



FOR A BETTER WORLD

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Mr John Pierce
Chair, Australian Energy Market Commission
Level 6, 201 Elizabeth Street
Sydney NSW 2000

Lodged via: AEMC website

10th June 2015

Dear Mr Pierce,

Re: AEMC Stage 1 East Coast Gas Markets and Pipeline Frameworks Review Draft Report

Visy welcomes the opportunity to make comment on the AEMC's Draft Report on Stage 1 of its East Coast Wholesale Gas Markets and Pipeline Frameworks Review. We acknowledge the lateness of our submission – we have kept the content brief.

Visy looks forward to continuing engagement in the AEMC's review of east coast gas markets and pipeline frameworks and also to seeing further detail and direction on Stage 2 of the review.

Yours sincerely,

(Royce DeSousa)

GM – Energy & Sustainability, Visy Industries Australia

Visy

Visy Industries Australia (Visy) is a manufacturing company with approximately 5,000 employees in Australia. Many of its operations are energy-intensive. Apart from being a significant user of Natural Gas, Visy has been a participant in the Victorian DWGM since the market commenced and is also a recent (and, at this stage, relatively small) participant in the Brisbane and Sydney STTMs.

As an energy-intensive company which is also highly trade-exposed, Visy has serious concerns about the future landscape of gas pricing and possible Natural Gas accessibility issues that may emerge. We recognise the AEMC's review will target efficiencies and structure of existing wholesale and downstream markets but we also recognise that part of the cause of our concerns, upstream supply and competition, remains outside the current scope of the AEMC's review.

STTM Simplification and move to Balancing Market

Market complexity and ancillary functions

Visy agrees with the contention that the STTMs are somewhat complex markets in that there are a large number of risks and processes involved in the markets that are ancillary to and separate from energy price only – this means more complexity for participants to manage and potentially a greater spectrum of financial risks to deal with. Partly these processes are a necessity given that the STTMs currently perform a number of functions beyond being a purely balancing market. However, Visy suggests that a review of ancillary risks and functions be conducted with the aim of simplifying where practical and where negligible risk of compromising system security and integrity exists. The comments in this paragraph apply generally to the DWGM also. If one of the aims of this review is to encourage greater competition and efficiency in markets, reducing complexity as well as processes to be undertaken to register in and participate in a market needs to be a point of focus as difficulty in registration and complexity in interaction may have been an impediment to market entry for some intending participants in the past.

Importance of STTMs and DWGM to price transparency

The above comments aside, Visy does not support the scaling back of STTMs to 'balancing markets' only and does not believe that participation in STTMs (nor DWGM) should be voluntary.

This possible alteration being considered by the AEMC seems to be partly premised on the assumption that the STTMs provide no or little transparency on price and market dynamics. Visy disagrees. While it's acknowledged that pricing in the STTMs, and for that matter in the DWGM, in part may reflect parties' 'long' and 'short' positions and other factors, ultimately they evidence the price point at which sellers and buyers agree on every single day. Some argue that these prices do not reflect where gas is traded bilaterally but, as pointed out by a senior AEMO representative during the AEMC's current review process, the long run average of spot prices in the facilitated markets (DWGM and STTMs) has converged to contract prices over time. While the DWGM is certainly a more mature and more liquid market than the STTMs, the STTMs are increasing in

liquidity as is the amount of gas being traded on the STTMs relative to total gas flowing through the hubs as highlighted by AEMO in its submissions to the AEMC's review.

Facilitated market pricing provides another advantage for information transparency in the context of an increasingly dynamic east coast caused by massive, rapid swings in demand driven by batch-style LNG tanker fills – currently an emerging phenomenon in Gladstone, Queensland. The AEMC in its Stage 1 Draft Report noted anecdotally how Brisbane STTM prices temporarily spiked when the first Gladstone LNG tanker was loaded signaling a temporary shortfall in supply – a critical piece of information for all observers of wholesale gas flows and markets. Further, daily price movements provide important insights to observers as to dynamic changes in physical conditions in the market place which long term bilateral deals, even if transparent, are incapable of doing.

Importance of STTMs and DWGM to consumers - options for gas supply

Another key reason for maintaining the essence of the facilitated markets is the value they have for consumers in providing options for competitive supply.

