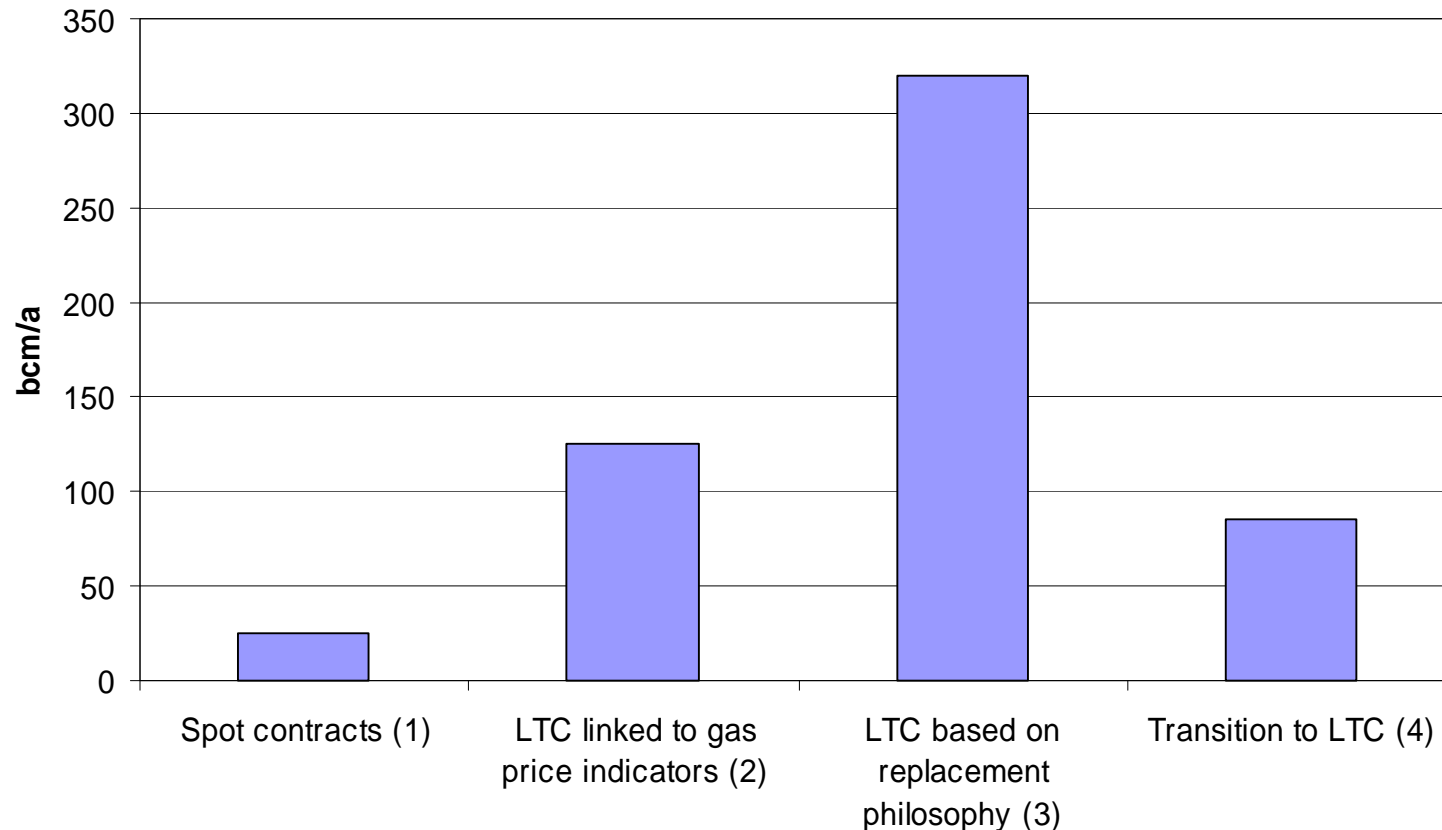


**GAS PRICING: INDEXATION VERSUS  
GAS TO GAS COMPETITION  
(Chairman's opening remarks to the  
Round-Table 2 Discussion)**

