

## **CWA Speech**

Snowy Hydro Limited is greatly misunderstood – misunderstood with regard to what it does, how it does it, and who cares for it. It is misunderstood because the Snowy Scheme has changed “forms” over the years. The services it provides have changed and the markets in which it operates have also changed over the years. Even the assets have changed, but the way we use the assets has changed even more; what is expected of the Snowy Scheme and its “offspring” Snowy Hydro Limited has over the last decade changed and changed forever.

It has changed because of the needs of the “markets” it serves and because of its unique capability to meet the evolving needs of these new markets.

So what does Snowy Hydro now do?.....

### **Water**

We do not own water, we do not sell water! We are controlled by a Government water licence.

We collect and store water, and we release a fixed amount each year, as per our water licence, into storages controlled by the New South Wales’ Government (Blowering Dam) and the Murray Darling Basin Commission (Hume Dam) – both dams are from where the New South Wales’ Department of Natural Resources and the Murray Darling Basin Commission – not Snowy Hydro – release to the

irrigators. Snowy Hydro Limited does not control annual releases to the irrigators.

But we are now able to do more than release an annual amount of water from the Scheme into Government dams. We now greatly help irrigators and farmers in ways not previously undertaken.

Since corporatisation, and since being restructured such that we henceforth function as any normal market, growth and shareholder return oriented company, Snowy Hydro Limited has been able to offer, when most needed, supply risk management products to the irrigators downstream of the dams owned by the Murray Darling Basin Commission and New South Wales Department of Natural Resources. In essence, by making special arrangements with the Governments' Agencies (Murray Darling Basin Commission and Department of Natural Resources), and after understanding the needs of the irrigators and then by coming to sensible and mutually beneficial commercial arrangements directly with the irrigators, we have been able to offer special timing of release commitments. In this way we have been able to assure the irrigators that they will get a specified amount of water in specified months.....this is not something the Government owned Snowy Mountains Hydro-electric Authority would or could do – and so we are now meeting the special needs of irrigators and this has

substantial and demonstrable benefit to country towns where economies depend on farming success.

This form of innovation, discouraged under the pre corporatised business model that was “Snowy Mountains Hydro-electric Authority”, has been particularly valuable to those irrigators and farmers who understand best the climate and weather risk, and the year-on-year variability of rainfall. It has been particularly beneficial for irrigators and town and country economies in the last three years of worsening drought and uncertainty. This is water supply risk management by Snowy Hydro Limited in practice.

This supply risk management service is increasingly being valued by the irrigators, particularly on the Murrumbidgee.

## **Electricity**

With regard to electricity, profound change has occurred due to the creation of a National Electricity Market in 1996, and the very substantial growth in the demand for electricity, particularly at peak times (due mainly to the widespread installation and use of air conditioning).

Snowy Hydro Limited should **not** now be thought of as a generator of electricity – we only generate 14% of the time – the reason being that we conserve water where we can, biasing our releases to better “fit” environmental concerns and irrigator/farmer needs, having identified future possible climate change impacts some six years ago. We are now a

generator of last resort rather than a generator of electricity to earn revenue to meet a budget. This thinking means we can be a more effective (and co-operative) water manager while achieving better financial outcomes for our shareholders.

Let me explain briefly how we do this risk management thing with regard to electricity.....

Retailers charge you for the electricity you use. The price per unit is constant over the medium term, say \$50.00 per MWh. But the retailer has first to buy the electricity sold to you.....but the price to be paid by the retailer can vary between \$zero and \$10,000.00 per MWh and it can vary every 5 minutes as the market operates on a bidding system. Now the retailer cannot pass on the price movement to you, the consumer, so the retailer takes out insurance against such rapid and large price movements. We, Snowy Hydro Limited, provide the insurance policy or, as we call it, a financial hedge contract. If the price goes above what the retailer is willing to risk having to pay, then we pay the retailer the difference in the form of cheques that offset the price over and above the level the retailer is willing to buy at over the long term. We can do this because we have fast start equipment that generates in minutes and we then earn the prevailing higher price for the electricity that we put into the National Electricity Grid, fully offsetting the cheques we have paid out to the retailer. And for this

price risk mitigation the retailer pays us a substantial and long term “insurance premium”. It works well for us, it works very well for the retailers and it keeps your electricity prices from fluctuating widely and arguably from the prices increasing due to the risk that would otherwise have to be priced in to the cost of electricity. This is electricity price risk management by Snowy Hydro Limited in practice.

So you can now see we do something similar for both the water side of our business, the irrigators, and for the electricity side of the business, the electricity retailers and thus indirectly for the individual electricity consumer – it is called managing supply risk for the irrigators and managing price risk for electricity retailers and consumers.

That explains how far we have evolved from being the simple Snowy Scheme electricity generator and we have evolved this way because the electricity market was created in 1997 and because environmental and climate conditions and expectations have changed, and also because the users/consumers and the industry technologies have required and arguably forced us to evolve and adapt. Viewed from both a water user’s perspective and from an electricity consumer’s perspective we are now an “insurance” company.....we manage other people’s risks.

