

2015 Strategic Priorities for Energy Market Development

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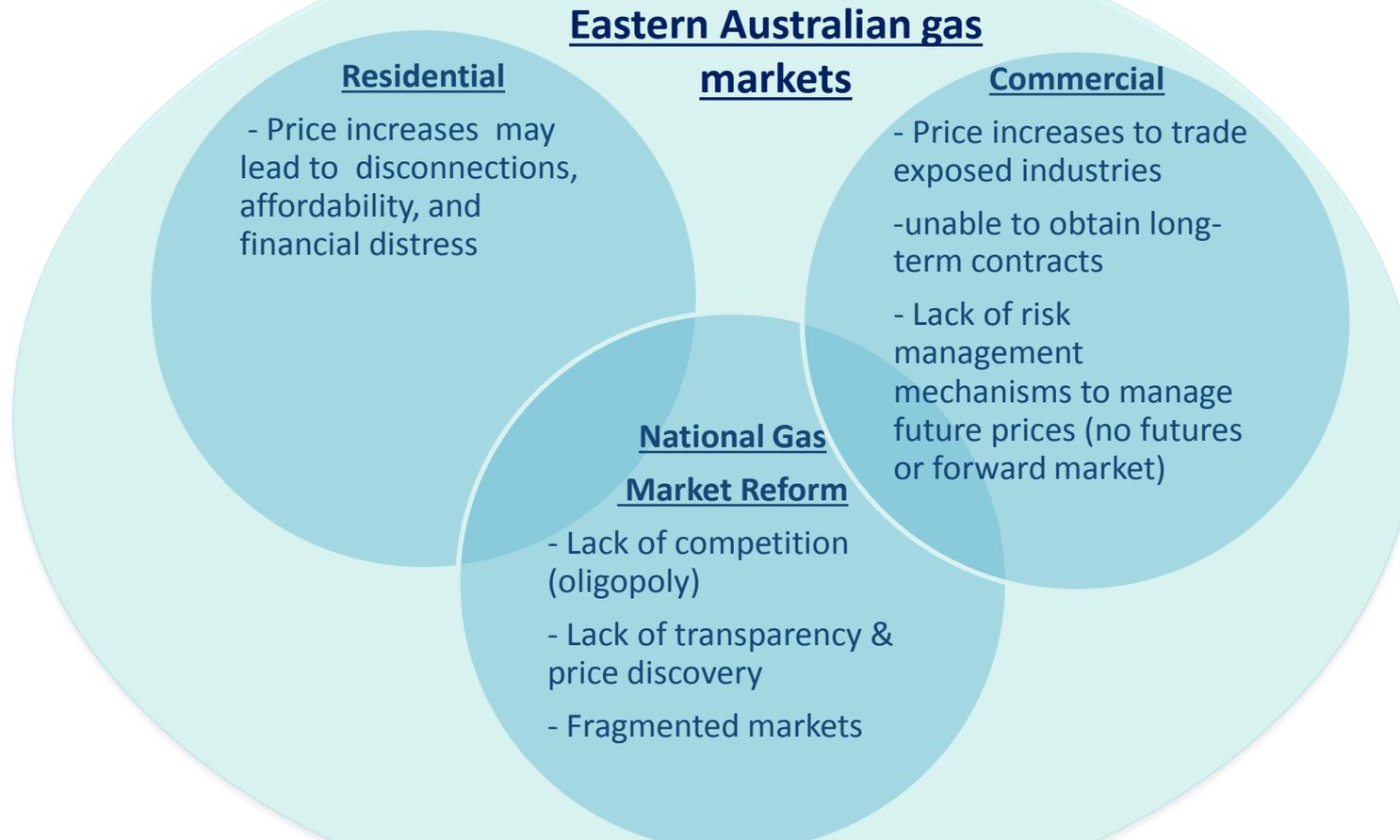
Victorian Department of Economic
Development, Jobs, Transport and
Resources

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Gas market problems



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Eastern gas markets are fragmented & lack transparency, liquidity & competition, & compare poorly with overseas markets

The transformation of the east coast gas market will lead to risks and opportunities

