

Electricity Networks Association

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Dr Mark Berry
Chair,
Commerce Commission
PO Box 2351
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Dear Mark,

The Electricity Networks Association (ENA) commissioned Larry Kaufmann from Pacific Economics Group (PEG) to complete a study of productivity trends in electricity network businesses (ENBs) in New Zealand. PEG finds that there has been negative productivity growth for ENBs for the last decade. This is a similar result to the Commission's report, completed by Economic Insights.

PEG also completed a review of the Economic Insights report. This report explains why the Commission must use consistent measures of output in its opex forecast formula, and why negative productivity can be appropriate in price controls.

We are providing these reports to you as early as possible so that you are able to give due consideration to these important findings.

ENA notes that the Commission has relied upon the following statement from Economic Insights as the basis for its conclusion that an opex partial productivity factor of 0% would be appropriate:

"An opex partial productivity growth rate of zero would strike the appropriate balance between recognising the apparent changed circumstances facing electricity distribution over the last decade while anticipating a return to more positive output growth, albeit reduced compared to the period before 2007, while providing an incentive for efficiency improvements."

ENA would note that while Dr Lawrence is a recognised expert in calculating productivity measures, he is not an expert in the specific operations of electricity distribution businesses, and his recommendation amounts to no more than wishful thinking without any evidential basis offered in support of the recommendation. The fact is that there is a measured long-standing trend decline in operating expenditure partial productivity (in both the PEG and EI reports) and there are numerous factors that are unaccounted for in the functional specifications that explain this trend

decline, not least of which are maintenance of aging assets, increasing requirements for health and safety with the current and upcoming changes to the legislation, ongoing increases in regulatory requirements, growing customer demands for quality of service (e.g., arising from the CGA), and greater awareness of quality issues that must be remedied (arising from the deployment of smart meters). ENA submits that the opex productivity assumption has a significant impact on the allowable revenue calculations and the onus is on the Commission to establish a robust case based on quantitative evidence for over-riding the empirical evidence generated in the EI and PEG reports.

ENA will make further comments on productivity in our submission on the draft decision on 15 August.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Alan Jenkins', with a long horizontal flourish extending to the right.

Alan Jenkins
Chief Executive