The critics of the planned listing of Snowy Hydro Limited on the ASX (IPO), last year, I would suggest, have not understood the changed market and customer needs and

demands. Nor have they understood the safeguards built into our water licence and other guiding legislation. Fortunately, the designers and builders of the Snowy Scheme had an abundance of foresight and vision even if they could not have known precisely what would be expected of their Scheme and its capabilities today and tomorrow. It should be well noted that because of the new and changing roles demanded of the Company, ie managing risk, governments are arguably not appropriate owners any more – there is too much risk in the markets we now critically and unavoidably serve.

Contrary to the misinformation put about at the time of the IPO, the evolution of the National Electricity Market and the establishing of Snowy Hydro Limited with a strong profit and a reinvestment motivation has turned our role from being an electricity generator, incidentally releasing water, to a company well able and needing to balance water and electricity demands to the benefit of all stakeholders, including shareholders, whoever they may be.

In summary, it is a given that we will meet our water release obligations to irrigators/farmers on the western rivers, and we also run the business to meet our obligations to the electricity users across the National Electricity Market but we try to limit our generation to only peak demand times – and in this way we make sound profits in order to pay attractive dividends to our Government shareholders or

future investors. The way we run the business today is how any competent private sector company would run it.

But to play this new role and to do all this we have to maintain a strong credit rating or the retailers will not deal with us and the business will decline with all the usual implications – and in turn in order to maintain a strong credit rating we have to be profitable and diverse in capability. Governments do not provide us or our customers with guarantees to back our debt. Government do not want to put more funds into the business.

We have to be profitable in order to have a sufficiently strong cash flow just to maintain our assets, dams, pipes, power stations etc at a very high, reliable and safe standard and we have to continually upgrade our very complicated and sophisticated communications and control systems, which operate in a harsh environment across 5,000 square kilometres of the Snowy Mountains. Remember, our shareholder Governments do not put cash/equity, or debt, into our Company; they only take out dividends.

Like any business we have to grow as our markets grow, we have to offer secure employment, we have to maintain our assets and we have to keep pace with the very sophisticated technology used by the market managers, by our customers and by our competitors and we have to invest to ensure a safe work environment for our people. And increasingly we have to provide water, at no cost, for

environmental flows. All this requires that we make profits and it also requires that we should have access to new or additional equity or new debt, both of which were denied to us with the withdrawal of the planned listing of Snowy Hydro Limited on the ASX last year. Those that spoke loudest in order to stop the IPO are now silent on how to solve the problem they have caused.....Snowy Hydro Limited is suffering starvation of capital!!

Over and above keeping the existing business at the standards we have achieved since corporatisation, we now have other pressing reasons to need capital.....related to meeting the threat of climate change.

We have a scarce resource, water, and we foresee greater variability in future weather patterns and behaviours – bushfires, longer dry periods, hotter weather over more often continuous days. To conserve water for when it is needed most we need greater flexibility in how we generate electricity, in when within the year we release water into the New South Wales Government/Murray Darling Basin Commission dams and, when and to what extent, we continue to make whatever special arrangements we can make for irrigators by better planning timing of releases of water etc – above all, we need new and additional generation capacity and additional fuel flexibility so as to be able to best meet the often conflicting requirements for



water release and electricity needs. These needs will only get more demanding and more complicated and urgent.

The answer to this future potential dilemma is not more dams. It is the building of gas fired electricity generation plant that will substitute for using water for generation – using gas as the fuel rather than scarce water, saving the water for release not when required primarily by electricity needs but when required for irrigation and water storage needs. It makes obvious sense to sometimes use gas instead of water as our “fuel”.

Snowy Hydro Limited adopted this fuel substitute vision four years ago when it ceased to be “The Authority” and now has over 600 MWs of gas fired electricity generation plant in Victoria with plans to develop plant in South Australia and New South Wales. If we can get the necessary capital.

Just to conclude, and as a point of interest, Snowy Hydro Limited is now also an electricity retailer – we market as RED ENERGY, based in Victoria. RED is wholly owned by Snowy Hydro Limited and you will soon see the brand marketed in country New South Wales. It is also now marketing in South Australia. This move into retail further protects the Snowy Scheme from declining relevance in a growing and changing electricity market. Particularly as we see our customers growing as vertically integrated electricity suppliers.

Snowy Hydro Limited has come a long way since the days of the Commonwealth Government owned Snowy Mountains Hydro-electric Authority – it has terrific people, well incentivised and motivated to do a good job for all its stakeholders and clearly it is demonstrating it can achieve very good outcomes in the extraordinarily difficult times of the last few years.....now that it can operate largely as a private sector company supporting private sector customers and stakeholders.....now that Snowy Hydro is free to operate as would a private sector company serving a diverse range of customers and needs. But.....the future is clouded by a lack of access to capital, either debt or equity, because in this regard it is not fully “private sector” – a constraint that must be remedied if the Company is to deliver on the Snowy Scheme’s original vision and on the “mission” as it has evolved over the years.

We respect our history but we think in the future as those who built the Scheme did!! Snowy Hydro must eventually be given the other leg that underpins any successful private sector company – we have water licence obligations that protect farmers and irrigators and we have legislated obligations for water environmental releases – now we need the ability to raise capital from whoever our shareholders may eventually be; to raise funds to grow to meet the changing needs of all our stakeholders.