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MEDIA ANNOUNCEMENT

*Address by Mick McCormack, Chief Executive Officer & Managing Director, APA Group, at the Committee for Economic Development of Australia in Sydney, 3 August 2017*

## The Role of Gas in Australia's Energy Future

Thank you to CEDA for bringing together this group of people who are obviously very interested in the energy industry, including one of Australia's leading scientists to talk about an issue of critical national importance – our nation's energy future.

### 1. *Intro/setting the political scene*

We are all here today because Australia has a major problem – a problem that has resulted from the absence of an effective national energy policy, indeed any national energy policy. And this is now affecting all Australians – my fellow farmers in the bush, you, me and particularly low-income earners who are struggling to make ends meet because energy prices have risen markedly over the last few years.

This is completely unacceptable in a first world country as rich in natural energy resources as Australia is. Something needs to be done – and I don't mean more talk or more inquiries. Action needs to be taken to reduce prices now, and ensure national energy security at affordable prices for all Australians well into the future.

I'm a farmer and always have been; and I live in country Queensland, so I like to think I am one of the most qualified people in corporate Australia to offer a view on matters that might concern the pub test.

I'll be upfront and declare my self-interest – corporately APA and I are pro gas. Gas supply is key to the solution: And first and foremost, the solution is facilitating more gas supply. It's simple economics - increasing the supply of the commodity is the most effective way to put downward pressure on prices.

For well over a year now, I could count on one hand the number of days that energy hasn't featured on the front page of a major newspaper. We've had the South Australian blackouts, Finkel, the Prime Minister's energy "trilemma", domestic gas supply and price concerns, and the list goes on. There is no doubt that energy is one of, if not the most, highly charged and emotive political issues around.

So far, there has been a lot said about government policy, technological advances, macro-economic factors and industry regulation. There's been a lot of talk about the factors that affect this industry. But what we've lost sight of is how our industry affects every day people on an everyday basis.

With so much noise, I'd like to keep things simple. Whichever way you cut it, gas is critical to energy security and affordability now and well into the future. Gas fired power generation is critical to keeping electricity prices down. Gas currently accounts for around 40% of mid merit and peaking generation capacity in the National Electricity Market.

It is that generation that determines the ultimate price paid by consumers for electricity, so it stands to reason that the lower the gas price, the lower the electricity price.

Sure – renewables will be part of the future energy mix – but the technology simply isn't as advanced as where it needs to be to enable renewables to be our primary source of energy any time soon. In addition, today's battery technology is just not capable of delivering the scale and the reliability and at a price that Australia needs.

And with coal increasingly unattractive to investors and most politicians – gas has well and truly come to the fore as an essential energy source this country needs.

Gas isn't just critical to Australia's energy future – it's the obvious choice. Gas generation can come online quickly to meet peak demand and has historically been dispatched at lower prices than other peak generation such as renewables, keeping electricity costs lower.

Gas produces half the emissions of black coal, a third of brown coal and the best part is – it is in plentiful supply right here in Australia.

No one disputes the importance of gas in the energy mix going forward, but the key is to get the delivered price down.

## **2. About APA**

But first, a bit about APA and how we fit in to the energy mix. We are Australia's largest transporter of natural gas and have invested over \$13 billion in building and developing a network of over 15,000km of interconnected gas pipelines across mainland Australia. Our network has been instrumental in opening up new gas fields and bringing gas to market for our customers.

Over the years we've worked hand in hand with our customers, gas producers and all our stakeholders to provide the infrastructure needed to do this. These massive, long-term projects require significant investment, so our ability to bring gas to where it is needed is dependent on appropriate policy settings across the supply chain.

## **3. Gas Price Crisis, not a Gas Supply Crisis**

When it comes to gas prices, the commissioning of the three LNG export projects at Gladstone from 2014 changed everything. It resulted in a trebling of gas demand on the east coast almost overnight. Production forecasts for gas fields supporting the projects turned out to be optimistic, with shortfalls needing to be drawn from the domestic market.

