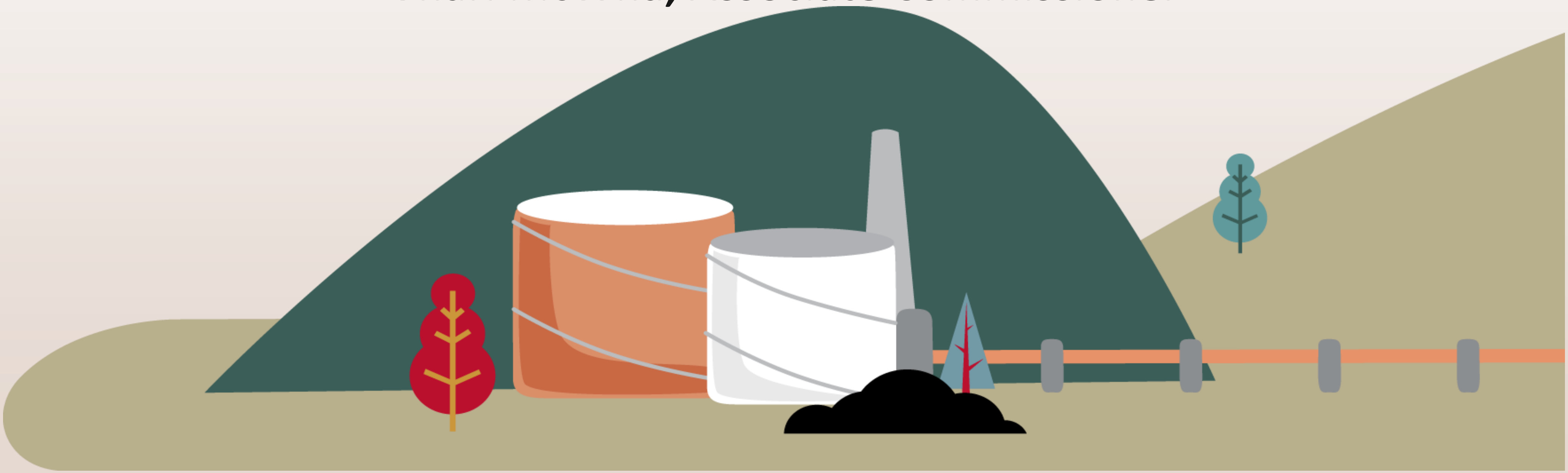
Default price-quality paths for gas pipeline businesses from 1 October 2022 to 30 September 2026

31 May 2022

Vhari McWha, Associate Commissioner



Introduction

Today we publish the default price-quality paths for five gas pipeline businesses for the 2022-2026 period.

Outline of presentation:

- Our task and the transition to net zero emissions
- Key aspects of our decision
- Allowable revenue for the GPBs
- Impact of the decision on consumers

Our task

- Part 4 of the Commerce Act requires us to set price-quality paths for the natural gas pipeline businesses by 31 May 2022, including:
  - The maximum revenue gas pipeline businesses can earn
  - Quality standards businesses must meet
- Promote long term benefit of consumers as set out in the Part 4 purpose statement
- Commission regulates the supply of natural gas by pipeline only
- Ensure safe and reliable pipeline network supplying natural gas
- Final decision follows public consultation on draft decisio

