

12 April 2021

Attention: Mr Joshua Runicon, Mr Brendan Staun,
Australian Competition & Consumer Commission

LNGnetbackreview@acc.gov.au

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RE: ACCC review of the LNG netback price series – Issues Paper

Dear Sirs,

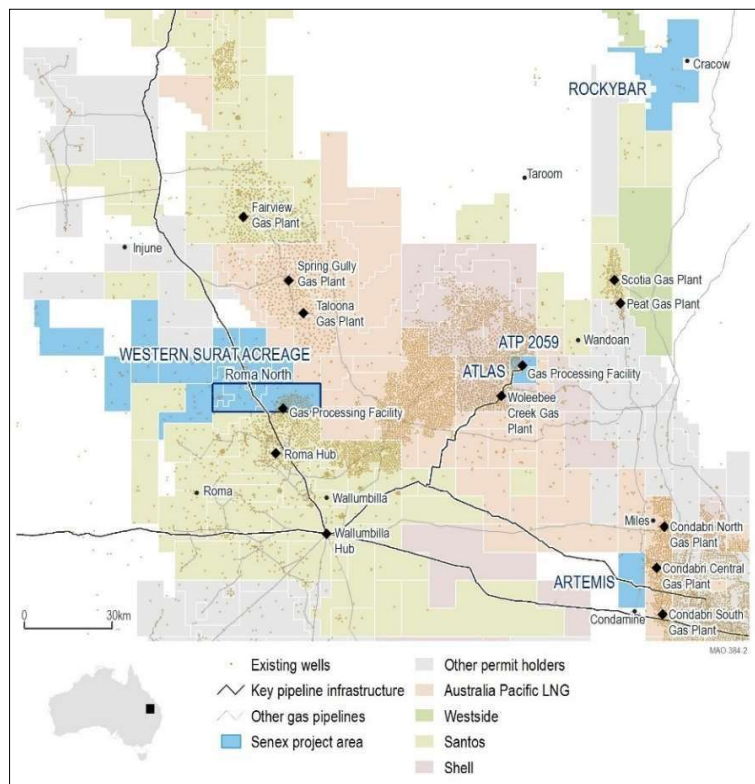
Senex Energy Ltd (Senex) welcomes the opportunity to respond to the Issues Paper for the ACCC review of the LNG netback price series.

Senex supports the Federal Government’s view that natural gas has a major role to play in Australia’s economic recovery. We note that this review of the ACCC LNG netback price series is part of the broader range of measures announced by the Government to achieve the policy objectives of increased, reliable and secure gas supply at competitive prices, and to support jobs. Senex is ready to work with all branches of Government, including the ACCC, to help deliver these objectives for the benefit of all stakeholders.

Our company is an established and growing natural gas explorer, developer, and producer on the east coast of Australia that supports jobs, communities and the economy.

Senex has two foundation gas producing assets in the Surat Basin of southern Queensland: Atlas and Roma North. More than \$500 million has been invested in developing these assets during the past three years. The map *at right* shows the location of these operations as well as Senex’s exploration projects for additional future production: Artemis in the Surat Basin; and Rockybar in the Bowen Basin.

Our production is equivalent to about 10 per cent of Queensland’s domestic demand.



Atlas, about 20km south-west of Wandoan, has a production capacity of 12 petajoules (PJ) a year, and is supplying the east coast domestic market with gas delivered at the Wallumbilla Gas Hub under long-term gas supply agreements. Plans are being progressed to increase Atlas’s production capacity to 18 PJ/year. Natural gas from Atlas is sold to domestic users including commercial and industrial customers: CSR Building Products; Orora; Visy Glass; Alinta Energy; CleanCo Queensland; SouthernOil Refining; and Ampol (Lytton Refinery).

Roma North, about 30km north of Roma, has a production capacity of 6 PJ/year and supplies the Santos-operated GLNG venture. Expansion to 9 PJ/year was approved in 2020, and plans are being progressed to increase the production capacity to 18 PJ/year.