Much focus has rightly been placed on the difficulty faced by consumers in being able to take supply from very few, large players.

The facilitated markets most certainly provide other avenues to gas supply for large gas consumers.

For example, both DWGM and STTMs allow users to contract directly and bilaterally with producers such that these markets allow users to balance the difference between their contracted supply with the producer, which maybe fixed or somewhat inflexible, and their total gas demand - this allows users an avenue to supply, other than through an individual gas retailer.

Additionally, a user may decide that in addition to, or separate to, purchasing gas bilaterally from a producer, it will be some or all of its gas directly from the facilitated market. There may be significant commercial risks inherent in such a strategy – nonetheless, if users are unsuccessful in acquiring gas at what they see as a reasonable price through conventional supply arrangements, this at least provides an alternative path to gas supply. The advantage here is that users have an avenue to supply, other than through an individual retailer *and* potentially other than an individual producer, significantly enhancing competition in that part of the supply chain.

It is healthy for users to have these alternatives at their disposal, in Visy's view, particularly when faced with a market which is highly illiquid – east coast gas market illiquidity is a fact acknowledged by all interested stakeholders in this review.

Large users would appear to be voting with their feet about the value of these alternative supply avenues - as the AEMO has pointed during the AEMC's review process, a significant number of large consumers have very recently enlisted in STTMs demonstrating a material shift from long run history in the way large users are prepared to serve their gas requirements.

Visy understands that the STTMs and the DWGM have been an avenue to market not only for large users but also for small-tier and new entrant retailers who may otherwise not have ventured into the wholesale gas market.

In Visy's view, having STTMs and the DWGM as a measure of market price does not obviate the need or potential for other platforms for gas trading on a different time scale which may offer information to the market for those trades.

Importance of STTMs to consumers - options for gas transport

The STTMs are situated at 'city gates' and downstream of transmission pipelines which connect major production and wellheads with major demand zones

This allows a user to potentially buy gas at a city gate without having to have contracted transmission capacity to haul gas from the wellhead. As the AEMC's review has pointed out, many stakeholders are concerned about the inability to access gas pipeline capacity which is fully or heavily contracted, yet unutilised. If a user is either unable to (a) contract with a retailer to include transmission pipeline access at a reasonable price, (b) contract directly with the pipeline owner for access, or (c) attain capacity rights through a secondary pipeline capacity market or platform, the STTM may well be its only alternative to effectively procure the transmission of gas it requires.

In short, the STTMs provide a real alternative to large users who maybe otherwise reasonably unable to acquire gas *delivered to the city gate*. Again, while this avenue may present significant commercial risks to consumers, it nonetheless represents another avenue to gas supply for consumers, which is a good thing for competition in the wholesale gas and transportation markets.

Changing character of STTMs and price implications

Given the alternatives for consumers outlined above which AEMO indicates are being taken up by consumers, STTM energy pricing is likely to become more than simply a price which is the outcome of balancing of participant positions and therefore is likely to be a more important indicator of market dynamics than ever before.

Costs of operating STTMs and DWGM

Visy agrees that the costs of the operation of the facilitated markets by AEMO be reviewed and reduced and processes refined and simplified where feasible.

Visy believes though, that while current costs can certainly be reviewed, the market should not be simplified with the aim only of reducing cost. Some cost is justifiable, for a properly functioning market. Put in context, AEMO costs of operating the facilitated markets are second or even third order relative to the growing cost of gas commodity (and transmission).

Survey-based price information

While Visy recognises the value in having transparency around contract price information, particularly in an illiquid market where little bilateral deal price information is available, Visy is not convinced that a survey-based approach would provide real indication of market pricing. As a voluntary regime, participants involved in deals could reveal deal information that may suit their own commercial interests by signaling price at a particular level for particular terms and conditions. Participants may also choose *not* to reveal deal information where they believe publication of the deal maybe counter to their broader commercial interests. These exceptions could result in a very distorted presentation of price outcomes.

The value of STTM and DWGM pricing to understanding the market

As highlighted above, while there are limits to the ways in which STTM and DWGM price information can be interpreted, they do nonetheless provide valuable information about the condition of the market, particularly given the dearth of bilateral contract price information.

Perhaps qualification of STTM price information can help to characterise its relevance. For example, clearer moving information on the % of gas traded on the STTM could be published.