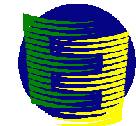
**Dr. Andrey Konoplyanik,  
Deputy Secretary General,  
Energy Charter Secretariat**

**The European Gas Conference 2008,  
23-25 January 2008, Vienna**

# Estimated International Gas Trade (2005): Different Pricing Mechanisms for Main Regions



Source: BP (2006) (1) LNG to USA, UK and other spot LNG; arbitrage on the UK-Belgium Interconnector  
(2) Pipeline Canada-USA, pipelines to UK (BBL, Langeled) and new Dutch exports  
(3) All imports by Continental Europe (incl. accession countries) less spot LNG under (1)  
(4) Trade with FSU now in transition from quasi-barter deals to LTCs, 2004 figures



# A Typical Net Back Gas Price Formula & its Review

$$P_m = \left\{ \begin{array}{l} [P_o] \\ + [0.60] \times [0.80] \times 0.0078 \times (LFO_m - LFO_o) \\ + [0.40] \times [0.90] \times 0.0076 \times (HFO_m - HFO_o) \\ + [...] \text{ (coal)} \\ + [...] \text{ (electricity)} \\ + [...] \text{ (gas-to-gas competition)} \end{array} \right.$$

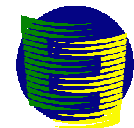
NB: [...] – parameters in brackets usually subject of renegotiation

Long-term evolution of price review mechanism:

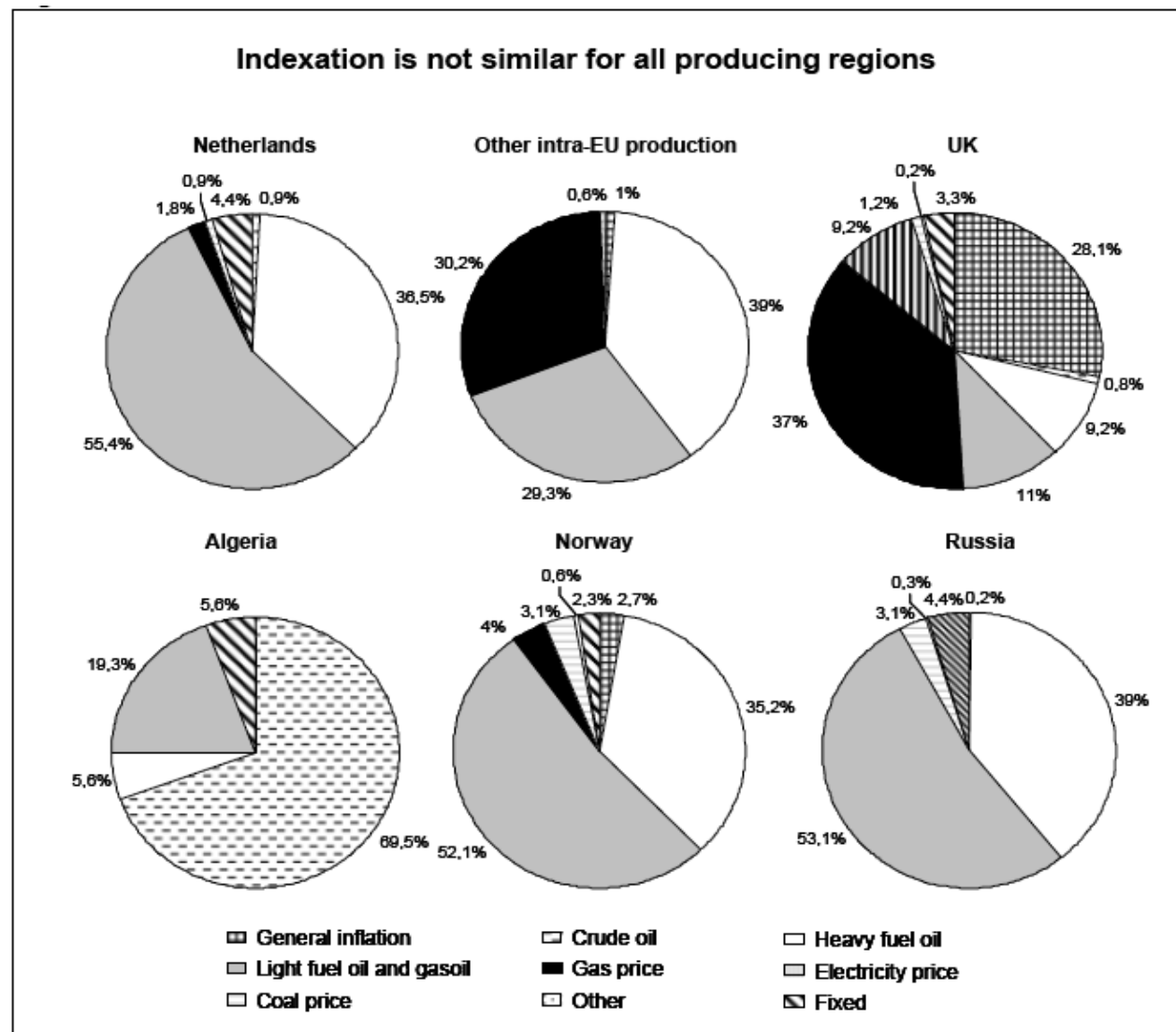
- reflect its adaptation to the new state of development of energy markets,
- changing shares of existing competing fuels (LFO/HFO ratio in favour of LFO) and incorporation of new competing fuels and gas to gas competition,

