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Michael Houghton
Assistant Director Gas Inquiry Unit
Australian Competition & Consumer Commission
Level 17 Casselden Place
2 Lonsdale Street
Melbourne Vic 3000

14 February 2018

Dear Mr Houghton,

Please find attached AGL's submission in response to the ACCC consultation on LNG netback series.

Yours sincerely,

Samantha Roberts
Head of Legal -
Wholesale Markets & Group Operations

AGL submission to ACCC consultation on LNG netback series

General Comments

AGL is undertaking a feasibility study into the potential importation of LNG into Australia, but is not currently in the LNG market and is unable to provide a detailed submission on all questions asked by the ACCC. We understand that the ACCC intention in publishing a LNG netback price series is to create greater transparency and to provide better information and bargaining power to users in negotiations with gas suppliers. AGL considers that the ACCC proposed methodology for calculating a LNG netback price is not soundly based and that it will create unrealistic expectations for gas users, ultimately creating dissatisfaction and distortions in the operation of the market.

Ultimately, the price which users will be able to purchase gas on a particular day for a particular period, will be determined by a range of factors, including the gas the retailer has available in its portfolio, pipeline transportation considerations, the volume the user is seeking to purchase, the length of the contract, take or pay percentage, load shape, the credit risk of the user, commercial negotiations, as well as market dynamics.

The key deficiency in the ACCC's methodology is to base the forecast on the international spot price rather than LNG contract price. Spot LNG prices are volatile and can vary substantially in a short time period. We note that current spot prices are 30% higher than the ACCC's LNG spot price assumption in the interim December report.

There is no obligation on producers to supply to the spot market and so the relationship it may have with domestically sold gas is arbitrary. Publishing prices that have a high risk of being commercially inappropriate would be detrimental to customers, including because the customers may rely on the unreliable information to defer or accelerate decision making in relation to the domestic procurement of gas.

We also note that the information used by the ACCC in its interim report to determine a benchmark LNG price is in the public arena and is therefore available to sophisticated business consumers.

Specific Questions

1) LNG prices

(a) *whether the ACCC should also publish an LNG netback price based on prices under long-term LNG contracts*

This will depend on what the ACCC is trying to achieve by publishing a theoretical price and whether the ACCC is intending to publish the price with or in the absence of a coherent framework describing what the pricing represents and how it should be used.

Prices must be considered together with the contractual terms they relate to. For example, a one year contract is likely to have a very different price to a 20 year contract, even if all other terms are the same. AGL notes that it is not uncommon for long term wholesale natural gas contracts between producers and retailers to contain a market price review provision, where confidential gas contracts are obtained by subpoena so that a 'market price' can be determined. This is a complex process usually involving sophisticated analysis of the price impacts of differing terms and conditions of each contract and there are many differing methods of making such adjustments. It is unclear how the ACCC proposes to make these assessments.

(b) *whether an LNG spot netback price based on prices in Asian LNG spot markets is appropriate*

As there is no liquid traded "Asian LNG" market, we assume that the ACCC may be envisaging using a price indicator such as the JKM (Japan Korea Marker), which publishes a benchmark price assessment for spot physical cargoes delivered ex-ship into Japan and South Korea based on recent trades. If so, AGL would be concerned about the commercial relevance of these price indicators, including because Australia is currently unable to purchase LNG from Asia. In our view the JKM is not a reliable source of information regarding the Australian domestic LNG price or reflective of Australian market conditions.

LNG Producers have long term contracts to fulfil and have invested billions of dollars of risked capital to construct facilities for the export of LNG under long term contracts (necessary to ensure the viability of the infrastructure investment). These facilities do not provide a gateway for the physical import of LNG into Australia.

Asian LNG spot markets do not represent markets in Australia. When buying gas in a State such as Victoria, the seller and the buyer would not consider the market conditions in Asia or even Queensland, as they are not sufficiently relevant in Victoria to have a material impact on the price of traded gas.

Accordingly, AGL does not agree that a benchmark LNG spot netback price based on prices in the Asian LNG spot market is appropriate.

(c) what would be the most appropriate source of information on Asian LNG spot prices – taking into consideration the representativeness and reliability of the price measure and the methodology used by the reporting entity

There is no transparent, liquid Asian LNG spot market that quotes prices. AGL does not consider there to be any suitable source of information on Asian LNG spot prices appropriate to determine an Australian domestic benchmark price.

2) Shipping and liquefaction costs

AGL has no comment.

3) Forward-looking LNG netback price

(a) what would be the most appropriate source of information on market expectations of Asian LNG spot prices for a forward period of up to 2 years

AGL does not believe there is a sound basis on which the ACCC could determine forward-looking LNG netback prices for up to 2 years for the reasons stated in our answer to question 1(b). Further, like many commodity spot markets, the Asian LNP spot "markets" are volatile and unpredictable. Publishing forecast prices that have a high risk of being wrong may mislead and be detrimental to customers, including because they may rely on the unreliable information to defer or accelerate decision making in relation to the domestic procurement of gas.

(b) whether it would be appropriate to assume that shipping and liquefaction costs do not change in real terms over the forecast period.

AGL considers that, as shipping and liquefaction costs are determined by negotiated contracts, it would be inappropriate to assume such costs do not change in real terms.

4) Publication of LNG netback price series

The ACCC is seeking your views on the following issues:

(a) whether an LNG netback price at Wallumbilla, published regularly on the ACCC's website, would be useful and desirable

A price determined in one location is not relevant to the entirety of the domestic market as the price offered to a customer will vary based on location. AGL does not consider that regularly publishing an LNG netback price would be either useful or desirable.

(b) whether the publication of an LNG netback price would be enhanced by the publication of indicative tariffs for key east coast pipelines

Publication of indicative tariffs for key east coast pipelines would only be useful if adjusted for factors such as utilisation. When purchasing gas transportation contracts, it may be cheaper if transportation capacity is bought in bulk over long time periods. There also needs to be sufficient capacity to transport gas through key east coast pipelines to ensure that the maximum consumption is covered, however the contracted capacity might not be needed every day of the contract term. Contracting is an inexact science. Without this context, indicative tariffs may be misleading to customers as the capacity may not be available for their particular load at the prices quoted.

Accordingly, an "indicative tariff" for key east coast pipelines is unlikely to be indicative and in AGL's view, would not enhance any information provided on LNG netback price.

(c) whether the usefulness of an LNG netback price would change if it were to be published on either a weekly, monthly, or quarterly basis

AGL has no comment.