Aggregation of Return on Debt Data

Version: Final
Dated: 28 April 2018

CHAIRMONT
ADVISERS+IMPLEMENTERS

Table of Contents

1 EXECUTIVE SUMMARY

1.1 SCOPE OF WORK

In summary, this exercise was to collect and examine debt raising evidence from regulated service providers and create an index of their debt cost. The Terms of Reference (TOR) are contained in Appendix A.

1.2 OUR APPROACH

Our approach to this exercise was to develop an index which does not weight or adjust the raw data from the companies. The purpose is to produce a 'pure' unadjusted index which reflects actual debt raising costs without modelling adjustments to target a theoretical benchmark.

1.3 KEY OUTPUTS AND FINDINGS

The key output of this comparative analysis is the creation of the Energy Infrastructure Credit Spread Index (EICSI). Its key characteristics are that it is:

- based on the spread which companies pay on their debt above a market benchmark rate, interpreted as the swap rate or the floating Bank Bill Swap Rate (BBSW). This spread can be loosely considered as the credit spread or Debt Risk Premium (DRP);
- an unadjusted index, except interest rates are all re-calibrated to quarterly. EICSI does not apply weights for differences such as term to maturity or credit rating; and
- measured as a 12-month rolling average, meaning that the first index value calculated is January 2014, using the data from the prior 12 months.

The highlights of EICSI performance from January 2014 to December 2017 are:

- it has been considerably less volatile than market credit spread indices such as those from the Reserve Bank of Australia (RBA) and Bloomberg, which the Australian Energy Regulator (AER) uses to calculate their cost of debt allowance. EICSI's range was 33 basis points (bp) while AER's 10-year BBB bond margin range was 113bp;
- the stability can be largely explained by variations in the term to maturity of debt raised by the industry. When spreads are high, providers raised shorter term debt and vice versa. Additionally, the average credit rating of debt issued by the industry has varied, typically further depressing volatility of the margin; and
- it has been constantly lower than market credit spreads for 10-year BBB debt measured by AER. The difference has varied significantly from 136bp to 19bp.

1.4 CONCLUSION

EICSI is intended to provide an unadjusted measure of actual raising costs for firms and hence reflect any efficient financing decisions made by the firms compared to the unresponsive market measures.

By definition EICSI includes bank loan facilities that are not included in market-based measures, thereby providing a more complete measurement of debt raising activities. The use of a longer data time series would provide further insight. See Appendix B on the data series request.

The lower margins incurred by the industry from 2014 to 2017 do not necessarily indicate that AER's cost of debt allowance methodology is inappropriate. Industry outcomes for debt cost are a combination of taking refinancing risks, good judgement of broad market cycles, and debt terms and amounts forced on them by the market, in part dependent on investor and lender appetite. A more thorough examination of these factors is outside the scope of this report.

A similar index approach may also be relevant for other regulated industries.

2 DESCRIPTION OF RESPONSE DATA

The sample includes data from privately owned service providers for calendar years 2013-17.

The data requested included debt from any source, including bond issuance, syndicated loans, bilateral bank loans and inter-company financing provided by corporate group entities. A copy of the template excel file and request letter are contained in Appendix B.

Vanilla debt, similar in ranking to the market rate indices, was used to create a debt cost index.

3 USE OF SURVEY DATA IN A BUILDING BLOCK APPROACH

The TOR refers to a comparison between the company-specific debt raising costs for this industry and the broad market debt yields embodied in data from the RBA, Bloomberg, Thompson Reuters and Standard & Poor's.

As noted in earlier Chairmont work[1], the total yield on a bond can be broken down into a market-wide fixed base rate which is the swap rate, and a company-specific margin which is the credit spread. The latter is akin to AER's terminology of a Debt Risk Premium (DRP).

When examining debt raising patterns of service providers, it is important to keep in mind the decision process that corporates undertake to instigate new debt. It is the credit spread in AUD which is the key variable driving debt raising decisions. Therefore, the greatest value of the data provided by the networks is their company-specific credit spreads.

Swap base rates are the same (within a small margin) for all companies in the market at any point in time. The total fixed rate can then be managed by use of interest rate swaps, which is the predominant process revealed by the network survey data. This behaviour has been examined and explained in relation to AER's Benchmark Efficient Entity (BEE) and constitutes Efficient Financing Practices.[2]

It is considered that a building-block approach to examining the cost of debt should be adopted. The important building-blocks are the spread index and the relevant swap rates. Understanding these contributes to a better understanding of the cost of debt as they may be transacted at different times, as usually occurs in this industry.

[1] Chairmont, 'Comparative Hedging Analysis', June 2013, p.14
[2] Chairmont, 'Financing Practices Under Regulation: Past and Transitional', October 2015

4 CREATING AN UNADJUSTED INDUSTRY INDEX

4.1 NATURE OF THE INDEX

4.1.1 Index versus Curve

The term 'index' rather than 'curve' is deliberately used here. A yield curve is determined by plotting interest rates for a range of terms to maturity at a point in time. This is the approach that external market providers use. Whereas, the unadjusted industry index used in this exercise is term-unaware, i.e. spreads are combined equally regardless of the term to maturity of that spread observation. This is a key concept when interpreting the survey data and index.

4.1.2 Spread Index

Chairmont has created the EICSI based on the spread payable over BBSW, or over the relevant fixed interest rate swap rate at the time the debt was priced. The reason for this is explained in Section 5.

4.1.3 Model Risk

EICSI is a simple average without modelling adjustments and assumptions, apart from interest rates being adjusted to quarterly payment frequency. The intention is to keep this index model-risk free.

