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Paradigm Change in International Natural Gas Markets and the Impact on Regulation

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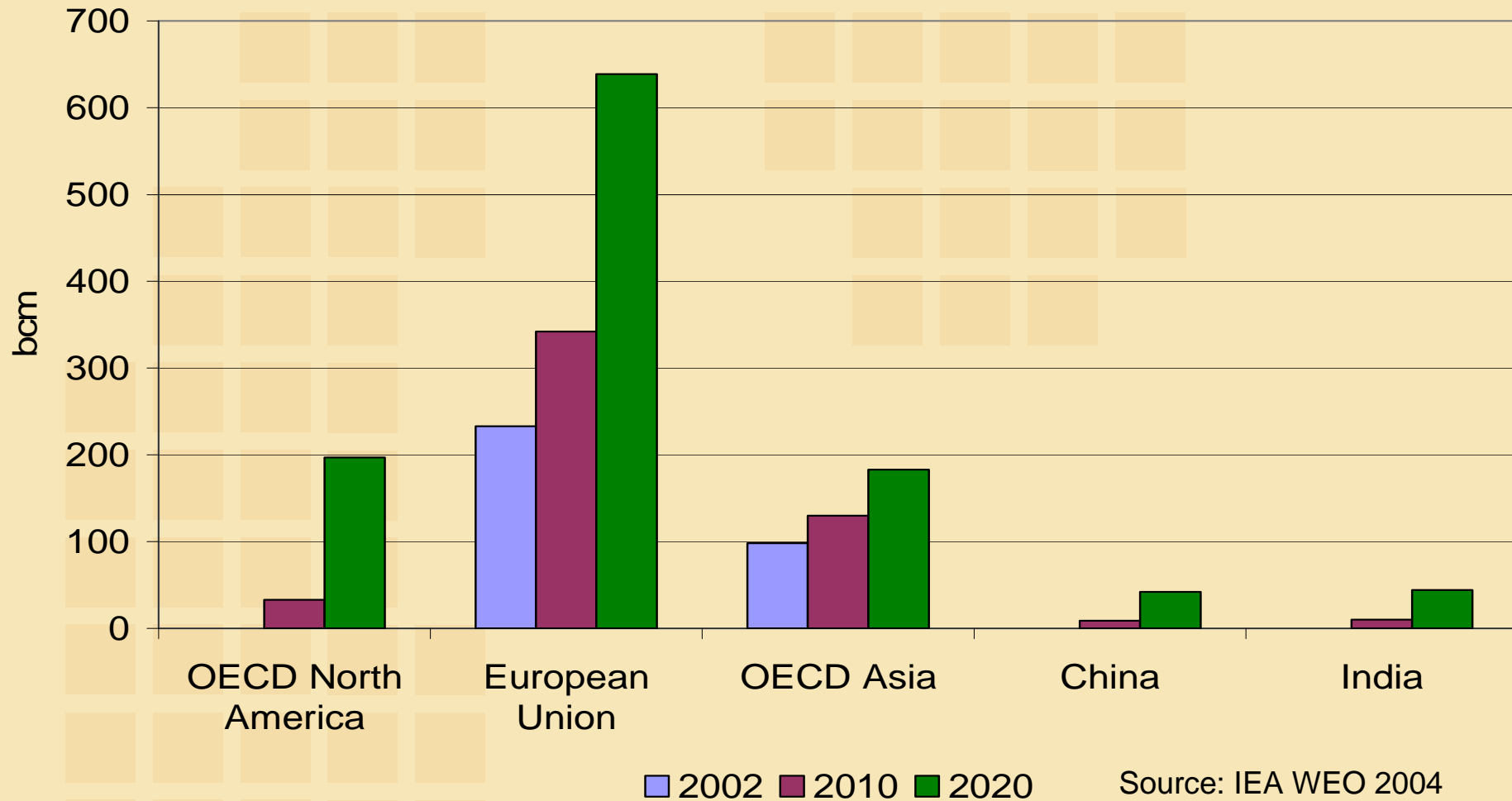
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Recent Developments in International Natural Gas Markets

- Paradigm Change:
 - From regional markets developing into an international market
 - LNG connects large consumer markets
 - Domestic supplies in traditional natural gas markets not sufficient to satisfy growing demand
 - Import dependency growing in traditional natural gas markets and new markets in emerging economies
 - Current tightness of natural gas markets: long lead times, regulatory uncertainties and (under) investment impact the future organisation structure

Increasing Import Dependence



Recent Developments in Energy Policy

- Energy policies are under review due to:
 - changing supply/ demand balances
 - changing perspective on the organisation structure of the natural gas value chain
 - Politisation of energy relations
- Security of supply and security of demand a main issue in energy policy-making
 - SoS: uncertainty about supply levels, price and market power of national gas companies which could invoke partial diversification away from natural gas
 - SoD: uncertainty about market access for national natural gas companies from supplier countries, uncertainty about demand levels and long term contracting which could hamper investment in new capacities in the gas value chain.

