

# Attachment L

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## WACC parameters

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Natural Resources  
Access Regulator



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# 1 WACC parameters

This pricing proposal uses a real post-tax Weighted Average Cost of Capital (WACC) of 3.6%. This is based on the parameters listed in the Table 1 below.

This placeholder WACC represents an increase from the allowed rate of return of 3.0% for the 2021 WAMC Determination and reflects the increase in government bond yields that have occurred since 2021.

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## Rate of return

### Proposed method and rate of return

The return on capital covers the cost of servicing our debt and provides a return for capital investment. It is calculated by multiplying the value of our regulated asset base (RAB) by the rate of return on capital.

WAMC proposes to apply IPART's 2018 Weighted Average Cost of Capital (WACC) method for determining the rate of return on capital. As part of IPART's methodology, we understand that IPART will update market data closer to the Draft and Final Determinations, with the cost of debt allowance updated during the determination period. For this pricing proposal, our 'placeholder' WACC is 3.6%.

The WACC is the minimum ('benchmark') rate of return an investor requires to commit capital to an investment given its risk. It is the weighted average of the required return on debt capital and the required average equity capital.

### Why is it important?

The return on capital (based on the RAB multiplied by the WACC) contributes to approximately 1.5% of WAMC's Notional Revenue Requirement to meet our customer and statutory obligations.

In determining the appropriate rate of return, regulators seek to set an allowance that is commensurate with the true WACC, which must be estimated because it cannot be observed directly. This ensures that customers do not pay more than the efficient cost of capital that the business must pay to finance the assets required to deliver regulated services.

If IPART sets the allowed rate of return below the true WACC, the business may not be able to attract the capital it requires to invest in infrastructure for water management services. This could encourage inefficient under-investment and negatively impact on the quality of services to customers and other stakeholders.

If IPART sets the allowed rate of return above the true WACC, consumers would pay more than the efficient cost of delivering regulated services, and the business would be incentivised to over-invest. Since neither of these outcomes would promote the long-term interests of customers, IPART should seek to adopt methodologies for estimating the WACC that are as accurate as possible.

Table 1: Placeholder WACC and WACC parameters

WACC Parameter	Current	Long-term	Midpoint
Nominal risk free rate	3.0%	2.6%	2.8%
Inflation forecast	2.5%	2.5%	2.5%
Debt margin	2.4%	2.4%	2.4%
Benchmark gearing	60%	60%	60%
Market risk premium	8.2%	6.0%	7.1%
Gamma	0.25	0.25	0.25
Corporate tax rate	30%	30%	30%
Equity beta	0.7	0.7	0.7
Cost of equity (nominal post-tax)	8.7%	6.8%	7.8%
Cost of equity (real post-tax)	6.1%	4.2%	5.1%
Cost of debt (nominal pre-tax)	5.4%	5.0%	5.2%
Cost of debt (real pre-tax)	2.8%	2.4%	2.6%
Nominal Vanilla WACC	6.7%	5.7%	6.2%
Post-tax real WACC	4.1%	3.1%	3.6%