Strategic Priority 1:

# An environment for efficient investment

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# OVERVIEW

- This priority focuses on investment in generation
- Design of the NEM is for investment to be delivered commercially
  - Reduced role of State governments financing investment
- Barriers to investment must be minimised

**Predictability in the regulatory and market environment is key**

- Ensuring processes for regulatory change (Market Rules) are transparent, objective, well understood
- Carbon policy challenge

# STRENGTHS OF CURRENT FRAMEWORK

- High degree of transparency over how AEMO establishes dispatch levels and prices
  - Important in signalling the value of new capacity
- Spot price volatility (and impact on profits) provides discipline on market participants for efficient supply
- Ability to calibrate risks and hedge risks through contracting
- Centralised, transparent pricing mechanisms being introduced to gas market
  - Commencement of STTM in September 2010

# HIGHER RISK ENVIRONMENT

- Debt providers requiring greater equity since the GFC

- Dominance of the “gentailer”
  - Financing generation investments from their own balance sheet
  - Potential for reduced liquidity in the contract market

- Increased wind generation has the potential for higher spot price volatility

# CARBON PRICING POLICY UNCERTAINTY

The uncertainty surrounding carbon policy is difficult to calibrate (and hence hedge against)

- Investors will allocate capital to lower-risk markets if they can earn similar returns
  - Increased difficulty in financing base-load and mid-merit power generation
  - Investment in peaking plant is less risky (due to increased wind generation, increasing peak demand and lower capex costs) but may not be the least cost plant to meet future demand requirements
- Long term policy arrangements desirable to minimise risk
  - Reduce financing costs
  - Attract a wider source of capital

The AEMC can work with Government to advise on policy settings that will minimise market distortions and costs for customers

# RETAIL PRICE REGULATION

- Retailers bear the risk of wholesale market volatility
  - potential for increased risks associated with a carbon price
- Regulated price methodology not consistent across states

Removing regulated tariffs where there is effective competition mitigates the risk that retail prices will not be fully cost reflective

- AEMC is responsible for reviewing competition in retail markets

The AEMC has recommended the removal of retail price regulation in VIC, SA, and ACT

# NEXT STEPS

- The AEMC can work with Government to advise on policy settings that will minimise market distortions and costs for customers
  - Importance of long term goals and enduring policy settings
- Financing challenges?
- Impacts of increasing trends towards vertical integration?
- How are the Statement of opportunities (ESOO and GSOO) used and what is their potential?

AEMC