4.1.4 No Fees

Issuance fees relate to primary market activities, whereas the external market data is sourced from the secondary market. Therefore, EICSI does not include issuance costs such as upfront or ongoing fees.

4.1.5 Rolling 12 Months

There are too few companies, and therefore debt raising events, to calculate a meaningful index on a monthly basis. For this reason, the calculation of EICSI averages the spread of each debt raising over the previous 12 months, regardless of the size, term of debt or any other characteristic difference between debt raisings.

4.1.6 Behavioural Influence

The decision to create an unadjusted index means it is impacted by all funding choices of the service providers. The variability in funding choices depends on the flexibility of each company's funding requirement calendar and the strategic policies of that company.

Debt characteristics which the networks need to decide include:

- Type of debt product, e.g. loan facility, bond issuance, etc.
- Pricing and issuing dates
- Term
- Amount.

These decisions are influenced by a range of factors, both internal, i.e. company decisions and external, i.e. market and structural considerations.[3] Consequently, it is important to recognise that the actual debt characteristics observed for companies are a combination of the outcomes imposed by debt market conditions at the time and outcomes resulting from their 'free choice' decisions. To

[3] See Chairmont, 'Financing Practices Under Regulation: Past and Transitional', October 2015 p.18 for a full description.

the extent their funding needs give them flexibility, the debt characteristics are usually determined based on current and expected credit margins for that company.

In summary, EICSI reflects both behavioural factors as well as simple market prices. On the other hand, external bond yield time series report the market prices of any secondary market bonds on a regular (e.g. monthly) basis, keeping static criteria for term to maturity, rating and any other restrictions set by those market rate providers.

4.1.7 Debt Type Exclusions and Fee Inclusions

EICSI seeks to include only senior vanilla debt, similar to the structural restrictions of market data indices. Special case debt, involving credit-adjustment criteria or special purpose conditions, is removed. This includes working capital, bridging loans, leases and subordinated debt.

Fees associated with debt raising are only included if they act as an additional borrowing margin, such as line fees or commitment fees, as these are constant costs that are sometimes applied in place of a higher lending margin on bank debt. Other fees such as undrawn fees or establishment costs are not considered part of the borrowing margin. The former is a substitute for the borrowing margin, when the loan is undrawn, while the latter is a debt raising expense, which AER treats separately in its allowance consideration.

4.2 CAVEATS ON COMPARABILITY

4.2.1 Importance of Comparability

The "analytical goals" set by AER for this data gathering and aggregation exercise centre on the use of the industry data to inform AER's decisions about which external data series to use in calculating its allowed return on debt.

The comparability of industry data with external data series, and limits to that comparability, is central to any interpretation of results.

4.2.2 Portfolio Composition

The composition of its constituents is a point of difference between EICSI and the external data series. The market indices use reasonably static criteria for inclusion of bonds in each of their reported time series. Typically they restrict inclusion to factors such as term to maturity (e.g. close to 10 years), rating (e.g. broad BBB) and the volume of each issue outstanding.

On the other hand, EICSI is based on all debt raised by the industry, regardless of whether it is bonds or loans, the term, rating or size. The result is that the debt portfolio, (i.e. bonds and loans) underlying EICSI can be quite different to the bond portfolio underlying the market indices.[4]

[4] The imperative of comparing the constituents of different indices or curves has been a common and essential theme in efforts to measure a return on debt from market prices. Prior to the creation of the current Guidelines published by AER in 2013, Chairmont produced a paper emphasising the importance of using like-for-like debt constituents if the resulting yields are to be directly compared. At that time the emphasis was on finding market prices which adequately matched seniority (senior debt), structure (e.g. non-optionality), perceived credit risk and industry comparability. (Chairmont, 'Debt Risk Premium Expert Report', February 2012, p6). Similar principles need to be kept in mind in the current exercise as wherever characteristics of the debt constituents of two indices differ, the resulting yields or spreads are not directly comparable. Nonetheless, once aware of the differences, the outcomes can provide valuable information as part of understanding the overall picture.

4.2.3 Observation Timing

Market indices measure prices on a regular basis, at least monthly, so that an average for a given year is based on evenly spaced data observations. Whereas, EICSI receives observations whenever providers raise debt. It is not unusual for providers to raise debt at similar times to one another, reflecting their behaviour of taking advantage of favourable debt market conditions at that time (pricing date clustering).

4.2.4 Impacting Factors

Table 1 contains the factors influencing EICSI in any particular 12 month period include:

Factor	Direction	Variability
Size	-	Small
Term	+	Significant
Rating	-	Significant
Pricing Date Clustering	Normally -	Significant

