

South Australia Draft Decision Conference

13 May 2015
Adelaide

Bruce Mountain

Outline

- What the equity analysts say
- Overview of revenues, capex, opex
- RAB and WACC comparisons
- Opex comment

What 10 equity analysts covering SKI say

Recommendation Trends				
	Current Month	Last Month	Two Months Ago	Three Months Ago
Strong Buy	0	0	1	1
Buy	6	6	6	6
Hold	3	3	2	2
Underperform	2	2	2	2
Sell	0	0	0	0

Morgan Stanley

SKI Price Target: 26 February 2015: \$1.71/share

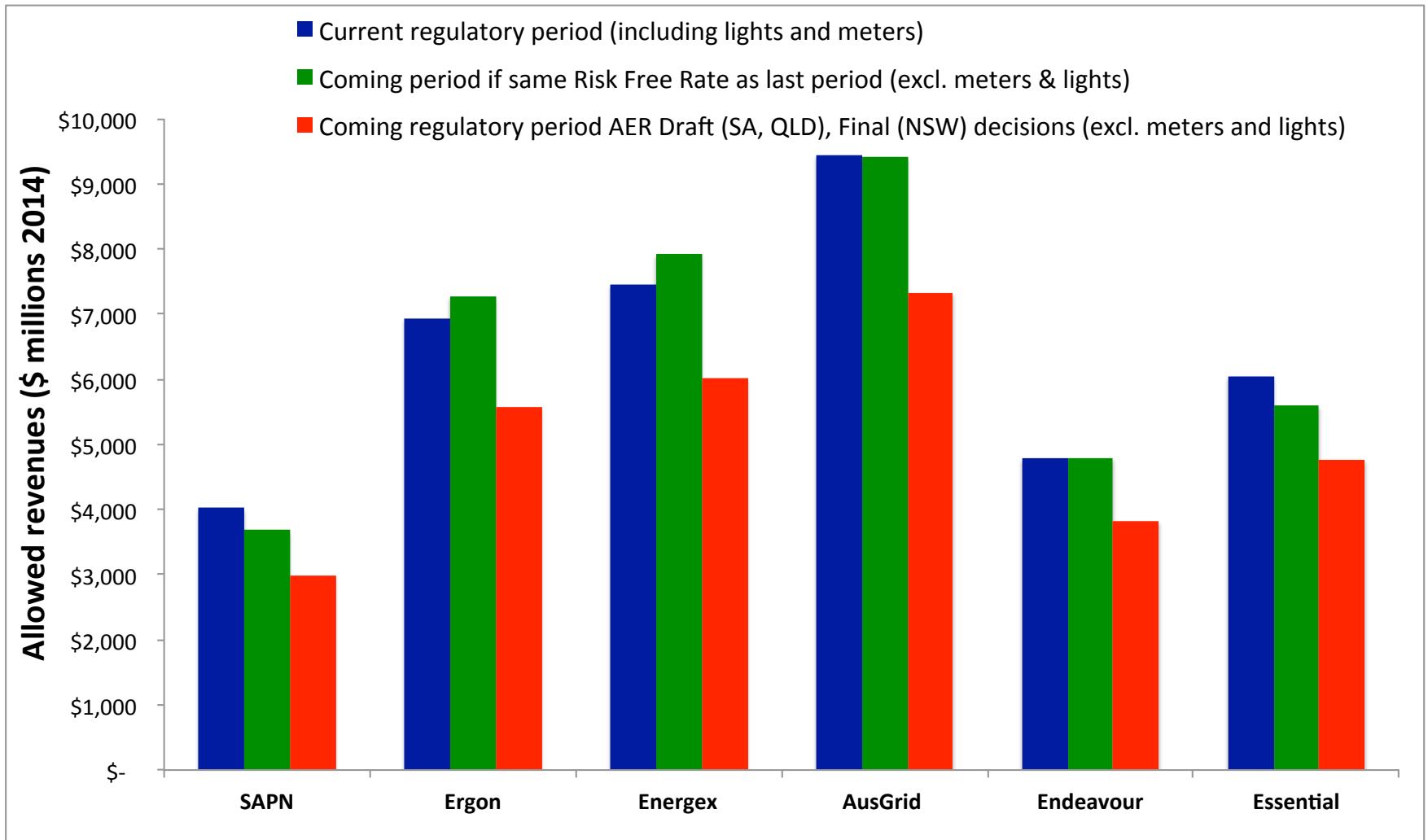
SKI Price Target: 1 May 2015: \$2/share

Valuation & Ratios	FY13	FY14	FY15e	FY16e	FY17e
Enterprise Value					
Share Price (Fiscal Year Average, Adj)	1.70	1.86	1.95	1.95	1.95
Fiscal Year Closing Share Count	1,327	1,466	1,466	1,466	1,466
Market Cap (A\$m)	2,249	2,727	2,859	2,859	2,859
+ Net Debt	3,315	3,642	3,572	3,579	3,635
+ Loan Notes	851	853	665	573	792
- Loans to Associates	(746)	(746)	(746)	(746)	(746)
Enterprise Value (A\$m)	5,670	6,477	6,351	6,266	6,541
RAB	4,224	4,421	4,680	4,887	5,104
EV / RAB (x)	1.34x	1.47x	1.36x	1.28x	1.28x

