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Australian Energy Market Commission
Level 6, 201 Elizabeth Street
Sydney NSW 2000

Reference: GPR0003

Dear Sir/Madam

**EAST COAST WHOLESALE GAS MARKET AND PIPELINE FRAMEWORKS REVIEW – Stage 2
Draft Report 4 December 2015**

Executive Summary

We refer to Adelaide Brighton's submission in August 2015 to you in response to the Stage 1 draft report in which we strongly advocated for continuity of the Adelaide Short Term Trading Market (STTM) and provided the important perspective of a large industrial user. We were significantly concerned at the recommendations contained within the Stage 1 report and considered the changes, if adopted would have potentially threatened Adelaide Brighton's domestic production in South Australia.

We are therefore very pleased and encouraged to see the Stage 2 draft report restates the National Gas Objective (NGO) which seeks to achieve a well functioning, workably competitive market promoting the long term interests of consumers of natural gas. Adelaide Brighton is one of those consumers, with a long history and a clear intent and capability to continue as a major domestic manufacturer into the future.

Critically, the Stage 2 report defers any changes to the Adelaide and Sydney STTM's until at least 2020, recognises the interplay between pipeline access, wholesale gas trading markets and information availability, and requires liquid trading at virtual hubs as a prerequisite.

However, once again with concern, Adelaide Brighton Cement Ltd (ABC) notes the recent speech by the AEMC Chairman to the Committee for Economic Development of Australia (CEDA). The speech implies the intent of the reform being proposed by the AEMC may not be in the interests of Australian consumers of gas. The notion of ensuring gas flows to where it is most valued can be translated into promoting the highest possible price for gas producers. Further ABC is most concerned at the suggestion that consumers should be satisfied if it is transparent that the high price of gas they are paying is also being paid by the

next person. As a business trying its hardest to compete against import pricing, the absolute cost of gas is of fundamental concern, not one person's cost compared to another's.

In addition, the speech claims that "issues relating to gas production or levels of competition in the production and pipeline sector largely fall outside our remit". Adelaide Brighton does not accept that the proposed gas market reform can be properly undertaken without specific consideration as to the impacts which any reform measures may have upon competition within the market. Parallel reform addressing the lack of competition in the production and pipeline sectors should also take place to ensure the NGO is achieved.

Economic contribution and gas market participation

ABC's listed parent company is Adelaide Brighton Ltd (ABL), an S&P/ASX100 company with 1400 employees. ABL is a leading Australian integrated construction materials and lime producing group of companies with operations in all Australian states and territories. The Group is comprised of three operating businesses, Cement and Lime, Concrete and Aggregates and Concrete Products.

ABL has been able to report record profits for more than a decade. It has achieved these outstanding results in difficult economic conditions. Significant reinvestment and proactive management of its operating costs has ensured sustained competitiveness of its operations as well as an environmentally and socially sustainable footprint.

With its registered office in Adelaide and representation of all three operating divisions in South Australia, Adelaide Brighton is an important and valuable contributor to the South Australian economy.

Adelaide Brighton directly employs 453 (FTE) people across South Australia, supports a further of 2,976 (FTE) jobs in the South Australian economy (850 of these are located in the north west metropolitan area and 226 in the Barossa region), spends \$315 million per annum in the state and contributes approximately \$404 million to South Australian GDP. (Adelaide Brighton – Contribution to the South Australian Economy (2014 data) prepared by Barry Burgan, Economic Research Consultants.)

ABC is an integral part of the Cement & Lime division which accounts for approximately 60% of Group revenue. ABC's Birkenhead and Angaston facilities in South Australia are important clinker, cement and lime producing assets for the Group and for South Australia.

The Birkenhead plant manufactures approximately 1.3 million tonnes per annum of clinker (the intermediate product in cement manufacture) and 1.6 million tonnes per annum of bulk and bagged cement to the South Australian and Victorian markets. It is a world class and world scale operation, and one of South Australia's biggest manufacturers.

Significantly contributing to Adelaide Brighton's success over the last decade is the Company's commitment and ability to think and act progressively to continually improve its operations. ABC leads the Australian industry in the development of environmentally sustainable cement products and the use of waste derived fuels (WDF) in cement production.

