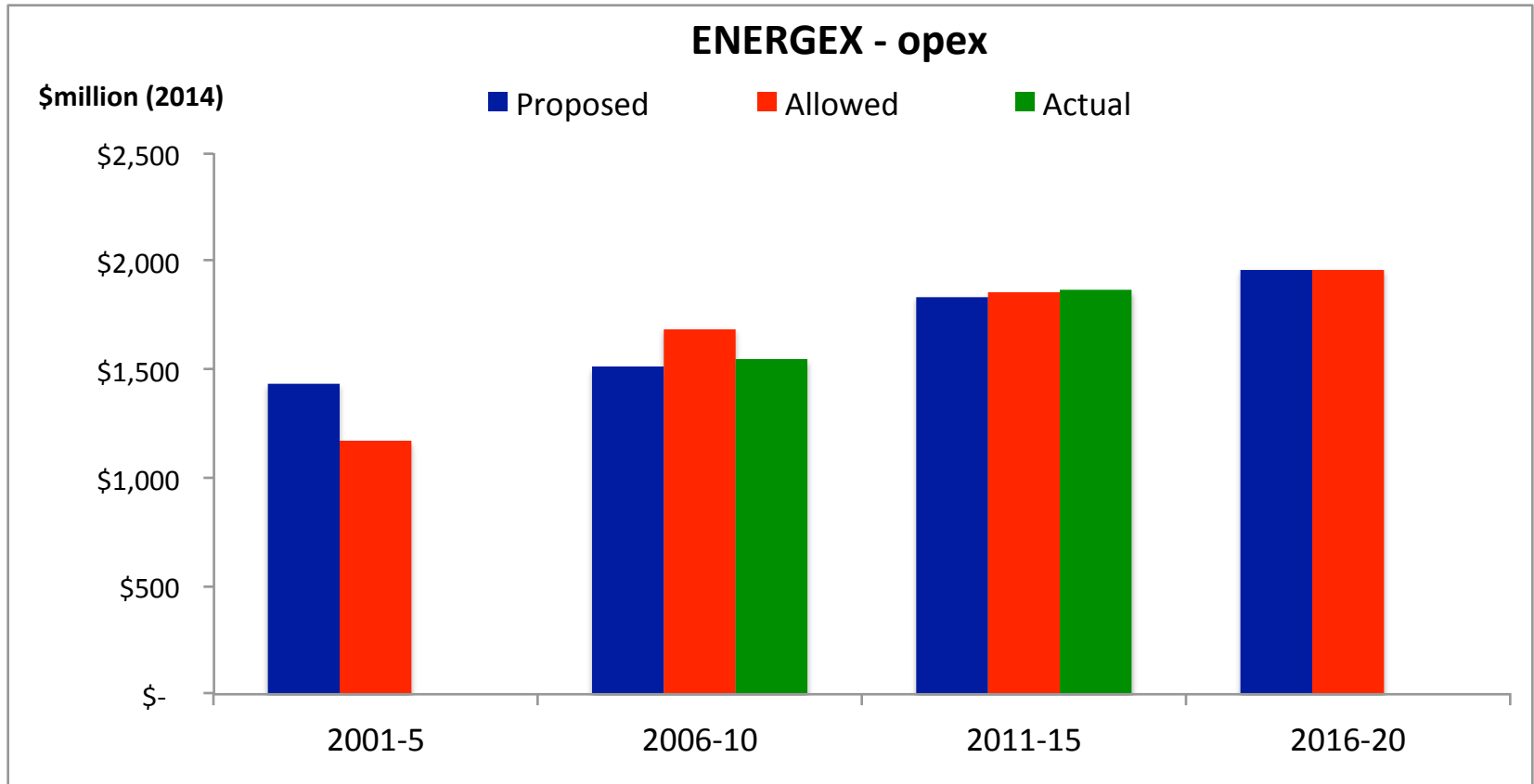
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# Overview of revenue, capex, opex

# If the Risk Free Rate was the same in the coming regulatory period as the current, network prices in NSW & QLD would not be lower

