

Estimates of efficient base year opex for Energex and Ergon Energy



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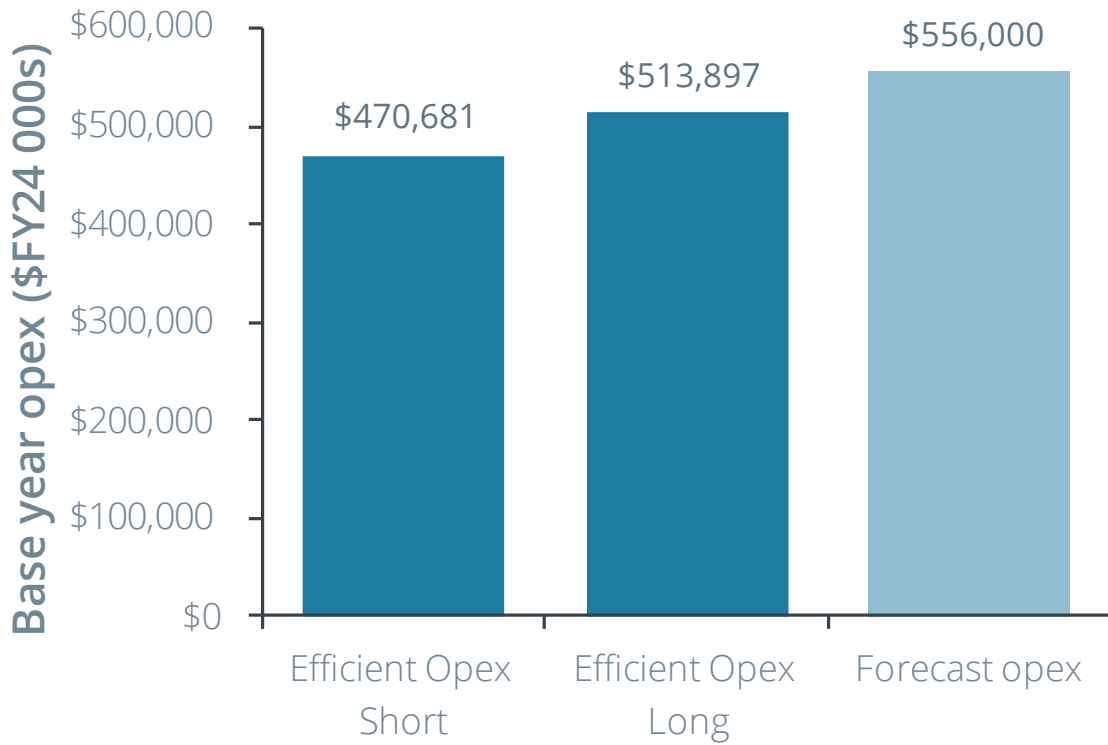
Estimate of efficient base year opex

1. Energy Queensland has instructed us to assume, for the purposes of modelling Energex's and Ergon Energy's efficient base year opex, that the relevant base year for both DNSPs will be 2023-24.
2. In addition, EQL has asked us to derive estimates of efficient base year opex for Energex and Ergon Energy:
 - a Using 2023-24 as the base year for forecasting Energex's and Ergon Energy's opex requirement for the 2025-30 regulatory period;
 - b Employing the AER's existing benchmarking method, as applied in the most recent determinations (including for the NSW and ACT DNSPs);
 - c Historical data used by Quantonomics in the 2024 Preliminary Benchmarking Report (the latest dataset available at the time of preparation of this report);
 - d Historical opex including all capitalised corporate overheads and defined using Energex's and Ergon Energy's 2022 Cost Allocation Methodology (consistent with AER's new approach to accounting for differences in capitalisation practices);
 - e The latest data on backcast capitalised corporate overheads submitted by Ergon Energy and Energex to the AER; and
 - f Using the latest Operating Environment Factor (OEF) adjustments employed by the AER and relevant to Energex and Ergon Energy.
3. We follow the AER's method for estimating an overall efficient level of base year opex, which involves:
 - a Estimating an efficient level of opex over the relevant historical benchmarking period, using each statistical model that is not rejected due to monotonicity violations (i.e., the 'valid models');
 - b Rolling forward each of those estimates to the base year (using the AER's roll-forward procedure); and
 - c Averaging the estimates across all of the valid models.¹
4. The resulting estimates are presented in Figure 1 through Figure 3 below.

¹ First averaging to obtain short and long sample estimates, then averaging the short sample and long sample estimates.

