Summary of CME Report

Rising electricity prices in Queensland: Evidence and Reasons for Action

Introduction from CANEGROWERS

CANEGROWERS commissioned Mr Bruce Mountain, from CME to analyse the reasons behind recent rapid price increases for electricity in Queensland. Electricity is an important input for the Queensland sugarcane industry. 55% of sugarcane growers irrigate all the time and a further 15% irrigate selectively, particularly in dry periods.

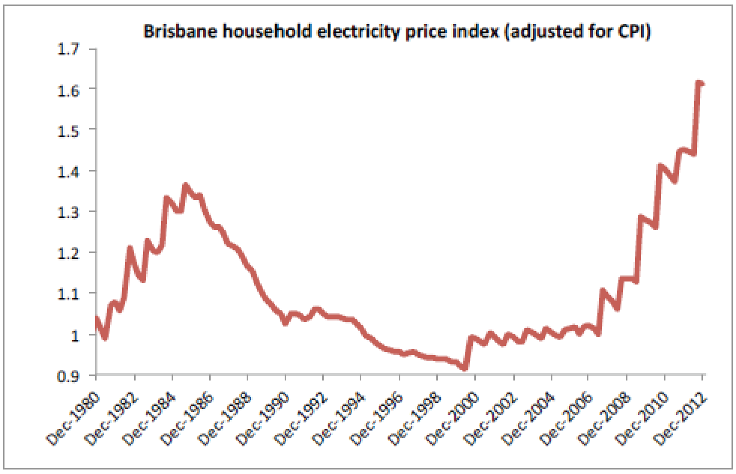
The majority of irrigation pumps in Queensland are electric. Pumps, where converted to electricity from diesel to increase utilisation across the network in off-peak times, use latent generation from Queensland's state-owned energy assets. But now, the price of electricity is out of control – having increased by 90% (nominal) between 2008 and 2014.

Summary of CME Report

Data from the Australian Bureau of Statistics shows that electricity prices paid by households increased by more than 60% (constant currency) between 2008 and 2012.

Analysis by CME unambiguously shows that the large increases in power prices have delivered large financial benefits to the Queensland Government – a compounding 114% growth in financial returns every year.

Figure 1. Electricity price increases to households in Brisbane



Source: CME analysis, ABS data

The CME report outlines four reasons why it is reasonable for the Queensland Government to reduce network charges, and in turn **reduce** the price of electricity in Queensland.

Reason 1. Queensland's networks are state owned and should deliver electricity cheaper

The Federal Government regulates electricity network assets in the National Energy Market through the Australian Energy Regulator (AER). However, the AER assumes that all network companies are privately owned – this is not the case in Queensland, New South Wales or Tasmania.

This means that the Queensland Government receives additional income from a range of sources, such as:

- Debt fees, the difference between the cost to the Queensland Treasury and the private rate for debt.
- Corporate tax equivalents, the company tax Ergon, Energex and Powerlink would pay if they were a private company.
- A higher WACC (Weighted Average Cost of Capital) than would be incurred in the private sector.

Any private business operating in a competitive market would not receive these pecuniary benefits.

If the Queensland Government was to forgo these benefits, prices could be immediately reduced by 10-20 %.

Reason 2. Regulated asset values are inflated

Ergon, Energex and Powerlink charges are calculated on capital expenditure of $14 billion over the current 5-year regulatory price period based on the expectation forecast of increase in demand for electricity.

In reality, overall demand hasn't increased at forecast rates and Ergon, Energex and Powerlink have spent $11.6bn on network infrastructure.

Under the current AER regulatory regime, Energex, Ergon and Powerlink are able to recover a capped amount of revenue, regardless of the amount of utilisation. This is an unsustainable pricing model (higher prices = less customers = higher charges = higher prices).

Further to this even though it is not used or useful, all of this expenditure will be included in the regulated asset base and the costs of this (depreciation plus 9% return) are "recovered" from users in AER's regulated charges.

In a competitive private business, the poor investment decisions would be written down by the owner and not charged to the consumer. The Queensland Government should not be charging energy users (including depreciation and a 9% return on assets) for assets that aren't used or useful.

Reason 3. Less is being spent, but more is being collected

In light of the analysis in reason two, the Queensland Government has been placing pressure on Ergon, Energex and Powerlink to cut excess expenditure. While the Queensland Government is investing less, the AER allows full "recovery" of the existing determination. This means Queenslanders are paying more for less.

It is only fair that the Queensland Government passes on any reduction in cost to Queensland businesses, households and irrigators.

Reason 4. Assets are being stranded

Electricity prices are so high that customers of all descriptions are looking for ways to off-set their power prices. Households are using less or investing in photovoltaics, industry is investing in coal and gas and irrigators are converting their pumps to diesel. The contraction in demand while the economy is expanding is evidence of this trend. The effect of this is to leave users with stranded electrical assets while the Queensland Government has a guaranteed and substantial return.

Low asset utilisation is also a major issue for the future of Queensland's electricity assets, as identified by the Costello Commission of Audit. Any actions by the Queensland Government to reduce electricity prices will not only reduce the extent of energy users' asset stranding, and welfare-reducing demand reductions, but will also reduce the extent of stranded NSP assets.

The full report can be downloaded from the CANEGROWERS website:
www.canegrowers.com.au/page/electricity

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