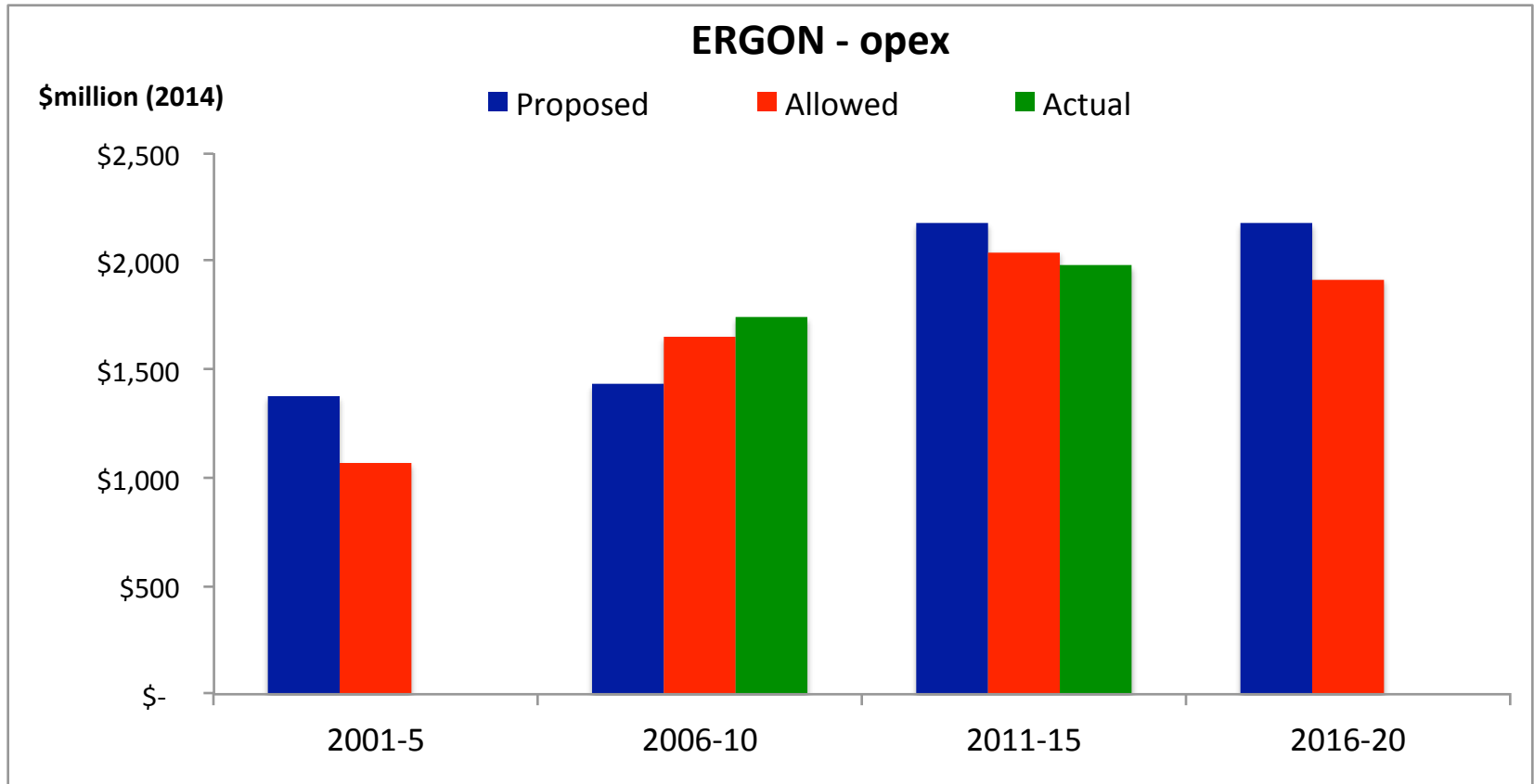


# Energex is being allowed to charge consumers for even more opex than they asked



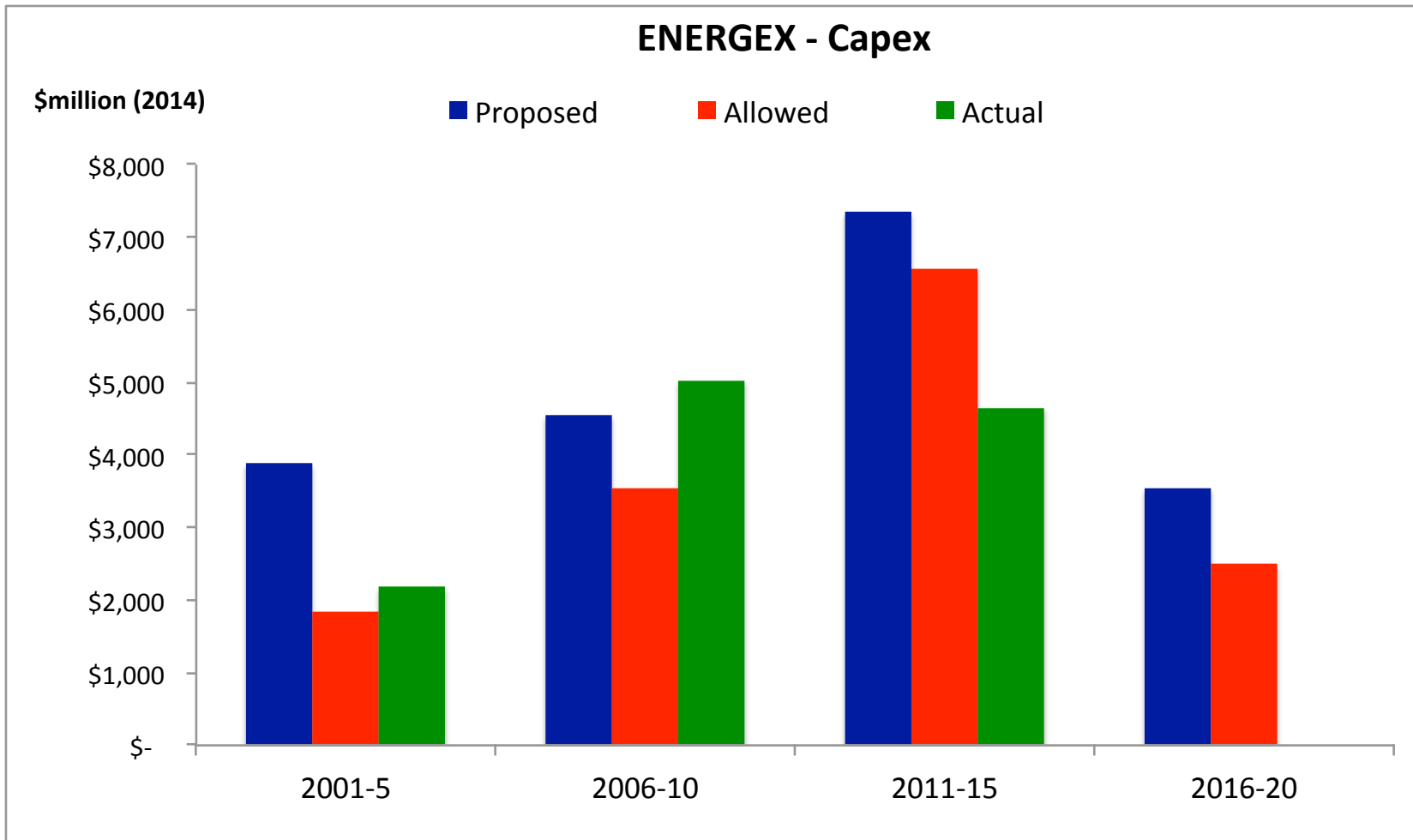
Source: regulatory decisions, CME analysis

And for Ergon, future opex is only slightly lower than allowed and much the same as actual, in last period