Table 1: Impacting Factors

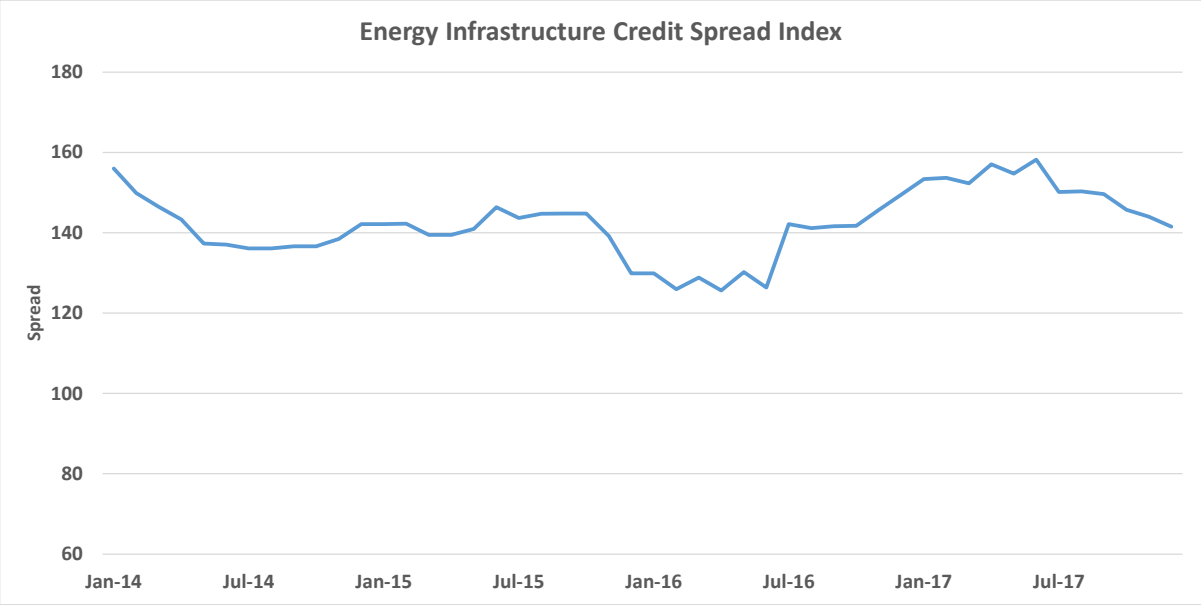
For example, in years where the average debt raised has a term significantly shorter than AER's benchmark assumption of 10 years, EICSI can be expected to be lower than the market data average. Similarly, where the majority of issuance is undertaken by firms rated A- or higher, the index can be expected to be lower than the market measures which are based on broad BBB ratings.

5 INDEX RESULTS

5.1 INDEX 2014-2017

EICSI begins in January 2014 as it is a 12-month historical average of the data collected from January 2013. Using the methodology described in Section 4, the service providers' data produced an EICSI as shown in Graph1. The level refers to the average credit margin experienced by the industry in the preceding 12 months. Graph 1 shows the level at that time to be 156bp. This means that the simple average of credit spreads of the industry's new debt priced between the beginning of January 2013 and the end of December 2013 was 1.56% above the variable 3-month BBSW rate.

Graph 1 indicates that the starting observation of EICSI was also near its peak. In 2013 markets were still recovering from the Global Financial Crisis (GFC) and the European debt crisis, hence it is not surprising that the industry also had to pay higher than normal credit spreads. EICSI then fell quickly through the first half of 2014 before slightly rising from the third quarter of 2014 to third quarter 2015, but not again reaching the high point at the start of 2014 until briefly in June 2017. From the initial high levels it fell to its lowest point in February to June 2016 to a low of 125bp. It was the year of June 2016 to 2017 that saw the index rise to slightly above the 2014 starting value again, reaching 158bp. The second half of last year again saw it easing back to finish the year at 141bp.

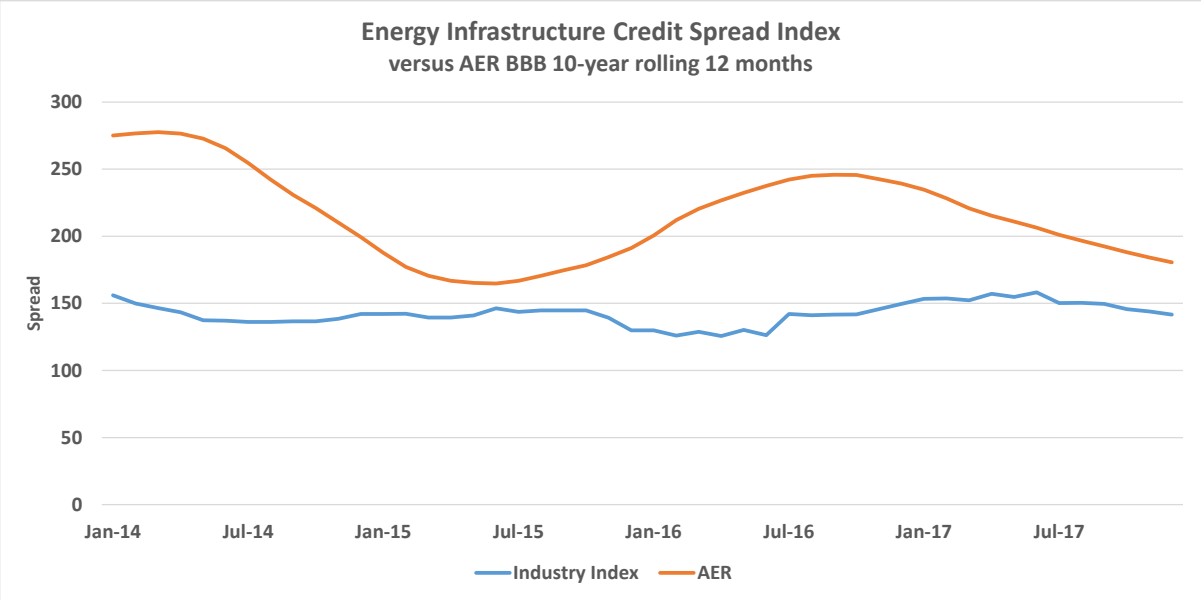


Graph 1: Energy Infrastructure Credit Spread Index

5.2 EICSI VERSUS THE MARKET

To provide further context for EICSI, Graph 2 plots it against the rolling 12-month average of AER's market spread indicator. It shows spreads on 10-year BBB bonds using AER's return on debt methodology drawing on data from the RBA and Bloomberg.[5]

[5] AER use a simple average of the 10-year BBB rated bond yield published by the RBA and the 10-year BBB BVAL bond curve data from Bloomberg, after extrapolating both to an exact 10-year term. To calculate the spread for the graph, AER subtracted the 10-year swap rate at the time. Chairmont relied on AER's modelling and data.