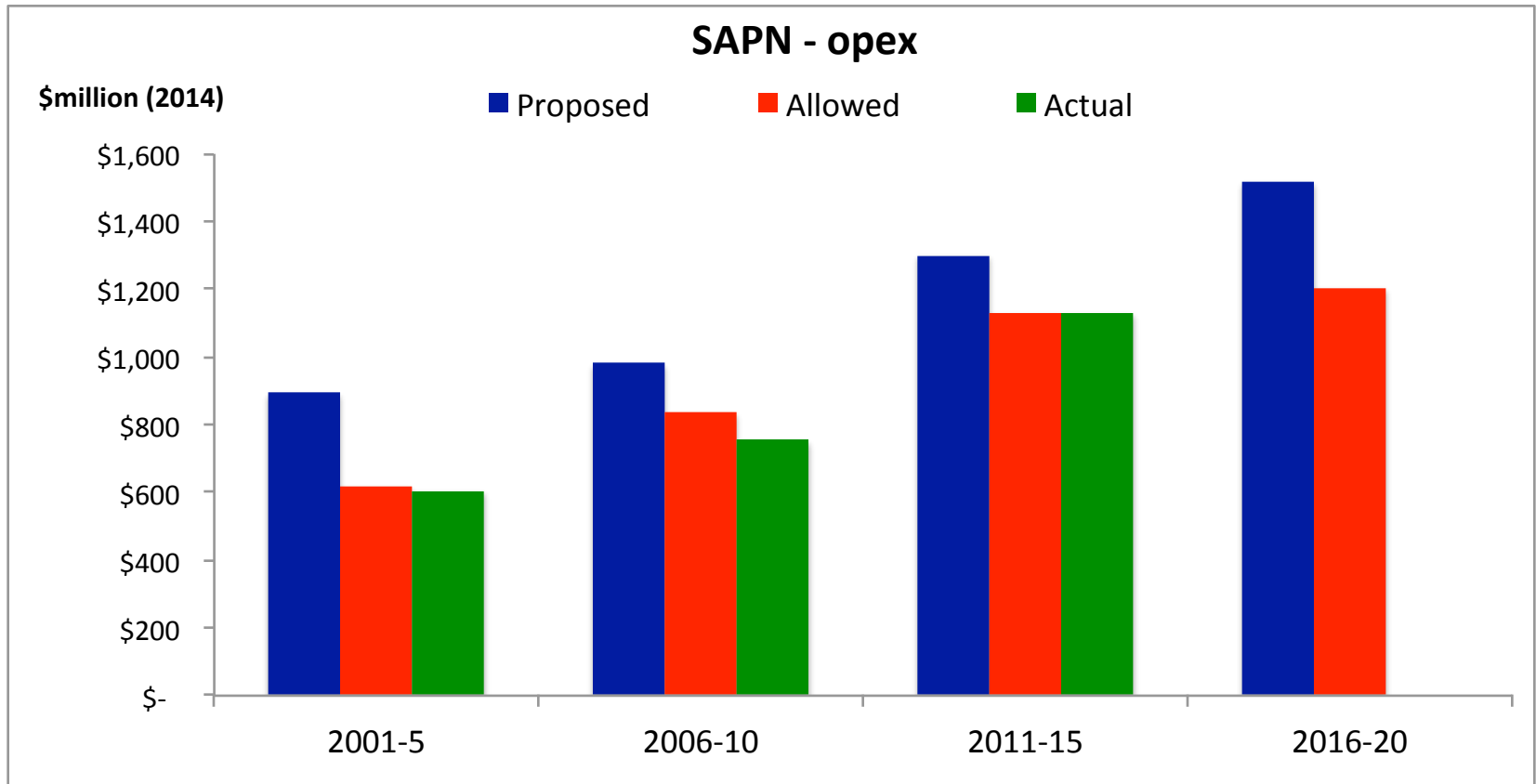
CBA Global Markets Research

- Share price target \$2.25 (compared to 30 April price \$1.95),
- “WACC of 5.45% ... reflective of current bond rates”
- “ ...given the high leverage within this business, any risk free rate led reduction of WACC will also lead to a fall in interest costs.”
- “Two-thirds of the fall in WACC will largely be offset by lower interest costs, the lower gamma was expected (and a known future risk)”
- “Opex and capex were OK for a draft decision.”
- “Given SAPN was one of the best scoring assets in the recent bench marking study, the company’s ability to argue both opex and capex allowances should be significantly easier when compared to the NSW assets.”

If the Risk Free Rate was the same in the coming regulatory period as the current, network prices in SA would be about the same

