



29 October 2015

## **ASX RELEASE**

### **UNITED ENERGY DRAFT REGULATORY DECISION**

DUET Group (DUET or the Group) notes the attached release by United Energy (UE) in relation to the AER's Draft Decision for UE's 2016-20 Electricity Distribution Price Review (EDPR).

Key points to note from the AER's draft decision include:

- 7.3% nominal post-tax return on equity
- 5.7% increase in the operating expenditure allowance compared to the 2011–2015 period regulatory allowance (in 2015 Real terms)
- 4.6% reduction in the capital expenditure allowances compared to the 2011–2015 period regulatory allowance (in 2015 Real terms)
- 8.7% reduction in real tariffs in each of calendar years 2016 and 2017
- 5.3% reduction in expected smoothed revenue compared with the 2011-2015 regulatory period (in 2015 Real terms)

The building block revenue components, capital expenditure allowances and tariff path proposed in the AER's draft decision are set out in an attachment to this release.

This draft decision sets tariffs for calendar year 2016 only. UE will respond with a revised proposal by January 2016 and the AER's final decision is expected to be published in April 2016. The final decision will set tariffs for calendar years 2017– 2020 (including any true up for any under/over recovery of revenues in 2016), subject to any appeal of the final decision by UE.

The AER's proposed tariffs are based on a lower risk free interest rate compared with the previous regulatory period. Importantly, UE will reset its base interest rate hedges for the 2016 period during the AER's observation period in November-December 2015, resulting in significantly lower interest costs.

The AER found that UE is one of the most efficient service providers in Australia. However, it provided allowances for operating and capital expenditure based on a reduced scope of work and lower demand forecasts. UE will work with the AER to clarify our capital expenditure proposals to ensure UE can achieve the regulator's targeted network performance standards.

UE will also review the outcome of the current NSW electricity distributors' appeal, including their appeal relating to the cost of capital and tax allowances, prior to lodging its revised proposal.

DUET's Chief Executive Officer, Mr David Bartholomew, said "The tariffs proposed in the AER's draft decision reflect the current low interest rate environment. By re-setting its base interest rate hedges, UE expects to benefit from material reductions in interest expense. DUET's distribution guidance of 18.0 cents per stapled security for FY2016 remains unchanged as does our medium term distribution growth target."

For further information, please contact:

Investor Enquiries:

**Nick Kuys**

GM Operations and Investor Relations

Tel: +61 2 8224 2727

Email: n.kuys@duet.net.au

Media Enquiries:

**Ben Wilson**

Public Affairs Manager

Tel: +61 407 966 083

Email: bwilson@gracoswaypr.com.au

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## **AER's draft determination on electricity network regulatory proposal**

United Energy welcomes the Australian Energy Regulator's draft determination on its 2016-20 regulatory proposal and recognises the amount of work involved in assessing multiple proposals across the National Electricity Market.

The draft determination will reduce network investment by 4.6% compared to the current regulatory period.

UE Chief Executive, Tony Narvaez said the draft decision appeared to underestimate the impacts of ageing assets on the network, which increase the risk of equipment failure and reduced reliability.

"Our proposal set out a prudent investment plan to maintain a network that matched the needs and expectations of our community. We are concerned that the cuts contained in the draft determination may compromise our ability to manage the issue of ageing infrastructure over the next five years," he said.

"It is also notable that while our capex allowance has been reduced the AER has not amended the framework that sets network reliability targets. We will continue to engage with the AER on these aspects of its draft decision."

United Energy's proposal included a price cut for a typical residential customer of around \$70, while at the same time introducing initiatives to improve customer service outcomes.

"We are very focused on energy affordability. We welcome the AER's recognition of our commitment to stakeholder engagement. However, we are disappointed that key initiatives from this consultation have been rejected, including those designed to improve customer service and ease of interaction with United Energy," said Mr Narvaez.

"We will now work through the detail of the draft decision and consider how we might reprioritise our network investment to minimise disruption for our customers. Our objective is to remain among the most efficient network operators nationally."

United Energy will submit its revised proposal in January 2016, following further stakeholder consultation.

### **Media enquiries:**

Samantha Porter  
United Energy  
0418 307 139

# 2016-2020 AER Draft EDPR Summary (Real 2015)



UNITED ENERGY

## AER Proposed Revenue Building Block Summary

\$real 2015	UE Proposed	2011-2015 Allowance	AER Draft Decision	% Change Allow – Draft
Return on capital	824.9	811.6	649.7	-19.9%
Reg Depreciation	360.5	311.3	292.5	-6.0%
Operating Expenditure <sup>1</sup>	706.0	623.9	659.5	5.7%
Revenue adjustments (EBSS and shared assets)	25.0	-37.2	26.6	171.5%
Tax allowance	138.9	90.2	78.5	-13.0%
Total Revenue (unsmoothed) <sup>1</sup>	2,055.4	1,799.9	1,706.9	-5.2%