Transition to net-zero

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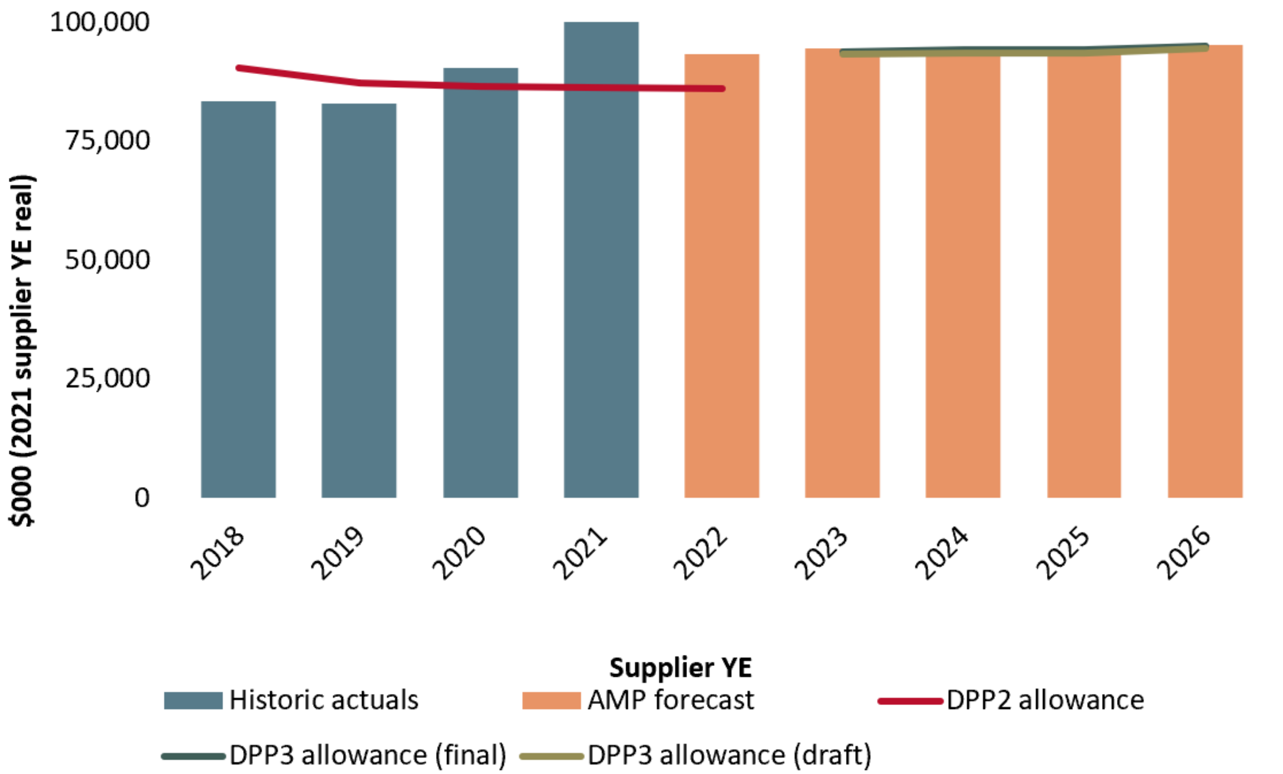
- New Zealand is transitioning to net-zero carbon emissions by 2050
- Natural gas pipelines are currently essential infrastructure for 300,000 consumers and some large users
- The Emissions Reduction Plan includes phasing out the use of natural gas (and other energy objectives)
- We are at an early stage in the transition
- Uncertainty about the rate at which natural gas use will decline over time and detail of future government policy
- The natural gas network now has a shorter expected life

