POJ1395J – Ports of Jersey Long Term Pricing Framework – Assumptions: Call for Information

Contents

Question 1: ***Do you agree with PoJL's proposal that the Case for Incorporation and the Air & Sea Ports Incorporation (Jersey) Law provide an appropriate starting point for the assumptions to be used for a long-term pricing framework? If not, what alternative(s) should be considered, and why?***

Yes, we agree.

Question 2: ***Do you agree with PoJL's proposal that 3% general inflation should be used as an assumption for a long-term pricing framework? If not, what alternative(s) should be considered, and why?***

Yes, we agree that 3% general inflation is a fair assumption.

Question 3: ***Do you agree with PoJL's proposal that long-term growth rates of 0.8% for air passengers, 0.0% for sea passengers and 0.53% for freight and fuel should be used as assumptions for a long-term pricing framework? If not, what alternative(s) should be considered, and why?***

Yes, we agree that the long term growth rates can be considered a prudent assumption for growth. Please see our response to Question 20

Question 4: ***Do you agree with PoJL's proposal that the amounts assumed by PoJL for the airport and phase 1 of the harbour 'Master Plans' should be used for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

We are not qualified to provide an informed opinion on the costings produced for the airport and phase 1 of the harbour 'Master Plans' but we recognise the need for investment in these areas.

Question 5: ***The amounts noted in paragraph 5.7 above are included in the £286m for the LTCP. In addition to specific comments in relation to the 'Master Plans', do you agree with PoJL's proposal that £286m (uninflated) of investment in the next 25 years across the facilities operated by PoJL should be used as an assumption for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

In the absence of more granularity on the projects included here it is difficult to comment meaningfully.

Question 6: ***Do you agree with PoJL's proposal that the 'commercial projects' and associated forecasted cash flows should be used as assumptions for the long-term pricing framework development? If not, what alternative(s) should be considered, and why?***

Yes, we agree that these cash flows should be used as assumptions for the long-term pricing framework.

Question 7: ***Do you agree with PoJL's proposal that it should use a limit of 2.5-3.0x EBITDA for net debt on its core activities as an assumption for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

We agree that this is a reasonable assumption based on the comparators provided.

Question 8: ***Do you agree with PoJL's proposal that it should use a net cost of debt on commercial projects based on the terms that may be available from institutions and partners on a project-specific basis as an assumption for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

We agree

Question 9: ***Do you agree with PoJL's proposal to use a cost of debt of 3% in the medium term and 5% in the long term as an assumption for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

We agree

Question 10: ***Do you agree with PoJL's proposal that it should use an efficiency target of 0.2% (in real terms) operating cost reduction for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

Based on the information provided we agree that PoJL should use an efficiency target of 0.2% operating cost reduction for the long-term pricing framework. We are unable to scrutinise whether the reported segmentation of cost by level of control is accurate.

Question 11: ***Do you agree with PoJL's proposal that it should use a depreciated replacement cost methodology based on the Jersey Financial Reporting Manual (JFREM) for calculating depreciation in business plans on which the long-term pricing framework will be based? If not, what alternative(s) should be considered, and why?***

Yes, we agree

Question 12: ***Do you agree with PoJL's proposal that it should assume for the long-term pricing framework that its obligation to provide PSOs as currently set out in law and that the associated costs and revenues will continue? If not, what alternative(s) should be considered, and why?***

We agree that PoJL are mandated to deliver and fund the PSO's. Any net inflows (chiefly CICA) should be used to offset levies charged to users of the ports.

Question 13: ***Do you agree with PoJL's proposal that it should assume for the long-term pricing framework that it will continue to support community activities in the same manner as before incorporation? If not, what alternative(s) should be considered, and why?***

The purpose of incorporation of PoJL as set out in the incorporation law does not extend to the types of support listed in the submission from PoJL. Blue Islands' view is that such activities should be separated from the long-term pricing framework that should focus solely on core operational activity.

Question 14: ***Do you agree that PoJL's proposal that no cash dividends will be paid until PoJL is financially self-sustainable is an appropriate assumption for the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

Yes, we agree that it is an appropriate assumption for the long-term pricing framework that no cash dividends will be paid until PoJL is financially self-sustainable. Even then, consideration should be given to the use any distributable profits to reduce levies on users of the ports for growth or investment in further enhancements at the airport and harbour.

Question 15: ***Do you agree with PoJL's proposal that it should assume for the long-term pricing framework that funding for capital investments will come from a combination of cash generation from core operations and commercial projects, as well as debt raised without States of Jersey guarantees? If not, what alternative(s) should be considered, and why?***

No we do not agree. We believe that any debt raised should be with a States of Jersey guarantee to enable PoJL to achieve the best possible rate within the marketplace.

Question 16: ***Do you agree with PoJL's proposal to use a single till? If not, what alternative(s) should be considered and why?***

Yes, we agree with the proposal to use a single till.

Question 17: ***Do you agree with PoJL's proposal that it should not explicitly separate harbour operations from airport operations or make any other possible divisions such as separating public service obligations in the context of the long-term pricing framework? If not, what alternative(s) should be considered, and why?***

We agree that that PoJL should not explicitly separate harbour and airport operations. Practically and given the 'lumpiness' of costs then pooling of funds to invest is appropriate treatment. However, as stated on P.43 of the PoJL submission it should be expected that in the long-term investment in the Airport and Harbour should be funded by the users of each respective port and not through a cross-subsidy.

Question 18: ***Do you agree with PoJL's proposal that a 10 year period for a pricing framework is appropriate? If not, what alternative(s) should be considered, and why?***

Yes, we agree

Question 19: ***Do you consider the range of assumptions covered by PoJL's submission to be complete in the context of setting a long-term pricing framework? If not, which further assumptions should be considered, and why?***

Yes, we consider the range of assumptions to be complete.

Question 20: ***Do you have any further comments regarding any part of PoJL's submission which may have a bearing on the development of a long-term pricing framework?***

Should profitability or cash generation significantly out-perform forecasts then a mechanism should be in place to reduce charges appropriately and pass any outperformance to service users.

A base set of assumptions is of course required for the development of the framework. However, any departures from these assumptions could have a significant impact on revenue generated by PoJL, and revenue required to fund capital investment. Therefore, a mechanism is needed to enable periodic review during the 10 year period to ensure that performance does not deviate materially from the base assumptions and to review the framework if appropriate. Such factors include, but are not limited to, the following:

- Passenger growth
- RPI
- Commercial Project performance
- Cost of Debt
- Final cost of capital improvements

We would add that if pricing is set purely to cover the capital investment requirement of PoJL, there is a risk that sight could be lost of the critical role that the ports play in the economic and social wellbeing of Jersey PLC. The States of Jersey, as shareholder, should act as the safeguard to such a situation.

Finally, there are a number of options available to PoJL to increase its charges that may not be immediately apparent looking at the charge sheet. The charging basis of certain services may be altered, resulting in a significant increase in cost to its customers despite there being only a modest change in the headline rate. For example, one service is now charged on an "hour or part thereof" basis as opposed to a "minutes used" basis. While the headline price may not have changed, the basis of charging has and this results in marked changes in PoJL revenue / customer cost.