## WACC Parameters

	UE Proposed	2011-2015 Allowance	AER Draft Decision
Real Rf – equity only	0.14%	2.44%	0.24%
Implied DRP	3.03%	3.89%	2.58%
Equity Beta	0.89	0.8	0.7
MRP	8.2%	6.5%	6.5%
Gamma	0.25	0.25	0.40
Gearing	60%	60%	60%
Real Vanilla WACC	4.76%	6.74%	3.53%
Post tax Real ROE	7.27%	7.51%	4.68%

## Expected Revenue (smoothed)

\$real 2015	UE Proposed	2011-2015 Allowance	AER Draft Decision	% Change Allow – Draft
Total revenue	2,054.4	1,798.9	1,702.0	-5.3%

## Capital Expenditure

\$real 2015	UE Proposed	2011-2015 Allowance	AER Draft Decision	% Change Allow – Draft
Augmentation	166.6	205.3	124.3	-39.5%
Connections	249.1	283.3	244.0	-13.9%
Replacement	585.1	368.1	405.4	10.1%
Non-Network General <sup>2</sup>	133.3	149.3	132.6	-11.2%
<b>Total gross capex</b>	<b>1,134.1</b>	<b>1,006.0</b>	<b>906.2</b>	<b>-9.9%</b>
Less customer contributions	91.3	152.0	91.3	-39.9%
<b>Total Net Capex</b>	<b>1,042.8</b>	<b>853.9</b>	<b>814.9</b>	<b>-4.6%</b>

## AER Proposed Tariff Path

	2016	2017	2018	2019	2020
Draft Decision	CPI – 8.72%	CPI – 8.72%	CPI – 0%	CPI – 0%	CPI – 0%

1. The 'UE Proposed' opex has been reduced by \$94.5m to reflect the AER decision to include AMI-related operating expenditure under Alternative Control Services.
2. The 'UE Proposed' Non-Network General Capex has been reduced by \$61.5m to reflect the AER decision not to include the Power of Choice and RIN collection initiatives. Should these initiatives be implemented, it is expected that tariffs will be adjusted on a pass-through basis.

# 2016-2020 AER Draft EDPR Summary (Nominal)



## AER Proposed Revenue Building Block Summary

(\$m nominal)	UE Proposed	2011-2015 Allowance	AER Draft Decision	% Change Allow – Draft
Return on capital	890.9	773.7	701.0	-9.3%
Reg Depreciation	388.2	298.1	315.4	-5.8%
Operating Expenditure <sup>1</sup>	761.0	594.0	711.2	19.7%
Revenue adjustments (EBSS and shared assets)	26.2	-35.7	28.9	180.9%
Tax allowance	149.1	86.2	84.6	-1.8%
<b>Total Revenue (unsmoothed)<sup>1</sup></b>	<b>2,222.8</b>	<b>1,716.3</b>	<b>1,841.2</b>	<b>7.3%</b>

## WACC Parameters

	UE Proposed	2011-2015 Allowance	AER Draft Decision
Rf – equity only	2.64%	5.08%	2.76%
Implied DRP	3.03%	3.89%	2.58%
Equity Beta	0.89	0.8	0.7
MRP	8.2%	6.5%	6.5%
Gamma	0.25	0.25	0.40
Gearing	60%	60%	60%
Nominal Vanilla WACC	7.38%	9.49%	6.12%
Post tax Nominal ROE	9.95%	10.28%	7.30%

## Expected Revenue (smoothed)

(nominal)	UE Proposed	2011-2015 Allowance	AER Draft Decision	% Change Allow – Draft
Total revenue	2,220.6	1,715.0	1,832.3	6.8%

## Capital Expenditure

(nominal)	UE Proposed	2011-2015 Allowance	AER Draft Decision	% Change Allow – Draft
Augmentation	179.4	195.6	132.3	-32.4%
Connections	268.5	269.3	263.1	-2.3%
Replacement	628.8	349.7	436.4	24.8%
Non-Network General <sup>2</sup>	143.7	140.3	143.4	2.2%
<b>Total gross capex</b>	<b>1,220.4</b>	<b>954.9</b>	<b>975.3</b>	<b>2.14%</b>
Less customer contributions	98.6	144.6	98.6	-31.8%
<b>Total Net capex</b>	<b>1,121.8</b>	<b>810.3</b>	<b>876.7</b>	<b>8.2%</b>

## AER Proposed Tariff Path

	2016	2017	2018	2019	2020
Draft Decision	CPI – 8.72%	CPI – 8.72%	CPI – 0%	CPI – 0%	CPI – 0%

1. The 'UE Proposed' opex has been reduced by \$101.8m to reflect the AER decision to include AMI-related operating expenditure under Alternative Control Services.
2. The 'UE Proposed' Non-Network General Capex has been reduced by \$65.1m to reflect the AER decision not to include the Power of Choice and RIN collection initiatives. Should these initiatives be implemented, it is expected that tariffs will be adjusted on a pass-through basis.