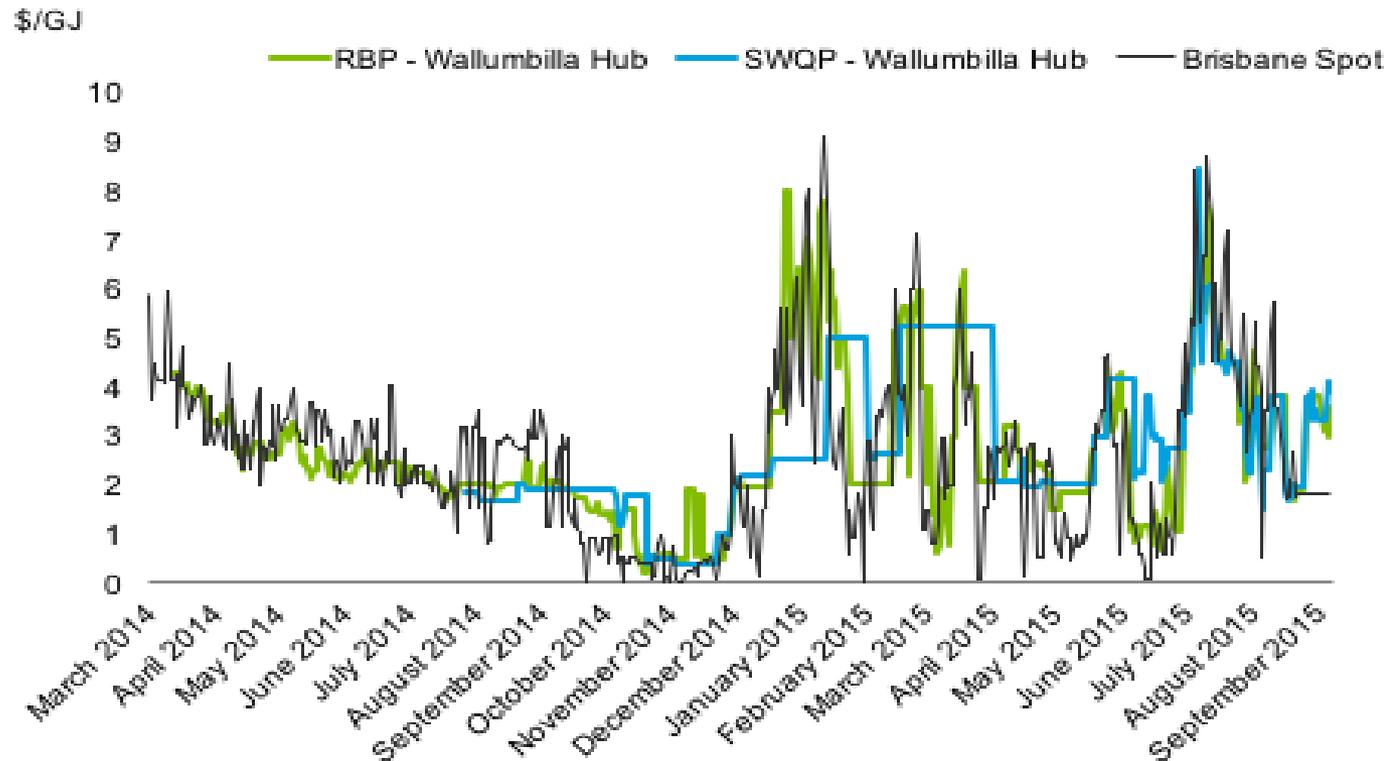
'Ramp gas' –

- The need for the CSG wells to be running flat out as soon as gas is required by the LNG plant creates a supply of so-called "ramp gas" in the months leading up to start-up.

'Wedge gas' –

- To cover potential shortfalls in CSG as CSG fields increase production.

Wallumbilla trading – day ahead price



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Commitment to COAG Energy Council's gas market 'vision'

Enhancing transparency & price discovery; improving risk management; removing unnecessary regulatory barriers

.... "establishment of a liquid wholesale gas market that provides market signals for investment and supply, where responses to those signals are facilitated by a supportive investment and regulatory environment, where trade is focused at a point that best serves the needs of participants, where an efficient reference price is established, and producers, consumers and trading markets are connected to infrastructure that enables participants the opportunity to readily trade between locations and arbitrage trading opportunities"

Commitment to COAG Energy Council's gas market 'vision' (continued)

12 specific outcomes that the Council will pursue, including amongst other things:

- Provision of accurate and transparent information on pipeline and storage facility operations and capacity
- Harmonised interfaces across Australian gas markets to facilitate inter-regional trading of gas
- **Harmonised pipeline capacity trading arrangements which are flexible, comparable, transparent on price and non-discriminatory**
- Development of liquid and competitive wholesale and forward markets for gas to provide tools for participants to price and hedge risks.

