

Report on the effectiveness of information disclosure regulation at Auckland Airport

Briefing for financial market analysts

31 July 2013

Overview



Report to Ministers on how effectively information disclosure is promoting the purpose of Part 4 for Auckland Airport

We did not consider whether other types of regulation should apply to Auckland Airport

This presentation summarises:

- our task under s 56G of the Commerce Act
- the analytical framework we have used
- our conclusions

Our task under s 56G



Report to Ministers on how effectively information disclosure (ID) regulation is promoting the purpose of Part 4 of the Commerce Act

Report must be made 'as soon as practicable' after prices set in or after 2012

We will provide further advice to Ministers if the Input Methodology (IM) merits appeals are successful in a material way

Report considers effectiveness of ID regulation of Auckland Airport

Summary of conclusions



Auckland Airport has made a number of positive changes to its approach from PSE1 to PSE2

We have found ID is effective in a number of areas:

- limiting excessive profits, innovation, quality and pricing efficiency

It is too early to conclude in other areas:

- operating expenditure efficiency, efficient investment and sharing of efficiency gains

Regulated services under Part 4



ID regulation applies to specified airport services:

- aircraft and freight activities
- airfield activities
- some passenger terminal activities

Car-parking and retail activities are not regulated under Part 4

Analytical framework



We assessed performance (historical and projected) and conduct in each performance area

We considered whether performance had moved closer to outcomes found in workably competitive markets as a result of incentives provided by ID regulation

We use the cost of capital IM as a benchmark in assessing Auckland Airport's returns

For other areas, we compared performance and conduct before and after Part 4 ID was implemented

Our approach is consistent with that taken for Wellington Airport

Conclusion – limiting excessive profits (I)



ID regulation is effective in limiting Auckland Airport's ability to extract excessive profits over time

Auckland Airport set prices such that its expected return over PSE2 is equivalent to 8.0% when the information disclosure framework is applied

This target return lies just within the Commission's estimated range of acceptable returns (7.1% to 8.0%)

- it is above our assessment of a normal return
- but not so high as to suggest it will earn excessive profits

Conclusion – limiting excessive profits (II)



We estimate Auckland Airport's expected returns for PSE2 *and beyond* to be 7.9%

- the value differs slightly from that presented in the draft report due to the inclusion of noise mitigation costs

This is also within the Commission's estimated range for acceptable returns (7.1% to 8.0%)

Our approach to assessing Auckland Airport's expected return



Our analysis of Auckland Airport's expected return uses an asset valuation that is consistent with the IMs but reflects Auckland Airport's moratorium on asset revaluations:

- the IM-compliant 2009 valuation was 'rolled forward' to 2012 without revaluing the assets used for pricing

Based on guidance provided by Auckland Airport, we assumed the moratorium continues after 2017 (or Auckland Airport adopts an approach with an equivalent effect)

Conclusion - innovation



ID regulation under Part 4 is effectively promoting appropriate innovation at Auckland Airport:

- the level of innovation appears to be appropriate
- airlines generally consider that Auckland Airport facilitates airline-led innovation
- while ID regulation has not had an additional impact on incentives to innovate, it has not negatively affected existing incentives

Conclusion - quality



ID regulation is effectively promoting the provision of quality at a level that reflects consumer demands:

- airlines are generally satisfied with the quality of service
- Auckland Airport generally seeks to ensure quality reflects consumer demands
- Auckland Airport facilitates improvements in quality or efficiency for services provided by its consumers (eg, airlines)
- while ID regulation has not had an additional impact on incentives in this area, it has not negatively affected existing incentives

Conclusion – pricing efficiency



ID regulation is effectively promoting efficiency of pricing:

- prices for the PSE2 period are more likely to promote efficiency than those previously in place
- Auckland Airport has introduced new charges and increased existing charges to better ensure optimal use of scarce resources
- Auckland Airport has adjusted existing charges to limit the likelihood of cross subsidisation
- Auckland Airport has indicated that ID had an impact through the requirement to transparently outline its pricing methodology

Conclusion – operating expenditure efficiency



We are unable to conclude whether ID regulation is effectively promoting improvements in operating efficiency (opex):

- we do not have a sufficiently long time series on actual opex under ID regulation
- evidence is mixed: unit opex increased in 2011 and 2012 but the forecast of declining unit opex through PSE2 may indicate improved future efficiency
- Auckland Airport has sought to improve its opex efficiency (eg, through initiatives such as the 'LEAN forum')

Conclusion – efficient investment



We are unable to conclude whether ID regulation is effectively promoting incentives to invest efficiently:

- we do not have a sufficiently long time series on actual capital expenditure (capex) under ID regulation

ID regulation appears to have promoted an efficient investment plan for PSE2

- Auckland Airport's consultation with airlines has resulted in an investment programme for PSE2 which airlines consider is efficient

Conclusion – sharing of efficiency gains



We cannot conclude whether ID regulation is effectively promoting sharing of efficiency gains:

- there is limited evidence of historic efficiency gains that could be shared

Next steps



The calculations supporting our analysis of Auckland Airport's returns will be made available on our website shortly

We are aiming to release our draft report on the effectiveness of information disclosure regulation at Christchurch Airport in September

Questions?



For more information	
Please contact:	Ruth Nichols Regulation.branch@comcom.govt.nz
Or visit:	http://www.comcom.govt.nz/section-56g-reports/