Key decisions we have made

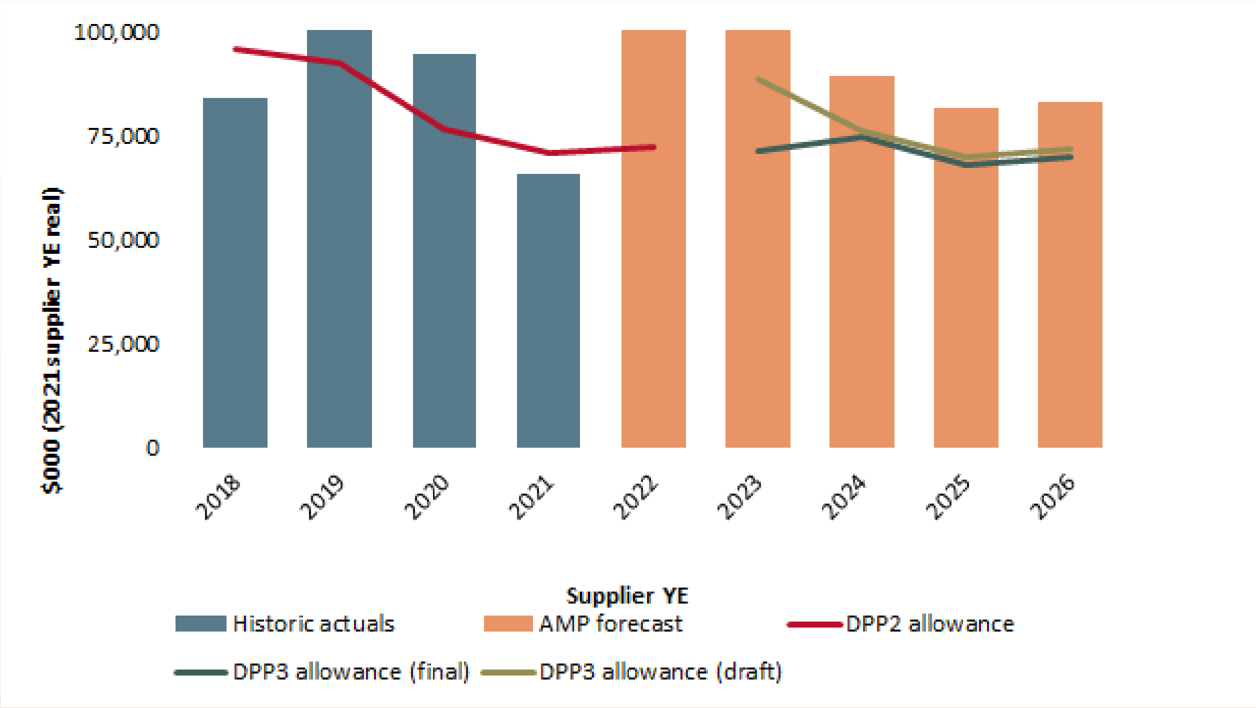
- Four-year regulatory period so we can review settings sooner:
  - Government proposes to develop a Gas Transition Plan (due 2023) and an Energy Strategy (2024)
  - Comprehensive IM review has commenced (2023)
- Prices based on assessment of profitability
- Final weighted average cost of capital is 6.14%
- Small changes to opex and capex allowances since the draft
  - Includes data from 2021 disclosure year
- No change to form of control or quality standards
- Smooth increases in price over time to minimise price impacts

Key decisions - opex



- Base, step, and trend approach
- Forecasts for DPP3 are higher than DPP2
- Allowance for the investigation of blended gases

Key decisions - capex



- Top-down historical average approach
- No 10% uplift
- Reopener for unforeseen projects and network maintenance