Graph 2: EICSI in Context of AER 10-year BBB Spread

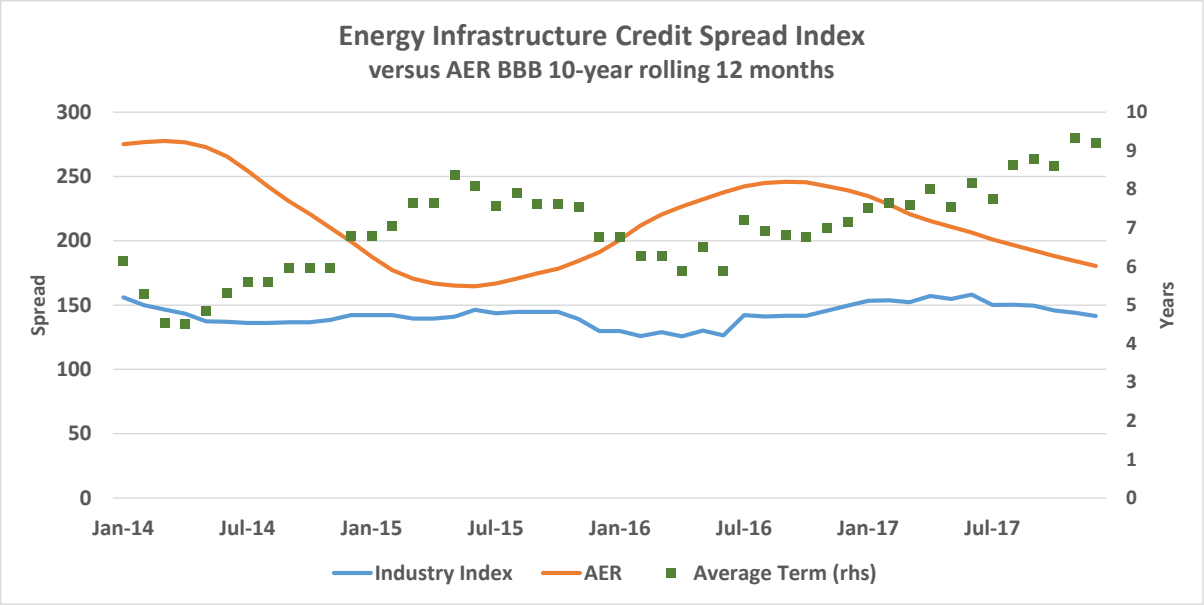
Graph 2 displays the type of discrepancy between the two concepts foreshadowed in Section 4.2 above. At times the two measures of credit spread differ significantly. For example, in the second quarter of 2014, AER was measuring the spread over swap as being almost 140bp more than EICSI. The AER market measure is thereby double the spread recorded by the industry. The graph also displays the large variations in that difference between the two measures over time.

It is essential to understand that the gap between the indices is significantly explained by actions taken in the period for which data was provided. It is not a predictor of the relationship between the measures in the future or a descriptor of the longer term past. It is possible that in the future the order of the indices could reverse, whereby EICSI exceeds the AER calculation. This could arise due to any of the factors explained in Section 4.2 and especially in a time where the industry issues predominantly long term debt, e.g. 17 years, or where AER's market rates drop quickly after the industry has already issued most of its annual debt requirements, (i.e. causing pricing date clustering described in Section 4.2).

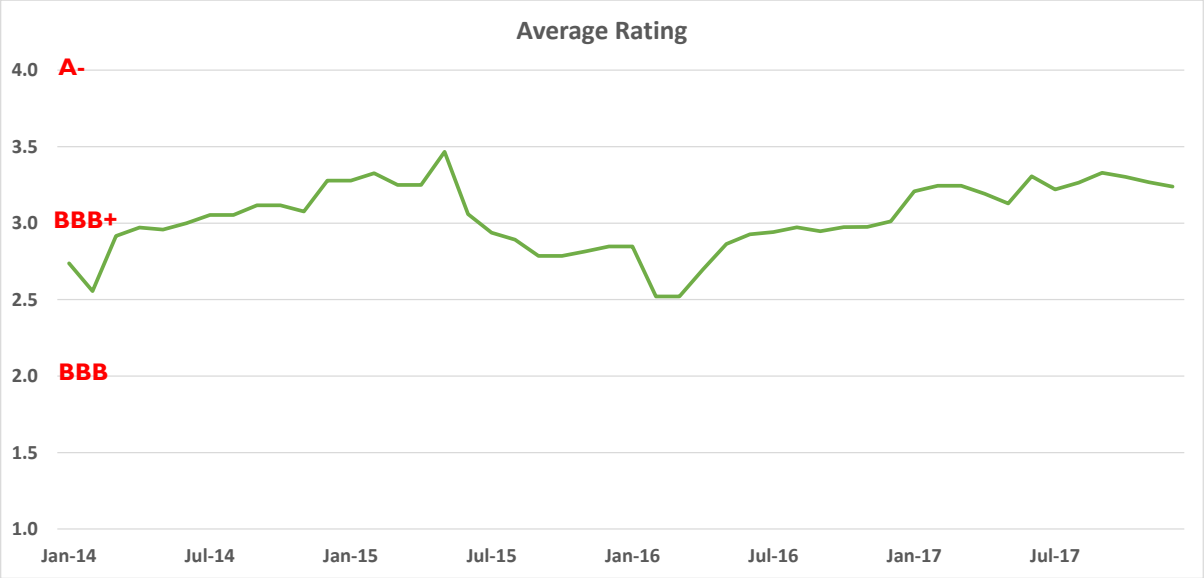
5.3 Importance of Index Composition

As noted in Section 4, the debt characteristics underlying EICSI at a particular point in time may differ significantly from the bonds underlying the AER or other market data indices. It is in the portfolio composition that much of the behaviour of EICSI can be understood. Two of the key influences on credit spread are the term to maturity and the rating of the debt. Graphs 3 and 4 below measure these elements to help explain the spread difference between EICSI and the market indices.

