Qenos

6 August 2021

LNG Netback Price Series Review
Australian Competition and Consumer Commission
LNGnetbackreview@accc.gov.au | www.accc.gov.au/gasinquiry

Joshua Runciman
Director, Gas Unit
Australian Competition & Consumer Commission
Level 17 Casselden Place
2 Lonsdale Street, Melbourne 3000

Re: ACCC LNG Netback Series Draft Decision Paper – Qenos Feedback Submission

Dear Joshua,

Thank you for the opportunity to respond to the ACCC's July 2021 LNG Netback Review Draft Decision Paper. Our feedback submission, recommendation and comments below are in addition to our 12 April 2021 submission to the ACCC.

Qenos understands that the ACCC's review of the LNG netback price series, published regularly on the ACCC website, is part of its ongoing inquiry into the east coast gas market. We also understand the original purpose for publishing this series in 2018 was to provide a measure that would improve the transparency of gas prices in the east coast gas market.

Qenos has reviewed the ACCC's Draft Decision Paper, and stands by the changes we have previously recommended in our 12 April 2021 submission, namely:

1. Reference to Henry Hub as the more appropriate gas-on-gas price marker (adjusted for US export and transport costs delivered into the North Asian market)
2. LNG netback pricing based on long-run costs, with liquefaction capital and fixed costs deducted
3. Updated liquefaction and pipeline cost assumptions to reflect actual costs incurred

We note that in making its draft decision, the ACCC has relied on the Wood Mackenzie Preliminary Report dated 24 June 2021, which makes specific reference to, and counter arguments for the first two of these points raised by Qenos. This is despite the ACCC's stated intent to improve the transparency of domestic gas prices that reflects the true alternative value for all gas producers, and address the currently dysfunctional east coast market.

To level the playing field in the market, Qenos believes that the ACCC should provide a broader range of relevant and transparent 3rd party data for reference in all east coast gas supply negotiations by making the following improvements to the ACCC's published LNG netback price series:

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1. Also publish a Henry Hub linked netback price

Qenos supports the ACCC's proposal to create a longer-term 5-year price series. The ACCC has recommended an oil-linked curve. However, we urge you to also create a gas-linked series using Henry Hub LNG delivered into North Asia.

As noted by the ACCC, Henry Hub is an important global gas marker and will be increasingly so in years ahead. This is consistent with our forward planning requirements for major plant capital investment decisions.

As a trade-exposed major user of gas as a feedstock and for energy, Qenos is reliant on long-term gas contracts to underpin its investment decisions and to compete with gas-intensive imported products. LNG exports need to be globally competitive in order to win contracts in the global marketplace. Gas producers should therefore be in the best position to ensure that their cost of production enables them to provide domestic gas consumers like Qenos with their own requirement for globally competitive inputs.

That is why achieving internationally competitive gas price is important to manufacturers like Qenos, and we recommend you also create a 5-year gas-linked Henry Hub based index for comparative purposes.

This should not be a challenge, given the quality of global price data that already exists, the work the ACCC will do with consultants on an oil-linked series, and the ACCC's netback model which can easily accommodate an oil marker such as Brent, or gas-based marker such as Henry Hub LNG into North Asia.

Including an international gas-based series using a globally recognised and deep trading market such as Henry Hub is complementary to the inclusion of an oil-based series and provides the ability to view 'internationally competitive gas prices' through an international gas market lens.

2. Publish both long-run and short-run netbacks

We recommend the ACCC publish its LNG netback series on both a long-run and short-run basis for the 2-year price and 5-year price series.

The LNG export facilities built in the past decade are now running at or above capacity. As an example, in its most recent market report (June 2021), independent consultant EnergyQuest has highlighted that APLNG and QCLNG are running above nameplate capacity.

As the 'Developing A Robust Domestic Gas Marker' report that formed part of Chemistry Australia's April submission, "*LNG netback pricing should be based on the long-run cost that reflects a competitive gas market"* rather than short-run costs which hide the impacts of a vertically integrated and concentrated market.

LNG exporters have a choice in how they manage their facilities, either supplying their export market contracts, selling at spot, or leaving the gas in the ground. Future investment will need to cover more than just marginal cost.

Publishing both a long-run and short-run series will increase transparency, and also enhance public understanding of:

- The opportunities before an LNG producer to either export, supply the local market, or leave the gas in the ground;
- The incentive to invest in new capacity and the range of costs and margins an LNG exporter may achieve;
- An export parity price for capital-intensive processed liquefied gas (i.e. LNG); and
- Where a fair price fits for less capital-intensive non-LNG gas in the domestic market

3. Publish an Australian Domestic Netback Price (ADNP)

We also support the proposal shared by the Energy Users Association of Australia (EUAA) at the ACCC's Roundtable on 20 July 2021 of an Australian Domestic Netback Price (ADNP) series.

With LNG exporters providing approximately 40 per cent of the east coast market it makes sense to understand and compare the opportunity costs and price premium of the domestic producers supplying the other 60 per cent that do not have LNG sunk capital.

Qenos also provides further feedback on the specific issues addressed in the ACCC's Draft Decision Paper as follows:

The length of the forward LNG netback price series

1. Is the ACCC's draft decision to continue publishing a 2-year forward LNG netback price series appropriate? Should the ACCC continue to publish a 2-year forward LNG netback price series	Continuing a 2-year short term forward series and including a minimum 5-year forward horizon is appropriate. However, the series should include the full range of netback pricing recommended in this submission.
2. Is the ACCC's draft decision to publish additional longer-term forward LNG netback prices appropriate? Should the ACCC publish additional longer-term forward LNG netback prices?	
3. Over what length of time should the ACCC publish additional longer-term forward LNG netback prices (such as 3 or 5 years)?	

