# "Re-engineering"

# Detrimental to Long Term Contracts

A View of Gazprom Export

Alexey Golubnichiy

Deputy General Director Gazprom Export

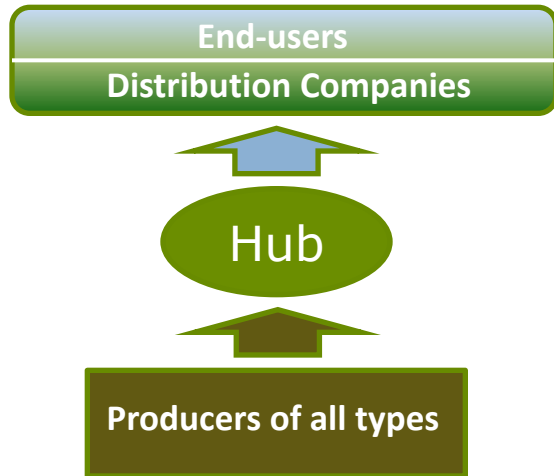BRUSSELS, APRIL 27, 2012

# Optional Pricing Models for Continental Europe Gas Market

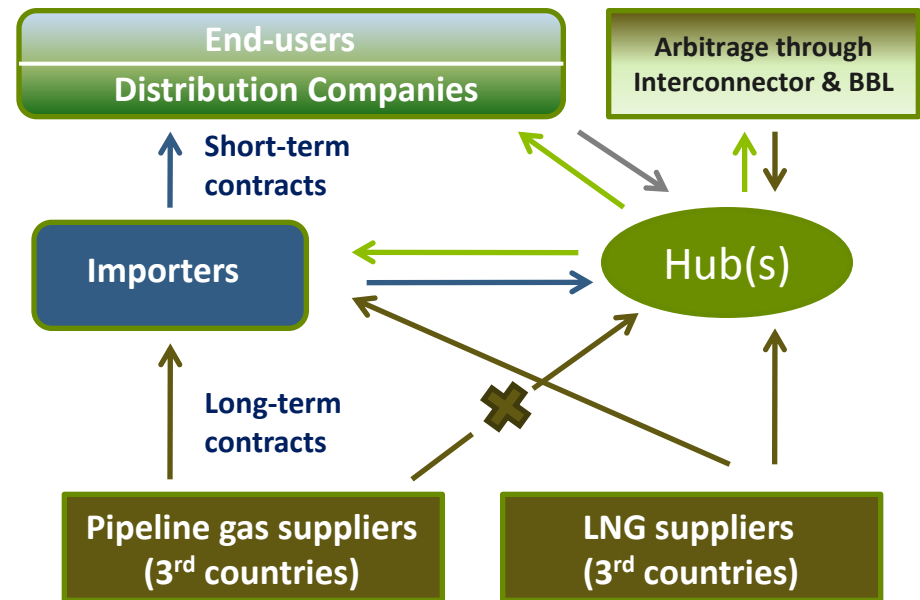| Model | Applicable To | Description | Supplier Acceptance |
|---|---|---|---|
| Oil Indexation | Asia | • LT contracts<br>• 100% indexed to oil<br>• No hubs. | Yes |
| Hybrid | Continental Europe | • Primarily, LT oil/oil product indexed contracts<br>• Minimal gas-indexed component in LT contracts<br>• Hub pricing | Yes |
| Modified | Continental Europe (?) | • LT contracts linked to gas indexes<br>• Hub pricing | No |
| Hub | North America | • Absence of LT contracts<br>• Pricing based on supply & demand | Not the best option for Continental Europe |