Visy also believes the AEMC should investigate ways in which liquidity in the STTMs and DWGM could further be promoted – if achievable, this will promote further competition and then naturally increase the relevance of prices cleared in these markets to stakeholders understanding of the broader market landscape. While ease of STTM/DWGM market entry is not perceived by Visy to be a major issue currently, this is an example element of the markets that could be targeted to improve liquidity. Tackling risk management issues in the market (eg ancillary risks such as uplift) should also be focused on as a means of promoting liquidity – a market with fewer or more manageable risks will be more conducive to attracting new entrants and to encouraging more active trading in the STTMs/DWGM.

Bulletin Board – One Stop Shop

Visy strongly supports the increased use of the Gas Bulletin Board (GBB) to enhance information provision to stakeholders and agrees the sentiment behind the COAG Energy Council rule change proposal about Bulletin Board information.

Visy believes that, with the base that has been established for the GBB, further information needs to be provided that will provide greater clarity to participants and stakeholders as to the state of and change in the market including. Major shifts in production, demand as well as pipeline flows and the directions of those flows are emerging as the east coast enters a new era. Additionally, formerly largely static and steady flows of gas will become increasingly dynamic and volatile – the importance of understanding the physical aspects of the market is stronger than area. The following areas require focus regarding GBB development.

Gas demand zones

Major new demand points and zones (primarily new LNG facilities) have the potential to dramatically and dynamically change the gas supply and demand balance on the east coast - it is critical that all of these points

are identified including dedicated pipelines feeding these points. Visy understands there is the potential for demand zones/points to apply for exemption from reporting of data via the Bulletin Board but believes that dynamic and large demand points and related pipelines (of the scale of LNG facilities) should not be eligible for exemption.

Pipeline utilisation

Distinct from actual pipeline flow information, contracted pipeline capacity information also needs to be made available in a way that enables the market to identify the gap between utilisation and capacity.

Additionally, *uncontracted* pipeline capacity information needs to be made available.

As the AEMC has suggested, this capacity information could be used as a platform for more comprehensive pipeline capacity trading. While some pipeline owners have made commendable efforts to promote a level of secondary trading, with respect to those pipeline owners, promotion of secondary trading between pipeline customers and other third party shippers is not likely to be primarily in the commercial interests of pipeline owners who may otherwise be able to sell the same pipeline capacity twice – first as ‘firm capacity’ and secondly as ‘as available’ if physically unused as firm.

Formatting

More comprehensive formatting of existing information will aid with transparency of market condition. For example, individual gas production volumes are shown in a particular gas production zone but then these individual gas production volumes are not summated ‘on screen’ which misses the opportunity to indicate the ‘energy balance’ between linked production and demand zones at a high level.

Other changes proposed in the COAG Energy Council rule change proposal. Visy supports many of the other measures proposed in the rule change proposal such as (a) detailing flow data by receipt point as well as delivery point (b) detailed facility data for production, pipeline and storage which could facilitate a more comprehensive and meaningful dynamic pictorial representation of the market

“One stop shop” concept

As stated, Visy strongly supports the increased use of the Gas Bulletin Board to publish meaningful and useful information to the market.

However, Visy does not necessarily see that the Bulletin Board needs to be the repository of all relevant information. As highlighted earlier in this submission, Visy believes the STTMs and DWGM provide valuable information about market condition, and this should continue to be the case.

Alignment of market ‘Gas Day’ start times

Visy certainly cannot understand how various east coast markets have evolved with such varied start times and timelines for nominations and bids – opportunities for alignment in the past have clearly been missed.

Visy strongly supports the alignment of gas day start times between markets. The particular start time is not of importance per se but should be determined based on minimising change and disruption when considering all east coast markets together. Additionally, mechanisms need to be in place to require gas sellers to accommodate new market times which do not strictly align with gas day start times agreed in current and legacy gas supply contracts.

Additionally, a change to gas day start times should be used as an opportunity to align windows and horizons for bidding and nominations in respective markets. This will reduce transaction and system costs for parties participating in or across multiple markets.

DWGM Rule Change process

Visy supports the AEMC's suggestion to remove the current process specifically applicable to DWGM rule changes and apply a rule change process consistent with other jurisdictions.