

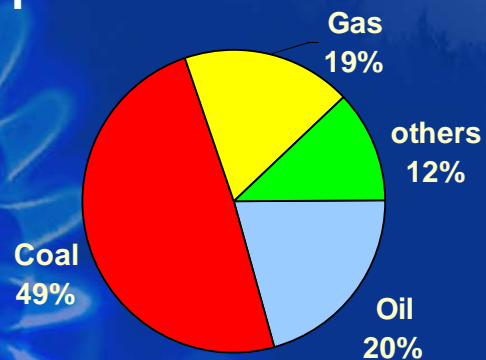
New Challenges in the Central European Gas Market

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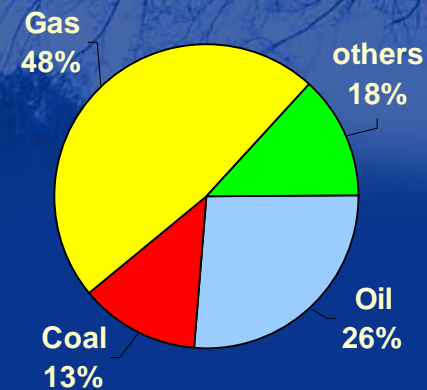
- **Main players in the region**
- Legislation/Regulation
- Market Liberalisation
- Reliability of gas supply
- Conclusions

Primary energy consumption of CE countries

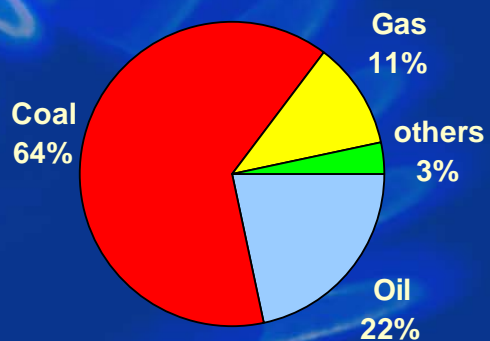
Czech Republic



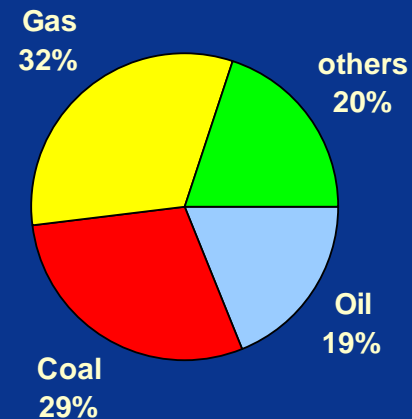
Hungary



Poland



Slovakia



Source: UNECE Gas Centre

Natural Gas Market in the Region

- Natural gas transforming from slow growth monopoly into rapidly expanding and globalizing business
- Strategic role of transit corridor
- High gasification SK, HU; Poland – low penetration and strong potential
- Dependence on Gazprom gas supplies (effective customer choice = illusion)
- Enough demand to accommodate alternative supplies (PL, power)
- Natural gas not used efficiently (potential for change for all CE countries)

RWE Transgas

- Sole importer of natural gas, largest storage importer
- Storage capacity: 2 055 mill. m³
- Pipeline network: 3 640 km
- Revenues: 1 928 € million
- National Gas Sales: 101.7 TWh
- Employees (Ø 2004): 1 298

GDCs

- RWE holds majority in 6 of 8 distribution companies
- No storage capacity
- Pipeline network: 68 585 km
- Revenues: 1 878 € million
- Gas Sales: 100.4 TWh ~ 10 Bcm
- Employees (Ø 2004): 4 777

Other

- Furthermore, there is a small market share of individual companies such as MND, which is the sole producer of natural gas, owns and operates some storage facilities in the Czech Republic

Source: RWE 12th CEGC, Budapest, June 2005

The Polish Gas Industry

PGNiG

- Sole importer of natural gas, (70% of gas supply is imported)
- Largest producer of natural gas
- Natural gas resources 170 Bcm
- Production: 26,8 mmboe (4,3 Bcm)
- Storage capacity: 1,5 Bcm
- Pipeline network: 15 450 km
- Revenues: 6th largest company in Poland

- National Gas Sales: 13,7 Bcm
- Employees (Ø 2003): 7 785
- State ownership: privatization – target date for IPO June 2005

GDCs

- PGNiG owns all 6 distribution companies
- No storage capacity
- Pipeline network: 109 860 km