# The Choice Europe Confronts

## U.S. Pricing Model

**End-users**

**Distribution Companies**

**Hub**

**Producers of all types**

$PH_{US}$ – hub price in the USA
$S_{US}$ – total supply
$D_{US}$ – total demand

$$PH_{US} = F (S_{US}, D_{US})$$

## Hybrid Pricing Model

**End-users**

**Distribution Companies**

**Arbitrage through Interconnector & BBL**

**Short-term contracts**

**Importers**

**Hub(s)**

**Long-term contracts**

**Pipeline gas suppliers (3rd countries)**

**LNG suppliers (3rd countries)**

$PH_{CE} \neq F (S_{CE}, D_{CE})$

$PH_{CE}$ – hub price in Continental Europe
$SH_{CE}$ – total supply = $SHI_{CE} + SHEU_{CE} + SLNG_{CE} + SUK_{CE}$,
where:
$SHI_{CE}$ – sales to hubs by importers
$SHEU_{CE}$ – sales to hubs by end-users (ToP obl.)
$SLNG_{CE}$ – LNG supply to hubs
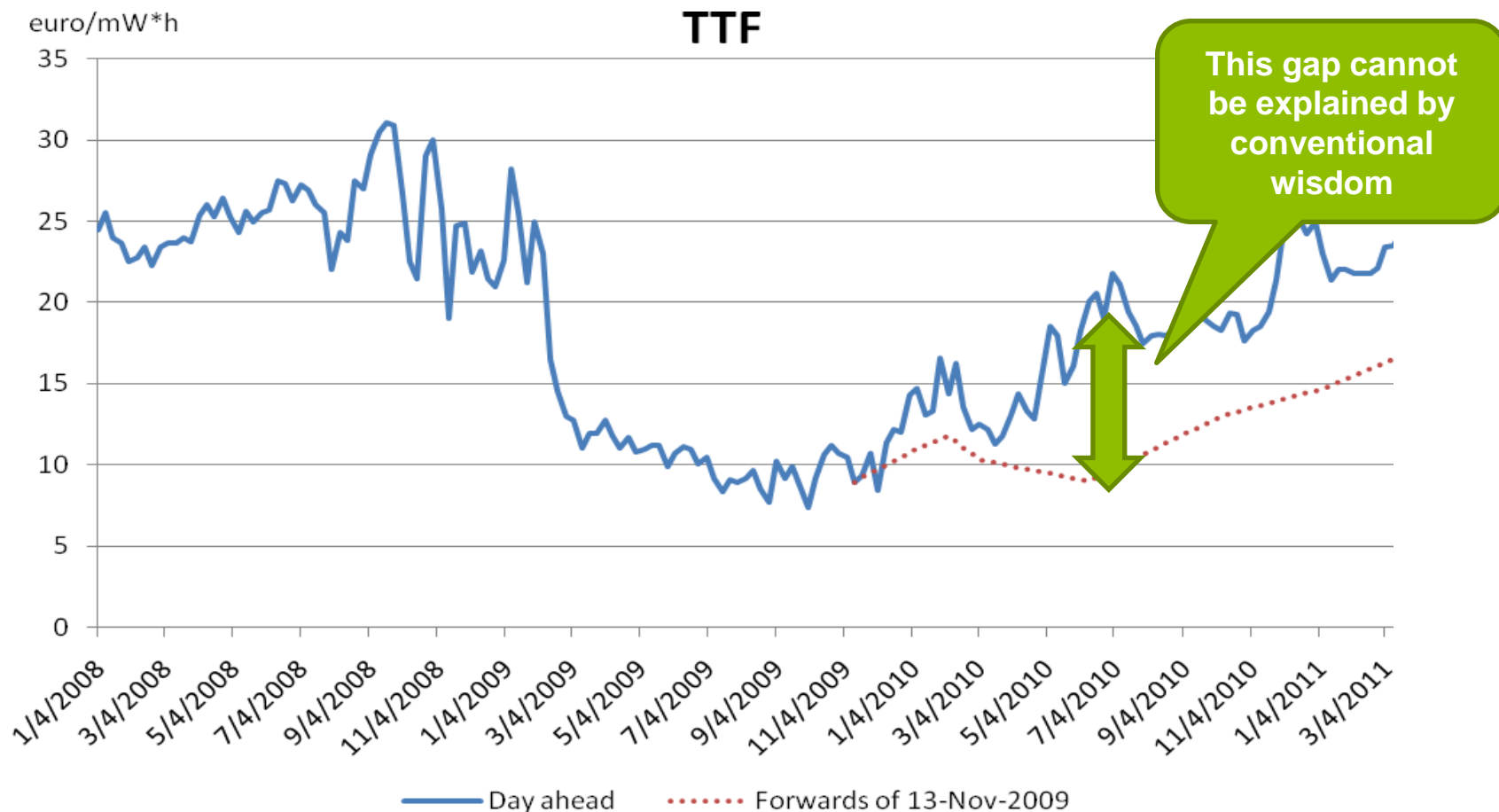$SUK_{CE}$ – UK supplies through the Interconnector & BBL
$DHI_{CE}$ – demand by importers for hub gas
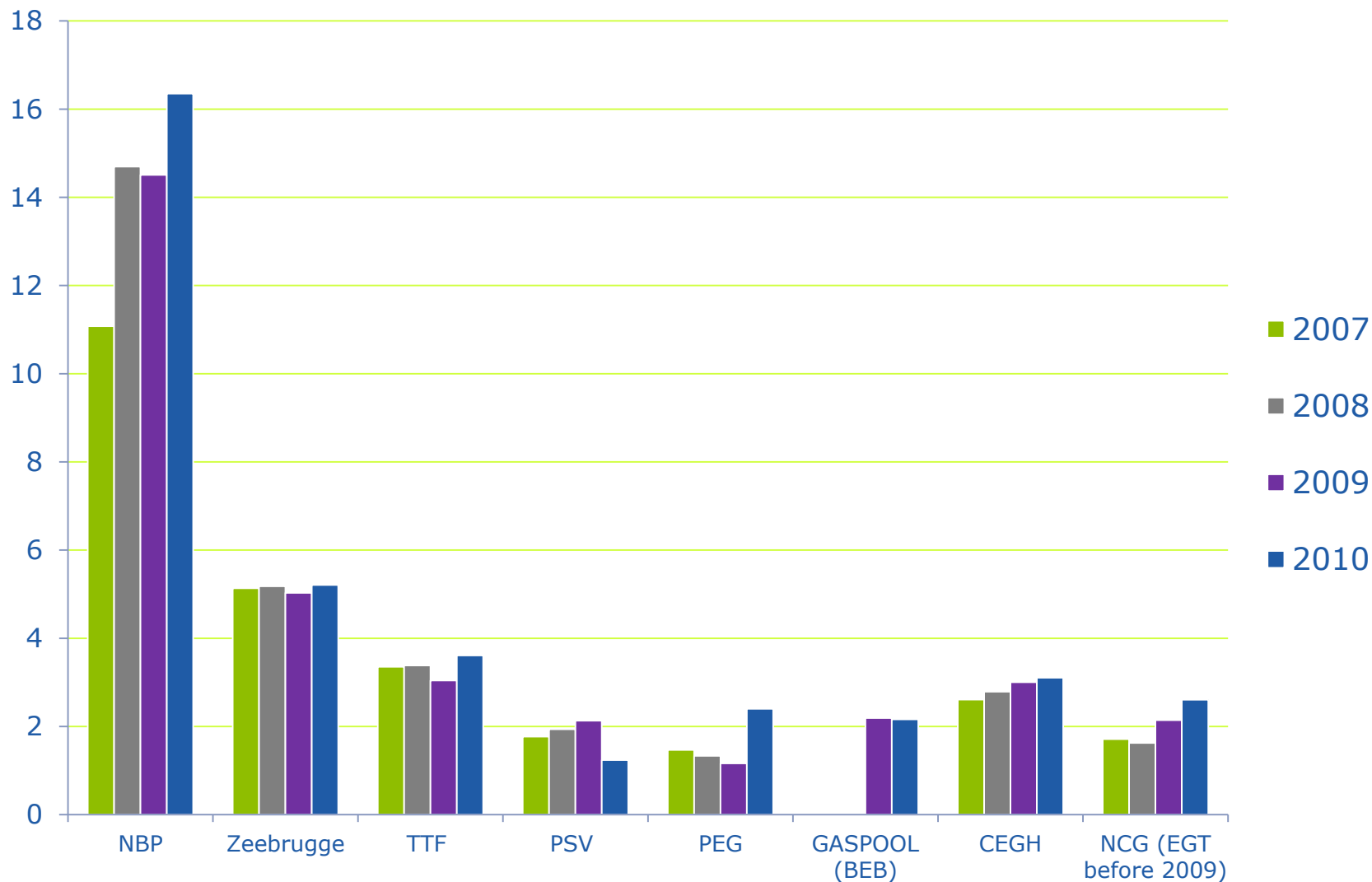$DHEU_{CE}$ – demand by end-users for hub gas
$DUK_{CE}$ – UK deliveries through the Interconnector and BBL