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Importance of pipeline access – short, medium and long term

The competitiveness of gas markets are largely defined by its conduits – the high pressure pipeline systems for gas transportation

Contracts are bespoke, which impedes buyers from trading capacity – no uniform terms and conditions that can facilitate trading across regions

Lack of liquid capacity trading hubs, lack of anti-hoarding rules

Without efficient and non-discriminatory access to transport, liquid and competitive upstream and downstream markets will struggle to develop

This is not only about short term access – it is also about long term access and signals for investment in pipeline infrastructure

Australia's pipeline capacity trading arrangements are opaque and there is no uniform system for pipeline access

Anti-hoarding of pipeline capacity

Capacity allocation mechanisms are required to prevent anti-hoarding

Mandate for pipeline owners to auction spare capacity at a zero reserve price –

- This will assist with non-discriminatory access.

Allocating daily 'use it or lose it' will not cause free-rider problems –

- Shippers would be highly unlikely to back their trading portfolio on 'UIOLI'.
- UIOLI can also be defined so as not to affect firm rights

Offering short term 'as available' capacity at a premium to firm capacity is uncompetitive –

- This does not represent marginal cost.

In the UK, short term interruptible or daily capacity is released at a zero reserve price via auction

Creating valuable and tradable pipeline capacity products - Makhholm observations

Define physical gas transport rights –

- Define the physical pipeline capacity, and the nature of the capacity rights and shippers' rights and obligations – standardise this across pipelines

Predictable cost basis for capacity rights –

- Set distanced-based pipeline tariffs to recover publicly disclosed historical nominal costs.

Frictionless exchange –

- Mandate shippers trade capacity on a transparent web-based platform.

The flexibility to trade and transport gas to those parties that value it most is vital for managing risks and promoting efficiency

Standardised terms and conditions

Standardisation of rights can assist with facilitating competition and enhancing allocative efficiency –

- It achieves this by allowing comparisons between rights at different prices and at different locations
- It also means that that rights can be more easily transferred and traded between parties, which reduces transaction costs
- Standardisation may also assist with facilitating transparency and promoting liquidity.

Robust governance

Standardisation of contracts will need to be supported by uniform governance arrangements

This cannot be achieved by industry led initiatives

For example, a **single east coast pipeline access code** that standardises the terms and conditions to promote ease of trading –

- Shippers, pipelines and participants could propose changes to the 'code', which would be independently assessed by the AEMC.

Enhancing transparency

The effectiveness of the market also requires detailed and transparent information to be readily available. This includes:

- Accurate market making information on pipeline and large storage facilities operations and capacity, upstream resources, and the actions of producers, export facilities, large consumers and traders.