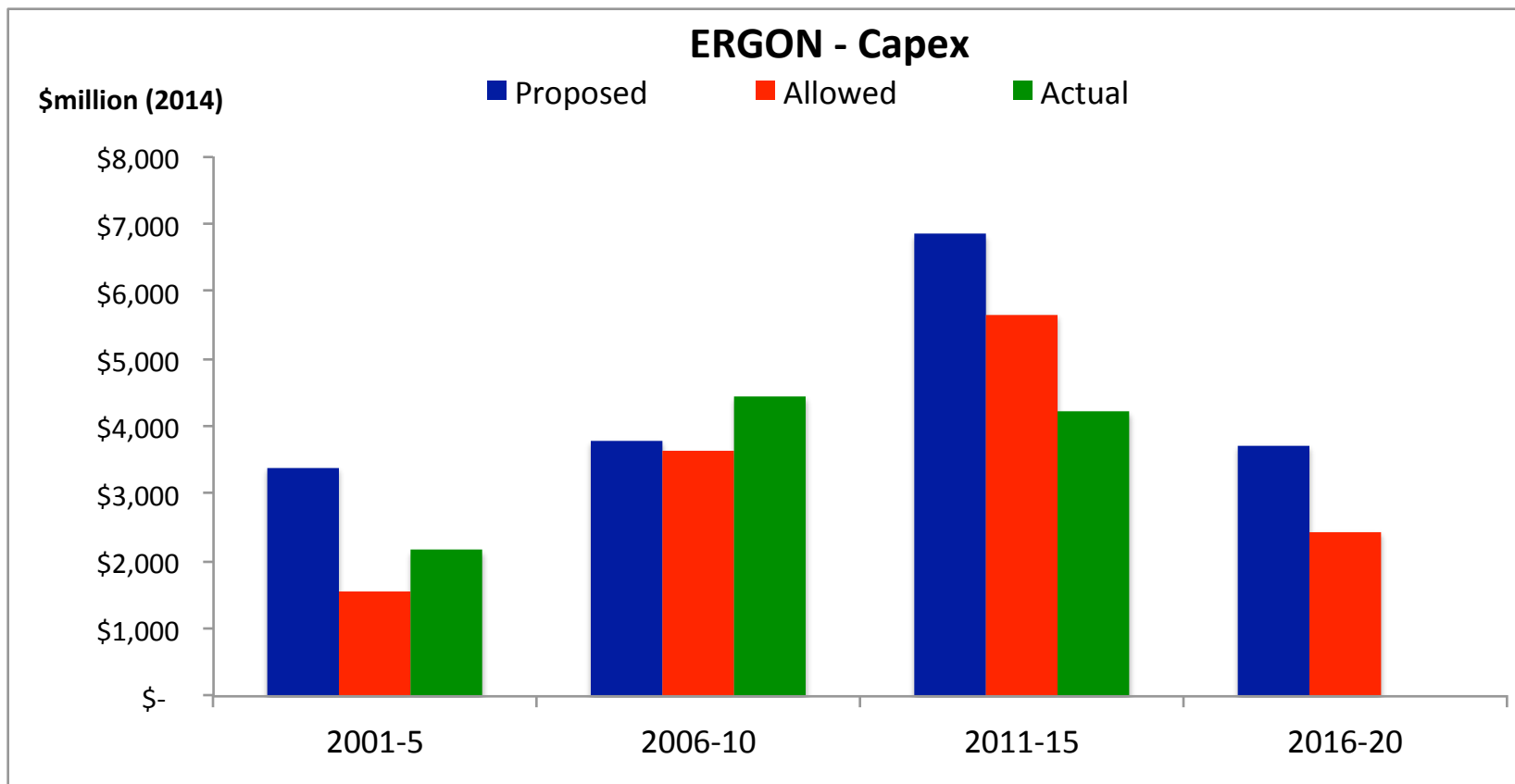
Source: regulatory decisions, CME analysis

Capex is lower, but with so much excess capacity, why not lower still?