Source: PGNiG 12th CEGC, Budapest, June 2005

The Hungarian Gas Industry

MOL

- Sole importer of natural gas, (82% of gas supply is imported)
- Largest producer of natural gas
- Production: 3,015 Bcm
- Storage capacity: 3,34 Bcm
- Pipeline network: 5 270 km
- Revenues: 7 770 € million
- National Gas Sales: 15 Bcm

GDCs

- 6 distribution companies
- No storage capacity
- Pipeline network: 71 280 km

Source: MOL, 12th CEGC, Budapest, June 2005

The Slovak Gas Industry

SPP

- Sole importer of natural gas, (98% of gas supply is imported)
- Storage capacity: 2 Bcm
- Pipeline network: 30 534 km
- Transmission pipeline network: 2 270 km
- Revenues: 2 015 € million
- National Gas Sales: 6,53 Bcm
- Transmission volume: 82,7 Bcm
- Employees (Ø 2004): 5 472

- Main players in the region
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EU Law Governing the Gas Industry

- **Directive No 98/30/EC** concerning common rules for the internal market in natural gas (valid until 01/07/04)
 - lays down the first principles of market opening
 - the result is a various degree of market opening in individual EU member states
- **Directive No. 2003/55/EC** concerning rules for the internal market in natural gas repealing Directive No. 98/30/EC (implementation date – 01/07/04)
 - continuation of the liberalisation process
 - schedule for complete market opening
 - legal separation requirement (unbundling)
 - obligation of member states to establish an independent regulatory authority

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Regulatory Period 1&2 – Czech Republic

Period 1 (2002-2004)

Significant facts

- TSO monopoly status
- 100% of market protected customers
- Gas imports, transportation, storage, distribution and sale regulated by ERO. Only unregulated business: Gas transit
- Energy Act in effect as late as Dec. 31, 2004

What was done

- Created reporting lines with regulator
- Unbundling preparations, examples:
 - Since 2002, business process internal analysis in GDCs and TG
 - Shared Services & IT – infrastructure analysis: SAP, procurement, HR
 - Risk Management
 - Development net-codes for TSO and DSO

Period 2 (2005-2009)

Significant facts

- Competitive market
- 2005: 28% of customers eligible (< 15 mill. m³)
- 2006: 70% of customers eligible (all but households)
- 2007: 100% of customers eligible

What has/will be changed

- Unbundling
 - TSO, legal by Jan. 2006
 - DSO, legal by Jan. 2007
- Result will be full transparency
- Commodity price negotiated (from 01.01. 2007 for all customer segments)

Source: RWE 12th CEGC, Budapest, June 2005

Regulation in Slovakia

- Network Industries Regulatory Authority (ÚRSO), for the activities of which the Regulatory Council is accountable, has been established in 2001.
- Price regulation based on
 - Households regulated until Jan 1, 2007
 - Commercial customers – Brent formulas
 - Big industrial customers – negotiated prices
- Regulated subject SPP, a.s., with 100% share in the market + 19 trade licence holders
- Eliminated cross subsidies (transit, distribution, trade)
- Market Rules issued by Regulator on March 1, 2005
- Transit Network Operator Code, SPP, a. s.;
- Distribution Network Operator Code, SPP, a. s.;
- Underground Storage Facilities Operator Code, Nafta, a. s. and Pozagas, a. s.

Regulatory Period 1&2 – Poland

Period 1 (before July 2004)

- Transmission tariff (includes storage tariff) covers cost base only
- Distribution tariff covers cost base only
- Tariff regulatory review period of 1 year
- TSO created as a separate legal entity 100% owned by PGNiG
- TSO operates transmission network

Period 2 (after 2005)

- Potential gradual exclusion of domestic gas production from Trading tariff
- Potential Return on Book Equity in Transmission tariff
- RAB (Regulated Assets Base) in Distribution tariff
- Potential extension of regulatory review period (3 years?)
- TSO collects transmission tariffs and leases all transmission assets from PGNiG

Source: PGNiG, 12th CEGC, Budapest, June

2005

Regulation in Hungary

- The Highest authority to supervise the NG market is the Hungarian Energy Office (HEO). Market players pay much attention statements by HEO in respect of communal gas pricing, of new opportunities for entering the free market, of amendments to the current Network Code.
- Price regulation based on
 - Households regulated until July 1, 2007
- Regulated subject MOL, a.s.+ 13 trade licence holders (three of them provide services to the clients on the free gas market currently)
- Eliminated cross subsidies
- MOL activities - Unbundling
 - MOL Natural Gas Storage Plc.
 - MOL Natural Gas Transmission Plc.
 - MOL Natural Gas Supply Plc.