At the same time, new production was prevented due to certain blanket State Government approvals restrictions and production moratoriums. Demand trebled, and supply growth was stymied – and when that happens, there is only one-way prices are going, and it isn't down.

Concerns about Australia running out of gas and a "gas supply crisis", made it into the headlines. I have long been on the record as saying there is no gas supply crisis. How can there be a supply crisis when Australia has sufficient gas reserves and an ability to produce the amount that it needs? – a view backed up in the Australian Energy Market Operators latest forecast.

Eventually, the headlines caught up to the facts, and the discussion in recent months has shifted from a "gas supply crisis" to a "gas price crisis". There is no doubt that gas prices have risen substantially off the

back of exposure to the global LNG export market. The good old days of cheap gas at the \$3 per GJ mark are long behind us.

This is compounded by the fact that gas production is a more expensive undertaking than it used to be. It's easy to understand the combination of factors that have driven prices up.

The question is what we – the industry and the government, working together - can do to start bringing them back down again. And you'll be relieved to know that there is much we can do to make this happen.

#### **4. *The solution: Increasing gas supply***

In a free enterprise society the best cure for high prices is high prices. So when the market is left alone it will respond to the high price signal with new supply. And therein lies the problem. We can all agree that more supply is needed to put downward pressure on gas prices.

But blanket production moratoria and restrictions on project approvals in some States are preventing this from happening.

I am a great believer that policy must be made on the basis of facts and evidence. The reality is, we need more gas supply and we have leading scientists like Mary saying that further gas production can be safely managed.

So why, then, do we have some State Governments introducing production restrictions and moratoria which mean we can't get the gas out of the ground and into the Eastern Market where it is needed most?

I have no issue at all with environmental and other approvals being run on projects on a case by case basis. However, blanket restrictions that affect all projects regardless of environmental merit are heavy handed, unjustified and ultimately hurt consumers.

We find ourselves talking about bringing gas from the Northern Territory or even Western Australia, when pretty much anywhere you walk along the eastern part of Australia there is gas in one form or another beneath you.

Developing these resources is the cheapest and most effective way to put downward pressure on gas prices. That in turn, will make a meaningful difference to the low income households struggling to afford heating for their homes, or to Australian manufacturers struggling to stay competitive for want of more affordable energy.

APA is doing all we can do get more gas to market. We have a number of gas pipeline projects ready for development. The most progressed is Santos' Narrabri project. Kevin will no doubt speak to it, but as the pipeline development partner on the project, we see it as a critical step towards addressing the east coast's gas price issues.

The project in northern New South Wales is for the potential development of up to 200TJ of gas per day. That is half of the average daily demand for gas in NSW or more than 10% of total east coast domestic demand. Bringing on such significant quantities of gas, right on the doorstep of the East Coast, will no doubt put significant downward pressure on price.

APA recently announced agreements to work with gas producers in the Bowen and Galilee Basins for the development of gas reserves and resources equating to roughly 10 years of East Coast domestic demand.

In addition, Origin's recent announcement of its find in the Beetaloo Basin in the Northern Territory, also represents more than 10 years' worth of East Coast domestic demand.

There is no doubt that connecting these resources to market would have a significant impact on reducing gas prices. For APA's part, we stand shoulder to shoulder, ready to work with our customers to bring the gas to market for the benefit of Australian consumers.

It's what we have always done, and what we will continue to do.

## **5. *The long-term impacts of poor energy policy***

Community and environmental concerns regarding project developments are real and need to be respected. As an industry, it is incumbent on us to work constructively with communities to address their concerns so that all can benefit from the projects.

I do, however, want to draw a distinction between the views of the communities affected by the projects, and the noise created by broader interest groups, many of whom live in our large inner cities or overseas, pursuing general environmental and land activist anti-fossil fuel agendas.

It's a real shame when people believe every piece of unsubstantiated garbage they see on the internet, but disregard the facts based work of leading Australian scientists like Mary.