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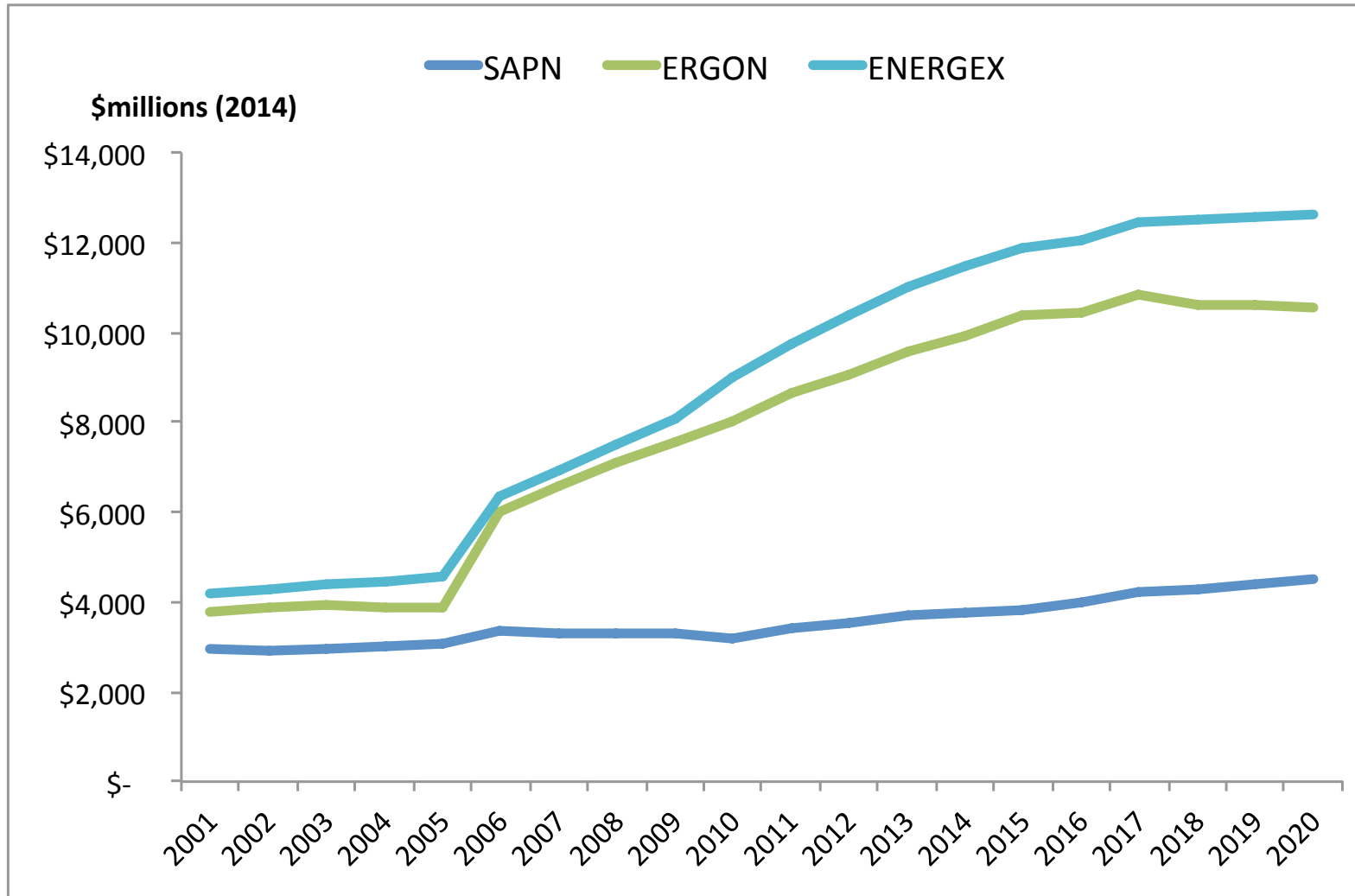
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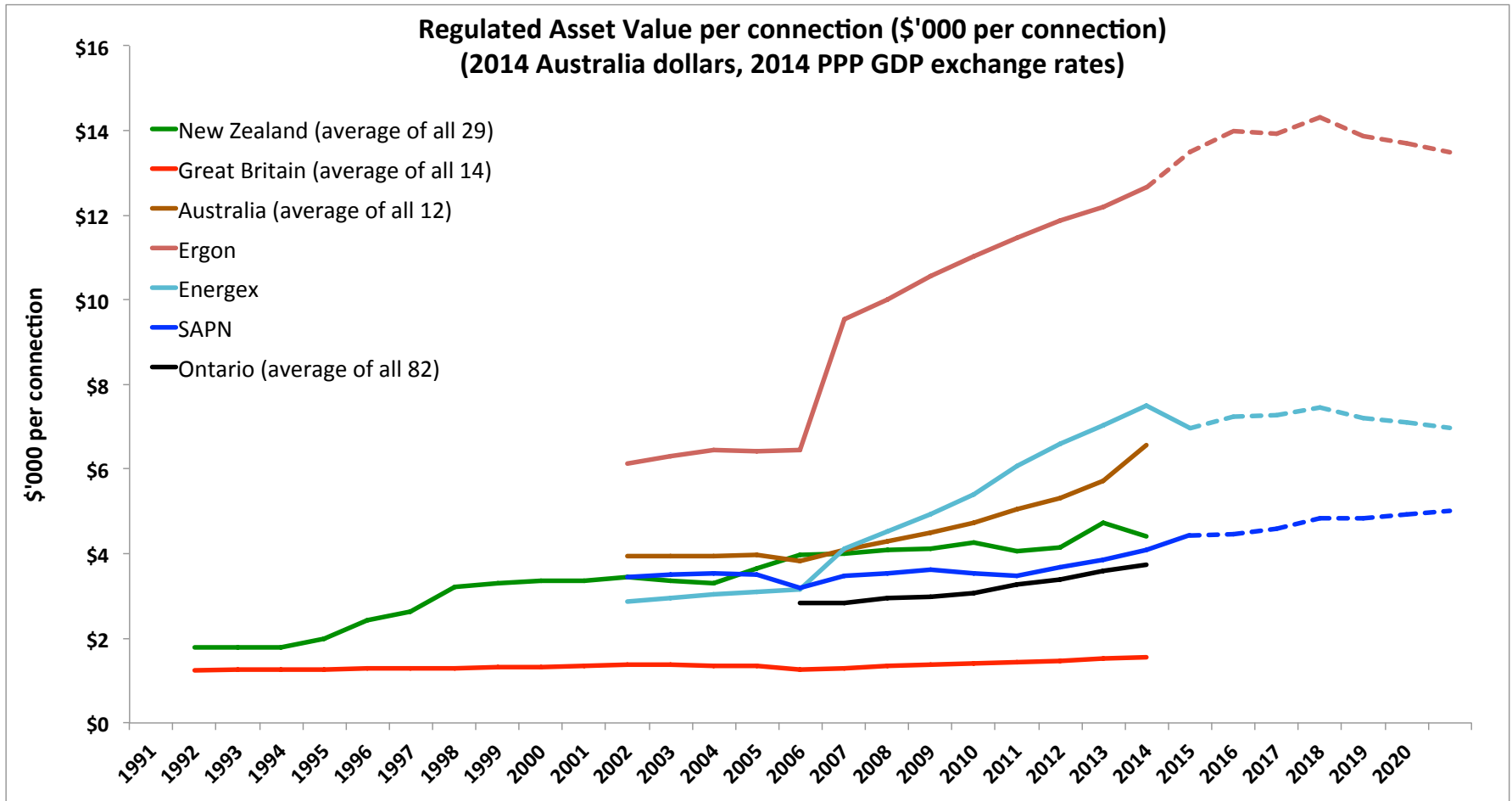
RAB