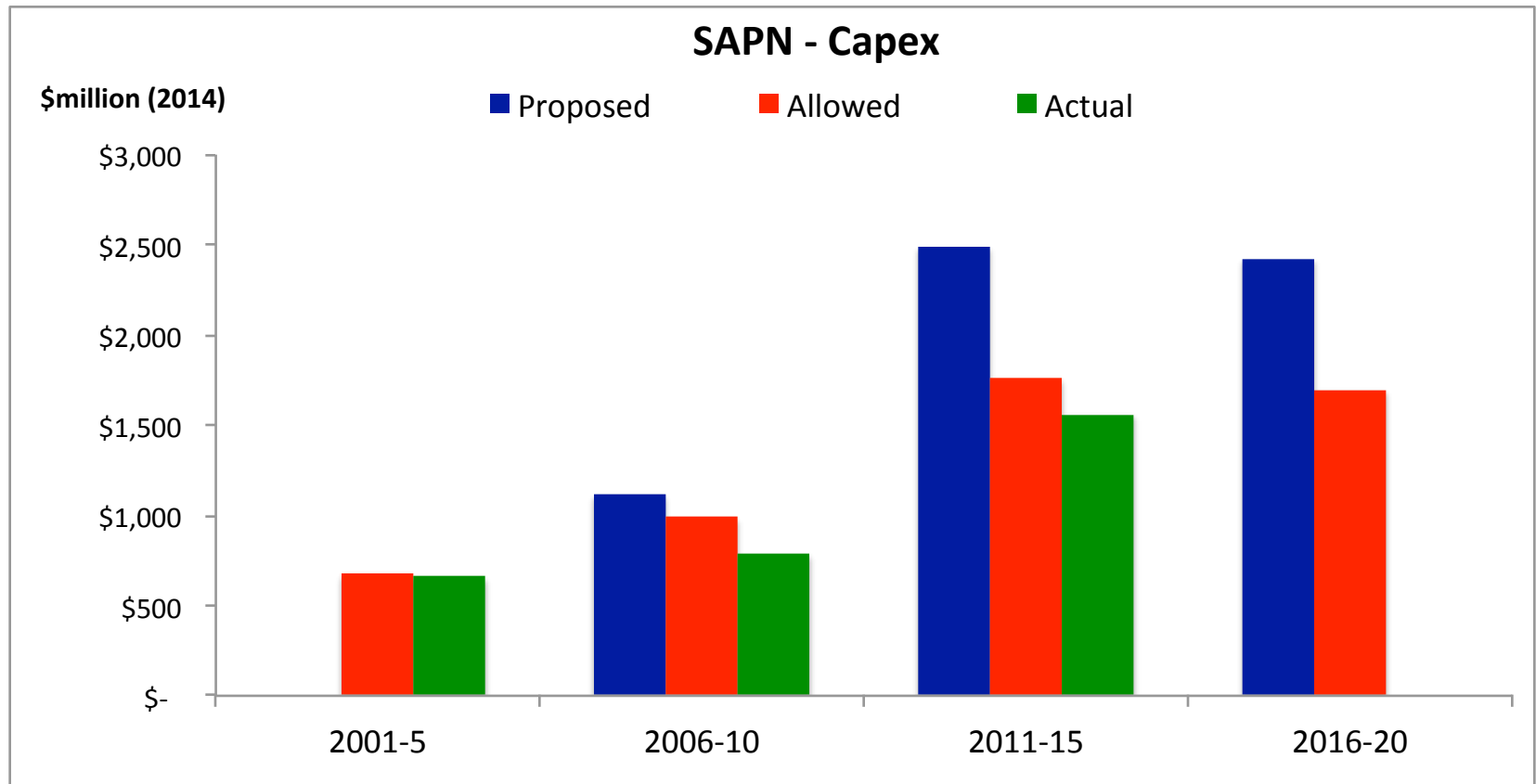


Allowed opex in future is higher than in current period