Graph 3 overlays Graph 2 with a new factor being the average term of the debt raised by the industry in that period. Graph 4 shows the average rating of issued debt for that period. The rating is graphed separately in Graph 4 and placed directly under Graph 3 to demonstrate the combined influences. These are discussed below.



Graph 3: Relating Debt Term to Spread Difference



Graph 4: Average Rating of Industry Debt Issuance

A striking feature of EICSI compared to AER's market measure is its relative stability. Over the entire period it varies by less than 35bp, while the market data records a range of almost 115bp. Graphs 3 and 4 display EICSI's varying composition and go a long way to explaining its stability. For the first months of the time line the market spread was at its highest, which coincides with the time that the industry was issuing debt with some of the shortest average tenors, down to 4 ½ years. There is usually a significantly lower credit spread for a 4 to 5-year term (as in EICSI) than for a 10-year term (as in the AER index), especially in times of generally higher credit spreads.

Further examination along the time line in Graph 3 shows the AER measure declined through the middle half of 2014, while EICSI remained reasonably constant. This is coincident with an extension of the term of debt being issued, i.e. increasing to almost 7-year maturities by December.

In the period from mid-2014 through to mid-2015 Graph 3 shows a key behavioural feature of the industry. Specifically, as market rates fell, networks extended the average term of their debt to almost 8 ½ years, making EICSI closer to the 10-year assumption of AER. This explains EICSI rising when the market 10-year spread fell. A similar effect occurred again from late 2016 to mid-2017. Counterpoised to that, the increase in market spreads up to mid-2016 was associated with a reduction in the average term of debt raised.

This negative correlation between the industry's debt term and market spread is one of the main explanations of a more stable EICSI. Section 4.1.6 noted that the term of debt is partially forced on companies and partly their own decision.

To examine the behaviour of the average credit rating of debt raised in EICSI, Graph 4 should be read with reference to Graph 3. The two periods of trending improvement of the average rating were the first 18 months of the index and from March 2016 through to late 2017. Overall, the average rating can be seen to be significantly correlated with the average term of raising from Graph 3. This correlation does not imply causation, as both are typical of favourable credit market conditions. However, their positive correlation goes a step further in explaining the stability of EICSI despite significant swings in market rates.

There has also been a structural, or at least cyclical, change in the average rating of the industry. Most of the firms operating currently have seen their credit ratings raised compared to five years ago. Graph 4 should be interpreted not only as displaying the different composition of debt raising between companies in the industry, but also a trend of the whole industry.

An example of different market circumstances which could occur again in the near term can be seen in the period May to November 2015, where the average rating dropped sharply from high BBB+ to high BBB. At the same time the term to maturity was reasonably constant as market rates were beginning to rise. This is a typical late stage credit market reaction. When margins reach a low level, investors become willing to accept more debt from lower rated companies as the investors chase higher yield. Similarly, from the supply side, lower rated issuers are usually keen to lock in longer term funding in larger amounts, as they understand that rising market margins will affect them more than higher quality credits.

6 POTENTIAL TO CREATE AN ADJUSTED EICSI

6.1 EICSI ADJUSTMENT CONSIDERATIONS

Differences between the concepts of the market debt cost indices and the unadjusted EICSI raise the question of whether an adjusted EICSI can be created which would be more useful in comparisons.

One approach to potentially minimise discrepancies between EICSI and external market indices is to calculate an adjusted EICSI, whereby weightings are applied to reflect differences in those compositional factors affecting price.

There are a range of adjustment methods that may be used to create an adjusted EICSI. Some of these are outlined below, however a weighted index would introduce significant model risk. There is no uncontroversial method to weight reported spreads for factors which influence the relative spread level. The danger is that any adjustment method could reduce the clarity and informational benefit of collecting and aggregating actual industry spread data. This is an area which AER and the industry may wish to further explore.