# SAPN and Energex rising RAB, Ergon about constant



Source: regulatory decisions, CME analysis

# The astonishing RAB gap continues

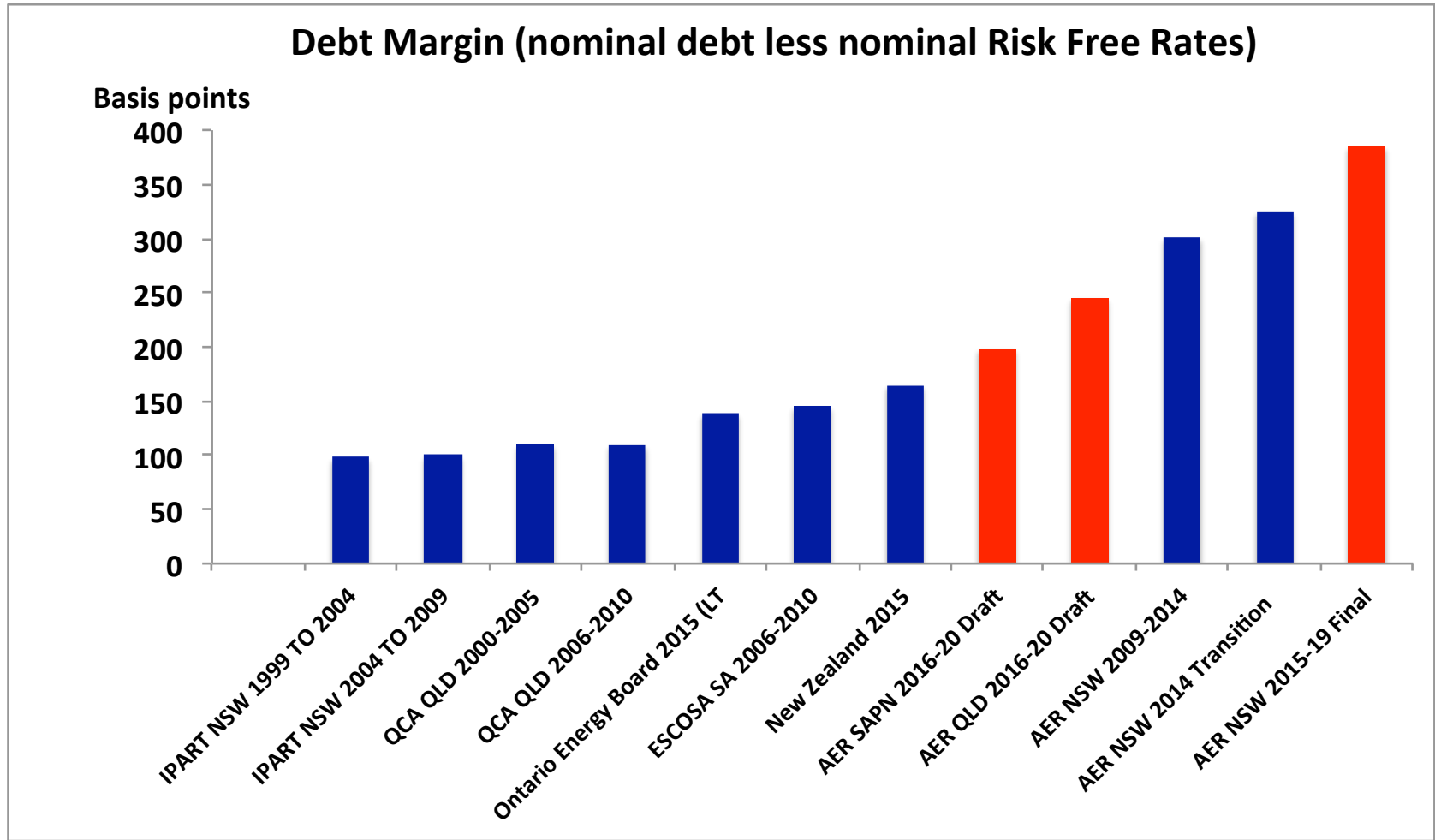


Source: regulatory decisions, CME analysis

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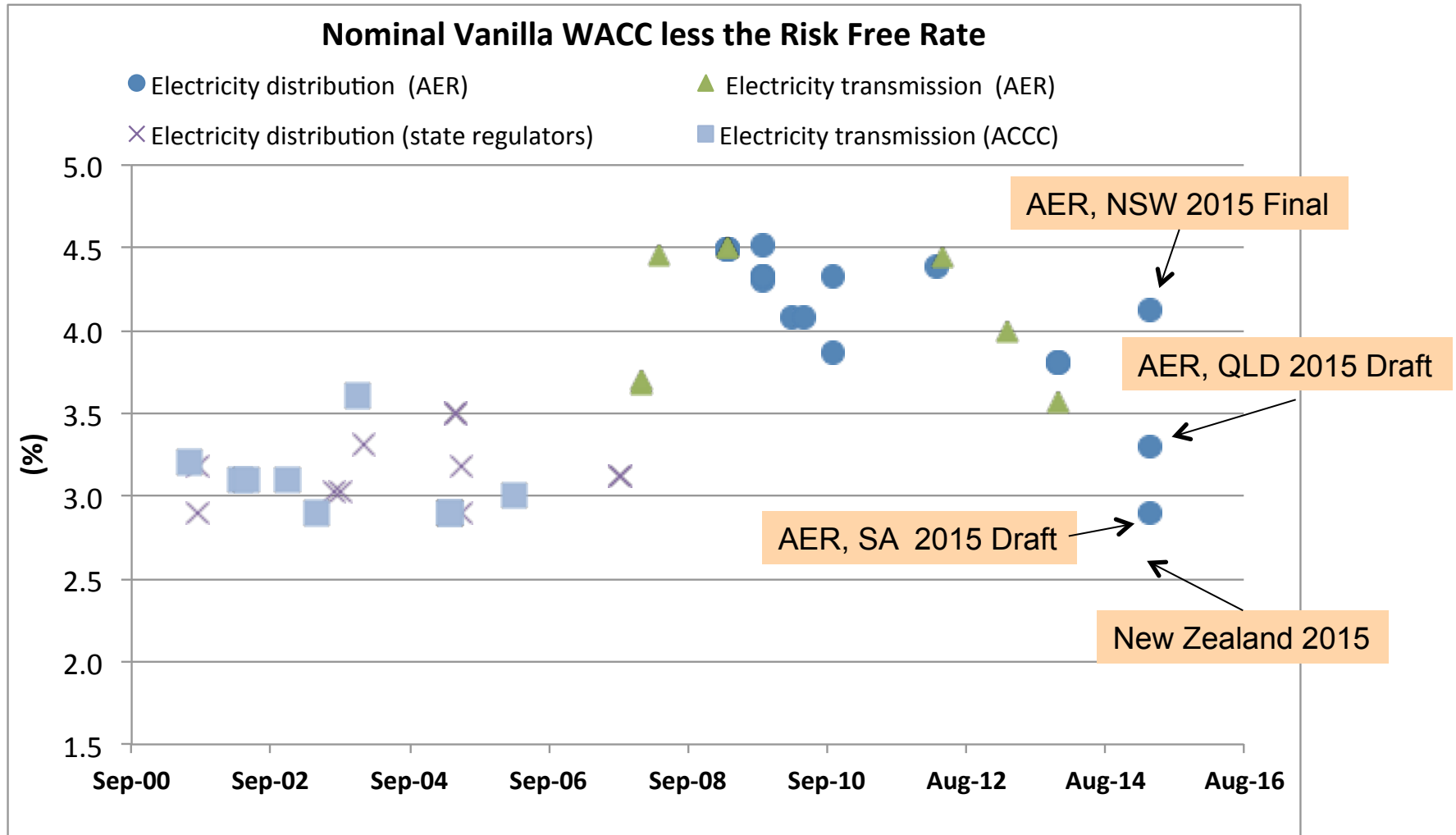
WACC

AER NSW 2015 decision on cost of debt is the highest premium to RFR we have ever seen (anywhere). QLD and SA Draft more moderate but still above other regulators



Source: regulatory decisions, CME analysis

# AER NSW Final Decision WACC less RFR close to all-time high; AER QLD Draft near mid-point of ACCC and state regulator decisions



Source: regulatory decisions, CME analysis

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Opex: benchmark v allowance

## Comments on AER's benchmarking

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- AER's consultant (Economic Insights) has done a fabulous job:
  - Careful, thoughtful, expert and honest advice
  - Uses well accepted, standard, explanatory factors and widely used models;
  - Replicable (and we have replicated it);
  - Robust;
  - Results are entirely plausible.
  - Comprehensively responded to (mostly) half-baked criticisms from network service providers' "advisors"
- The gap between the AER's advice and its decision is not credible.



The AER's opex decision sets an opex allowance that we estimate is 70-90% higher than its benchmark evidence

