Australia

Business Environment and Challenges

The Australian power sector has continued to witness consolidation of the de-regulated generation and retail markets, as well as the public listing of regulated energy businesses mainly involved in distribution.

There have been significant changes to the regulatory environment, with the Australian Energy Market Commission (AEMC) responsible for rule-making and market development in the National Electricity Market (NEM) and the Australian Energy Regulator (AER) responsible to oversee the rules and to regulate transmission, commencing operation on 1 July 2005. The AER will progressively take up responsibility for retail and distribution regulation. Until this occurs, the state regulatory bodies will remain responsible for retail and distribution regulation. Distribution regulation is expected to occur in 2007, while the timing for retail regulation is not yet determined.

In the NEM a very mild summer and winter led to continuing low prices, although wholesale electricity prices started to trend upwards with recent volatility experienced in Victoria, New South Wales (NSW) and South Australia. Overall, wholesale prices in the NEM still remain below a level which most operators believe to be sustainable in the long-term. Rational market behaviour continues to suggest that there will be limited and targeted new investment by all generators until the balance between supply and demand is restored and market prices rise to new entrant level.

Competition in the Australian power sector is most advanced in Victoria and South Australia. However, there are signs of market reform in other major Australian States. In Queensland, the Government has been considering major changes to the electricity sector, which is presently almost fully Government-owned, with only limited private sector ownership in the generation sector. In September 2005, the Queensland Government announced its intention to open the residential and small business sector to retail contestability in both gas and electricity from 1 July 2007. The Government has also commenced the review of the structure of Government-owned corporations. The results of this review will be known in early 2006 with potential outcomes including privatisation or other forms of private sector participation in retail and generation. The Government has, however, indicated that electricity distribution and transmission will continue to be Government-owned.

In NSW, Australia's most populous state, the State Government is still considering the policy response to a number of looming electricity sector challenges. In particular, the Government is looking for investment in generation to maintain supply reliability, for that investment to come from the private sector and for this to contribute to lowering greenhouse emissions intensity. Power station developments, such as TRUenergy's proposed 400MW Tallawarra gas-fired generation project are ideally positioned to respond to Government's policy objectives.

Q: **Mr. Chris Forsterling** *General Manager, VIC/SA/TAS/NZ, Thiess Pty Ltd.* (left)

The recent acquisition of TRUenergy has seen CLP move from just power generation to power generation and energy trading and mass market retailing. Does CLP have a strategy for major growth in Australia and if so is it likely to be in power generation, or retail, or both?

A: **Richard McIndoe** *Group Director – Managing Director Asia Pacific* (right)

The TRUenergy model provides CLP with a broader, more stable platform for growth in the NEM. We intend to grow both the generation and retail businesses organically and, potentially, through acquisition. However, we will look to maintain the overall balance between generation and retail exposure. The integrated energy model, which balances these two business lines, has proved to be the most effective and sustainable business model in deregulated markets elsewhere, predominantly in Europe. It is CLP's intention that TRUenergy becomes the leading integrated energy player in the NEM.

Year 2006

In 2006, TRUenergy's objectives will be to:

- grow our retail and generation base by
  - maintaining existing retail customers and increasing market share in our core markets of Victoria and South Australia through organic customer growth and the evaluation of retail acquisitions on a case-by-case basis;
  - starting construction of the Tallawarra 400MW gas-fired combined cycle plant in NSW and investigating opportunities to develop peak load generation capacity; and
  - developing retail operations in NSW as retail margins become more attractive.
- maximise the value of our assets through
  - improving efficiency and achieving cost savings, including through implementation of the strategic review which has been undertaken of the TRUenergy business;
  - improving Yallourn availability by selective additional expenditure on maintenance; and
  - successfully managing the flexibility provided by the diverse range of generation, fuel and retail assets in the wholesale gas and electricity markets.

Beyond 2006

We intend to position TRUenergy so that it has the capability to enter the Queensland market in the light of full retail competition anticipated from mid-2007.

The NSW Government's energy review may open up major acquisition and business opportunities in NSW. We will be closely monitoring the outcome of the NSW Government initiatives in this regard, with a view to enabling TRUenergy to take advantage of the investment and business opportunities that may emerge.

We will also aim to develop and manage constructive and balanced relationships with the new electricity regulatory bodies, namely AEMC and AER.

Q: **Mr. David Clark** *Director, Head of Utilities Research, Asia, Deutsche Bank AG, Hong Kong Branch* (left)

The Yallourn plant commenced operations between mid 70s and early 80s. Could CLP indicate how much longer this plant could operate and whether there is any significant capex or maintenance expenditure planned for Yallourn over the next several years?

A: **Peter Littlewood** *Group Director – Operations* (right)

There is sufficient coal at the Yallourn mine to support operation for another 25 years. Obviously this period extends well beyond the original design life of the generating plant. However, based on our assessment of the key plant components and also by reference to growing experience generally in the power industry for extending the useful life of coal-fired units, we believe that it is feasible to continue operation for this period. There will indeed be a need for significant capex to replace and refurbish various components, and maintenance expenditure will be somewhat higher than required for younger plant. However, we keep all these factors under close review and make appropriate provisions in our budgets. Yallourn will continue to be a low cost provider to the market.