



MAJOR ELECTRICITY USERS' GROUP

Notes for discussion with Goldman Sachs and other financial analysts, 2nd July 2012

Demand GWh pa	MEUG member Use ≈ 27% total NZ demand	Onsite generation	Sector	Primary location
4,000+	Rio Tinto	-	Aluminium	SI, Southland
≈ 1,000	Carter Holt Harvey	Yes	Pulp & Paper	NZ wide
	Fonterra	Yes	Dairy	NZ wide
	Norske Skog	Yes	Pulp & paper	NI, Bay of Plenty
	NZ Steel	Yes	Steel	NI, Sth Auckland
100 to 600	Fletcher Building Limited	-	Building materials	NZ wide
	Pan Pac	Yes	Pulp & timber	NI, Hawkes Bay
	Refining NZ	-	Oil refining	NI, Whangarei
	Winstone Pulp International	-	Pulp & timber	NI, Ohakune
	Whakatane Mill	-	Pulp	NI, Bay of Plenty
< 100	ANZCO	-	Meat	NZ wide
	Holcim	-	Cement	SI, West Coast
	Dongwha Patinna	-	MDF	SI, Southland
	Heinz Wattie's	-	Food cannery	NI, Hawkes Bay
	Lion Breweries	-	Brewing	NZ wide
	Oceana Gold	-	Gold mining	SI, Otago, West Coast
	Ravensdown	Yes	Fertiliser	NZ wide
	Solid Energy	-	Coal mining	NZ wide
Industry group members:				
Business NZ				NZ wide
Wood Processors Association				NZ wide

Mission Statement: To add value to MEUG members' management of electricity costs and risks through market intelligence, networking, facilitating solutions to improve competition, maintain reliability, promote efficient operations and regulate monopolies to achieve outcomes consistent with competitive markets for the long-term benefit of electricity consumers.

Strategic objectives

1. Facilitate better information & capability for MEUG members to manage electricity costs & risks;
2. Improve competition, maintain reliability and promote efficient operations;
3. Regulate monopolies to achieve outcomes consistent with competitive markets;
4. To have excellent MEUG governance and operations

MEUG contact: Ralph Matthes, ralph@meug.co.nz, T: 04 472 0128, M: 0274 760 500

Level 1, 93 The Terrace, Wellington 6011, New Zealand
PO Box 8085, The Terrace, Wellington 6134, T +64-4 472 0128, info@meug.co.nz, www.meug.co.nz

Timeline	Recent past	Present	Future
<p>Industry structure, governance, policy and politics</p>	<p>Improved NZ Energy Strategy revised 2011.</p> <p>EA replacement of EC Nov-10 de-politicised the sector and set a more focussed efficiency purpose.</p> <p>Role of Ministers now limited to appointing EA members and SOE directors and agreeing SCI.</p> <p>VAS & Tekapo transactions has reduced regional and island dominance.</p> <p>MOMS.</p>	<p>Stable apart from politicisation of MOMS.</p>	<p>MOMS success linked to success of improving competition, i.e. dependent on partially listed SOE efficiency gains being passed through, and being seen to be passed through, to consumers.</p> <p>Review System Operator governance.</p> <p>EA and GIC merger to be considered.</p> <p>Risk of policy flip flop back to policies to lift renewable at expense of cheaper thermal generation.</p>
<p>Competitive sectors</p> <p>2 listed, 3 SOE, \$3.5b pa spot turnover¹ and ≈ \$0.5b retail margin.</p> <p>A few new entrant retailers and more small local generators.</p> <p>Ancillary services markets (frequency keeping and reserve markets small but can influence energy market).</p> <p>Small but growing demand side response in energy, ancillary service and transmission alternative markets.</p>	<p>Section 42 policies OK except stress test (adopted instead of a floor during public conservation campaigns). Other s24 policies included compensating households during public conservation campaigns, FTR, DSBF/DD, facilitate hedge market and more standardised EDB tariff.</p> <p>ASX futures gained momentum and will be a permanent feature of the market.</p> <p>TOU consumers started to consider alternative hedges and providers such as trading banks.</p> <p>Late 2011 to present extreme dry event well managed without political and media beat up.</p> <p>Very successful "what's my number" campaign changed retail consumer and supplier behaviour.</p>	<p>Ongoing incremental Code improvements targeted by very effective EA market monitoring. Detailed work but a lot of gains possible. S 24 roll out continues.</p> <p>Urgency to implement Dispatchable Demand (DD) to improve spot price discovery, contestability.</p> <p>Ex post energy only spot market will remain paradigm for near future. Managing transient market power (net pivotal situations) is challenging, eg major event 26-Mar-11 and recent small local events.</p> <p>Post 13-Dec-11 blacking out of 16% of NI, changes underway on Under-frequency management and AUFLS regimes, plus improving ex ante spot price f/casts to better match ex post invoiced prices when market stressed.</p>	<p>No change to key drivers of D=f(GDP) and spot price volatility = f(rainfall and unexpected outages). Latter constraint driven price spikes will reduce as grid upgrades completed.</p> <p>Few years to bed in 2009-10 reforms and then have a stock take. If inefficiencies or sustained excess rents still occurring; then look at other structural or market design options.</p> <p>Apart from new fuel resource discoveries (ie gas), RMA and ETS important drivers of new generation investment.</p> <p>Supplier's ability to increase margins limited by real increases in Transpower & EDB charges.</p> <p>Technology changes important, eg smart meters, lower cost DG, dynamic line rating.</p>

¹ 39,000 GWh pa @ \$90/MWh

Timeline	Recent past	Present	Future
<p>Line monopoly Transpower, \$0.8b pa</p>	<p>≥ \$3½ b grid investments approved. Only few hundreds of millions yet to be requested for approval by Transpower. Transpower O&M practices inefficient but CC decided to give Transpower time to improve; consumers therefore bearing higher charges to cover inefficient level of O&M costs until next IPP reset.</p>	<p>Multiple large projects being built. Some cost overruns. Some delayed because D f/casts lower than when approved. Transmission Pricing Methodology (TPM) review and the prize of a huge wealth grab by SI generators if they can shift HVDC costs to consumers will remain controversial and litigious.</p>	<p>Individual Price-Quality Path (IPP) reset 01-Apr-15 will create better efficiency drivers, setting of customer specific service levels and accountability on Transpower. Increasing use of transmission alternatives is supported by CC. TPM for HVAC may be improved to better align incremental grid upgrade costs for remote generation.</p>
<p>29 EDB, \$1.5 b pa</p>	<p>Implementation of Part 4 of Commerce Act regulation of monopolies enacted 2008 is bogged down with judicial reviews.</p>	<p>Input Methodology merit review by High Court starts Sep-12 (appeals cover cost of capital, asset valuation and taxes). Details of Information Disclosure, Default Price-Quality Path, Customised Price-Quality Path and Starting Price Adjustments and what to do with Orion are complex and resource intensive. EA review of distribution pricing is and will become more controversial.</p>	<p>Litigious rent seeking behaviour by some EDB and possibly Transpower continues. Review of whether Part 4 has worked as intended including lack of equal countervailing power of consumers in merit review process. Policy review to consider if 29 EDB too many? Regulatory innovations with Transpower IPP including mimicking normal contractual basis with service levels and accountability may migrate to regulation of EDB.</p>
<p>Taxes EECA electricity efficiency levy \$13m pa</p>	<p>Strong opposition to this tax</p>	<p>Strong opposition to this tax</p>	<p>Strong opposition to this tax</p>
<p>Total \$6.3b pa</p>			