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Ms Keston Ruxton
Chief Advisor, Regulation Branch
Commerce Commission
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20 August 2014

Dear Ms Ruxton,

Investors Mutual (IML) is an Australian based fund manager with approximately AUD 5.2 billion under management on behalf of a wide range of investors including many retail investors. IML takes a long term approach to investing and we look to invest in companies which generate a high level of recurring income, have competent management, and can grow their earnings and dividends over time.

Since our inception in 1998, we have been a long term shareholder in many New Zealand listed companies, including Sky City, Fletcher Building, GPG, and Mighty River Power. We are attracted to New Zealand because of its relatively stable economy, and in the past, its generally predictable and transparent legal system. However, recent regulatory uncertainty has threatened this reputation.

The best outcomes for New Zealand will be achieved when regulation provides both incentives for companies to invest in providing new products and services, and consumer protection. Investment in infrastructure, such as telecommunications networks, carries long term risks which we believe have been under-appreciated in consideration of access prices to date. Recent decisions have surprised and disappointed investors, leading to large falls in the Chorus share price. The government has also been surprised, and in August 2013 the Minister’s Telecommunications Act Discussion Document noted that “the pricing outcome was not expected at the time the Telecommunications (TSO, Broadband and Other Matters) Amendment Act 2011 was passed.”

From our analysis, the initial price of $34.44 does not seem supported by the valuation of other types of networks in New Zealand, nor the costs being incurred in building the UFB fibre optic network. We are aware, for example, that the Christchurch network builder, Enable, has indicated needing a monthly price of $50.50 per connection to recover the cost of its fibre network.

Given the above, we welcome the Commission’s recent reference to “reasonable investor expectations” in the context of its preliminary views on TSLRIC modelling. The expectation of a commercial return on investment should carry through to how the Commission approaches each element of its TSLRIC model, including replacement cost for assets, operating cost structure, demand assumptions and the weighted average cost of capital. In each case, investors expect that the approach to modelling will be grounded in reality.

Related to the above, we believe the Commission should also take a real world view of the certainty of customers transferring away from Chorus' network to other fibre networks – it is already happening in those areas where Chorus is not the fibre network builder and ultimately affects the sustainability of their business model, especially when they are now required to operate two networks.

Naturally, the ISPs are saying that the Commission should not backdate pricing in this process. Clearly they are not the ones out of pocket, it is investors like us (including a lot of New Zealanders!) that are. The Commission's final pricing principle reviews are completely new processes and will ultimately substitute the initial benchmarking prices for UCLL and UBA with prices derived from a more thorough consideration of costs in New Zealand. It is our expectation, therefore, that the Commission will implement backdating to reflect this. Allowing the ISPs to pocket a windfall based on a less than rigorous process does not encourage a sense of regulatory predictability.

A timely and realistic process is essential if New Zealand is to fund future investments in critical infrastructure and services from the public markets. We trust the Commission will address these matters by completing its review as soon as practicable, and we look forward to a reasonable outcome being achieved. The recent regulatory uncertainty has led Chorus to suspend dividends to shareholders which is extremely disappointing. It is unique for a utility infrastructure provider such as Chorus to not be paying dividends, which are a key part of the return investors look to receive from an infrastructure investment.

Yours sincerely,

Simon Conn
Portfolio Manager