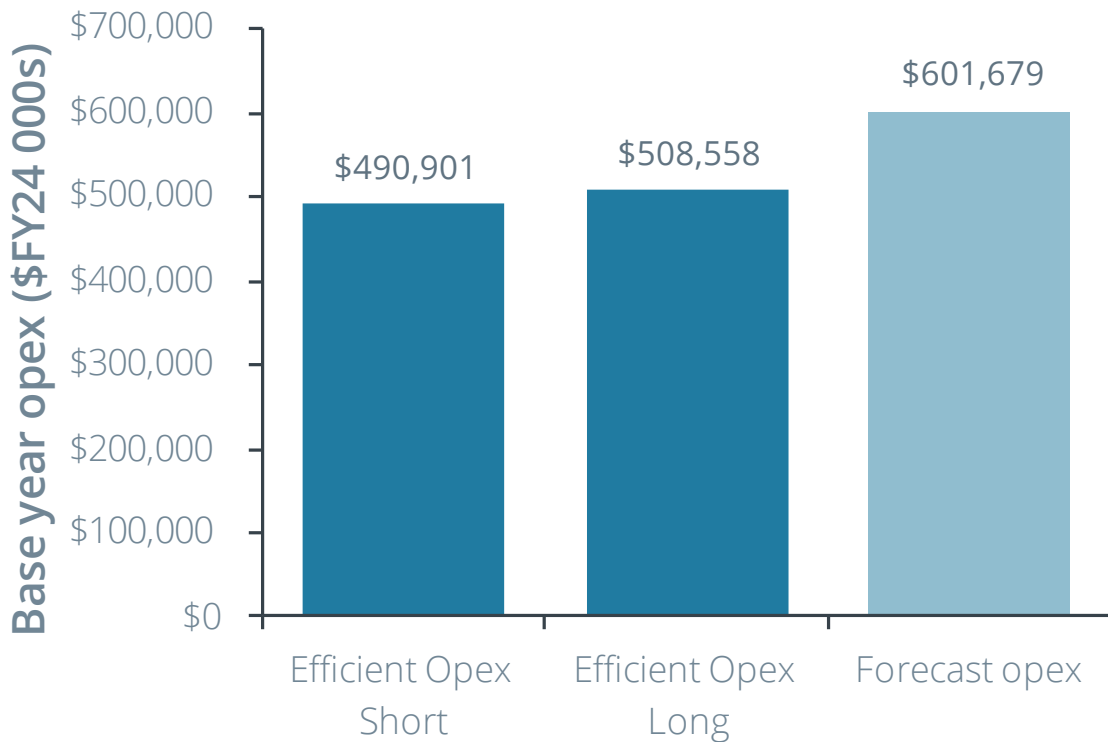


Figure 1: Estimates of efficient base year opex for Energen (\$FY2024)



Source: Frontier Economics analysis of EQL and Quantonomics data.

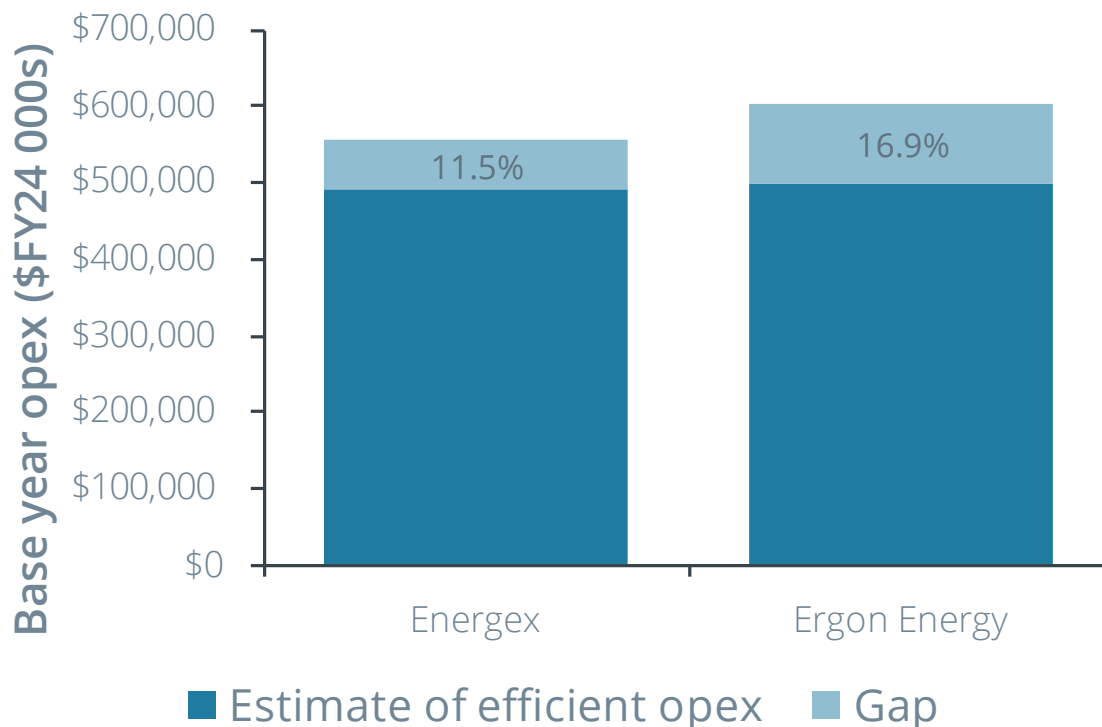
Figure 2: Estimates of efficient base year opex for Ergon Energy (\$FY2024)



Source: Frontier Economics analysis of EQL, ABS and Quantonomics data.



Figure 3: Estimates of efficient base year opex for Ergon Energy (\$FY2024)



Source: Frontier Economics analysis of EQL, ABS, and Quantonomics data.

5. We make the following observations in relation to the results presented in above figures:
 - a The current forecast of revealed opex for Energex and for Ergon Energy in 2023-24 is higher than the estimate of efficient opex obtained from the AER's benchmarking method:
 - i The implied efficiency adjustment for Energex is 11.5%; and
 - ii The implied efficiency adjustment for Ergon Energy is 16.9%.
 - b The AER would typically conclude, on this basis, that the revealed base year opex for both DNSPs is materially inefficient and therefore should be adjusted downwards. The adjusted estimate of efficient opex for:
 - i Energex would be \$481.1 million (\$FY2024) excluding capitalised corporate overheads (i.e., in current CAM terms); and
 - ii Ergon Energy would be \$484.6 million (\$FY2024) excluding capitalised corporate overheads (i.e., in current CAM terms).

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