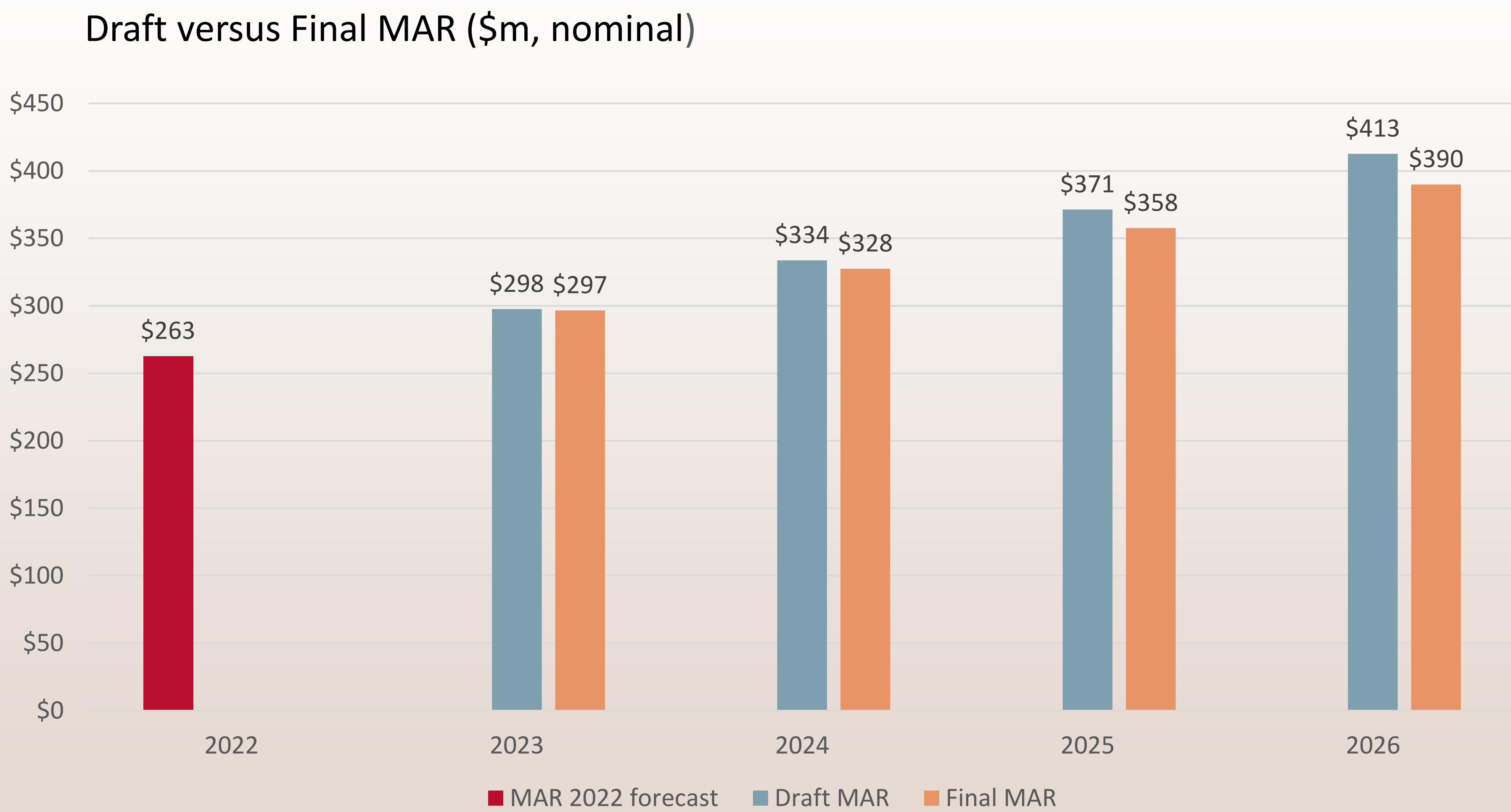
Recognising shorter asset lives

- We have recognised shorter assumed asset lives
  - Better reflect expected remaining economic lives
  - Not long physical lives (up to 80 years)
  - Demand is expected to decline and phase out is proposed
- We have updated the modelling in response to submissions, to consider a wider range of plausible future scenarios, e.g.
  - Our draft assumption that natural gas would end in 2050
  - Use of pipelines for natural gas may extend past 2050
  - And assets could carry other gas and so have residual value
- Price increases are lower than the draft decision

Future pipeline use remains uncertain

- GPBs are exposed to downside risk:
  - Demand could fall off more quickly than we have assumed leading to earlier pipeline closure
  - The total price of using gas relative to alternatives like electricity may, at some point in the future, encourage significant consumer switching
  - Government policy initiatives
  - Development of energy alternatives
- GPBs may be able to repurpose parts of their network to carry gases other than natural gas

Forecast allowable revenue at draft and final decision



Starting prices for gas pipeline businesses

GPB	MAR in 2021/22 ($m)	MAR in 2022/2023 ($m)	Rate of change
GasNet	4.4	4.8	CPI + 5.5%
PowerCo	51	58	CPI + 5.0%
Vector	51	58	CPI + 0%
First Gas distribution	25	29	CPI + 10.0%
First Gas transmission	132	147	CPI + 8.5%

Impact on consumers

- We have smoothed revenue increases to minimise price shocks to consumers
- Increase of about 3.8% on average across all household consumers in each of the next four years
- For a typical annual household gas bill of about $1,246 this would be an increase of around $48 per year
- Reduced proposed price increases informed by feedback

In summary

- Balanced decision in the context of the energy transition
- Prices will increase about 3.8% for an average household each year
- Provides incentives to invest and maintain safe and reliable pipelines to supply natural gas
- A four year regulatory period allows us to review settings as soon as possible
- Final decision informed by feedback from stakeholders

Questions

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