



25 September 2012

Mr E.J. Hall
Chief Executive
Queensland Competition Authority
Level 19, 12 Creek Street
Brisbane
QLD 4000

By email: rail@qca.org.au

Dear Mr Hall,

RE: Submission in relation to the QCA's Draft Decision of July 2012 on QR Network's Electric Traction Services Draft Amending Access Undertaking

Emission Capital is a specialist provider of investment management services and commercial, financial and technical advice to the energy sector.

QR Network is required to make below-rail infrastructure investment decisions with long horizons. In a regulatory structure designed to provide third-party access to the below-rail infrastructure on a competitive basis, QR Network's investment decisions need to be made in the context of uncertainty about the optimal mix of above-rail assets.

A regulated pricing structure that has the potential to bias the above-rail mix of assets will also bias below-rail investment decisions and may render previous investments uneconomic. Under the current regulated pricing regime for the below rail infrastructure, short run pricing strategies by diesel operators accessing the Blackwater system have the potential to make electric traction unviable as the burden of the electricity charge falls on a smaller number of users. Below some threshold usage level, electric traction will not be viable at all irrespective of whether the long term economics of the technology are fundamentally sound.

Given the uncertainty surrounding the long term risk-return characteristics of different traction technologies it is unlikely that a well-functioning market will yield an optimal mix of technologies that does not include a significant portion of electric traction.

We support QR Network in seeking an adjustment to the regulatory framework to ensure that:

- (i) long term infrastructure investment decisions are optimal in the sense that they do not bias the mix of traction technologies; and
- (ii) existing infrastructure investments cannot be rendered uneconomic by strategic behaviour from entities that have access to the regulated infrastructure.

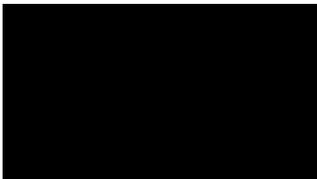
Below we focus on energy costs and energy price risk management to support QR Network's TCO analysis and our argument that electric traction will be a significant part of the technology mix in a well functioning market.



Energy Costs: The National Electricity Market (NEM) is an efficient and largely unregulated market that is generally considered to be competitive¹. The market is agnostic as to fuel source and will ensure that through time the generation mix will be constructed such that electricity is dispatched at the lowest overall cost. Costs associated with policy initiatives to reduce carbon emissions will be most efficiently handled through this market framework. This flexibility to accommodate differential changes in fuel input costs, technology developments that differentially impact production efficiencies, and pollution policies is not available under a rail haulage regime that is built around a single fuel source, i.e. diesel.

Energy price risk management: To the extent that haulage customers will benefit from long term energy price certainty, the use of electric traction will facilitate that objective. The ability of thermal generators to enter into long term fuel supply agreements with **domestic** fuel suppliers enables the generators to enter into long term (i.e. 20 yr +) fixed price electricity supply agreements. Likewise renewable generators, having no fuel or carbon price exposure, are willing to enter into long term fixed price off-take agreements. Conceptually, given certainty in electricity demand the owner of below rail assets would be in a position to pass on long term certainty in the Electric Charge component of the reference tariff. Australian diesel prices, on the other hand will be determined on the global markets for oil, refining margins and foreign exchange. Limits in the liquidity of these markets in long dated tenors imply a practical hedging limit on diesel price risk of about five years.

Yours sincerely,



Ted Quayle
Director

¹ See, for example, the assessment made by the RBA: <http://www.rba.gov.au/foi/disclosure-log/pdf/101115.pdf>