



COMPETITION
ECONOMISTS
GROUP

CEG Asia Pacific
Suite 201, 111 Harrington Street
Sydney NSW 2000
Australia
T +61 2 9881 5750
F +61 2 9252 6685
www.ceg-ap.com

Sally McMahon
General Manager Regulatory and Risk
ATCO Gas
81 Prinsep Road
Jandakot WA 6000
By email.

19 December 2014

Dear Sally

CEG report on new issue premium

Please find attached to this letter a CEG report which estimates the magnitude of the new issue premium on bonds issued by Australian corporate entities. This report was originally prepared for Citipower, Jemena, Powercor Australia, SA Power Networks, AusNet Services and United Energy.

All of these businesses are regulated by the AER and the AER's practice is to estimate the cost of debt using fair value yield estimates published by the RBA and/or Bloomberg. Both the RBA and Bloomberg derive their fair value yield estimates from estimates of the yield on secondary bonds in the secondary market (i.e., trades made subsequent to the bonds issuance) as reported by the data service Bloomberg.

The methodology that we adopted in the attached report is specifically designed to estimate the new issue premium relative to Bloomberg's published estimates of secondary market yields. Therefore, the results in that report are relevant to any estimate of the cost of debt in the primary bond market (i.e., the market for debt at the time of issue) that is being estimated using yield estimates of secondary bond market yields as reported by Bloomberg.

The ERA's proposed methodology for estimating the cost of debt, as expressed in its most recent draft decision for ATCO, is to estimate the cost of debt using a number of different curve fitting techniques.¹ The data used by the ERA in these curve fitting exercises is made up of secondary market yields sourced from Bloomberg.² Therefore, the results in the attached report are equally relevant to the ERA's estimation technique as they are to the AER's technique (based on RBA and Bloomberg fair value curves).

¹ See page 199 of ERA, Draft Decision on Proposed Revisions to the Access Arrangement for the Mid-West and South-West Gas Distribution System

² Ibid, p. 198, footnote 446.



COMPETITION
ECONOMISTS
GROUP

I also confirm that I am aware of no new information or analysis that would cause me to change the opinions expressed in the attached report.

Yours sincerely

Tom Hird
Director
Competition Economists Group