We have significant proved and probable reserves in the Surat Basin of 780 PJ and we have announced plans to invest in expanding production 50 per cent to help achieve our growth target of 60 PJ/year within five years – from 20 PJ/year today. This is the equivalent of the energy used in 1.1 million homes in a year, or more than total household gas consumption in Brisbane.

As a member of the Australian Petroleum Production and Exploration Association (APPEA), we support its response to the Issues Paper.

In addition, Senex, as a material and increasingly important developer and producer of natural gas for the domestic market on the east coast, wishes to take this opportunity to make specific comments on aspects of the Issues Paper and related topics that have the potential to impact us, similar Australia-focused natural gas producers, and the domestic natural gas industry as a whole:

1. **'Gas-fired Recovery' initiatives must support solid investment fundamentals**

This review of the ACCC LNG netback price series is part of the broad range of measures announced by the Federal Government as part of its vision of a *Gas-fired Recovery* for Australia's economy focused on:

- Unlocking supply,
- Efficient transportation, and
- Empowering customers.

Senex supports the Federal Government's view that natural gas has a major role to play in Australia's economic recovery, but such an outcome will only be achieved if the Government's initiatives result in an investment and regulatory environment that provides the industry with the confidence to invest.

Senex's experience is that maintaining reliable and secure gas supply at competitive prices in the market is most effectively accomplished by encouraging new gas supply and market participants, and maintaining a stable regulatory and fiscal regime.

Increasing gas supply relies on sound investment settings, regulatory stability and reasonable and sustainable prices that realise the necessary returns to the developer; returns that recognise the capital investment committed, and the risk taken.

This is especially true for Australia-focused domestic gas suppliers like Senex. Such producers are critical to ensure the domestic market is adequately supplied, and to increase supply diversity. For such producers to survive and continue to invest over the long term, gas prices through the cycle must be sustained at a level that delivers the necessary returns. This is more important for Senex than for the multinational LNG exporters for whom the domestic market represents a small share of their overall business and, therefore, they can absorb lower domestic prices on the back of higher contracted LNG prices.

As noted above, Senex has a very clear plan to expand and, over time, to increase our market share. That will require additional investment of more than \$500 million. With the right regulatory settings, and with customers committing to offtake gas to support development, these plans are achievable. However, **the overhanging threat of Federal Government intervention is creating an environment of uncertainty**; an environment in which the foundation gas agreements which need to be executed to underpin these investments are not being executed or are being deferred.

The investments the Federal Government is seeking to be made to increase supply are being put at risk because of buyer expectations of government intervention to force prices down. The resultant reduced level of confidence in the risk-adjusted project returns introduces risk that financing will be more difficult to secure, which in turn results in increased uncertainty as to whether a commitment in these projects can be made. Before committing to the significant investments these new natural gas developments require, shareholders and lenders expect to see a substantial portion of offtake sold at prices which demonstrate commercial viability.

Senex fundamentally supports an open market, and we support initiatives that will improve the efficiency, transparency and liquidity of an open domestic gas market. Such initiatives enhance reliability and certainty both for producers and customers which, in turn, encourages investment in gas supply and use, including from existing and new gas assets.

Senex recently made a submission to the Gas Fired Recovery Plan Consultation of the Commonwealth Department of Industry, Science, Energy and Resources broadly supporting the Government's intentions of the National Gas Infrastructure Plan and on the Wallumbilla Gas Hub.

2. LNG netback price series is of limited relevance to domestic-focused gas producers

Senex notes that the intent of the ACCC netback price series is to improve transparency of gas prices in the east coast market. However, as defined by ACCC¹, the LNG netback price is “the effective price an **LNG producer** would expect to receive for gas, at a specific reference location, if that gas were converted to LNG and exported”. The netback price effectively represents an indicative price at which LNG exporters should be indifferent to directing a spot cargo into the domestic market or selling such a spot cargo into the international LNG market.