6.2 INDEX ADJUSTMENT FACTORS

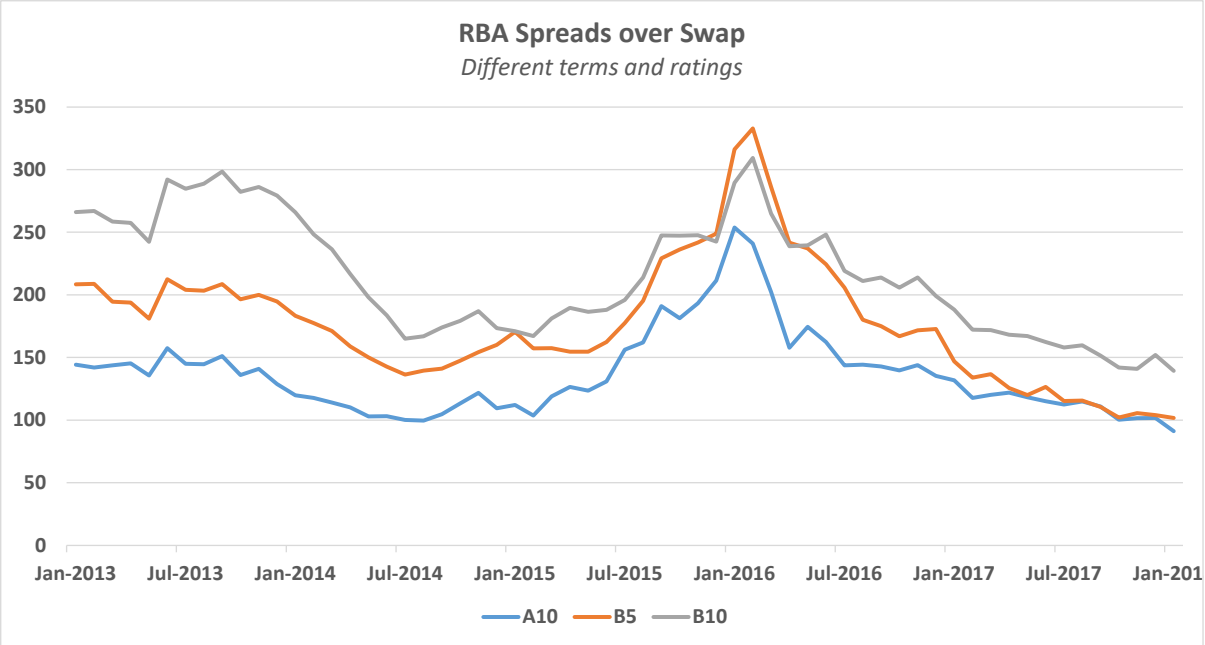
6.2.1 Size

Weighting the raisings for relative size is most likely to be the easiest adjustment, as it can be a simple percentage of the total for rolling 12-month period. This concept may be considered as a corollary to market capitalisation weighting used in share indices. While there will be some variation of the impact between larger and smaller raisings over time, the extent of impact will depend on other factors applying to the debt raising. For example, a debt raising may be for more than one reason, e.g. for a change of ownership.

6.2.2 Term

Adjusting for term to maturity is more complicated, as the term structure of the credit spread can vary considerably over time. Additionally, at any point in time the term structure is usually different depending on the rating of issuer. To appropriately weight reported spreads requires a time-dependent conversion factor reflecting the slope of the appropriate credit term structure at the time of raising. This would require using time series of spreads for various ratings and maturities. The most relevant time series in the context of AER's current allowance calculation are likely to be the RBA and BVAL time series for shorter maturities and broad A rating categories.

Graph 5 illustrates the variability of the relative spreads for corporate debt of differing term and/or rating. It draws on the monthly RBA time series for those debt types.



Graph 5: Corporate Bond Spreads for Differing Terms and Ratings (2013-17)

The complexity of the relationships is apparent from Graph 5, along with the importance of conducting deeper analysis of the data. For example, the RBA data reports that spreads for 5-year BBB debt (B5) were higher than spreads for 10-year BBB debt (B10) around the beginning of 2016. This is unlikely to be a true reflection of comparable bond pricing, but rather arises from different composition of issuers between the two bond sets at that time.

A simplified approach could be to apply a constant proxy to weight for deviations in term for an issue compared to 10 years. Given the time-variability of relative spreads across term and rating categories depicted in Graph 5, including this as an additional modelling assumption may dilute some of the benefit of having 'actual' debt raising data from networks.

6.2.3 Rating

Consistent with the Term factor, the difference in spread for various ratings will vary over time, as displayed in Graph 5 above. There are also secondary effects of rating differences which impact the EICSI result. Market conditions at times may dictate that only or mainly the higher rated companies are able to issue large amounts or longer terms of debt, which was observed in relation to Graph 4 in the previous section. This will bias the composition of EICSI in a particular year.

Nonetheless, if desired, the RBA and BVAL time series could serve as the weighting mechanism for rating differences. Similar to the caveat on using a constant adjustment factor for term differences, any constant proxy for rating differences would introduce greater model risk to EICSI instead of exclusively using pure data.

6.2.4 Pricing Date Clustering

Incidences of date clustering will typically occur when favourable spreads are available in the market. While that effect will usually mean a lower raising cost for EICSI compared to the yearly average used for AER's allowance calculation, it should not be adjusted for.

EICSI is intended to provide an unadjusted measure of actual raising costs for firms and hence reflect any efficient financing decisions made by the firms compared to the unresponsive market measures.

APPENDIX A: TERMS OF REFERENCE

Australian Competition & Consumer Commission

EXPERT CONSULTANCY PANEL REQUEST FOR QUOTE (RFQ): AGGREGATION OF RETURN ON DEBT DATA

FOR THE PROVISION OF CONSULTANCY SERVICES

Invitation to Quote

The Australian Competition and Consumer Commission (ACCC)/Australian Energy Regulator (AER) are seeking quotations from suitably qualified service providers for the provision of consultancy services.

In submitting a response, potential suppliers are required to comply with all the requirements set out in the Deed of Standing Offer. We have divided the services required into a main stage (stage 1) and a contingent second stage (stage 2).

- The services for stage 1 are required by 28 February 2018.
- The services for stage 2 would require participation in a series of conferences/sessions in March 2018

Requirements

AER determines the amount of revenue that electricity and gas network businesses can recover from customers for the use of their networks. A key component of this allowed revenue is the 'rate of return'. This is a forecast of the cost of funds a network business requires to attract investment in its network.

It enables network businesses to obtain necessary funds from capital markets to fund capital investments and service the debt they incur in borrowing the funds. The return on capital makes up approximately 50 per cent of a network business' allowed revenue. It therefore is a key driver of the amount of network charges that consumers pay.

AER has recently commenced its review of the rate of return guideline. This guideline must be completed by December 2018. Recently we have published:

- an issues paper setting out our initial views on priority issues for review;[6] and
- a positions paper detailing the review process.[7]

The choice of data series that we use to estimate the return on debt is one of the issues under review. Our current approach is to adopt a simple average of the debt data series published by the RBA and Bloomberg that match, as close as available, our current benchmarks of a BBB+ credit rating and a 10 year debt term. Specifically, our decision is to adopt a simple average of:

[6] Available here.
[7] Available here.