Source: MOL website

- Main players in the region
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Gas Markets Liberalisation

- ✓ The 1998 Directive: Eligible customers are all Power Generators, final customers consuming more than 25 Mcm/y.
- ✓ The 2003 Directive: all non-household customers eligible from 1st July, 2004; all customers, including households, from 1st July, 2007.
- ✓ Actual liberalisation in EU markets still below the targets of the Directive due to:
 - Dominant players keep large market share
 - Limited supply switching by customers

Market Opening - selected EU countries

	Declared market opening	Declared open Market size	Customer switch	Share of top-3 suppliers
	% of total	Bcm	% of eligible	% of market
Austria	100	7	9.5	90
Belgium	~90	11	64	54
Denmark	100	5	30	NA
France	70	28	25	88
Germany	100	82	9	15?
Italy	100	62	65	95
Netherlands	100	38	32	75
Spain	100	20	>55	83
UK	100	95	97	59

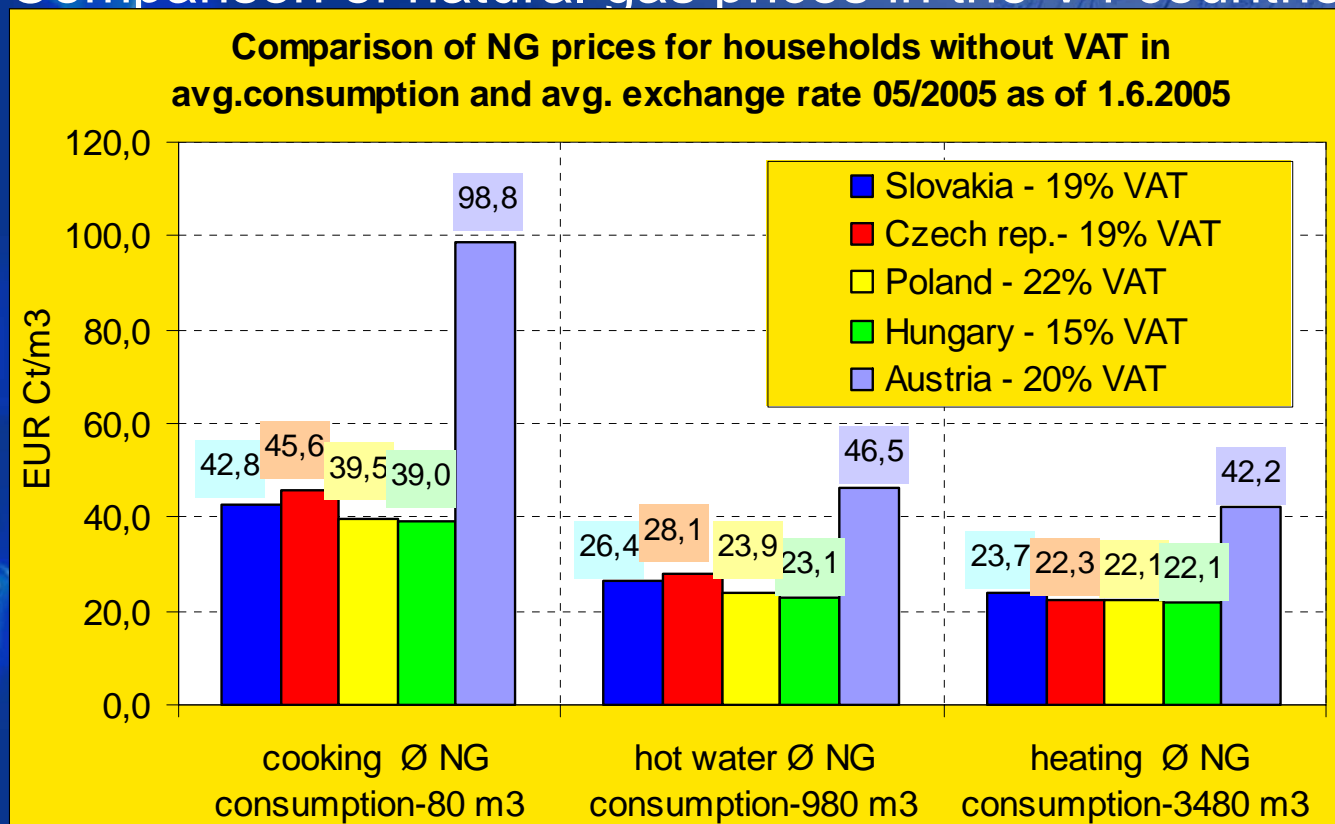
Source: IGU - PGCC

Key areas require attention

- **Energy Substitution**
 - Gas price still linked to oil price development
 - Increasing gas prices make customers to switch to substitute fuels