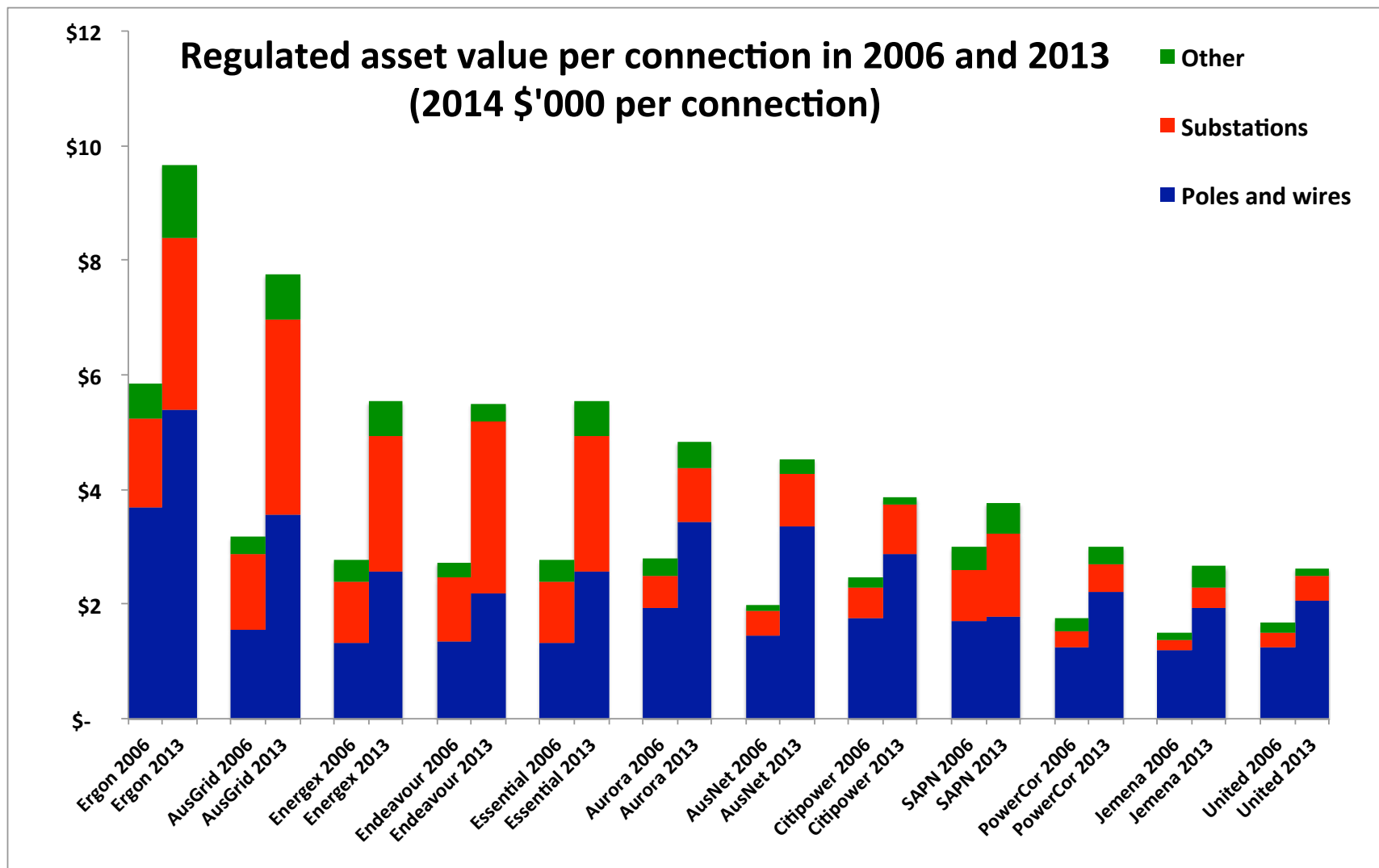
	<b>Ergon</b>	<b>Energex</b>	<b>SAPN</b>
Average opex 2006 to 2013 (2014\$million)	\$ 365	\$ 328	\$ 179
Efficiency gap to frontier (%)	52%	38%	16%
Efficient average opex 2006 to 2013 (2014\$millions)	\$ 175	\$ 203	\$ 150
Scale for annual change in demand, customer numbers, line length (Per EI Report)	1.50%	1.50%	1.50%
Efficient average opex 2016-2020 (2014\$millions)	\$ 196	\$ 228	\$ 168
Average AER Allowance 2016-2020 (2014\$millions)	374.6	383	240.8
Excess of average allowed above efficient (2014\$million), per year	\$ 178	\$ 155	\$ 73
Excess as % of efficient	91%	68%	43%

Source: EI Report, CME analysis

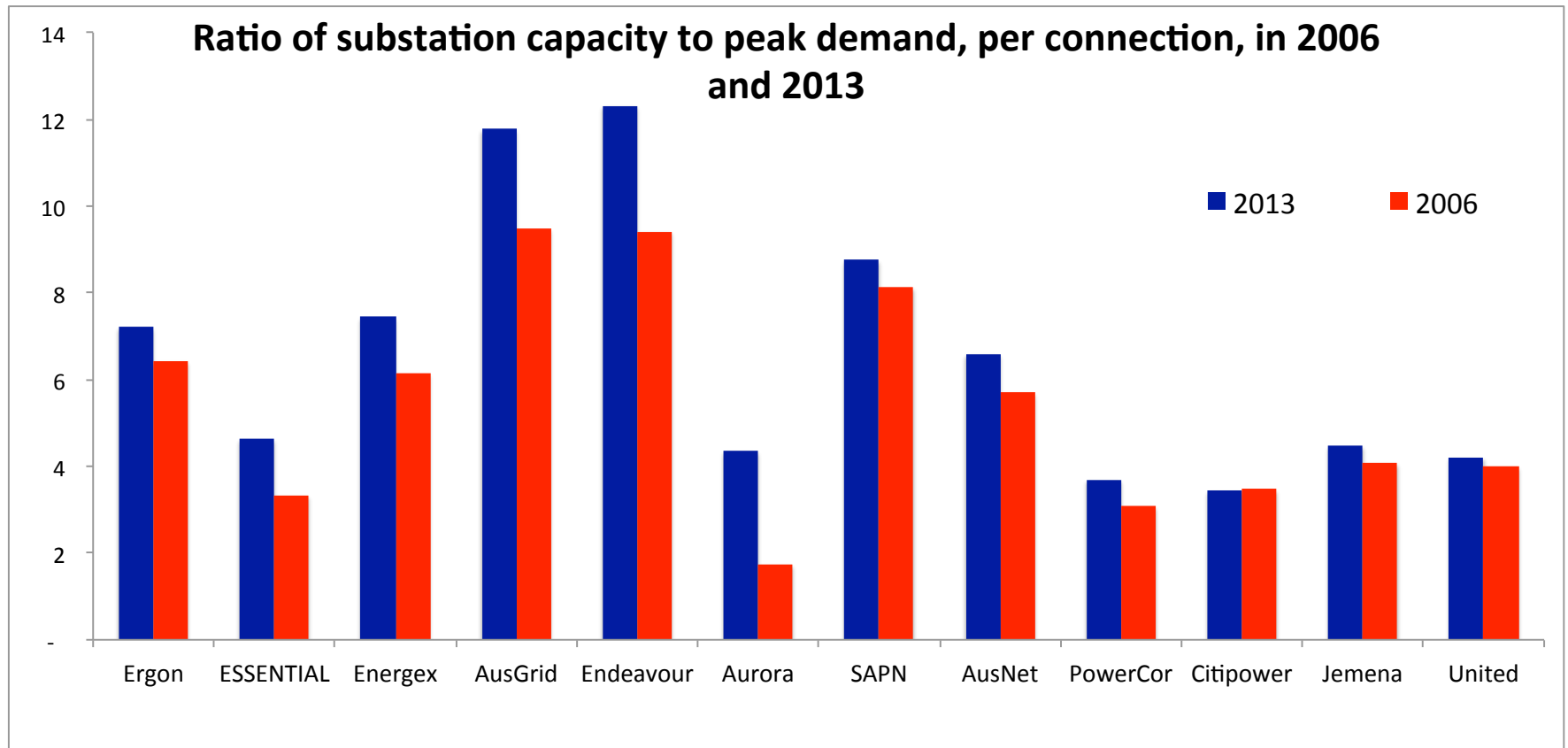
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So, why no progress in opex allowance ?