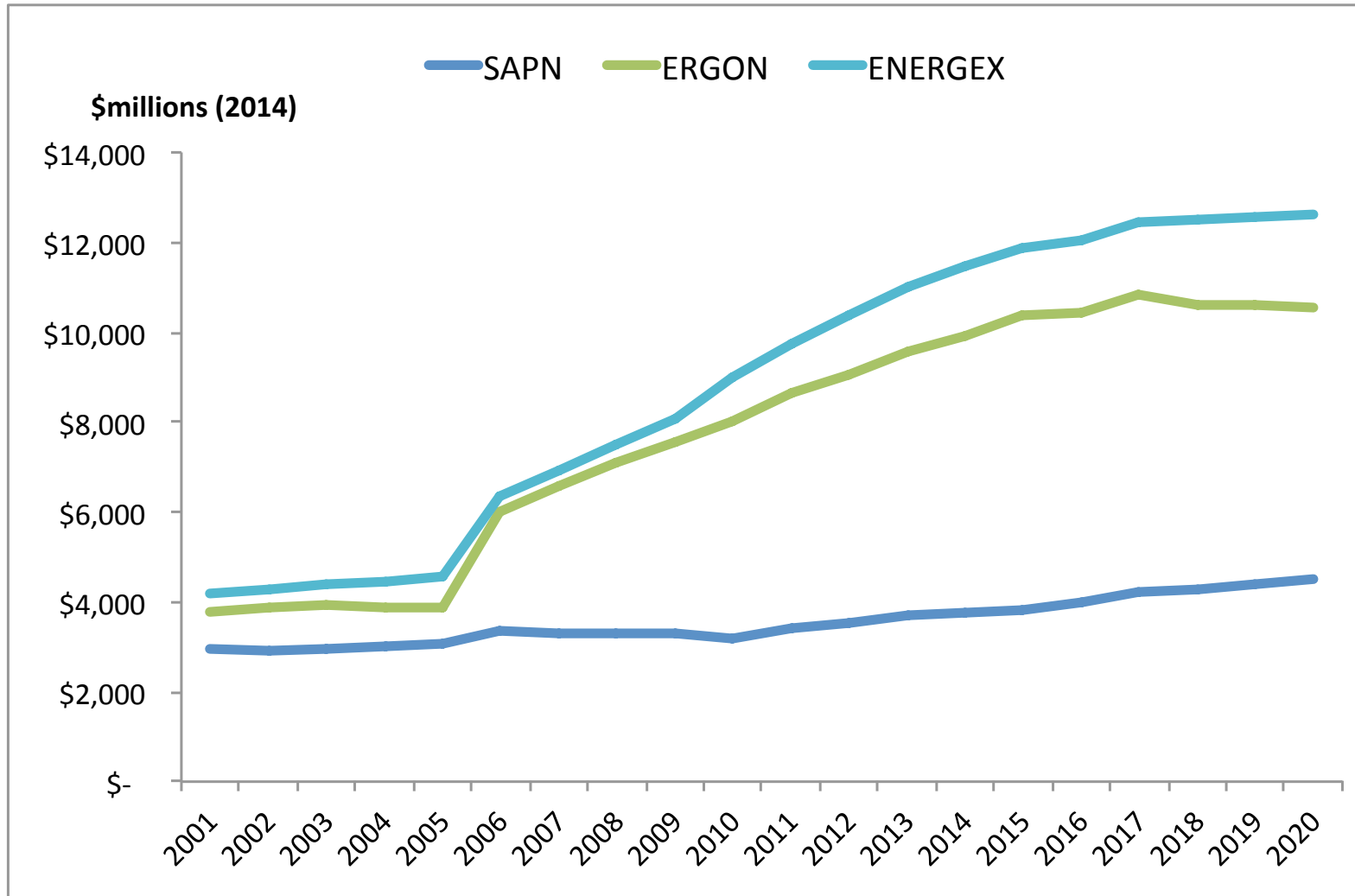
Source: regulatory decisions, CME analysis

