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Attn: Mr Richard Cheng
Economic Regulation Authority
4/469 Wellington Street
PERTH WA 6000

Dear Mr Cheng

Draft determination: 2023 Benchmark Reserve Capacity Price for the 2025/26 Capacity Year

Synergy welcomes the opportunity to provide feedback on the draft 2023 Benchmark Reserve Capacity Price (**BRCP**) for the 2025-26 Capacity Year (**Draft determination**) in which the Economic Regulation Authority (**ERA**) has proposed a 2023 BRCP of \$185,200 per MW per year. The 2023 BRCP is higher than the previous 2022 BRCP of \$165,700 per MW per year.

Synergy raises the following concerns regarding the cost escalation factors for consideration. In the determination of the 2023 BRCP, the ERA has engaged PricewaterhouseCoopers Consulting (Australia) Pty Ltd (**PwC**) to determine appropriate cost escalation factors related to the construction of a 160MW open cycle gas turbine (**OCGT**) generation facility. PwC's "proposed cost escalation factors reflect the dynamics of the relevant labour, financial and resources markets, and are affected by both macroeconomic factors and global events such as the COVID-19 pandemic and ongoing geopolitical tensions impacting supply chains and commodity markets¹."

The 2023 Draft determination notes that the 2023 BRCP is 11.8 per cent higher than the 2022 BRCP "mostly due to a higher cost of capital from rising debt market interest rates and slightly offset by lower forecast steel and copper prices"². The Draft determination assumes a 1.73 per cent increase in interest rates since the 2022 BRCP. As of end October 2022, the ten-year Treasury bond rate have risen to 3.92%³. Australia's interest rates have risen by 2.75 per cent from a low of 0.10 per cent. Additionally, major bank forecasts have indicated that further rate hikes are likely⁴. Considering this, the interest rate assumption in the Draft determination may be too conservative.

¹ PwC report: 2023 Benchmark Reserve Capacity Price – Cost Escalation Factors (August 2022): <https://www.erawa.com.au/cproot/22899/2/Consultant-Report---PricewaterhouseCoopers.pdf>

² ERA 2023 Benchmark Reserve Capacity Price for the 2025/26 Capacity Year Draft determination, page 1: <https://www.erawa.com.au/cproot/22897/2/Draft-determination.pdf>

³ Reserve Bank of Australia: Capital Market Yields – Government Bonds Monthly <https://www.rba.gov.au/statistics/tables/xls/f02hist.xls?v=2022-11-08-13-53-18>

⁴ National Australia Bank interest rate forecasts: <https://www.nab.com.au/business/international-and-foreign-exchange/financial-markets/interest-rate-forecast>

With respect to the steel and copper price forecasts, Synergy queries the assumption that prices will continue to trend downward. Market analysts have indicated an expectation that global decarbonisation efforts may increase pressure on demand for commodities in the long term⁵. Whilst consensus forecasts point to lower demand in the short term driven by global economic slowdown, there is risk of demand becoming more linked to the decarbonisation cycle instead of the broader economic cycle. This is already observed in other metals such as nickel and zinc, associated with growing demand to support transition to green energy⁶.

Synergy also notes that the Minister for Energy is considering penalties for high emission technologies⁷. These penalties have not been factored into the 2023 BRCP Draft determination. Should these penalties be introduced in future, they may apply to generators including the current OCGT reference generator. Accordingly, amendments to the BRCP Procedure will be required if these penalties apply.

Should you require additional information regarding this submission, please contact Genevieve Teo, Senior Regulatory Analyst, at genevieve.teo@synergy.net.au.

Yours sincerely



RUDOLF VORSTER
WHOLESALE STRATEGY & PLANNING MANAGER

⁵ Wood Mackenzie article: "The drive for decarbonisation: seven key charts from the Metals & Mining Forum" (28 September 2022): <https://www.woodmac.com/news/editorial/the-drive-for-decarbonisation-seven-key-charts-from-the-metals-mining-forum/>

⁶ Reuters article via MINING.COM: "Column: Metal markets brace for a downturn of a different kind" (27 October 2022): <https://www.mining.com/web/column-metal-markets-brace-for-a-downturn-of-a-different-kind/>

⁷ Energy Policy WA: "Draft Statement of Policy Principles: Penalties for high emission technologies in the Wholesale Electricity Market": <https://www.wa.gov.au/system/files/2022-08/Out-of-Session%20Meeting%20Papers.pdf>