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AEMO
GPO Box 7096
Cloisters Square, Perth, WA 6850

Submitted by graham.pearson@energycouncil.com.au to wa.operations@aemo.com.au

2020 Energy Price Limits Review

The Australian Energy Council (the “AEC”) welcomes the opportunity to make a submission to AEMO on the *2020-21 Energy Price Limits Review – Draft Report V2* (the “Draft Report”).

The AEC is the industry body representing 24 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

Gas fuel prices

The Draft Report uses the historical average maximum monthly gas prices from the gasTrading website to forecast the 2020-21 gas commodity price. The AEC does not support using spot prices or prices from the gasTrading website to forecast the 2020-21 gas fuel costs because it materially underestimates the gas commodity price for the following reasons:

1. WEM generators have firm fuel prices

WEM generators are required to have a level of firm fuel contracts to receive Capacity Credits. These contract fuel prices are generally fixed at higher historical prices and also contain a premium over spot prices to cover the additional risk of fixing the price. As a result, spot prices simply do not reflect the actual fuel costs for WEM generators and a regression analysis of previous spot prices understate the fuel costs.

2. Recent spot prices do not take into account changes in the market expected during 2020-21

Regression analysis of previous spot gas prices means that major market changes that are expected to tighten WA’s gas supply in the near term are not incorporated in the estimated 2020-21 prices.

While the Draft Report suggests that the current LNG market is oversupplied, AEMO noted in its *2019 Western Australia Gas Statement of Opportunities* that “WA domestic gas supply is expected to be underpinned by projects currently under development (“prospective supply”), including Browse, Scarborough, and West Erregulla.”¹ It was announced in March 2020 that a decision on Scarborough has now been materially delayed and the late 2021 target for a final investment decision on the Browse project has been dropped with no revised target set. This, plus the forecast decline in gas supply from 2020, is likely to put substantial upward pressure on gas prices over the 2020-21 period.² The analysis in the Draft Report does not incorporate these significant changes.

¹ See p3, [2019 Western Australia Gas Statement of Opportunities](#)

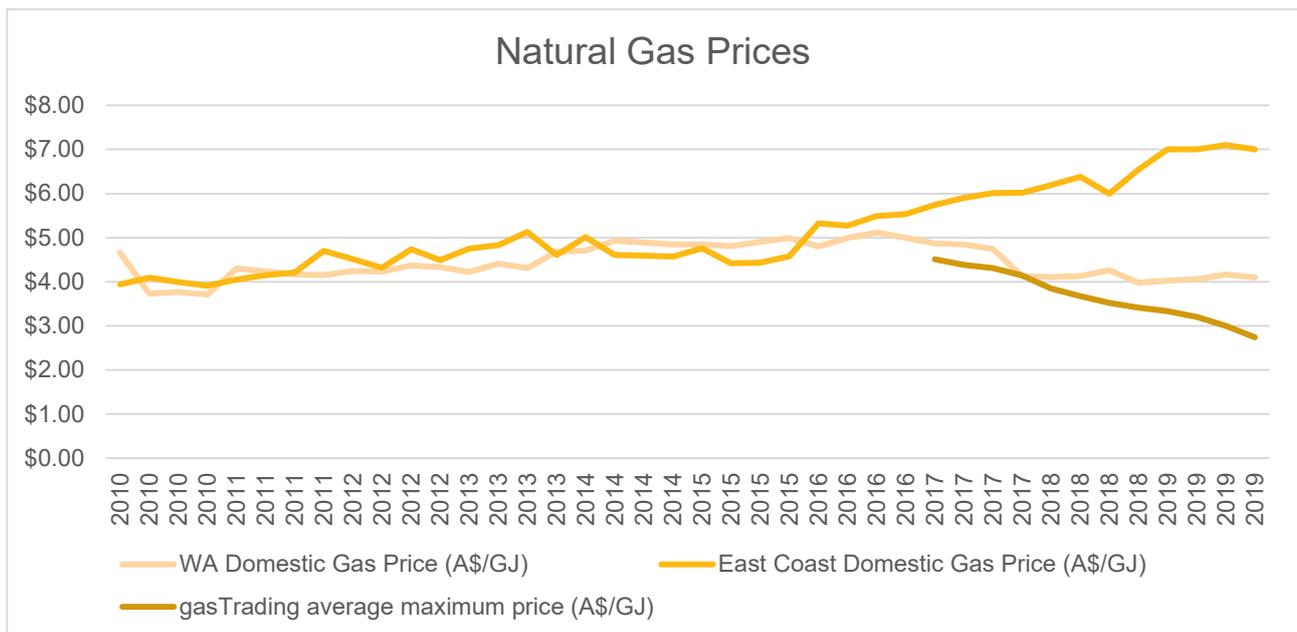
² See p3, [2019 Western Australia Gas Statement of Opportunities](#)

3. gasTrading prices are not accurate spot gas prices

The gasTrading website allows prospective buyers and sellers to make offers to purchase and bids to sell gas on a month-ahead basis at any gas injection point. It is used by a limited number of traders for specific purposes, and the traded volume is relatively low compared to the overall market. Instead, most gas is traded via long-term bilateral contracts or short-term private sales. The gasTrading website reflects only a fraction of the market and does not provide an accurate sample of spot gas prices.

Given the above, the AEC considers that the gasTrading spot price should not be used to forecast the 2020-21 gas price. The AEC recommends that the annual price published by the Department of Mines, Industry Regulation and Safety (DMIRS) is used instead because it is far more reflective of the true fuel costs facing WEM generators.³ These prices are used by AEMO in its *2019 Western Australia Gas Statement of Opportunities* to show the “actual WA domestic gas price”.⁴ The prices published by DMIRS uses data provided by all gas suppliers making it a much broader sample compared to the limited gasTrading website. Plus, being longer term, the prices are more likely to factor changes in market conditions compared to spot prices.

The gas price published by DMIRS is shown in Figure 1 and compared against the gasTrading average maximum spot price between Q1 2017 and Q4 2019. There is a consistent and material difference between the gasTrading spot price and the gas price presented by DMIRS, highlighting that the gasTrading spot price is not reflective of actual conditions faced by WEM generators. Whereas generators mostly have long-term firm fuel contracts, the prices on the gasTrading website are subject to specific short-term, even daily, conditions that impact prices.



Source: DMIRS⁵ and gasTrading⁶

Figure 1: Western Australian Average Domestic Gas Price

³ See the tab titled “Petroleum – Gas Prices” in the [2019 major commodities resources data](#)

⁴ See p60, [2019 Western Australia Gas Statement of Opportunities](#)

⁵ See the tab titled “Petroleum – Gas Prices” in the [2019 major commodities resources data](#)

⁶ See gasTrading [Price History Table](#)

Conclusion

The AEC appreciates this opportunity to provide feedback on the *2020-21 Energy Price Limits Review – Draft Report V2* and encourages AEMO to consider using the DMIRS prices to forecast the 2020-21 gas fuel costs.

Any questions about our submission should be addressed to Graham Pearson, Western Australia Policy Adviser by email to graham.pearson@energycouncil.com.au or by telephone on 0466 631 776.

Yours sincerely,

Graham Pearson
Policy Advisor, Western Australia
Australian Energy Council