- The 10 year estimate from the non-financial corporate BBB rated data series published by the RBA (the RBA curve), and

- The 10 year yield estimate from the Australian corporate BBB rated Bloomberg Valuation Service (BVAL) data series published by Bloomberg (the BVAL curve).

For further details on our approach and the adjustments made to the curves, see our recent decision for APA VTS.[8]

Since adopting our approach, we have become aware of two new debt series that could be used in our estimation process: the Thomson-Reuters AUD yield curve and the Standard and Poor's AUD yield curve. As part of our guideline review, we will re-evaluate which curve or combination of curves to use for estimating the return on debt.

As part of this process, we will seek actual cost of debt data from regulated service providers. The consultancy services required are to assist us in requesting appropriate data and in aggregating this data to assist with sector-level comparisons against our current approach. In particular, we aim to develop a representative annual series (**the aggregated series**) of the costs of issuing debt faced by the responders to the request. We aim to use this data to support our analysis of whether our current choice of data series or possible alternative choices of data series produce outcomes that are reasonably consistent with the actual costs of issuing debt faced by service providers (**the analytical goals**).

Services required

The advice required, without in any manner directing the Consultant, should include the following extensions/expansions to the stage one report:

Stage 1

1. Read our draft request and excel template and advise staff whether the data is sufficient and not excessive to achieve the **analytical goals** set out in the request. This may include recommended amendments. We expect this stage to take place in January 2017.
2. On receipt of the information request data, develop (to the extent achievable) **the aggregated series** of the costs of issuing debt faced by responders to the request. The aggregated series should be publishable. No individual responders' information should be identifiable from the series.
3. To accompany the aggregated series, develop a short document setting out relevant assumptions and/or adjustments made to the response data to aggregate the series. This series should be publishable. No individual responders' information should be identifiable from the series.

Stage 2

4. Depending on submissions, the services provided might require participation in an expert 'hot-tubbing' session. We describe this process in detail in our process paper. As it is unclear whether this topic will require attendance at such a session, please quote for this on a contingent basis.

Selection Criteria

This will be based on:

- expertise with debt markets and pricing debt

[8] The rate of return attachment is available here. The relevant section commences p 3–123.

- understanding of the CPI–X incentive regulatory framework applied under the NER and NGR
- potential or perceived conflicts of interest.

Key Considerations

Respondents should be aware that the contract amount will be capped.

Information

The Quote including all attachments and supporting documentation must be written in English. Quantities are to be expressed in Australian legal units of measurement.

Your response should also include:

- A summary of your understanding of the requirements and how you will address these issues;
- A statement concerning your organisation's capability to address the requirements and in particular expertise in relation to inflation, rate of return, and compensation for risk;
- A list of all previous work by the Consultant, whether in Australia or internationally, on related topics to those in the services required provided;
- A list of recent previous work by the Consultant, provided to Australian energy network infrastructure operators or advocates of Australian energy consumers, on topics unrelated to the services required;
- A list of referees which may or may not be contacted.

Responses which do not include this information may not be considered any further.

The ACCC/AER will only accept responses on the basis that you have:

- Examined this RFQ, any documents referenced in this RFQ and any other information made available by the Commonwealth to tenders for the purpose of Quoting;
- Examined all further information which is obtainable by the making of reasonable inquiries relevant to the risks, contingencies, and other circumstances having an effect on their Quotation; and
- Been satisfied by the correctness and sufficiency of the Quote including pricing structure.

Provision of this Quotation is made on the basis that the respondent acknowledges:

- They do not rely on any representation, letter, document or arrangement whether oral or in writing, or other conduct as adding to or amending these conditions other than amendments addenda issued by the ACCC/AER;
- They do not rely upon any warranty or representation made by, or on behalf of, the Commonwealth, except as are expressly provided for in this RFQ, but they have relied entirely upon their own inquiries and inspection in respect of the subject of their tender;
- The ACCC/AER shall not be responsible for any costs or expenses incurred by respondents in complying with the requirements of this RFQ;
- Neither these conditions nor the Quote give rise to contractual obligations between the ACCC/AER and the respondent; and

- They are not to make public statements in relation to this Quote without prior written permission of the ACCC/AER.

Lodgement Details

Your response is to be delivered via email as follows:

Attention:	Kevin Fincham
RFQ:	**Aggregation of return on debt data**
Email:	kevin.fincham@aer.gov.au

Responses must be lodged on or before 5.00pm Australian Eastern Standard Time on 18 January 2018. Quotes should be clearly marked.

Any queries on this matter should be directed to:

Kevin Fincham
Assistant Director, Network Finance & Reporting
Australian Energy Regulator
07 3835 4677
kevin.fincham@aer.gov.au

Esmond Smith
Director, Network Finance & Reporting
Australian Energy Regulator
03 9290 1956
esmond.smith@aer.gov.au

ACCC/AER Conditions

The ACCC/AER does not guarantee, warrant or otherwise represent that any business, revenue or other benefit or any minimum volume or value of business, revenue or other benefit will be earned or received by any successful respondent.

The ACCC/AER will decide on any further action after reviewing the responses to the RFQ. The ACCC/AER reserves the right to:

a. Vary the process and timetable relating to this process in its absolute discretion;
b. Vary the terms of the RFQ;
c. Cease the RFQ process;
d. Accept or reject any Quotes whether or not they are compliant;
e. Seek additional information or clarification from Respondents (including their sub contractors or agents);
f. Shortlist, select and negotiate with more than one Respondent;
g. Cancel, add to or amend the information, requirement, terms, procedures or processes set out in this RFQ; or
h. Approach the market with an open Request for Tender (RFT) or seeking further Quotations via an Expression of Interest (EOI).