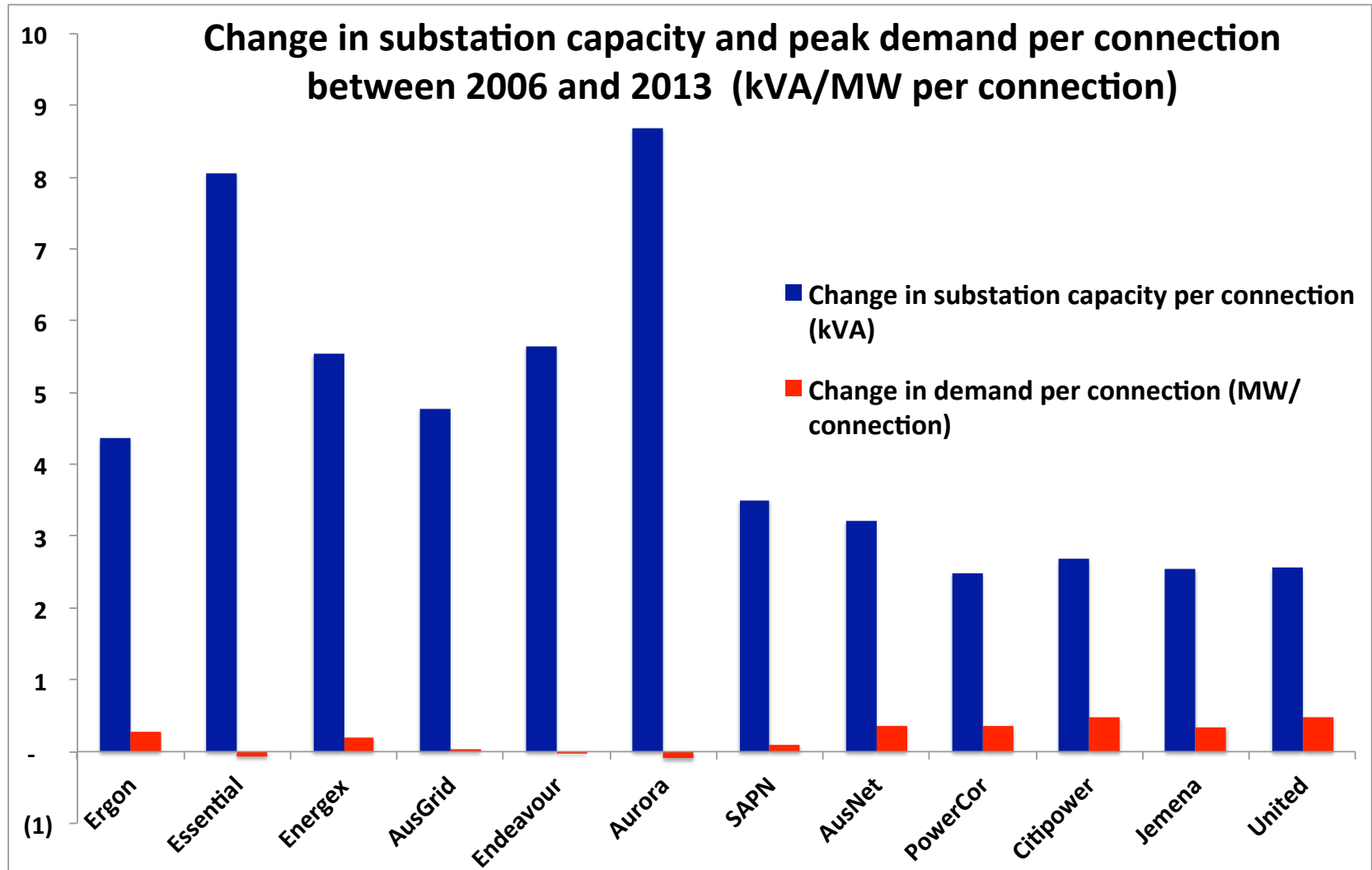
There has been massive increase in the regulated value of substations, poles and wires



