Chapter 2

The case for maintaining the joint marketing arrangements

A 'project based' market

2.1 In its submission to this inquiry, the North West Joint Shelf Venture argued that 'separate marketing of gas is not feasible…given the relative immaturity of the Western Australian market'. The hallmark of this 'immaturity', it claimed, is the 'project-based' nature of the domestic gas market. This is characterised by large and lumpy demand, inflexible transportation, a lack of storage options and no market clearing mechanism. The Venture argued that without joint marketing arrangements, the market would not attract the substantial capital investment for these large-scale projects and would be unable to clear, 'in a timely and efficient manner', the large trading imbalances.

2.2 Ms Eva Howell, Executive Director of the North West Shelf Venture, elaborated on these matters for the committee:

> …the ability of any gas producer to produce for the domestic market depends on having a commitment from purchasers in aggregate sufficient to underwrite the initial capital investment in the project and its ongoing operating costs. The volume of sales needed to underwrite these capital investments requires purchasers who are willing to commit to large quantities of gas for a long period of time. This is why we and every other credible commentator in the field, including the ACCC, the Ministerial Council on Energy, the Office of Energy and economic analysts, have previously characterised the Western Australian gas market as a project market where producers' projects and buyers' projects come together to create a viable business case for new supply to enter the market.[1]

2.1 The Venture claimed that an important part of creating a 'viable' business in this market is to jointly explore, develop *and* sell their gas products. Ms Howell argued that joint marketing arrangements are needed to give the companies confidence that the products in which they have jointly invested can then be sold. Only with these joint arrangements—from exploration to sale—can there be the certainty necessary to ensure continued investment in circumstances where 'each participant has similar revenue, cost and risk exposure'.[2]

2.3 Ms Howell contrasted the Western Australian gas market with the North American gas market. She noted that while Western Australia's market is based on a

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1 Ms Eva Howell, *Proof Committee Hansard*, 11 November 2008, pp. 2–3.

2 Ms Eva Howell, *Proof Committee Hansard*, 11 November 2008, p. 4.

small number of large buyers and sellers exchanging large quantities over large periods, the North American market has:

> …literally thousands of producers and production facilities that are generally of a much smaller scale, a very dense transportation network, storage facilities for gas, brokers and aggregators who act as intermediaries between the suppliers and the customers, and an advanced financial market for the purchase and sale of gas.[3]

2.4 Ms Howell also explained to the committee that the Western Australian gas market is different to the market for other products supplied by the Venture's companies. The companies' oil, condensate and LPG are sold separately because these markets are 'deep' and 'liquid' with storage facilities, brokers and aggregators and a related financial market. The Western Australian gas market does not have these characteristics.[4]

When would separate marketing arrangements become viable?

2.5 Based on the ACCC's 1998 determination, the Venture argued that there is a greater likelihood that separate marketing arrangements will become viable if there is:

- a significant increase in the number of customers;
- entry of new competitive suppliers;
- additional transport options;
- gas storage facilities;
- entry of brokers;
- creation of gas-related financial markets; and
- development of substantial short-term spot markets.[5]

2.6 However, the Venture claimed that a move to separate marketing arrangements at this time would introduce large costs and risks for the participants. This would harm efficiency and competition in the short term and have adverse effects upon future investment decisions.[6] Moreover, the Venture argued that its participants would not be able to formulate a workable and efficient mechanism to clear the trading imbalances that would arise from separate marketing arrangements. It added that given these separate marketing arrangements are not feasible, the current arrangement 'will not result in any lessening of competition'. Rather:

> …coordinated marketing has facilitated enormous investment by the NWS project participants in gas production and supply facilities that have

3 Ms Eva Howell, *Proof Committee Hansard*, 11 November 2008, p. 3.

4 Ms Eva Howell, *Proof Committee Hansard*, 11 November 2008, p. 3.

5 North West Shelf Venture, *Submission 3*, p. 4.

6 North West Shelf Venture, *Submission 3*, p. 5.

> serviced the Western Australian economy extremely well over a sustained period of time.[7]

Why did the Venture revoke its authorisation?

2.7 The Venture was asked why they chose to ask the ACCC to revoke the authorisation to conduct joint marketing arrangements. Ms Howell initially responded that the authorisation was no longer needed given the Venture believed they were complying entirely with the TPA. She then took this position further:

> It is probably a moot point that we needed the authorisation in the first place. But, obviously, when investment was made in the infrastructure, given the billions of dollars and the requirement to satisfy bankers and so on, a cautionary step was taken to have that authorisation. Now that the project is more mature we felt that that was no longer necessary and that there had never been any suggestion that we were not acting in accordance with the Trade Practices Act.[8]

Conclusion

2.8 The North West Shelf Venture has defended the need for maintaining its joint marketing arrangements on the basis that the domestic gas market in Western Australia is 'immature'. It cites lumpy demand, inflexible transportation, a lack of storage option and no market clearing mechanism. These are the same factors identified by the ACCC in 1998 upon granting the Venture its authorisation. Moreover, the Venture claims that for its domestic gas production to be commercially viable, all six companies need to have similar revenue, cost and risk exposures which could not be ensured if the joint marketing arrangements were terminated.

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7 North West Shelf Venture, *Submission 3*, p. 4.

8 Ms Eva Howell, *Proof Committee Hansard*, 11 November 2008, p. 8.