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Department of Industry, Science, Energy and Resources

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Canberra, ACT, 2601

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Dear Sir or Madam,

Gas Fired Recovery Plan – Consultation Paper

AGL Energy (**AGL**) welcomes the opportunity to inform the development of the Department of Industry, Science, Energy and Resources (**DISER**) gas-fired recovery plan. AGL is one of Australia's largest integrated energy companies and the largest ASX listed owner, operator, and developer of gas, hydro, thermal and renewable generation. AGL is also a significant retailer of energy and telecommunications, providing solutions to around 4.2 million across Australia.

AGL is supportive of measures to ensure Australia's gas market can continue to meet customer demand. Gas remains a critical transitionary fuel, and measures to improve supply, competition, market transparency and liquidity are critical to the efficient operation of the gas market.

The government has an important role to play in improving information for industry and identifying where expenditure will extract the greatest benefits. However, AGL has some concerns that government support in certain parts of the supply chain may cause unintended consequences or be an inefficient use of the government's resources. This could risk deterring future private investment away from the market, restricting future growth opportunities.

Our specific views on the two measures proposed for consultation are further discussed below.

National Gas Infrastructure Plan (NGIP)

The first NGIP will identify priority pipelines and critical infrastructure projects that can address the emerging southern supply constraints or deliver other significant market benefits in the near term. These projects will be identified through cost-benefit analysis and market modelling.

AGL suggests that this assessment of priority pipelines and critical infrastructure should consider not only the size, location and timing of supply and demand changes, but also the nature of any supply constraints identified. Constraints that are primarily due to inadequate pipeline capacity should have a different market response than constraints due to a supply shortfall. The assessment should also consider the most efficient overall outcomes. This would involve meeting the required demand through the most economic sources of supply (including the cost of delivery to the demand centres), which may be from multiple sources and locations. It could also involve considering the availability of alternatives to building out pipeline capacity to accommodate peak demand, such as managing constraints through demand response or swap products.

Where priority pipelines or critical infrastructure projects are identified, the assessment may further benefit by considering the potential barriers preventing the market from responding to that investment need. The government could accordingly examine options to minimise or avoid those barriers, to encourage a market response instead of relying on government interventions.

If the government does consider providing support for certain infrastructure, AGL suggests further consultation and considering the impacts of that decision on the market and investment incentives. Any interventions that affect the volumes and flows of gas will influence the economic decisions of others in the market. Depending on the type of assistance provided, the government should also consider the flow-on effects of any conditions that are tied to the government support, for instance, whether the government assistance would affect the access fees paid by users.

These considerations extend to examining any other unintended consequences of the priority infrastructure and projects proposed. For example, new supply projects in certain locations could potentially increase pipeline congestion in certain parts of the network. Addressing this congestion to accommodate the new project could then increase costs for all users. Alternatively, projects that minimise the need to build additional midstream infrastructure would be lower overall system cost.

AGL notes that servicing the southern markets with gas entirely from the north is likely to come at an extremely high cost given the pipeline investment required. Transportation tariffs can also create a barrier to moving gas efficiently around the east coast market. Therefore, it may be more cost effective to increase supply options within the southern states through the development of in-state reserves and LNG import terminals. We envisage the best outcome may involve developing gas supply from a variety of sources.

Wallumbilla Trading Hub

The second aspect of the DISER consultation process is requesting views about current constrains to trading liquidity at the Wallumbilla Gas Supply Hub. This follows the Government's announcement of their intentions to transform Wallumbilla into a "Henry Hub style" market, which is characterised by high market liquidity and provides a trusted price benchmark. AGL is supportive of working towards these characteristics in the Australian east coast gas market, particularly to facilitate greater levels of forward trading, which can underpin a transparent and trusted forward market price for gas.

AGL acknowledges that Wallumbilla is a key connection point between production in QLD and domestic markets. For the most part, it appears to be a sensible location for concentrating trading liquidity and establishing a price benchmark. However, AGL notes that a minor drawback is Wallumbilla's remoteness from the key domestic demand centres.

a. Establishing highly liquid physical and forward trading

AGL considers it will be beneficial to establish a more effective price benchmark based on physical forward trades. The current approach of using an LNG netback price for quotation of pricing at Wallumbilla, is potentially problematic and misleading. An LNG netback price related to the JKM benchmark does not reflect the cost of producing and selling gas in Australia or the pricing mechanism used in the majority of LNG export contracts from Australian or globally. A forward price for Wallumbilla gas would represent Australian gas prices and provide customers with more accurate price expectations.

Whilst forward trading is possible at Wallumbilla, the Gas Supply Hub prudential requirements impose a significant cost on long-dated trades and this has constrained forward gas trading. To address this, AGL is supportive of a current reform to create a financial product with physical delivery at Wallumbilla, which is

similar to the products traded at the Henry Hub. This financial product will be traded and managed through the ASX and expires 5 business days prior to the first gas delivery day of the given month. At this point the financial product becomes a Wallumbilla physical product with gas delivery obligations, as managed by AEMO.

This new product will help address current constraints on hub participation related to high prudential and administrative costs, as well as systematic credit risk and transparency issues. It will facilitate more transparent, longer dated physical trading, and provide an observable forward price curve, decreasing reliance on the LNG netback price as an Australian gas price.

However, we note that whilst developing a transparent forward price at Wallumbilla will be a step forward for the market, and a significant improvement to the use of LNG netback pricing, a Wallumbilla price may not be highly relevant for the south-eastern markets. The costs of transport, capacity constraints and likelihood that at least some supply for south-eastern states may come from other sources, is expected to lead to a differential between a quoted Wallumbilla price and the price at which gas can be physically delivered to Victorian customers.

The extent of gas production in the United States, including large volumes of associated gas from oil production feeding into a vast pipeline network is what enables Henry Hub to be an actively traded and liquid benchmark in the U.S. The remoteness of Wallumbilla and limitations of the Australian market means a Wallumbilla Hub is unlikely to become as interconnected or liquid as the Henry Hub is within the U.S. gas market. AGL suggests that DISER is transparent about these shortcomings with customers when promoting the Australian gas hub, to manage customers' expectations around prices in other parts of Australia.

b. Gas *Transportation through Wallumbilla*

AGL is aware that some market participants consider the need to have transportation contracts through Wallumbilla is a barrier to the future development of a liquid gas trading market.

However, AGL would prefer that no changes be made to the physical, voluntary and anonymous nature of the Wallumbilla market design over the short-medium term, whilst forward trading liquidity is being improved.

Too often, multiple reforms are implemented simultaneously, making the impact of each individual reform unclear. An incremental approach would allow DISER to evaluate the independent impact of the forward trading reforms, to appropriately re-assess if further resources are required for additional reforms.

c. Commodity Supply

No response.

d. Gas transportation from Wallumbilla to demand centres

No response.

e. Increasing participation at Wallumbilla

As mentioned above, we consider the new Wallumbilla financial product will help to lower the costs of entering forward contracts. We expect this to increase liquidity and participation at Wallumbilla.

f. Efficient administration of the Hub

No response.

If you have any queries about this submission, please contact Jenessa Rabone at JRabone@agl.com.au or 0498 022 634.

Yours sincerely,

Elizabeth Molyneux
GM of Policy and Market Regulation