Senex, and other Australia-focused producers like us, are not LNG producers. We do not export and we do not have such a “point of indifference”. Because the east coast market is our only market, Senex needs to secure from that market a price that reflects the supply and demand fundamentals of the market, and appropriately compensates us for the investment we have made (or could make), and the risk we have taken (or could take).

The price considerations for Senex that impact on the negotiation of long-term contracts into the domestic market include: our cost of supply (including development); supply quantity; duration of supply; terms and conditions sought by gas buyers; and our expectations of the local supply and demand dynamics over the period of the contract. **The apparent “point of indifference” for an LNG producer, as estimated by the ACCC LNG netback price series, is sometimes noted in our price discussions with customers and in our internal considerations but is often irrelevant.**

Further, as the ACCC LNG netback price series is referenced from an LNG spot price marker, it does not reflect a “like-for-like” sale with a longer-term domestic contract, a contract which needs to factor in the contract's duration, specific terms and conditions relating to delivery and the expected market dynamics for the contract term. These factors all expose the gas producer to additional risk and/or additional cost and need to be factored into the contract price. The result is that the contract price will deviate away from a spot LNG netback equivalent price marker.

The netted-back equivalent of a foreign market spot price which reflects the short-term volatility of gas supply and demand in that market is of little significance in the pricing considerations of a domestic-focused gas producer looking to enter long-term domestic gas contracts, and nor should it be.

3. Henry Hub has no relevance as an LNG netback price marker

As noted in the Issues Paper², the public debate on east coast domestic gas prices features assertions by a few large manufacturers that the ACCC LNG netback price series should be linked to Henry Hub prices.

Notwithstanding our comments on the irrelevance of LNG netback prices to non-LNG domestic producers in marketing their gas volumes, Senex considers that there are no logical bases for these assertions around Henry Hub gas prices as a suitable reference point.

The more relevant price marker for the ACCC netback price series is, as is currently the case, the Japan Korea Marker (JKM). As noted in APPEA's submission³ to the Issues Paper, the JKM is more relevant because it is a price marker that reflects the market to which Australia's east coast LNG exports are destined and the location to which LNG spot cargoes are sold.

¹ Issues Paper, Glossary, page 4

² Issues Paper, LNG netback price methodology, page 30

³ Chapter 2. ACCC LNG netback price series, page 12

4. LNG import pricing as an additional reference point

It is commonly referenced that the domestic pricing for gas should be at, or below, the ACCC LNG netback price series to be “internationally competitive”.

In light of the increased likelihood of LNG imports, with at least one LNG import terminal likely to be sanctioned and constructed on the east coast, it is suggested that the ACCC should consider the development of a price series reflective of the LNG import price (post-regasification).

Such a series would represent a more genuine international equivalent price for gas on the east coast (post-gasification), being the true equivalent of the price our regional competitors are paying for gas.

It would also be more useful for users as it would not only reflect a real price of equivalence but it would reflect price over a longer term (rather than spot) as reflected in any term of import.

Confidential concerns over prices paid could be overcome by referencing the average weighted cost of gas imports (post regasification).

5. Amendment to LNG netback price methodology

Notwithstanding our comments on the minimal relevance of LNG netback prices to non-LNG domestic producers in marketing their gas volumes, to the extent that an LNG netback price series provides additional information to the market, Senex considers that the ACCC’s current approach in calculating LNG netback prices represents the most appropriate approach.

It is noted that there have been suggestions that the current LNG netback price methodology inherently includes an amount which is a return on capital for the investment made in the LNG plant, and that this has no relevance in respect of the domestic market and should be expressly deducted. Senex considers that there is no logic or economic rationale for such deduction of capital costs⁴ incurred by LNG producers in the construction of the Gladstone LNG plants, as these returns are ignored by Asian-focused price markers (such as JKM) and, therefore, are not included in the netback methodology.