Capex in coming period about the same as last period and more than twice average from 2000 to 2010



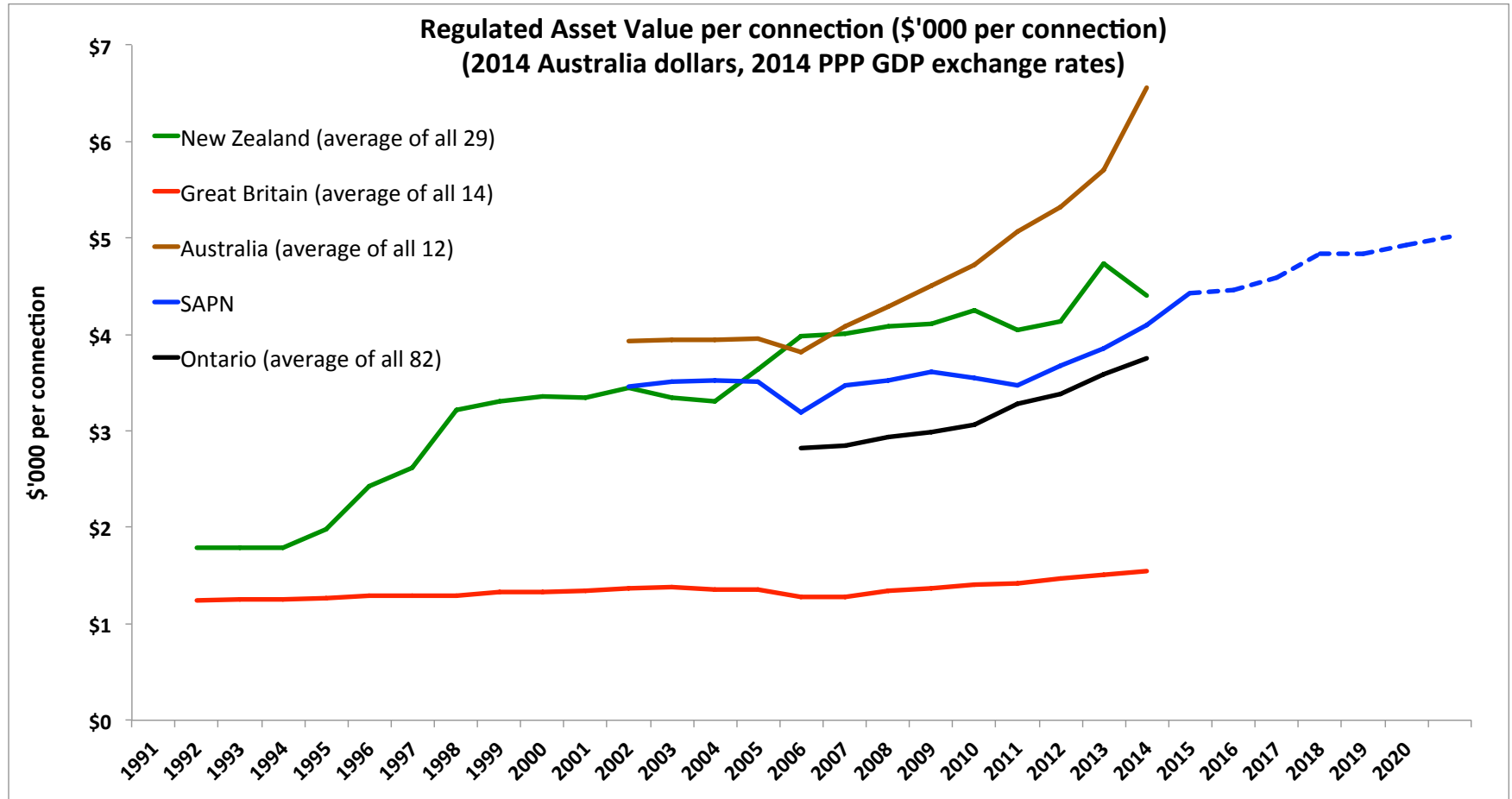
Source: regulatory decisions, CME analysis

