

Final decisions on our 2018 WACC method

20 February 2018



WHAT

We have released our Final Report and decisions on our 2018 method. While feedback from stakeholders broadly confirmed that our existing WACC method was working well, we have made incremental improvements to:

- ▼ estimate the historic cost of debt as a 10-year trailing average
- ▼ estimate the current cost of debt as a short-term trailing average over the length of the regulatory period, but using a 10-year bond tenor
- ▼ synchronise sampling dates for selected current parameters
- ▼ the combination of market risk premium estimates
- ▼ the calculation of the inflation adjustment, and
- ▼ our process for estimating equity beta and gearing at each price review.

Our reasoning for making these decisions and other minor amendments are discussed in our Final Report.



WHY

Since mid-2017, the Independent Pricing and Regulatory Tribunal (IPART) has been reviewing the standard method we use to decide the weighted average cost of capital (WACC).

The WACC is a key input for calculating the allowance for a return on assets, which is part of the building block approach we use to determine the revenue requirement of businesses we regulate.

We consider it important for our WACC method to reflect financial market conditions as accurately as possible for an efficient benchmark firm to finance its operations. However, this needs to be balanced with ensuring that the method is stable over time and can be replicated by stakeholders.



HOW

We consider that the incremental changes we have made will reduce refinancing risk for firms, and as such, will improve cost-reflective prices for customers.

Overall these changes should enhance the transparency and accuracy in our WACC calculations, and can be implemented without creating windfall gains or losses for firms or customers.



WHEN

Our 2018 method will apply to pricing decisions that take effect **on or after 1 July 2018**.



WHAT NEXT

We will update our WACC model spreadsheet on our website shortly.

In August 2018, we will publish our bi-annual financial market data using the 2018 WACC method.