Additionally, any proposal to deduct costs relating to capital returns on LNG plants fails to recognise the enormous scale of upstream development which has taken place i.e. the \$70 billion development of projects, including upstream development in the Surat Basin of southern Queensland, has underwritten the replacement of gas from Australia’s declining conventional basins: the Cooper Basin and Bass Strait. In the absence of the LNG industry and the gas developments that it has underpinned, much of the higher-cost, dry unconventional gas in the Surat Basin would not have been developed. The consequence of this would have been that instead of domestic prices being among the lowest in the Asia-Pacific region, as noted by the International Gas Union, gas users would more likely be paying prices based off LNG import prices. Such an outcome would allow gas users to achieve their desired outcome and source volumes directly linked to Henry Hub, but such prices would be a long way from the \$4-\$6/GJ the gas users believe they deserve.

6. In many instances negotiation asymmetry is in favour of gas users

The ACCC notes⁵ that there is “significant information asymmetry” between natural gas suppliers and users with respect to gas pricing, to the benefit of gas producers. Senex acknowledges that there can be asymmetry in the market as a function of the level of sophistication and size of the negotiating parties. However, Senex does not believe the asymmetry is systematically to the benefit of the gas producers. In fact, in many instances where there is asymmetry, it is in favour of the gas users. Many of the gas buyers are large, multinational, commercially sophisticated parties. Relative to small-to-medium domestic gas producers, they have much more exposure to the market as part of the numerous negotiations they are party to and are, therefore, likely to receive significantly more information on gas pricing.

Senex considers that the hypothesis that there is a systematic imbalance in the market in respect to information is wrong.

⁴ Issues Paper, LNG plant costs, page 33

⁵ Issues Paper, Why we publish an LNG netback price, page 9

Further, we would like to comment on the assertion in the ACCC Gas Inquiry 2017-25 interim report of January 2021⁶ that “price competition amongst suppliers has offered only a limited constraint in previous years”. Senex’s strong belief is that competition among suppliers is a major factor in the determination of the approach to pricing and negotiation. As Senex noted above, the price considerations which impact on the negotiation of long-term contracts include: our cost of supply (including historic and future development costs); supply quantity; duration of supply; terms and conditions sought by gas buyers; and our expectations of the local supply and demand dynamics for the period of the contract. The position we take on each of these factors is driven largely by our understanding and perception of our relative competitiveness in the market. Failure to do so will result in the gas buyer securing volume from a third party.

Summary

Senex supports the review of the ACCC LNG netback price series as part of a set of measures to achieve the Government’s policy objectives of increased, reliable, and secure gas supply at competitive prices, and to support job creation and economy-wide benefits. Senex is committed to working with all branches of the Government, including the ACCC, to help deliver these objectives for the benefit of all stakeholders.

With respect specifically to the review of the ACCC LNG netback price series, Senex notes:

- increasing gas supply relies on sound investment settings, regulatory stability and reasonable and sustainable prices that realise the necessary returns to the developer - returns that recognise the capital investment committed and the risk taken;
- an LNG netback price is of little significance in the pricing considerations of a domestic-focused gas producer looking to enter long-term domestic gas contracts;
- the current LNG netback price methodology is adequate, to the extent it is considered that an ACCC LNG netback price series need be maintained; and
- consideration be given to an alternate pricing point namely, LNG import gas prices (post re-gasification) as this may be even more relevant than a Wallumbilla LNG net back price.

We look forward to the release of the draft position paper scheduled for June 2021 and to further constructive engagement with the ACCC as the review proceeds to deliver a fair, balanced and sustainable outcomes for all parties.

Please contact the undersigned on [REDACTED] or at [REDACTED] if you have any queries.

Yours faithfully, [REDACTED]

[REDACTED]

Neil Sutherland,
Executive General Manager – Corporate Affairs and Sustainability
Senex Energy Limited