 - Key accounts evaluate using waste products as substitute for gas
- **Gas to gas**
 - Large international companies prefer one supplier for several countries and already prepare invitation for tenders
 - Already several key customers were approached by competitors
- **First gas offers from third parties (traders)**
 - Rising expectations on the customer side
 - So far limited volumes realised by new traders

Is the expected consequence of liberalisation – a reduction in gas prices – actually true?

- Comparison of natural gas prices in the V4 countries and Austria



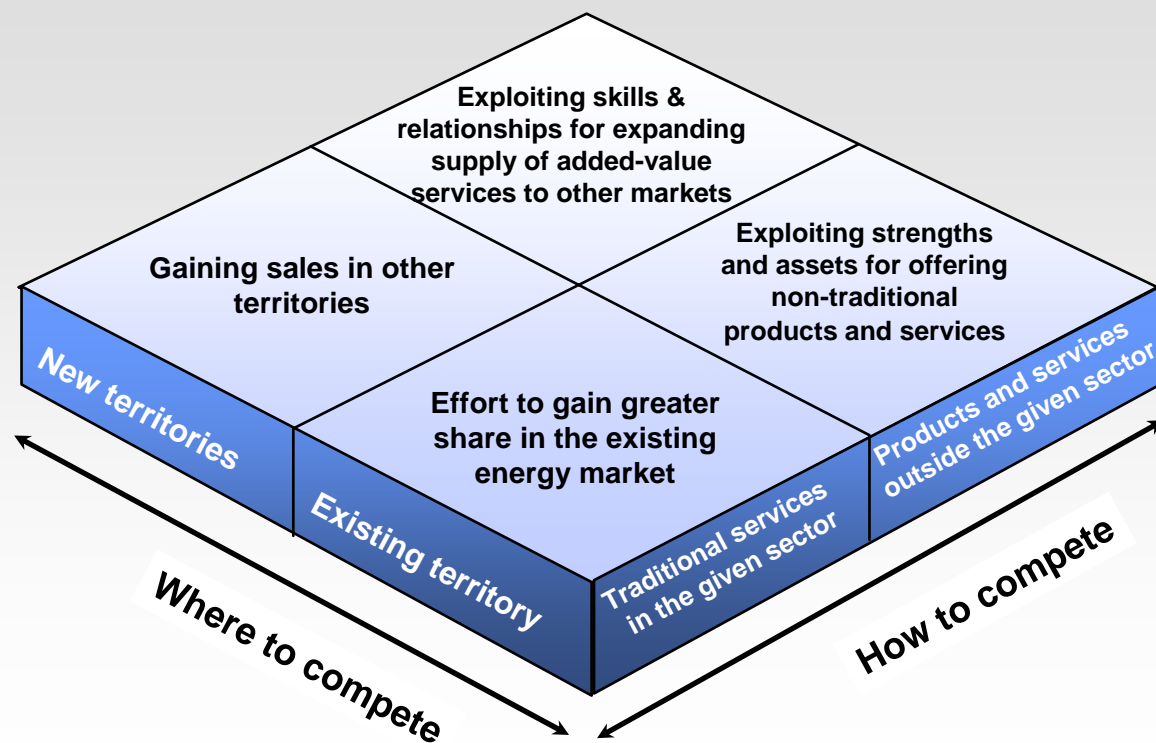
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Reliability of gas supply – main issues

- Role of the market – to ensure equilibrium between supply and demand
 - short-term
 - selection of reliable suppliers
 - peak-demand coverage
 - long-term
 - efficient allocation of resources and investment
 - to generate sufficient funds for investment in infrastructure (production, transport, storage, consumption)
- Customers have the choice, but are responsible for selection of supplier from the aspect of the supplier's reliability short-term
- Diversification of resources (LNG ?)