This is the point I make to my mates in the local pub at home, when they toss at me the latest bit of tripe from scaremongering radio shock jocks about the dangers of producing more gas.

And at the end of the day, these 'environmentalists' are not the ones hurting as a result of high energy prices; it's my mates and others who are pulling very modest wages at the local meat works or digging spuds, that are hurting.

And these environmentalists are not the ones losing their jobs because of Australian manufacturing businesses shutting down due to increasingly high energy costs.

In a world of 24 hour news cycles and politicians in constant re-election mode, it is perhaps not surprising that emotion and populism often sway political debate over facts and evidence.

That simply isn't good enough. Our political leaders are elected to make decisions for the public good, even if the decisions are difficult and unpopular with certain interest groups.

The consequences of poor policy decision making has a real cost for ordinary Australians, and in the case of blanket gas production restrictions and moratoria, it can mean the difference between someone being able to heat their homes or not.

## **6. *Over regulation of pipelines***

Now onto gas pipelines and the misconception that we can regulate our way back to the good old days of \$3 per GJ gas. With increasing gas prices, the pipeline sector has come under intense scrutiny.

Over the last two years, the sector has been the subject of at least five major regulatory reviews including by the ACCC, energy regulators and policy bodies and currently, by the Gas Market Reform Group.

Given energy affordability concerns, it is completely appropriate that each part of the industry be looked at.

I have no issue with that at all and I look forward to hearing the ACCC's findings following its review of the retail electricity market as much as the next Australian.

What I do take issue with, is poor policy development based on conjecture and misinformation, and hastily put together to ensure the appearance of Government action, rather than a genuine commitment to developing policy that is in the long-term interests of consumers.

For the last two years, the industry has been faced with numerous instances of policy being developed on the basis of fiction and folklore rather than fact and evidence – every pet shop parrot has a view on energy policy, and frustratingly for me, these pet shop parrots are assumed to be objective experts, and not what they are – pet shop parrots who are typically anything but objective.

Policy development processes have been truncated, submissions left unread, concerns not considered and Ministers making announcements on decisions prior to the close of consultation periods.

Speed of implementation has become the driver, with traditional industry consultation and other governance processes designed for effective policy making left by the way side.

Regulatory impact statements, impact modelling and cost benefit analysis all seem to have been side stepped when it comes to this round of energy regulatory reforms.

Most remarkably, the pipeline industry found itself in the position this week of having to comply with an entirely new regulatory framework that commenced on Tuesday this week, which it only got to see in final form later that day.

Given the uncertainty, we were forced to write to our customers to cut commercial negotiations short. Something neither we nor our customers wanted but we were forced to do. No winners there.

We've weathered a constant stream of inquiries, reforms and ongoing interventions – they've been part of our business environment for at least the last two years and will continue for at least the medium term. The public resources dedicated to these efforts have been vast and the process is clearly not conducive to effective government policy development.

But despite the procedural issues, there is an even bigger problem with these reforms. They are tinkering around the edges and detracting from the real issue.

The truth is that the energy prices we're seeing now have been a long time in the making. The issues in the gas market were entirely predicted by industry and many policy makers alike. It was obvious at the time of approval of the LNG export projects that the increased demand for gas would put upward pressure on prices – if for no other reason than the high crude oil prices prevailing at the time.

Now of course the issue is actually getting access to more gas. And yet the projects, all three of them and all at the same time, were approved nonetheless, with little or no consideration of how the industry would fare given the monumental disruption that was going to be unleashed upon it. All up, I'm surprised that people are surprised by what has played out.

Further, it is now clear to anyone with a genuine interest in solving the problem that getting more gas supply into the market is the solution to the gas price crisis. That of course requires State Governments to make some hard and unpopular decisions.

The Federal Government is considering restricting exports under the Australian Domestic Gas Security Mechanism.

On the face of it, this would be a pretty drastic move and won't help in confirming Australia's investment credentials as a safe haven when it comes to sovereign risk. I really do hope that industry can solve the issue so that we don't see the Gas Security Mechanism invoked.