4. What other issues should be considered when publishing longer-term forward LNG netback prices.	The series needs to also provide a guide on pricing to non-liquefied gas to domestic consumers requiring long-term contracts to underpin plant capital re-investment cycles, usually in the order of 5 to 7 years.

LNG price markers to calculate the LNG netback price series

5. Is the ACCC's draft decision to continue using JKM to publish historical and short-term forward LNG netback prices appropriate?	To meet the needs of gas consumers, the ACCC should also publish historical and short-term forward LNG long run netback prices based on Henry Hub (delivered to North Asia).
6. What is the minimum level of liquidity needed in JKM futures to extend the current forward LNG netback price beyond 2 years?	No specific view.
7. Is the ACCC's draft decision to use prices in medium-term oil-linked LNG contracts to calculate additional longer-term forward LNG netback prices appropriate? Should the ACCC publish additional longer-term forward LNG netback prices based on oil-indexes?	To meet the needs of gas consumers, the ACCC should also publish longer-term forward LNG long run netback prices based on Henry Hub (delivered to North Asia).
8. Is the ACCC's draft decision to use consultant estimates of an appropriate percentage, or slope, of the oil price to calculate longer-term forward LNG netback prices appropriate?	Yes - as long as it requires quality assurance validation. This should include the ACCC using its ability to audit and otherwise scrutinise the long-term contracts LNG exporters have in place that factors the range of oil-linked slopes used to develop a weighted average 'slope'.
9. What other issues should be considered in calculating shorter and longer-term forward LNG netback prices?	The ACCC should also calculate an Australian Domestic Netback Price (ADNP). A price series showing gas producers that do not have LNG facilities, but have the option of selling gas domestically or tolling gas through an LNG facility.

Export costs deducted to calculate the LNG netback price series

10. Is the ACCC's draft decision to use the current approach to calculating forward LNG freight costs, for period up to 24 months, appropriate? Should the ACCC use an alternative approach?	The most appropriate approach is that which delivers the greatest amount of transparency for consumers. This should include ACCC audits of actual costs compared with forward estimates.
11. Is the ACCC's draft decision to use consultant estimates of longer-term forward LNG freight costs appropriate? Alternatively, should the ACCC:	
12. What other issues should be considered in estimating future LNG freight costs?	
13. Is the ACCC's draft decision to use its current approach to deducting liquefaction costs to calculate additional longer-term forward LNG netback prices appropriate?	No. The short-run approach which includes large allowance for sunk capital is inappropriate for consumers who only need and can only purchase non-liquefied gas. The variables involved are many and complex, with greater transparency needed to re-balance the information asymmetry inherent in the market. As recommended, the ACCC should publish both long run and short run netback series to meet the needs of contract gas consumers.
14. What other issues should be considered when estimating and deducting LNG liquefaction costs?	As above and recommended
15. Is the ACCC's draft decision to use its current approach to deducting pipeline transportation costs to calculate additional longer-term forward LNG netback prices appropriate?	No specific comments.
16. What other issues should be considered when deducting pipeline transportation costs?	No specific comments.

Reviewing the LNG netback price series in 2024

17. Is the ACCC's draft decision to undertake another review of the LNG netback price series in 2024 appropriate?	No. Given the importance of: • the Federal Government's Gas-Fired Recovery initiatives;

	• the commitment by the Queensland LNG exporters under a Heads of Agreement to first offer excess gas to domestic consumers; and • the role that LNG netback and domestic reference price will play in a Gas Code of Conduct the ACCC should: **a)** align feedback on the netback with its six monthly Gas Inquiry Reports; and **b)** conduct a formal review in September 2022 before the next HoA is signed.

Further Feedback

Feedback is also sought on the preliminary report provided by Wood Mackenzie published on the inquiry webpage.	The recommendations provided by Wood Mackenzie in their preliminary report do not match the requirements of east coast gas consumers, or provide the required and available level of transparent information required in a properly functioning market where globally competitive inputs are needed to underpin capital investment cycles. Qenos' recommendations will assist with meeting these objectives.

Qenos is available to discuss its response and provide further detail regarding the proposed changes to the LNG netback series. Please direct any enquiries to myself or Campbell Thomas, Feedstock & Energy Manager at [redacted], or on [redacted].

Yours sincerely,

[redacted]

Stephen Bell

Chief Executive Officer

Qenos Pty Ltd

About Qenos

As Australia's only producer and leading supplier of polyethylene and ethylene, Qenos is a strategic manufacturing business of national interest. With manufacturing operations located in Altona, Victoria and Botany, NSW, Qenos is a large employer (650 direct employees and 350 contractors) with annual revenue of $800m, and payroll and other taxes of approximately $60m pa. Polyethylene is a critical raw material used as an essential input by hundreds of Australian polymer processors to manufacture products such as milk bottles, water tanks, pipes and packaging.

Qenos adds value to Australia's natural resources with over 24 PJ/a of ethane gas (a co-product of natural gas processing) supplied by Santos / Beach Energy and Esso / BHP as a feedstock to produce ethylene and polyethylene. Qenos sites also use 7 PJ/a of natural gas and 40 MW of electricity.