## But there is no evidence of capacity shortages in 2006

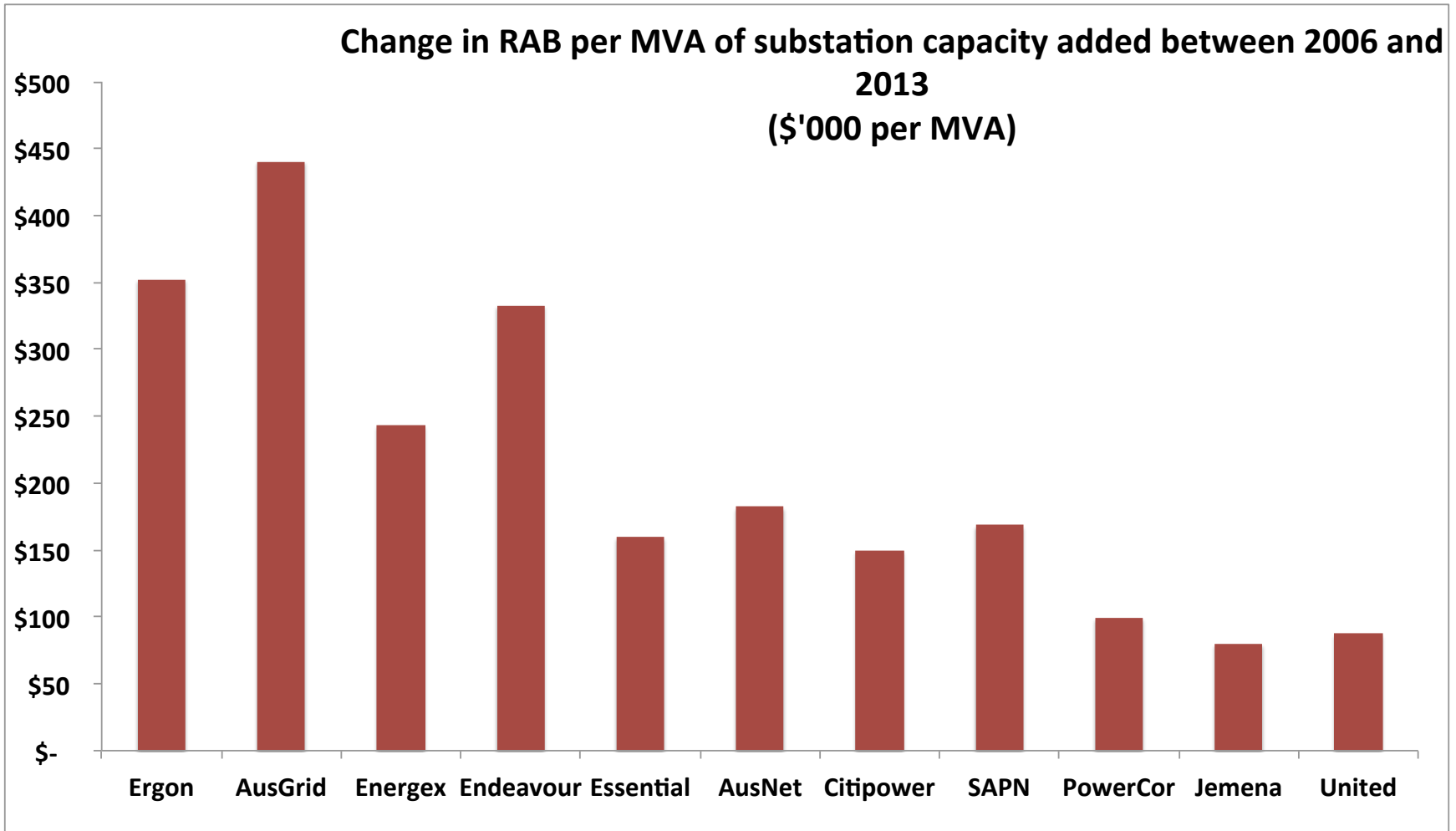


And the huge subsequent capacity expansion was clearly not needed



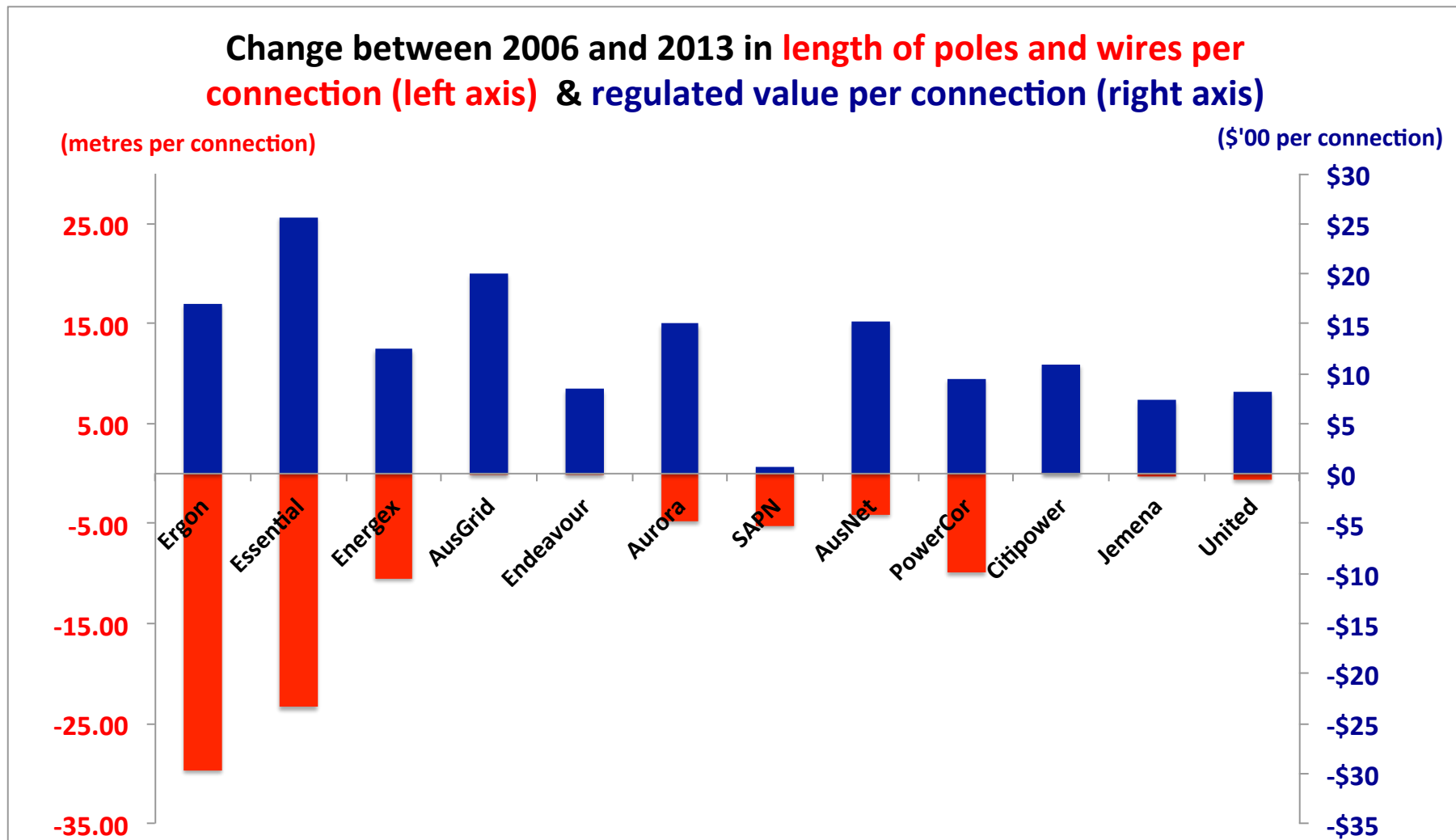
Regulatory information notices, CME analysis

... and some distributors added capacity far more cheaply than others



Regulatory information notices, CME analysis

Likewise for poles and wires, networks have all become more dense (particularly in Queensland) and yet the value of poles and wires has increased hugely



Regulatory information notices, CME analysis

## So why no progress in opex allowance?

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- The benchmarking analysis commissioned by the AER (correctly) calculates efficiency based on outputs not inputs. It has, as expected, shown up the inefficiency attributable (largely) to enormous capacity surpluses in NSW, QLD and TAS.
- The AER's rejection of the benchmarking evidence reflects the AER's decision that the distributors should be able to charge consumers for the cost of operating assets that are not used or useful.



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## Closing remarks