

24 August 2021

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Queensland Competition Authority
Level 27, 145 Ann Street
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(submitted via QCA Online Submission Form)

RE: QCA Draft Position Paper – Inflation Forecasting

Introduction:

The Queensland Resources Council (**QRC**), on behalf of the QRC's Rail Working Group, welcomes the opportunity to comment on the Queensland Competition Authority's (QCA's) July 2021 Draft Position Paper regarding Inflation Forecasting.

The QRC's Rail Working Group welcomes the QCA's proactive approach in considering and explaining the intended approach to issues such as this ahead of the commencement of undertaking review processes. We hope that this will encourage regulated entities to submit draft undertakings which are aligned with the QCA's expectations, or at least to explain the basis for any proposed departures from the suggested approach.

We do acknowledge that circumstances may change over time, and that the way in which inflation is applied to specific items within undertakings varies. Therefore, the method of forecasting inflation and the application of inflation within each undertaking will need to be considered for each new undertaking. In the case of the Central Queensland Coal Network, we understand that the QCA's current review will not have any impacts until after the expiry of the existing Aurizon Network Access Undertaking (UT5) on 30 June 2027.

Negotiation and the role of the QCA:

We note Aurizon Network's preference for certain matters to be negotiated directly with customers¹. While it is possible that certain matters may be negotiated between regulated entities and their customers from time to time, the QCA's role remains critical because:

- Agreement will not always be achieved;

¹ Aurizon Network – Response to QCA Issues Paper on Inflation – May 2021, page 2

- The expected regulatory outcomes create a baseline for negotiations; each party can assess the costs, risks, and benefits of a negotiated outcome against the regulatory alternative. The absence of a clear understanding of likely regulatory outcomes will impede the ability of the parties to reach agreement; and
- Even where agreement is reached, the QCA must consider whether that agreement is appropriate, taking into account considerations such as impacts on stakeholders which were not involved in the negotiation.

Comments on the QCA's Draft Positions:

The QRC's Rail Working Group generally supports the Draft Positions set out in Table 1 of the Draft Position Paper. In particular:

- We support the use of RBA data where this provides a reasonable measure of CPI or of a sector-specific change in costs. The independence, transparency, and ease of accessing this data are important considerations. In contrast, market-based measures may be less transparent and may require data manipulation and calculations which create significant scope for debate during the regulatory process.
- We support the QCA's draft position of forecasting CPI using short-term RBA forecasts for the first two years ahead and using a linear glide path to an anchor point to the fifth year ahead. We are less convinced that the proposed rules-based anchor points (2.25%, 2.50% and 2.75%, depending on the year 2 forecast starting point) are superior to a simpler 2.5% anchor-point (mid-point of the RBA's target range). Regardless of whether the year 5 anchor-point is fixed at 2.5% or allowed to vary between 2.25% and 2.75% based on the rules, the inflation forecasts for years 3 and 4 will be influenced in the direction of the year 2 forecast, due to the use of the glide path (in contrast to the previous practice of assuming an immediate jump to 2.5% after year 2). We are not sure that the variable anchor point adds any further precision.
- We support the use of Australian CPI for capital revenue purposes. Where a particular cost is to be escalation and the cost is more aligned to an alternative index such as a producer price index or Brisbane CPI, then alternative indices (preferably sourced from the RBA) should be considered.

Thank you for the opportunity to provide this submission.

Yours sincerely


Andrew Barge