*but*

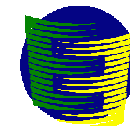
LFO & HFO are still dominant replacement fuels in gas pricing within long-term gas export contracts



# Long-term gas export contracts: Indexation by Producer

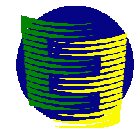


Source: Energy Sector Inquiry 2005/2006



# The most intriguing question

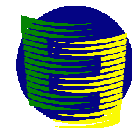
- is => the difficulties and risks of transition from a system with strong players to a system with one/few liquid market places & many players
- Representative of a gas-producing company at Energy Charter IAP meeting: “Producers are interested and know how to supply their gas to a market with deep liquidity, or to a market with low liquidity but with strong players; however, markets with low liquidity and weak players are difficult to supply” (Putting a price on Energy, p. 166)



# UK liquid market: whether it is immune from nudges and kicks?

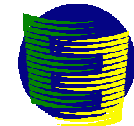
- “What seems to be happening is that the NBP and its lesser siblings in Holland and Belgium are increasingly feeling the stresses and pressures of playing in an international market. The UK market is large and liquid but it is not so big that it is immune from nudges and kicks from large players”

– “Gas Matters”, September 2007, p.38



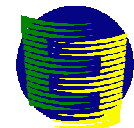
# 2004-2006 FLAME Polls on Gas-to-Oil Price Pegging

Q 2004-05: When will European LTC gas prices “break loose” from oil prices and be ruled by spot/futures quotations?			Q 2006: To what extent will spot pricing in gas markets replace oil price pegging formulas?	
By yearend 2005	1	-	Very considerably	4
By yearend 2008	-	5	Considerably	28
By yearend 2010	24	17	To some extent	44
By yearend 2015	36	23	Slightly	23
After 2015	15	30	Nil	1
Never	24	25		