$$PH_{CE} = F\{(SHI_{CE} + SHEU_{CE} + SLNG_{CE} + SUK_{CE}),(DHI_{CE} + DHEU_{CE} + DUK_{CE})\}$$

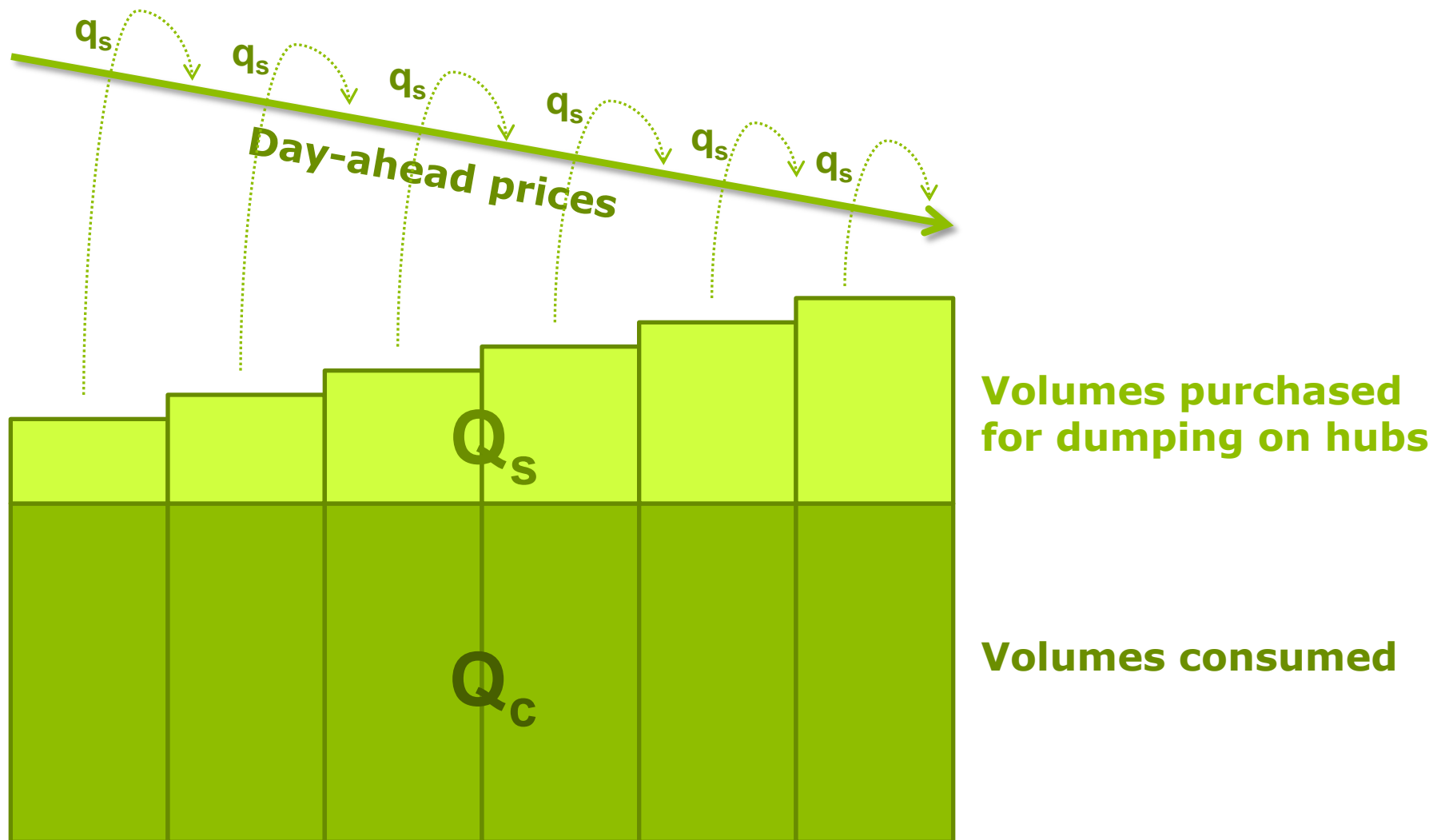# Continental Supply & Demand Does Not Dictate Hub Pricing