New International Business Environment

- Forward and backward vertical integration to guarantee access to supply and markets and to spread risks along the gas value chain
- Horizontal integration to guarantee economies of scale
- Public/private ownership

Recent Developments in International Gas Market Regulation

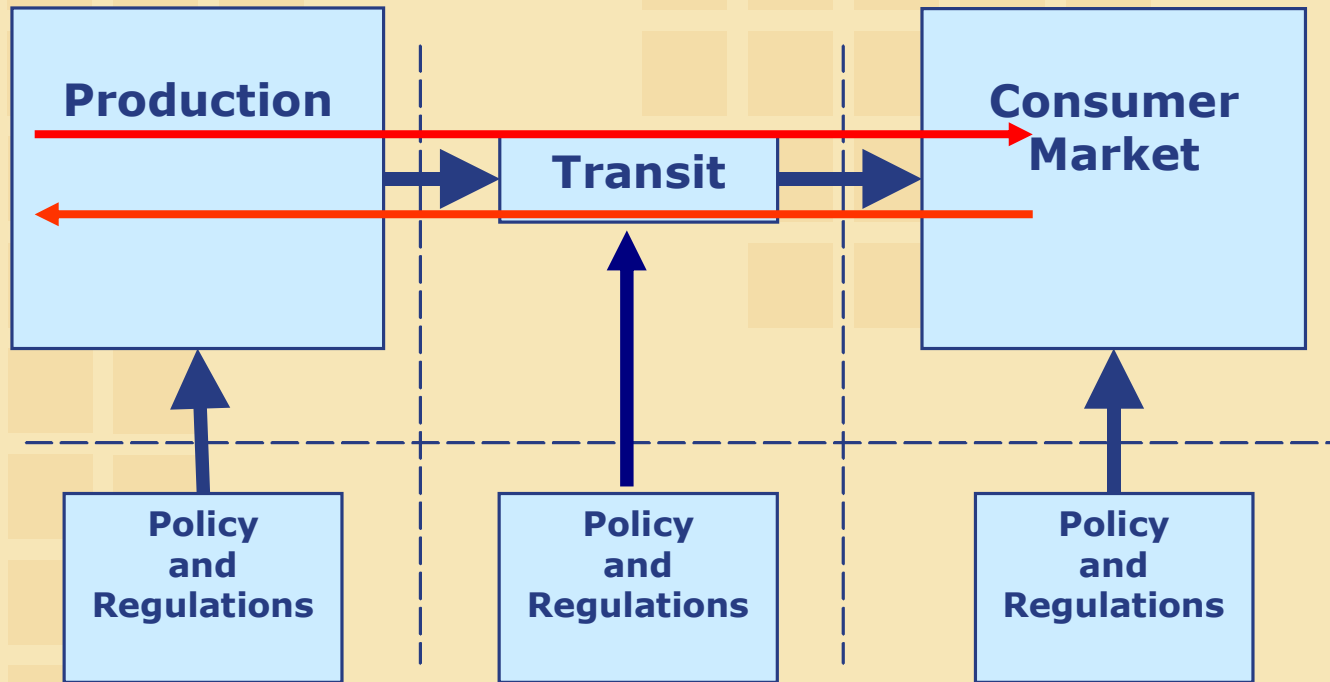
- Regulatory regimes are being revisited and adjusted in order to adapt to the new business environment
 - In main mature markets, the focus is on consumer benefits.
 - Recently consumer countries are increasingly focussing on security of supply and an investment climate that allows for a secure and timely availability of LNG, storage and pipeline facilities
 - In producer countries governments focus on capturing a fair share of the economic rents and secure demand to justify large upstream investments

Upstream

Transit/LNG

Downstream

Response:
Forward
and
backward
integration



WTO, Treaties, compatible regulation

Regulation

- Investment signals:
 - Liquid and unbundled markets do not by definition guarantee timely and sufficient signals to investors
 - New and old coordination mechanisms necessary (long term contracts for supply, transportation, forward and backward vertical integration and exemptions on TPA) to complement short term competitive markets.
- Therefore:
 - Regulatory frameworks should reflect domestic and international market realities (f.i. market structures, stage of development of market, buyers' or sellers' market) and include policy objectives that may vary across countries and regions.

Matching Regulatory Regimes

- Coordination of regulatory regimes along the gas chain and crossing different legal systems to support coordinated investments in infrastructure to maintain supply, are major challenges.
 - International frameworks, such as the Energy Charter Treaty, WTO rules, and bilateral treaties, have the function to support investment initiatives and to resolve disputes.
- Discussing and adjusting regulatory frameworks requires a new process of exchanging information .

Dynamic Markets and Regulation

- **It should be accepted that markets and regulatory models are evolving and that a transition phase from f.i. regulated regional monopoly (or ‘managed’) markets to fully liberalised markets with a stable regulatory regime could easily take 10 to 15 years and do only function in maturing markets.**
 - Before embarking on market liberalisation, it is important to assess if such a market model is suitable to achieve the policy objectives, given local market circumstances and the development stage of the market.
 - Markets cannot be expected to be overturned completely in a short space of time. A step-by-step (perhaps pragmatic) approach is necessary that gives markets sufficient time to adapt.
 - Markets should be given time to evolve and design themselves, under the influence of a wider set of factors.

Regulation and Competition

- It is very important to establish **how and where in the value chain sustainable competition can emerge**
- Horizontal and vertical integration and other strategic responses may follow certain regulatory decisions and unbundling
- The need for a sustainable balance between ex ante regulation, concentration and integration, industry stability, abuse of market power and competition policy may require a market design based on a broader perspective on the functioning of markets.
- Security of supply and demand should be an integral part of such an analysis on the functioning of the market
- There is no single recipe for regulation for the various markets



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