SAPN and Energex rising RAB, Ergon about constant



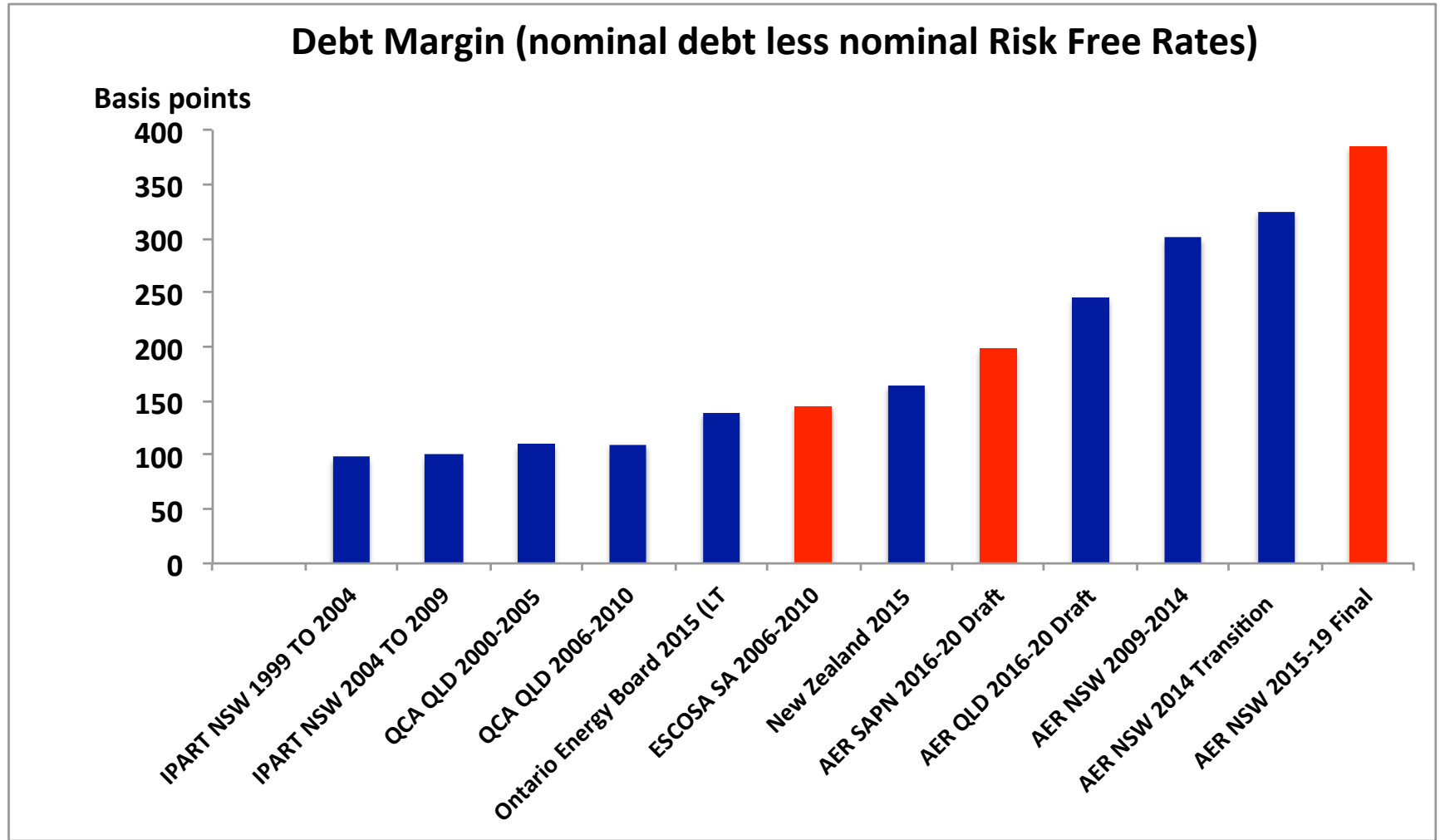
Source: regulatory decisions, CME analysis