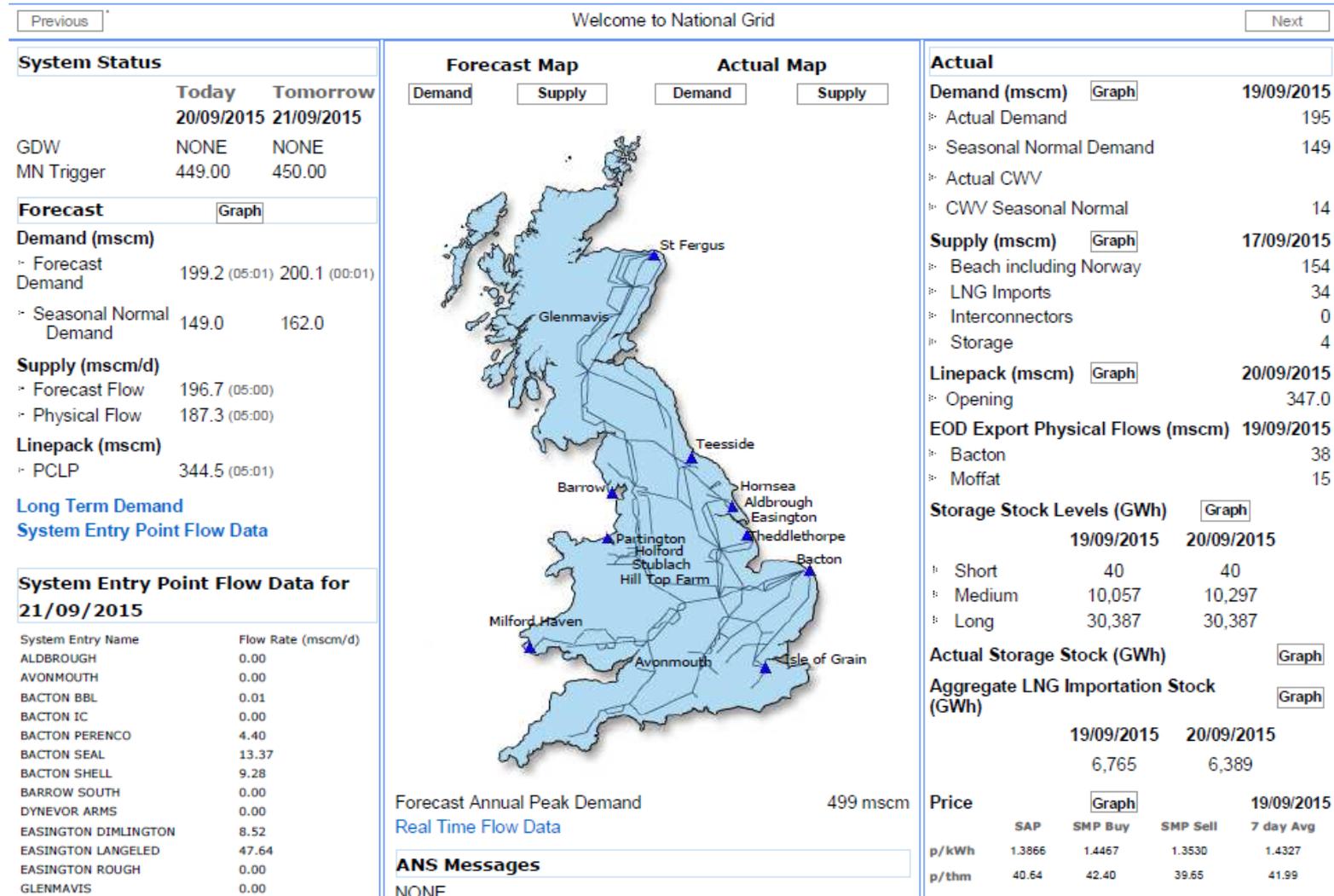
Arguments made by market incumbents against the release of information on the grounds of commercial sensitivity should be robustly assessed and evaluated against potential benefits

World's best practice in this regard should be explored and pursued:

- Further consideration of analogous markets (UK, Continental Europe and USA gas markets) or analogous industries (electricity) is required.

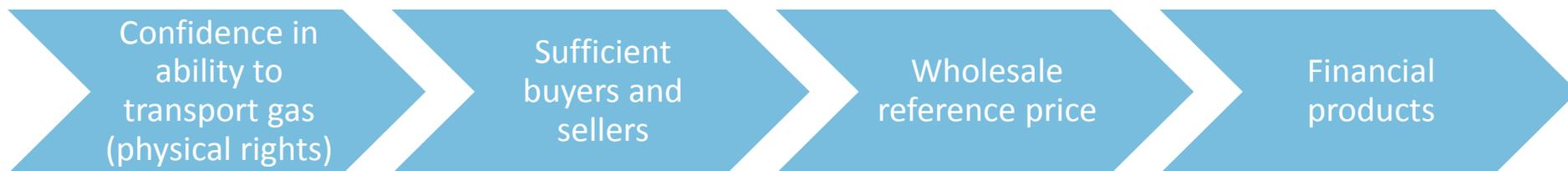
Information provision – international best practise

UK – real time information made available on injections, withdrawals and flows, with integrated projections



Development of liquid and competitive wholesale and forward markets?

This will take time. First we need the fundamentals in place –



ASX Wallumbilla Natural Gas Calendar Quarter Futures

[REFRESH](#)

<u>Expiry</u>	<u>Bid</u>	<u>Ask</u>	<u>Open</u>	<u>High</u>	<u>Low</u>	<u>Last Trade</u>	<u>Last Trade Date</u>	<u>Last Trade Time</u>	<u>Change</u>	<u>Traded Volume</u>	<u>Previous Settlement</u>
Sep 15											4.50
Dec 15											6.00
Mar 16											7.00
Jun 16											5.50
Sep 16											5.00
Dec 16											6.50
Mar 17											7.00
Jun 17											5.50
Sep 17											5.00
Dec 17											6.50
Mar 18											7.00

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Conclusion

Meaningful and ambitious reform may be challenging, but the benefits for gas users will be substantial

The AEMC reviews should be comprehensive and strategic in its approach – we expect clear recommendations that are underpinned by solid analysis and evidence

International experience should be given due consideration:

- Both the USA and Europe have pursued significant reform over the past decades, and the outcomes and applicability to Australia of different models trialled overseas should provide useful material for the AEMC to understand where improvement can be made.





Questions?