In the 10 years since commencement of its WDF project, the use of alternative fuels has conserved 120,000 tonnes of natural resources and 7.2 million gigajoules of natural gas, diverted 600,000 tonnes of combustible waste from landfill and abated 370,000 tonnes of greenhouse gas (GHG) emissions.

Other than the clear argument for reducing its carbon footprint, there is a very clear commercial imperative for Adelaide Brighton to minimise its energy costs. Production of cement is highly energy intensive and whilst there is some alternative fuel substitution, the

significantly dominant fuel for ABC is natural gas. Energy costs are second only to salary and wage costs for Adelaide Brighton.

Proactive management of energy costs through a sophisticated gas portfolio management strategy as a SA gas market participant is another example of progressive thinking. ABC is the only industrial user that participates to the full extent in the SA Gas market, alongside producers, retailers, pipeline owners and the regulator. Gas market/STTM participation has become ABC core business through necessity.

Adelaide Brighton operates two of the remaining five, fully integrated cement plants in Australia. The high cost of cement manufacturing in Australia has already seen the closure of several kilns in the last decade with the potential for more to follow. Adelaide Brighton's strategies to maximise its operating efficiencies including innovative energy cost management are a significant driver for its survival and long term viability. We believe there are reform opportunities that can support not only Adelaide Brighton's ongoing success and economic contribution, but also that of Australian producers and other market participants.

Reform that overrides Adelaide Brighton's ability to effectively manage its gas costs is not the balanced outcome the AEMC should be seeking to implement.

Advantages of current SA market design for participants within the Adelaide hub

The compulsory STTM market in SA has the following benefits:

- Security of gas supply (due to compulsory participation)
- Liquidity of pricing (again due to compulsory participation)
- Transparent daily "day ahead" market pricing which allows price driven decisions as to next day gas purchases
- Offers a real alternative to contractual gas. We can get all the gas we need to satisfy operational requirements on any day and STTM gas continues to trade at a significant discount to long term contractual gas.
- Allows for day to day fluctuations in the operational requirements of a manufacturing entity
- Promotes competitive short term bilateral gas contracting opportunities for an industrial user. Parties with surplus gas can negotiate mutually agreeable short term contracts at a competitive price as an alternative to selling at greater discount to the STTM
- Allows for a portfolio management approach combining commodity purchase, haulage and pipeline park facilities to minimise the total cost of gas
- Promotes ease of trading between market participants
- STTM price includes transportation, incorporates supply from two pipelines in South Australia and gives end users access to greater competition due to multiple supply points.
- Management of deviation/financial risks can be achieved through internal and external Market Schedule Variations (MSV's), acting as a Market Operator Service (MOS) provider, securing and using pipeline park and imbalance facilities etc
- Enables the cost of gas to be optimised through dynamic and flexible purchase strategy
- Market participation for a newcomer is achievable. The Adelaide STTM is simple in its design (day ahead market, single price, MOS balancing etc) and allows ease of entry for new participants.

Stage 2 Draft Report – ABC observations re key recommendations

1. Wholesale gas trading markets

We are pleased the AEMC has given consideration to Adelaide Brighton's comments as part of its Stage 1 Report review process. From the perspective of a large gas user, a very positive outcome was the decision to retain the current STTM market structure until at least 2020 and not before the effect of any other market changes are evaluated. We believe this is a necessary and prudent approach by the AEMC.

Any changes to the STTM should not occur in advance of the development of significant trading liquidity in both the Northern and Southern hubs and in pipeline capacity trading. Important to us is AEMC's comment on page 5 of its Executive Summary as repeated below.

"The Commission is aware that many participants in the STTM hubs, particularly large end users, highly value the certainty of supply provided. Whilst such a mechanism would be provided in the Southern hub, the Commission notes that there may also be a need to implement a mandatory balancing mechanism in the Northern Hub, if the liquidity of trading is insufficient to give participants certainty of delivery. This would be a pre-requisite to the simplification of the STTM design"

ABC submits that any simplification of the STTM hub design post 2020 must maintain security of supply and that the STTM must continue to provide existing or increased levels of price transparency and liquidity. In making any determination on a re-design, ABC is of the view that the AEMC must consult with and evaluate the impact of any changes on large gas users. This is consistent with the NGO.

2. Information to support the market

ABC's current daily gas procurement strategy looks at its production requirements, contracted requirements and STTM opportunities. The single most important attribute to sourcing the cheapest gas on any given day is the ability to nominate contracted gas volumes after the STTM ex-ante price is determined. The information ABC requires to set and action its daily strategy is its own or AEMO STTM's data.