The real issue is one of increasing supply, and sits squarely in Governments' balliwick to address. The focus on pipelines has been at best, misguided and at worst, deliberately diversionary.

In the frenzy of being seen to be doing something, the risk of getting the policy settings wrong when it comes to pipelines is high, and the consequences are great.

The result of such misguided government policy is less investment, less innovation and inefficiency.

Without pipelines being built and expanded, less gas will get to market. Ultimately, that translates to higher energy prices for consumers, well beyond the next election cycle.

### **7. *So, Are Pipeline Tariffs Too High?***

Now, to pre-empt some of your questions.

First, with the focus on gas affordability, are pipeline tariffs too high?

Pipeline tariffs make up around 8% of the delivered price of gas to the residential consumer. There has been no increase in real terms in tariffs since 2002 notwithstanding a trebling of gas prices during that time.

Now remember, it is in the commercial interests of pipeliners to have as much gas as possible flowing through our pipes. We do well when our customers do well. Excessive charging would mean our customer's projects wouldn't get off the ground and there would be no gas moving through our pipes.

High delivered gas prices are simply not in the pipeline owners' interests.

### **8. *Why Aren't Pipelines Price Regulated?***

Second, why is it that some pipelines are not fully price regulated, even though they are natural monopolies?

Regulation comes at a cost. Direct compliance costs are one obvious consequence. But the larger cost is more significant, and it is the cost borne by all Australians. The real cost of regulation is reduced incentives for investment and innovation.

I have been in the industry a long time and have seen the pendulum swing from heavy handed regulation applying to all pipelines, to the more targeted regime we have had up until now.

The reason for the swing was that heavy handed regulation resulted in inefficiencies, lost opportunities and increased costs that consumers ultimately had to bear. That was, until Tuesday of this week when the Gas Market Reform Group's new pipeline arbitration rules came into effect.

While its objective was to facilitate commercial negotiations with the backstop of commercial arbitration, in reality, the Rules are heavy handed and rigid, with little appreciation for the workings of the market or commercial negotiations.

As a result, we face a return to the bad old days of inefficiencies, inflexibility and fewer deals being done.

Pipeline customers did not want more pipeline price regulation and I quote from the Reform Group's examination report "[Pipeline Shippers] recognise that regulation is not a panacea": Yet, more regulation is where we are at.

We simply cannot regulate our way to greatness, and the sooner politicians and policy makers realise that, the better for the industry and for all consumers.

## 9. Conclusion

In conclusion, as an industry, we need to make sure we play our part to make gas more available and affordable. That means working together. It means partnering not just in developing new projects, but also in getting the facts and evidence out there and considered in public debate.

It means never forgetting that what we do as an industry impacts every Australian. The knee jerk policy responses, fuelled by political self-interest, need to stop. Governments owe it to electors to base decisions on facts, evidence and appropriate process. The government must be courageous in the face of self-interested protest groups who are making Australia's gas unacceptably expensive by world standards.

The consequences of an absence of effective energy policy to date are being severely felt, particularly by low income earners – like mates of mine in the bush in Queensland, or those staring down the possibility of losing their jobs because of industry shutting down.

And equally, the costs of getting it wrong again, whether it be policies on gas production, pipeline regulation or any other energy markets issue, are too great, with the costs ultimately born by ordinary Australians.

Thank-you.

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## About APA Group (APA)

APA is Australia's leading energy infrastructure business, owning and/or operating around \$20 billion of energy infrastructure assets. Its gas transmission pipelines span every state and territory on mainland Australia, delivering approximately half of the nation's gas usage. APA has direct management and operational control over its assets and the majority of its investments. APA also holds ownership interests in a number of energy infrastructure enterprises including SEA Gas Pipeline, SEA Gas (Mortlake) Partnership, Energy Infrastructure Investments and GDI Allgas Gas Networks.

APT Pipelines Limited is a wholly owned subsidiary of Australian Pipeline Trust and is the borrowing entity of APA Group.

For more information visit APA's website, [apa.com.au](http://apa.com.au)