

Canegrowers' proposal for lower irrigation tariffs

The QCA has analysed claims from Canegrowers that irrigation tariff prices can be reduced by one-third without affecting the revenue of the retailer (Ergon). In effect, the decrease would be better described as halving prices, given the forecast 15% increase in costs for these tariffs in 2014–15.

The Canegrower argument assumes:

- Reducing prices will lead to a large increase in demand from irrigators
- This increased demand will offset the revenue lost from reducing prices.

The QCA believes that these outcomes are possible but far from assured.

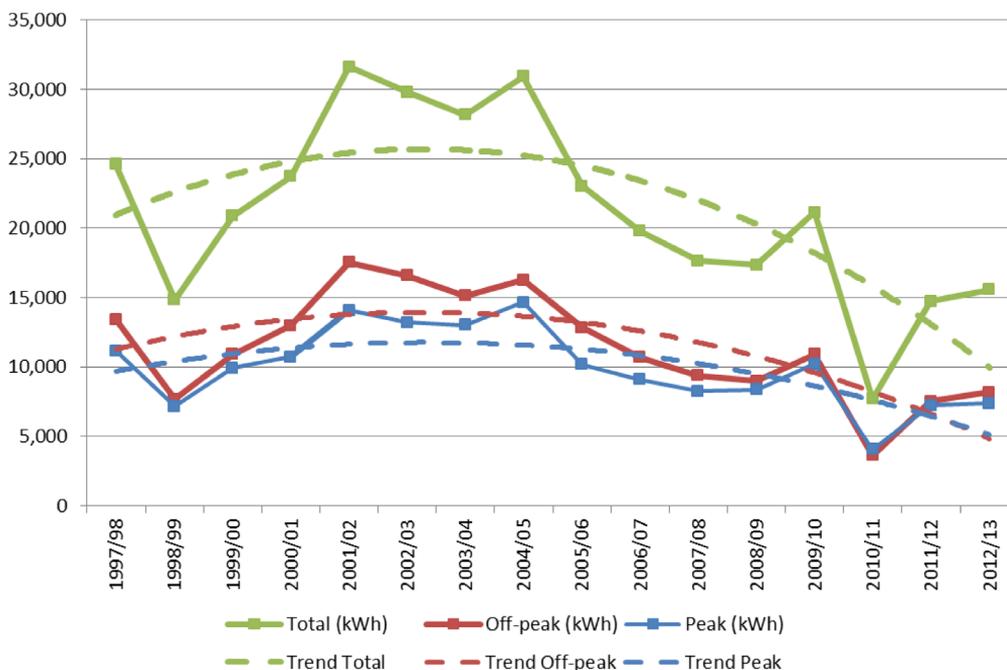
More importantly, it is certain that reducing prices will increase the cost to Queensland taxpayers of subsidising the 18,000 customers using irrigation tariffs.

Claim: Lower prices mean higher demand

Canegrowers claim that lower prices will lead to much higher demand from irrigators.

In previous submissions to the QCA, Canegrowers has stressed that rainfall is the most important factor in irrigators' demand for electricity. Canegrowers' analysis shows in the last two years that average consumption by irrigators increased as prices increased. According to Canegrowers, consumption by the average tariff 62 customer almost doubled after 2010–11; tariff 62 prices increased by 17% over the same time.

As important as prices are, it seems clear that price is not the only factor determining demand for electricity. Reducing prices may lead to higher demand but it is impossible to predict accurately whether any increase in demand will occur.



Source: Canegrowers' submission to the QCA

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Claim: Higher demand will not reduce revenue

It is possible that higher demand may offset lower prices, leaving Ergon with the same revenue. In 2014–15, demand would need to rise by more than one-third to deliver the same revenue to Ergon.

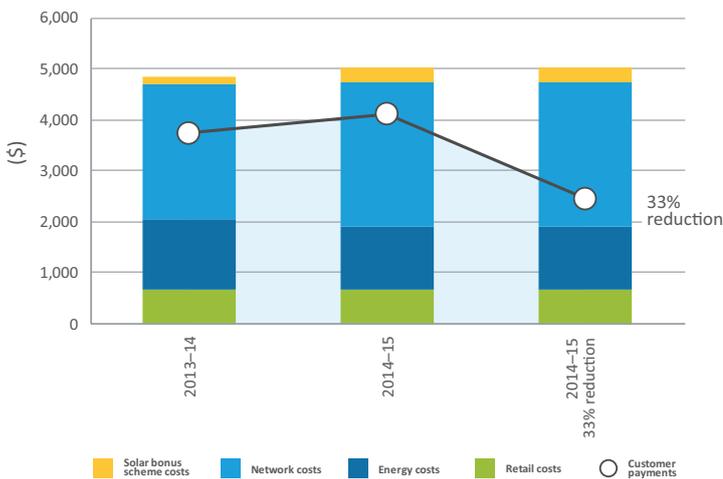
However, this claim misses the essential point. Revenue and costs have to be considered together. Achieving the same revenue while incurring greater costs is unsustainable for any business.

All irrigation tariffs are set below cost. Many irrigators are paying only half their actual cost of supply. Off-peak prices for irrigators, for example, are much lower than the prices paid by regional small businesses.

Selling more electricity at even lower prices will only increase Ergon's losses and therefore the cost to taxpayers.

Fact: Lower prices = higher public subsidies

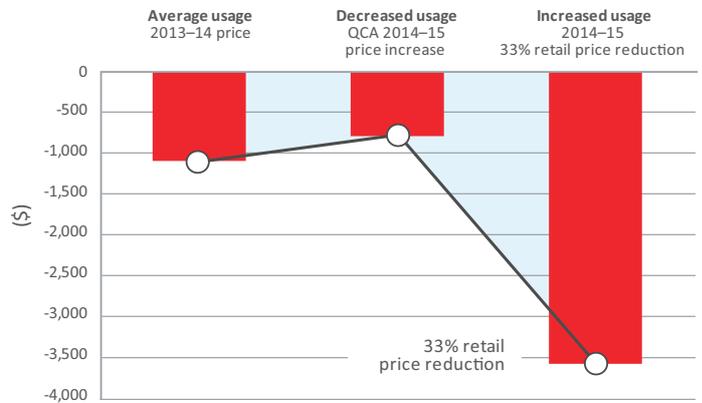
The figure below illustrates this point. The 2013–14 and 2014–15 columns show the costs incurred by Ergon in supplying the average tariff 62 customer. The last column shows the Canegrowers' proposed price reduction. The black horizontal lines represent payments by the customer. The public subsidy would increase significantly if there was no change in demand; if the additional demand predicted by Canegrowers occurred, the public subsidy would be even more.



The figure below shows the likely results from applying the Canegrower proposal, using Canegrowers' estimates for demand in 2014–15 (i.e. lower demand with a price increase, much higher demand with a price reduction).

Ergon's losses per average customer would be about four times higher under the Canegrower's 33% reduction scenario. The difference between the second and third scenario for all tariff 62 customers would be a minimum additional loss of \$30 million; this loss would have to be funded by taxpayers or other customers.

Applying the same price reductions to other irrigation tariffs would yield similar results.



Conclusion

The Canegrowers' proposal would significantly increase the cost of providing subsidised electricity to customers on irrigation tariffs, regardless of any changes in demand. If Canegrowers' prediction of higher demand did occur, the public subsidy to irrigators would rise from \$32 million (2013–14) to at least \$82 million (2014–15).