

24 October 2023

To: Commerce Commission
Wellington

By email: infrastructure.regulation@comcom.govt.nz

Response to the Consultation Paper for Review of Christchurch Airport's 2022-2027 Price Setting Event.

Kia ora

Thank you for the opportunity to respond to the consultation on the Commerce Commission's Review of Christchurch International Airport Limited (CIAL) Price Setting Event. BARNZ participated in this consultation process with CIAL. In preparing this response, I have reviewed both the Commission's Consultation Paper and those submissions made by BARNZ to Price Setting Event 4 (PSE4). I note that staff of BARNZ has changed since CIAL's price consultation for PSE4 concluded.

Estimating target WACC - justification for TAMRP uplift insufficiently described

CIAL estimated its WACC to be 6.65% against the Commission's mid-point estimate of 6.32%. This largely arises from the use of a higher tax adjusted market risk premium (TAMRP), uplifted by .5% from the Commission's TAMRP for airports of 7.0%, as was available in June 2022.

The Commission notes that CIAL relied on a TAMRP of 7.5% by referring to the fibre IM decisions, and to the gas transmission IMs from March 2022. Other than noting that TAMRP is an 'economy wide measure', it is not clear from the Consultation Paper why the Commission considers this uplift is justified. However, given CIAL is in fact targeting a return beneath their estimated WACC, the approach at the total level is acceptable.

Actual target return and exclusion of incentive payments

CIAL is targeting a return of 6.26% against a WACC it estimated to be 6.65% for the PSE4 period. This is achieved as CIAL is not seeking to cover route incentive payments from its existing airline customers. This decision is to be applauded. It has always seemed unusual

that regulated airports are able to recover incentive payments from existing customers – leaving customers in the unusual position of subsidising the entry of competition themselves, with the airport company as beneficiary of new customers avoiding the cost burden of attraction.

The exclusion of incentive payments was also applied by CIAL when setting returns in PSE3. BARNZ is pleased to note that the additional transparency about the effect of this exclusion has been provided by CIAL in PSE4. The effect of excluding the incentive payments on IRRs was explained, and it was made clear that the effect of these payments is included in the demand forecasts.

Given the recovery of international connectivity to CIAL has been slower than Auckland International Airport Limited (AIAL) which is the closest airport to most city-pairs, and has therefore recovered more quickly, it is particularly commendable that CIAL excludes incentive payments, as these are likely to be very necessary as CIAL continues its recovery.

BARNZ agrees with the Commission that CIAL's target return of 6.26% is reasonable, and is not likely to result in excessive profits.

Notes on other pricing related decisions

- BARNZ was supportive of the effort made by CIAL to reduce capital expenditure, deferring projects to PSE5 where they were not absolutely critical.
- BARNZ notes the effect of tilted annuity depreciation which assists to lower prices earlier in the period. BARNZ had supported a price smoothing approach during the consultation process, mindful of the slow recovery of aviation at that time. With the benefit of current data, and mindful of the effect of tilted annuity depreciation, BARNZ supports CIAL's decision not to introduce price smoothing.
- BARNZ continues to discuss the possible effect of PLEXIT (the potential purchase of power and lighting assets from Airways New Zealand) with CIAL.
 - We note that the purchase price of the assets is one consideration, and that future pricing will need to take into account any required investment in those assets.
 - Should costs be substantial, CIAL and airlines may need to consider treatment of these costs inside PSE4 or make consideration for PSE5.
 - PLEXIT costs may also need to be considered for airports that are not regulated in the coming years. BARNZ notes that power and ground lighting assets should continue to be maintained and invested in by Airways until (and if) any change of ownership occurs.
 - Costs of purchase and required investment in power and lighting assets are likely to be substantial at a national level. They will be passed directly into future airport pricing under current legislative and regulatory settings.

- BARNZ requests that the Commission continue to monitor these costs as they are understood, both in this process and in processes for other airports in the months and years ahead, to ensure consumers are not 'paying twice' for investments in these assets.

Promoting the purposes of Part 4

The Commission notes that as the price setting disclosures contain forward looking information, they do not provide fulsome information about some of the purposes of Part 4 such as innovation, service quality, or whether operational expenditure is efficient.

BARNZ notes that it is possible to comment on capital expenditure proposals as they are (or are not) efficient, and as they affect (or do not affect) service quality. Indeed, the Commission makes comment on capex, observing that it is compliance based, and appears to be reasonable. BARNZ agrees with this comment.

However, we make the point that the Commission is in fact able to consider service quality and efficiency of expenditure when considering price setting disclosures. Both quality and efficiency are extremely important to assess, as what is proposed to be built will (or will not) deliver to these purposes.

The backward-looking information disclosures do not consider whether capex is efficiently committed to – rather they measure progress or otherwise against existing commitments. Further, information disclosures do not make reliable assessment of service quality outcomes experienced by customers. BARNZ considers that assessment of service quality and efficiency should be built into future Price Setting Reviews. We would be happy to consult with the Commission about how this might best be achieved.

Ngā mihi -



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