# When and how gas-to-gas competition will play a role in European gas pricing?

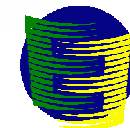
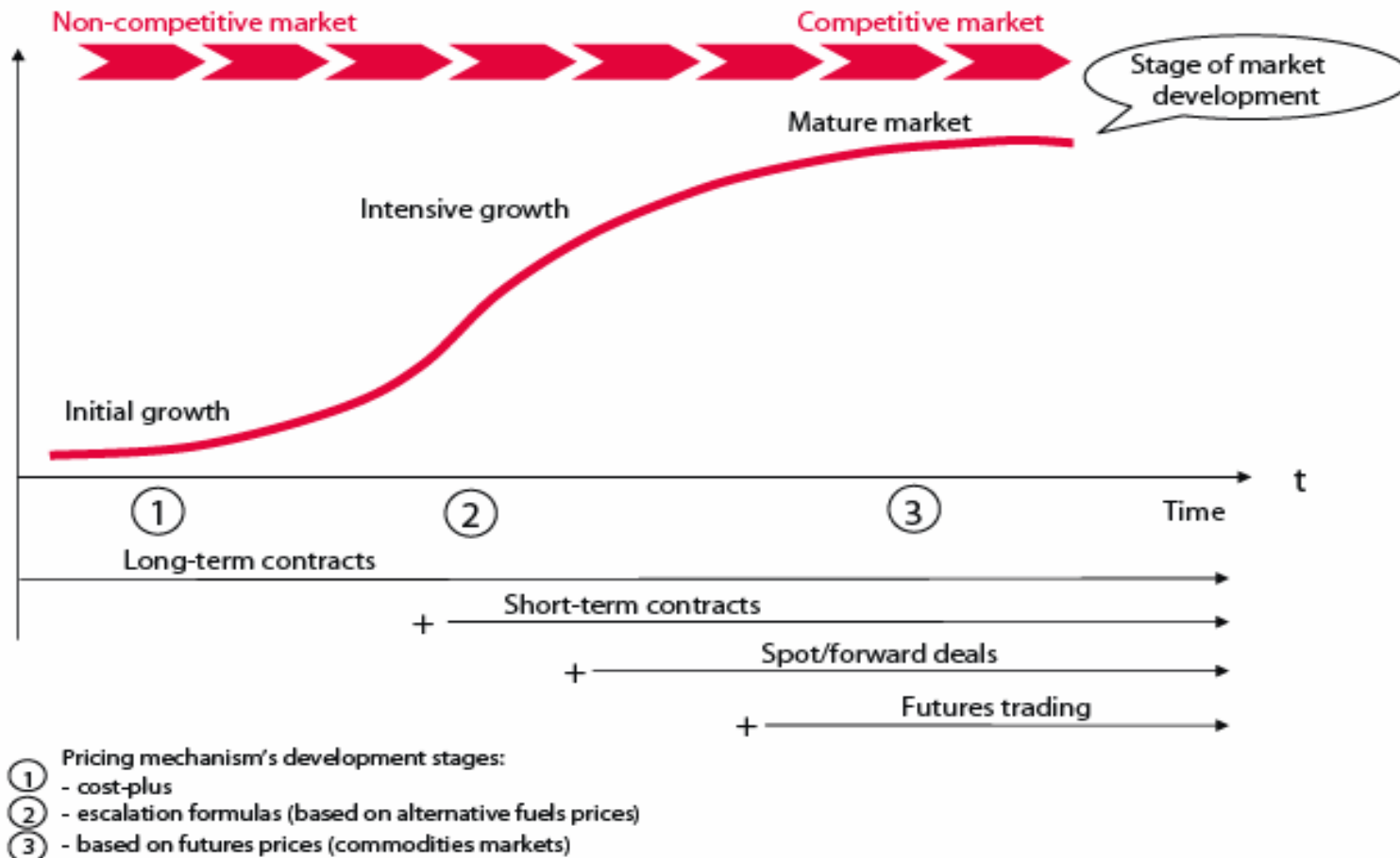
- European gas market is not yet ready to switch to gas-to-gas competition as to key pricing instrument
- There will be no revolutionary switch to gas-to-gas competition in pricing
- Pricing formulas within LTGEC will smoothly adapt to new stages of energy market developments by increasingly reflecting, where practical, gas-to-gas competition as one of ingredients