# Churn Ratio at European Hubs



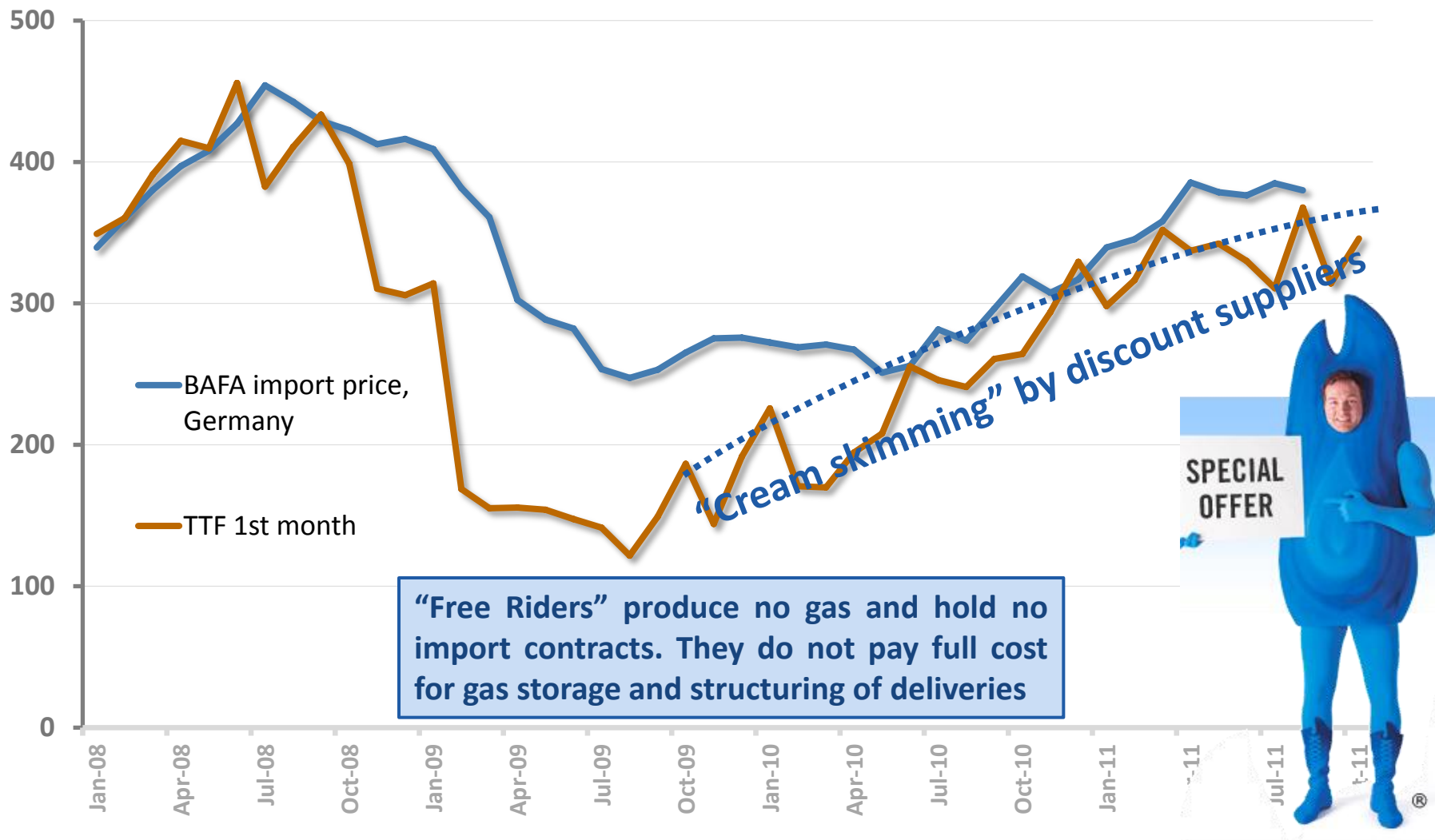*Source: IEA*

# Dumping by Buyers' Cartel in Case of 100% Indexation

$q_s$   $q_s$   $q_s$   $q_s$   $q_s$   $q_s$

Day-ahead prices

$Q_s$

$Q_c$

**Volumes purchased for dumping on hubs**

**Volumes consumed**

Dumping persists until $Q_s = Q_c$

# Reforms will sponsor "cream skimming" and "free riding". Competition will become unfair.



Legend:
- BAFA import price, Germany
- TTF 1st month

"Cream skimming" by discount suppliers

"Free Riders" produce no gas and hold no import contracts. They do not pay full cost for gas storage and structuring of deliveries

SPECIAL OFFER

# THANK YOU FOR YOUR ATTENTION!