RAB is heading in the wrong direction



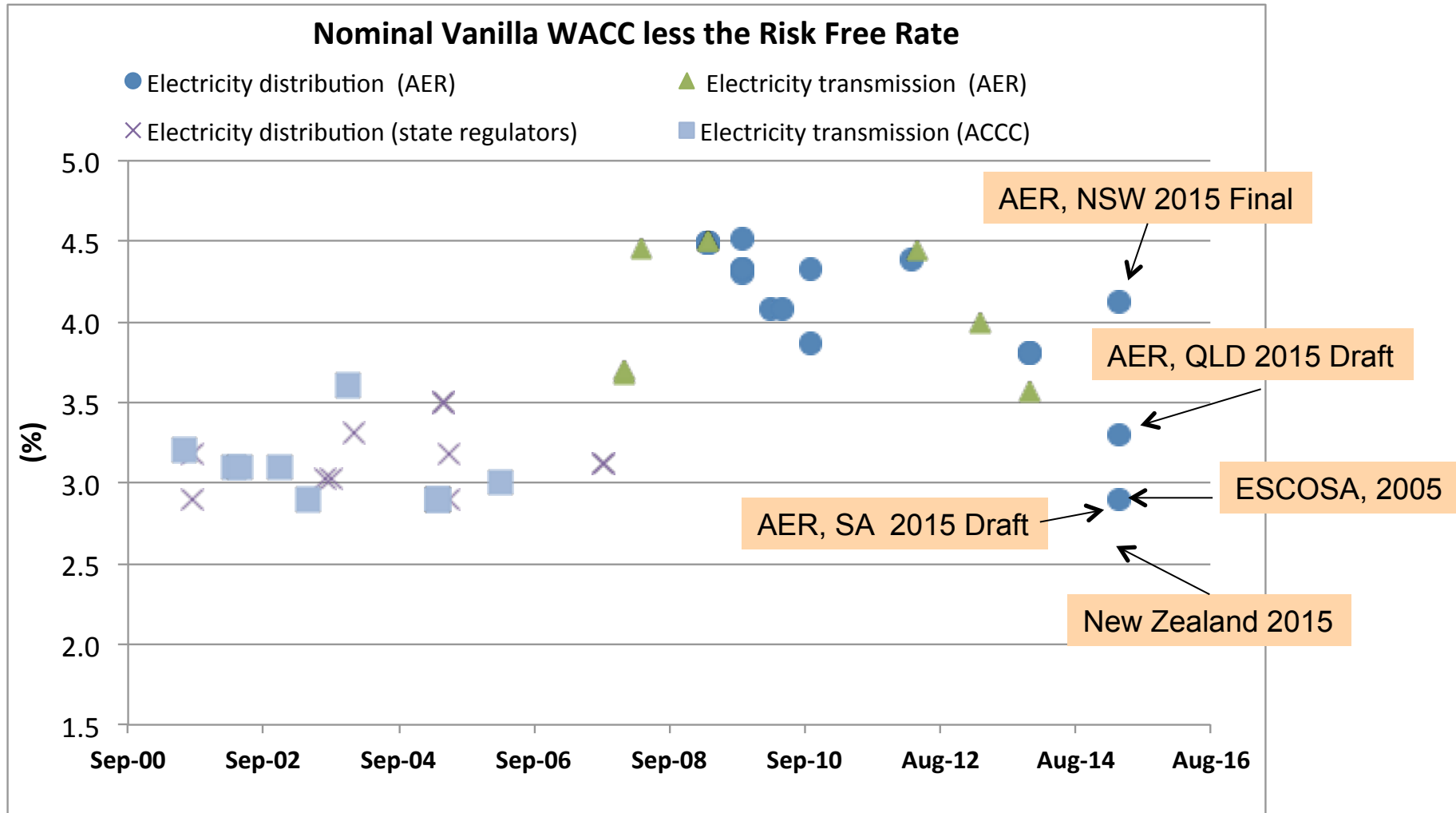
Source: regulatory decisions, CME analysis

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 close to all-time high; AER SA Draft same as ESCOSA in 2005



Source: regulatory decisions, CME analysis

Comments on AER's benchmarking

- 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

	Ergon	Energex	SAPN
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), per year	\$ 375	\$ 383	\$ 241
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

The AER's challenge

“The old saying of ‘sell into a draft and buy into a final’ will likely prove true once again”

“Ultimately (like NSW), we believe the final decision will be more lenient and the final numbers will sit somewhere closer to our forecasts”

(CBA, Global Markets Research), 30 April 2015