Whilst ABC does not need to access the Bulletin Board for its data requirements, in terms of the Commission's recommendations related to the Bulletin Board ABC believes the enhancements proposed (which include additional information from transmission pipeline operators, production facility operators, storage facility operators and the publication of a medium term outlook) are likely to be a positive step forward. This is provided it is done cost effectively and the costs are shared across all contributors including production facility operators, pipeline operators and storage facilities, and not just market participants.

ABC and its advisors, CQ Partners, would be happy to participate in or contribute to a targeted workshop aimed at finalising the Bulletin Board recommendations.

3. Pipeline capacity trading

ABC strongly supports the introduction of pipeline capacity trading and sees it as an essential element in creating a liquid and transparent market. We will be making a detailed submission regarding this initiative once the point to point capacity trading discussion paper is published by the AEMC in March 2016.

We generally support the introduction of pipeline capacity trading and the encouragement of investment in pipeline infrastructure to remove physical bottlenecks and allow better movement of gas between production facilities and users would work positively to achieve the NGO.

4. Southern Hub

In contrast to our support for pipeline capacity trading, ABC has significant concerns about the current Southern Hub concept.

ABC will also be making a further submission regarding the Commission's recommendations regarding the proposed transition from the current Victorian Declared Wholesale Gas Market (DWGM) and associated market carriage arrangements to a new Southern Hub design when the discussion papers are published, also in March 2016.

Essential to the success of the Adelaide hub is the compulsory participation model however we note the proposed Southern Hub design is premised on a voluntary exchanged based trading model. We do not believe a voluntary hub can achieve a liquid and transparent market with security of supply for end users.

5. Development of a Moomba Supply Hub

ABC is supportive of the continued development of a Moomba supply hub and is preparing to participate in this hub from 1 June 2016.

The Moomba gas pipeline facility is located at a critical point in a pipeline network that connects the gas markets in South Australia, New South Wales and Queensland, and acts as a transit point for gas flowing between hubs. It is also the location of oil and gas reserves, both in production and under exploration.

It therefore concentrates supply and transit and is a logical location for gas producers, large users and retailers to trade physical gas products. Development of a Moomba supply hub with compulsory participation will provide greater trading opportunities, liquidity and price transparency, and benefits to not only those producing gas at Moomba (now and in the future), the LNG proponents and large retailers purchasing gas at Moomba, but also end users who will participate and benefit from the establishment of this hub.

In contrast to this is the Wallumbilla Hub. Wallumbilla is serviced by only one pipeline and cannot act as a gas transit point other than to its LNG customers in Gladstone or on a much smaller scale, the Brisbane market. Leaving aside our consistent argument that participation in any trading hub be compulsory and noting both hubs are currently or proposed as voluntary, we believe the Moomba Hub is a more natural and logical candidate to be developed into a fully functioning gas supply hub than Wallumbilla.

Summary

The Adelaide STTM has provided material benefits to ABC through the ability to source gas from a liquid, transparent and competitive day ahead spot market.

With the emergence of the LNG export industry in Australia and changing market dynamics, long term competitively priced gas supply arrangements are becoming less and less available.

ABC does not have the ability to manage its gas price risk through demand or volume management. It operates on a fully utilised 365/24/7 day basis. If not for the currently effective STTM market in SA providing a viable, flexible, competitive spot market as an alternative to contracted gas, ABC's domestic clinker production and with it, its substantial contribution to the SA economy would have been put in jeopardy by unsustainable gas costs.

As the STTM continues to mature with its benefits filtering through the market with more large gas users contemplating participation, any changes to its existing structure should only be contemplated post 2020 if security of supply, liquidity and price transparency is further improved.

Adelaide Brighton continues to be a success and should be valued highly, not only by our shareholders, customers and employees, but also by South Australian and Australian governments and communities. Our recently announced 2015 results report another record result, however increasingly this is being threatened by areas of the business which are exposed to gas cost impacts. Clearly it is critically important that in order to retain the energy intensive components of our business such as clinker manufacture, we are able to access internationally competitive gas supply.

As a large, gas market involved, industrial user we look forward to the release of further details and active consultation.

Yours sincerely



Michael Miller
Regional Executive GM SA/NSW