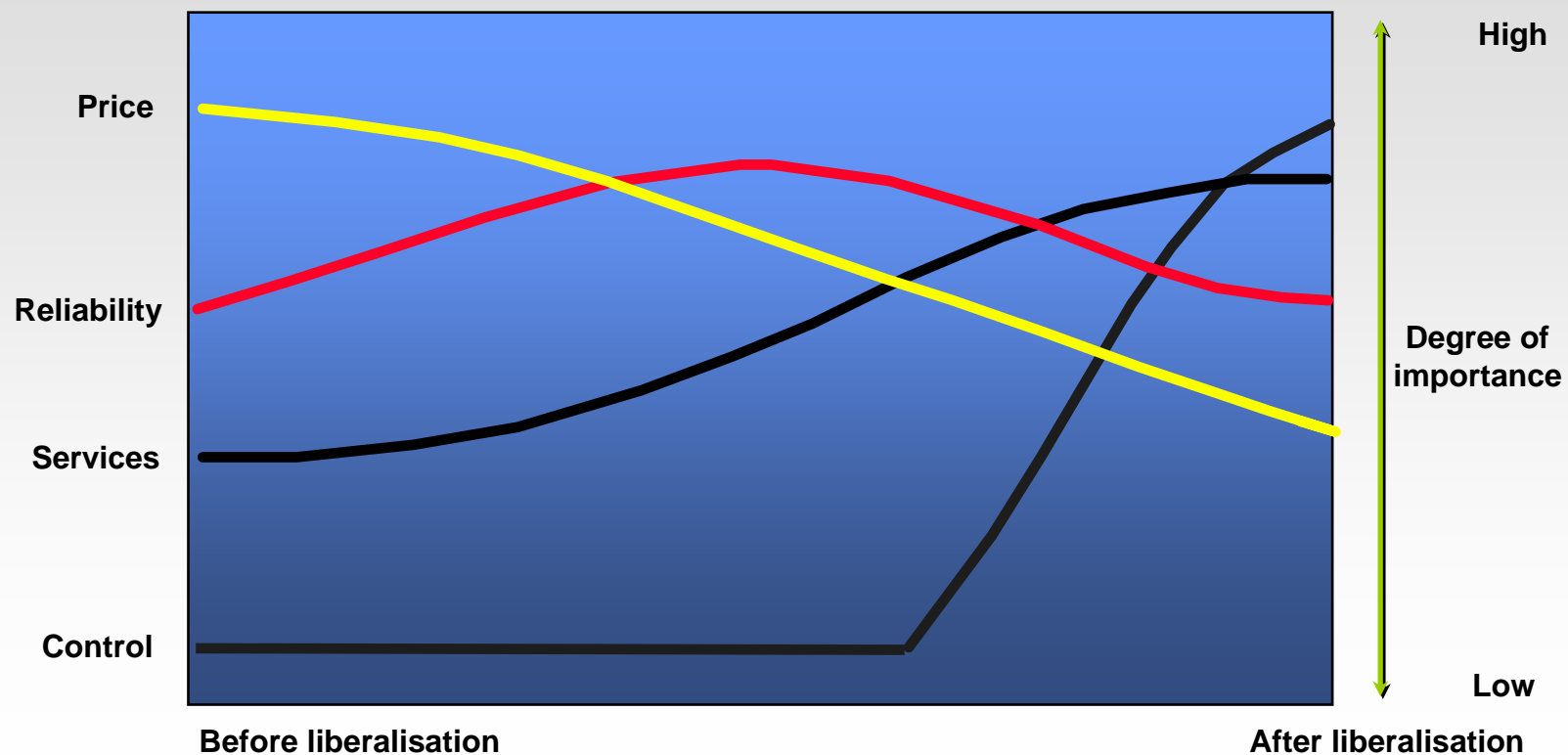
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- **Conclusions**

Energy suppliers are for the first time faced with the decision of how and where to compete



A successful marketing mix will eventually form even in the energy industry

Main factors influencing customers' decisions



Conclusions–Market Liberalisation in CE

- Oil price fluctuations, exchange rate factors, and energy demand influence level of energy substitution
- Natural gas price is the main decision maker throughout customers groups
- Energy suppliers for the first time faced with decision of how and where to compete (new territories, services, products)
- Reliability of supply – still a core issue
- New gas market conditions have to be absorbed by the customers as well as by new players /traders

SLOVENSKÝ
PLYNÁRENSKÝ
PRIEMYSEL



Thank you for your attention