Incitec Pivot Limited
INNOVATION ON THE GROUND

ABN 42 004 080 264
Level 8, 28 Freshwater Place
Southbank, Victoria 3006
GPO Box 1322
Melbourne, Victoria 3001
T: 61 3 8695 4400
F: 61 3 8695 4419
www.incitecpivot.com.au

6 August 2021
Australian Competition and Consumer Commission
Attention: Joshua Runciman & Brendan Staun
Via email

Re: Response to ACCC draft decision paper on the review of the LNG netback series

Further to our 12 April 2021 submission, please find enclosed Incitec Pivot Limited's submission to the ACCC's review of the LNG netback series.

The ACCC is to be commended for the quality of work it has done over the past five years in its inquiries into the dysfunction in the east coast gas market.

As we noted in April, the review of the LNG netback provides the ACCC with an opportunity to better internationalise and reset the east coast gas market given the significant market power of the integrated gas producers and LNG exporters.

As the recent spike in short term gas prices and the forecast rise in the LNG netback to +$16 GJ in February next year show, Australia's commercial and industrial users face significant challenges securing short, medium and longer-term gas contracts at prices that can sustain fresh investment and secure jobs.

The ACCC's LNG netback series can be improved in three key ways;

1) Publish Henry Hub linked netback.

We support the ACCC's proposal to create a longer-term 5-year price series. The ACCC recommends an oil-linked curve. However, we urge you to also create a gas-linked series using Henry Hub LNG into Asia.

As noted by the ACCC, Henry Hub is an important global gas marker and will increasingly influential in the years ahead.

The ACCC readily acknowledges the netback series takes an LNG producer's perspective. To only use an oil-based curve would further entrench the netback in favour of oil producers and cement government and public policy biases that "the only thing that really matters is the international oil price."

As trade-exposed major user of gas as a feedstock to produce fertilisers for farmers and explosives for the resources sector we are reliant on long-term gas contracts to underpin our investment decisions and to compete with gas-intensive imported products.

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

This should not be a challenge, given the quality of global price data that already exists, and the ACCC's netback model which can easily accommodate a gas-based marker such as Henry Hub LNG into Asia.

2) Publish long-run netbacks.

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

The LNG export facilities built in the past decade are up and running at or above capacity. Market reports highlight APLNG and QCLNG regularly running above nameplate.

As EY Port Jackson Partners noted in 'Developing A Robust Domestic Gas Marker' as 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.

As Chemistry Australia note in their August 2021 LNG netback submission to the ACCC, the 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 a long-run netback series poses no detriment to, and would not change:
- the gas volumes required for export
- the prices locked in LNG order books, or
- the 'commercial realities' LNG exporters face.

Publishing a long-run series will enhance disclosure and 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
- 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 low capital-intensive (non-LNG gas) in the domestic market.

3) Publish *an Australian Domestic Netback Price (ADNP).*

We support the proposal shared by the Energy Users Association of Australia (EUAA) at the ACCC's Roundtable on July 20 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.

Our comments to your specific questions are attached and we would welcome the opportunity to clarify and discuss any aspect of our response with you.

Your sincerely,

[redacted]

Uri Gordon
Vice President – Strategic Projects

Responses to ACCC request for comments on ACCC netback review draft decision.

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	Yes. Continuing a 2-year short-term forward series is appropriate. However, such a series should be based on Henry Hub LNG into Asia on a long-run netback methodology.
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?	Yes. It should publish a price series over a minimum 5-year forward horizon and utilise Henry Hub as the basis for the series.
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.	In addition to a gas-linked Henry Hub-based LNG series we endorse the proposal by the Energy User's Association of Australia (EUAA) of the creation of an Australian Domestic Netback Price (ADNP) series.

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?	No, it should utilise Henry Hub LNG into Asia.
6.What is the minimum level of liquidity needed in JKM futures to extend the current forward LNG netback price beyond 2 years?	The JKM is a relatively illiquid price series in comparison to Henry Hub. As the April 2021 submission by CME Group to the ACCC notes on Page 5 *"by calculating the monthly average of the daily settlement prices of Henry Hub front-month futures plus the typical charge of 15% paid by U.S exporters for gasification costs and a \$3/MMBtu fee to represent transport costs, we find that the resulting Henry Hub formula is less volatile than the ACCC LNG netback, while reflecting a similar seasonality."* And on page 6 of their submission- "*Compared to other natural gas and LNG futures prices, NYMEX Henry Hub futures remain by far the most actively traded natural gas futures contract in the world.*" And on page 8: "*The forward curve of Henry Hub futures reflects the same seasonality as a curve derived from JKM futures and TTF futures.*"
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?	No, the short-term and longer-term price series should utilise Henry Hub LNG into Asia.
8.Is the ACCC's draft decision to use consultant estimates of an appropriate	Yes. Use an independent consultant and ensure it reflects current trends of falling price slopes.

percentage, or slope, of the oil price to calculate longer-term forward LNG netback prices appropriate?	The ACCC should seek to avoid 'baking in' the higher slopes used in the LNG producer's foundation contracts. It should reflect more recent trends, including examples of ~10% slopes due to increased global competition. For example, see The Australian Financial Review article "Aussie LNG squeezed by Qatar's pricing tactics'. https://www.afr.com/companies/energy/aussie-lng-squeezed-by-qatar-s-gorilla-tactics-20200921-p55xlm
9.What other issues should be considered in calculating shorter and longer-term forward LNG netback prices?	It should be based on long-run netback methodology.

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?	No specific comments.
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 approach is not appropriate. It should publish the netback series on a long-run netback basis given a range of public views on nameplate capacity, plant utilisation rates and sunk capital costs.
14.What other issues should be considered when estimating and deducting LNG liquefaction costs?	As discussed above.
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. As in our April submission, long-run pipeline capex should be deducted from the series.
16.What other issues should be considered when deducting pipeline transportation costs?	

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. The ACCC should align feedback with: a) its six-monthly Gas Inquiry Reports, and b) conduct a formal review in September 2022 before the next Heads of Agreement is signed between the three Queensland LNG exporters and the Federal Government.