APPENDIX B: TEMPLATE REQUEST LETTER AND EXCEL FILE

Template Request Letter:

AUSTRALIAN ENERGY REGULATOR

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Our Ref: [redacted]
Contact Officer: [redacted]
Contact Phone: [redacted]

6 February 2018

[redacted]

Dear [redacted]

Re: Rate of return guideline review - Request of debt information – [redacted]

We recently commenced a review of our rate of return guideline, to be completed by 17 December 2018. Through our recent issues paper published in October 2017, we noted specific input we would like to receive to assist in reviewing the guideline.

Application of data series

One of the issues that we identified as a priority in our issues paper is a review of third party data series used for return on debt implementation. We currently estimate the return on debt using a simple average of the Bloomberg (BVAL) and RBA broad-BBB rated yield curves.

Since determining our current approach, we have become aware of additional data series that have become available. These are the yield curves published by Thompson Reuters and Standard & Poor's.

As we noted in our October issues paper, we intend to investigate the merits and limitations of the four data series, both in isolation and in various combinations. We also wish to support this analysis with reference to the actual debt issuance data.

Aim of exercise

The aim of this exercise is to gather actual debt issuance data to help inform our assessment of our debt approach. In particular, we intend to use this information:

- as a 'sense check' of the reasonableness of outcomes using our current approach
- to assist in considering the reasonableness of possible curve combinations using the existing and new curves.

We have engaged Chairmont Group to assist us in targeting the data requested and to help aggregate data for the industry to compare to the broader corporate debt market, rather than provide a comparison or analysis of any one company. See below on confidentiality.

We recognise that there may be variances between the published yield curves and the actual cost of raising new debt undertaken by providers in any particular year, and those variances may change from year to year, depending on the particular pattern of issuance undertaken by providers in that year. We will consult with all stakeholders on the approach we have taken to aggregating data and any analysis we undertake on it.

The request

Please provide details of:

- all debt outstanding at January 2013; and
- all debt raised from (and including) January 2013 until today using the spreadsheet attached to this request.

This can be compiled at the asset level or the corporate group level to reflect how debt is raised for each network.

The spreadsheet attached is similar to one sent to networks in 2015. We have refined the spreadsheet based on advice from Chairmont Group. We have worked with Chairmont to minimise the extent of this request while still meeting our objectives for the analysis.

Please provide your response by **COB Tuesday 20 February**.

Further information

If you believe that additional information is required to understand the debt raising costs of your company, please also include that with a simple explanation.

Confidentiality

If you wish to claim confidentiality over any of the material submitted in response to this request, please do so in line with the ACCC/AER's confidentiality guideline.

Yours Sincerely

[redacted]
General Manager
AER Network Finance and Reporting

Template Excel File:

Debt instruments

Table 1 - Debt instruments

No	1 Type	2 Pricing Date	3 Commencement Date	4 Original Maturity Date	5 Date of early repayment (if applicable)	6 Currency of issue	7 Face value at commencement date Issue currency $M	8 Face value at commencement date AUD$M	9 Name of issuer	10 Is the issuer a finance company ? (Y/N)	11 Country of issue	12 Private/Public	13 Senior Vanilla / Subordinated/ hybrid etc*	14 Facility (eg. Bond/term debt/revolving)	15 Lender	16 Type - fixed or floating	17 Credit wrapped or enhanced #	18 Embedded options#	19 Unadjusted coupon/ interest Total interest	20 Frequency	21 AUD Spread (over swap/BBSW) bp	22 Frequency	23 Fees Upfront total (k)	24 Ongoing total (bp)	25 Rating at the time of execution S&P/ Moodys/Fitch
1	MTN (example)	14-Jan-13	01-Feb-13	01-Feb-16	15-Mar-14	AUD	200	200	AAA Company Pty Ltd	N	AUSTRALIA	Public	SENIOR	Bond	Bond Investors	FIXED	NO	Early repayment option conditional to….	6.5000%	SEMI-ANNUAL	110bp	SEMI-ANNUAL	1,000	2bp pa	BBB+/Baa1/-
2	Bank debt (example)	15-Jul-14	15-Jul-14	15-Dec-19	n/a	USD	65	76	AAA Company Pty Ltd	N	US	Private	SENIOR	Term debt	Westpac	Floating	NO	N/A	BBSY + 1.25%	Quaterly	125bp	Quaterly	250	5bp on undrawn	BBB/Baa2/-
3																									

Financial instruments

Table 2 - Financial instruments

1 Type of financial instrument	2 Identify the debt instrument to which the financial instrument applies in tab 'Debt Instruments'	3 Deal date	4 Notional Amount (AUD millions)	5 Exchange traded or over-the-counter (direct or intermediary)	6 Counterparty	7 Intermediary	8 Start Date	9 Mat. Date	10 Early termination date (if applicable)	11 Hedged Item (for IRS - fixed for floating, floating for fixed or floating for floating; for cross currency swap - type of currencies traded; and for options - cap, floor, collar, foreign exchange call or foreign exchange put)	12 For AUD IRS Receive leg	13 Pay leg	14 For cross currency swaps Receive leg	15 Pay leg	16 Explicit or embedded option Early exercise features	17 Strike or exercise price	18 Dealer swap margin (bps) Credit Margin (bps)	19 Execution Margin (bps)	20 Comments
A$ IRS (example)	3	11-Apr-12	180	OTC	ANZ	n/a	31-Mar-13	31-Mar-17	11-Jan-17	Floating for Fixed	3mBBSW + 1.25%	5.3710%			N/A	N/A			