A STAR ALLIANCE MEMBER

AIR NEW ZEALAND

13 June 2022

Jo Perry
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Commerce Commission

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Dear Jo

Review of Wellington Airport's 2019-2024 Price Setting Event

Air New Zealand welcomes the opportunity to make this submission on the Commission's Review of Wellington Airport's 2019-2024 Price Setting Event. Air New Zealand considers these reviews to be an important part of the regulatory framework applying to the airports subject to information disclosure regulation under Part 4 of the Commerce Act.

Air New Zealand notes that the Commission has chosen to focus this review on the expected profitability of Wellington Airport over PSE4 and risk allocation between Wellington Airport and its customers, given the current operating environment may limit stakeholders ability to engage in a protracted or more complex process. Air New Zealand considers this a pragmatic approach at this time but does wish to highlight the importance of quality, innovation and cost efficiency to customers. It will be important that ongoing review of annual disclosures continue to focus on these elements also.

The Commission has indicated it is broadly satisfied with Wellington Airport's target return, equating to the 56th percentile of the Commission's own mid-point Wacc estimate and resulting in a revenue uplift over the period of ~$4.3 million.

The Commission does however highlight two areas where Wellington Airport has failed to adequately justify its departure from the WACC IM in assessing its own estimate of the cost of capital – the asset beta and the cost of debt.

Air New Zealand concurs with the Commission's assessment on these issues. TDB Advisory provided advice on these issues which Air New Zealand understands has been provided by BARNZ to the Commission.

The main factor driving Wellington Airport's asset beta uplift to 0.63 was the impact of the capital expenditure programme on WIAL's operating leverage. TDB noted that while the standard formula for estimating asset beta could result in an indicative adjustment of 0.02 in the asset beta, this tended to apply "…to a competitive firm that is not subject to any regulation.". In contrast, WIAL's high level of market power and the light-handed regulatory regime would likely reduce underlying revenue and asset betas "…because a regulated firm will have more certainty of future revenue when undertaking a capital project of this nature."

TDB noted also that the building blocks methodology offsets the need to compensate for increased operating leverage as the work-in-progress elements are compounded into the RAB and compensated for when the new asset enters the pricing RAB, regardless of economy wide factors impacting other airport revenue. WIAL did not adequately respond to these submissions.

The Commission has identified that Wellington Airport is including commercial land transferred to the aeronautical RAB at MVEU plus civil development costs, contrary to the IM's which specify that such land should be transferred at MVAU, consistent with the valuation of aeronautical land. WIAL contended that this had only a minor impact on PSE4 revenues. Air New Zealand considers that if it has only minor impacts, consistency with the IM's should take precedence.

The Commission has highlighted the range of revenue deferral and risk allocation measures adopted by Wellington Airport in its pricing decision. These were consistent with submissions made by Air New Zealand in the context of the seismic impact of COVID-19 and provide some relief for the sector as we seek to recover from the pandemic and return to a sustainable operating position. It should be noted however that Wellington Airport is in a unique position given the timing of the consultation, and deferral of the pricing decision until early 2021. Notwithstanding cashflow timing, Wellington Airport is alone in that it will earn a full recovery for the PSE4 period as a result of these revenue deferral arrangements.

Air New Zealand looks forward to further engagement with the Commission throughout this review process.

Please contact me if you have any queries relating to any of the above.

Yours sincerely

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Manager Aeronautical Suppliers