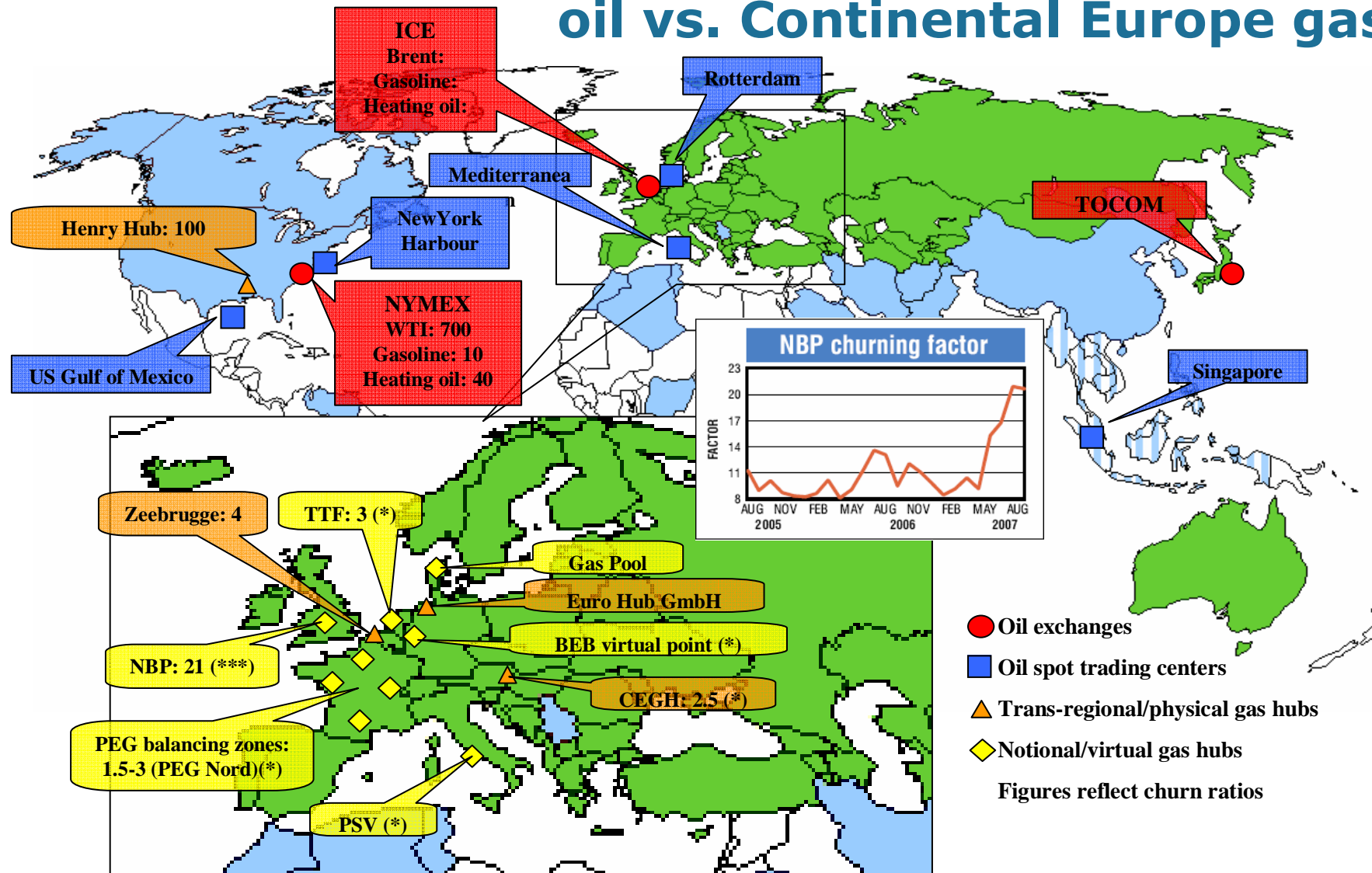


**Back-up slides**

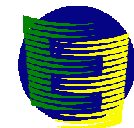
# Gas markets development



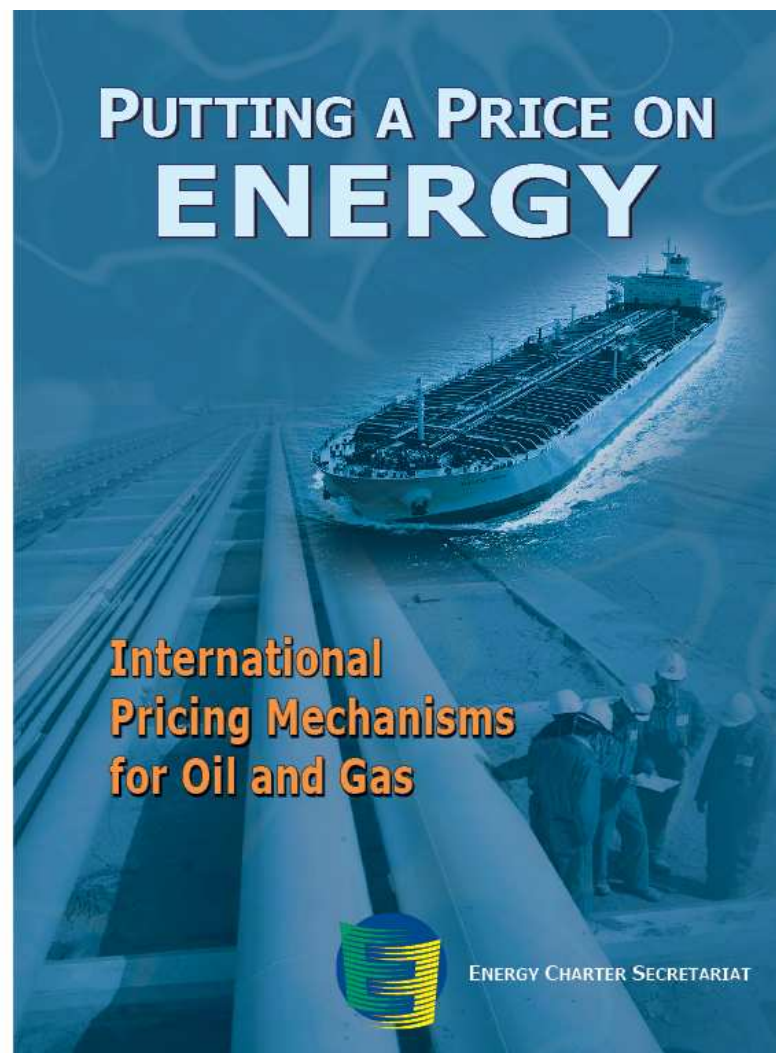
# Comparative liquidity of marketplaces: worldwide oil vs. Continental Europe gas



(\*) BEB hub = Bunde (Germany) at German/Dutch border, CEGH = Central European gas hub (Baumgarten, Austria), NBP = Notional Balancing Point (UK hub), PEGs = French hubs (GdF), PSV = Punto di Scambio Virtuale (Italian hub), TTF = Title Transfer Facility (Dutch hub);  
 (\*\*) 2004 – 2006 average; (\*\*\*) 8-14 during the 2004 – 2006 period



# Report by the Energy Charter



The Report can be downloaded free of charge at: [www.encharter.org](http://www.encharter.org)

A.Konoplyanik A., European Gas Conference 2008, Vienna, 23 January 2008, Round Table 2, Slide 11



[www.encharter.org](http://www.encharter.org)