Dampier Bunbury Pipeline
Part of Australian Gas Infrastructure Group

Dampier Bunbury Pipeline
L22 – 23, 140 St Georges Terrace
Perth WA 6000 Australia
PO Box Z5267, St Georges Terrace,
Perth, WA 6831 Australia
+61 8 9223 4300
info@agig.com.au
agig.com.au

Jason Dignard
Principal Regulatory Advisor
Economic Regulation Authority
Level 4, 469 Wellington St
Perth WA 6000

Dear Jason,

Thank you for the opportunity to respond to your issues paper on the replacement of government bond data formerly sourced from the now discontinued RBA F16 series. In this response we address both the initial issues paper, and the subsequent email from Jimmy Tran on 12 June 2023.

We agree with the ERA's suggestion to replace the F16 series with data from Bloomberg in the first instance and Yieldbroker data if Bloomberg becomes unavailable, and we commend the ERA for the clear, transparent and consistent analysis by which all alternatives were assessed. We make three comments which we hope will assist in improving the robustness of the Rate of Return Instrument (RoRI) and the process more generally, and which, we think, are congruent with the ERA's intent in making the change.

The first is a minor methodological point. In its quantitative assessment of the different options, the ERA discusses how close results of different series are to the Yieldbroker data. This is not quite correct. The ERA has not sourced the original Yieldbroker data but has rather made comparisons against the RBA's F16 series, which not identical to the Yieldbroker data, even though it is drawn from it.[1] We believe this F16 comparison is correct, as this is the series which informs the original RoRI, and so the issue is only with how the ERA has described its findings, not with the analysis itself.

The second is more substantive and refers to the changes the ERA proposes to make to the RoRI, although we note that the ERA's position in Jimmy Tran's email of 12 July is now similar to our own.

The ERA originally proposed to modify [26] in the RoRI. In our meeting, we suggested that Section 6.2.1 ([97] to [99]) would be a better place to make changes. Also, both we and the ERA appear to have formed the view that the original wording in the issues paper did not quite reflect the ERA's intent (with which we agree) to source all data from the same source. The ERA has now proposed to add [101], which reads:

> The data required to calculate the risk free rate for equity are the relevant individual bond yields and not an interpolated yield from another party. This data is to be sourced from (in order of preference) the Reserve Bank of Australia, Bloomberg or Yieldbroker. The data source chosen must be the one that has the complete set of information for the calculations necessary for the interpolation and averaging process, in the order of preference. The data source must also be consistent across the methods for the equity risk free rate and the expected inflation rate.

Adding an extra paragraph requires the ERA to re-number the RoRI from [101] onwards. We believe that [99] can be modified to give the same effect as intended by the ERA's proposed [101], but without the re-numbering. More substantively, however, we believe that the ERA should be more specific about which data it is using from the RBA, Bloomberg or Yieldbroker. Putting these two things together, we propose that, rather than adding [101], the ERA modify [99] in the following way (our additions to the current [99] in italics):[2]

> The ERA will estimate the risk free rate for equity by:

[1] The AER notes in its issues paper on this topic (here, p7), that the RBA round the Yieldbroker data.
[2] In the July 12 email, the ERA makes it clear in the text it proposes for [101] that the data used for the risk-free rate and for inflation be the same. This could be added to our proposed changes to [99] if desired, we just could not work out an elegant way to do so and believe that changing the inflation section as we propose should be sufficient.

- *Using Commonwealth Government Bond yield data from the F16 data series published by the Reserve Bank of Australia and, where this data source is not available, choosing, in order of preference and ensuring that the data source has the complete set of information for the calculations necessary for the interpolation and averaging process, one and only one of the following data sources:*
    - *The mid-rate setting of the BCMP data series published by Bloomberg.*
    - *The mid-rate setting of the XX data series published by Yieldbroker.*[3]
    - *Where a government department has published for more than 6 months and has undertaken to continue to publish Commonwealth Government Bond data which match exactly the RBA F16 series, that government bond data.*
- Using observed yields from 10-year Commonwealth Government bonds *in the relevant data set*.
- Using linear interpolation of observed yields of Commonwealth Government bonds *in the relevant data set*.

In the email from Jimmy Tran of 12 July, the ERA proposes that footnotes 3 and 4 read:

> Trading days are defined as days that Australian Commonwealth Government Security data is available in the RBA's statistical tables for capital market yields.

We note that the Bloomberg and F16 data series did not always line up exactly on dates in the past (Bloomberg sometimes includes holidays which the F16 series did not). We understand the intent of the wording in these footnotes to be to ensure that the dates used reflect exactly the dates which would be used if the F16 data series continued to be used. If this is the case, the phrase "available in the RBA's statistical tables" should be replaced by the phrase "available in the RBA's F2 statistical tables" (which does have the same dates as the F16 series had), to make it clear which statistical tables the ERA refers to. The ERA could add a contingency pointing to the data sources in [99] if it wished to cover the possibility of the F2 series being discontinued.

We note that the issues paper did not consider any changes to Chapter 8 of the RoRI which deals with inflation, even though it is the ERA's intent to use the same data-source for inflation and the risk-free rate. Jimmy Tran's email of 12 July addresses this issue, and we endorse this proposal as we agree that it adds clarity. However, rather than adding a paragraph to the end of Chapter 8 with essentially the same wording as proposed for [101], which would change the paragraph numbering in Chapter 9, we believe a simpler approach would be to alter the third dot-point of [131] so that its first sentence reads (italics added):

Two issues of each type of bond will be selected for the estimation of expected inflation *from the data source determined for use according to paragraph 99*.

Our third and final issue is one of signalling clear limits to changes to the RoRI. We appreciate that the ERA had little choice in this instance to make a change, given that the F16 series ceased to be published and no alternatives had been listed in the RoRI. However, we believe that this change goes beyond the simple correction of errors envisaged by the governing legislation which clearly intended to RoRI to be binding for all parties. For this reason, we believe it is important for regulators to make clear statements of intent in respect of the boundaries of change. This could be as simple as the ERA making it clear that it will only act to change the RoRI if a data-source becomes unavailable and it has not provided a back-up option. Such clarity provides assurance to stakeholders as to the operation of binding instruments.

If you have any queries in respect of this submission, please do not hesitate in contacting Stefan Mero whilst I am on leave at [redacted]

Yours sincerely,

[redacted]

Nick Wills-Johnson
Head of Economics

[3] *We do not know what the Yieldbroker data series is called and have left this as "XX" in this suggested wording.*