SHIFTING LNG MARKET DYNAMICS

As LNG markets evolve to become more flexible and increasingly more competitive thanks to a global glut, energy analyst Mahin Siddiqui examines how this has affected business

LNG markets are in a state of significant flux. Usually calm, the sector is now evolving to become more competitive and dynamic.

This change is largely brought about by the wide spread LNG glut – however several LNG market players have debated recently how much of glut there currently is. More than 100 million tonnes per year is set to enter global markets by 2020 reports Bloomberg. By 2019, this oversupply will peak at roughly 60 mpta.

Mostly, this oversupply is driven by the US and Australia in the global LNG market – 83 bcma of committed US capacity has received Financial Investment Decision (FID) according to Timera Energy, and most of it will be online by 2019.

The LNG glut is easier to address, rising demand from emerging economies will absorb most of LNG to keep live social and economic momentum. China alone will absorb 38 million tones of LNG in 2018. Last year, Japan consumed 83.5 million tonnes of LNG. South Asia's Pakistan is forecasted to consume 30 million tonnes per year through to 2020. In the Middle East – UAE, Egypt and Jordan will remain hungry for the liquefied gas commodity to power a growing population. Therefore, many analysts see the LNG market tightening by 2020 led by combined global demand.

To keep market share with old structures will be much more tough – the US is not only contributing to the glut, but also disrupting the way business was done previously through long term contracts and inflexible market pricing allowing buyers to flex their muscle with traditional sellers from the Middle East.

The need for all suppliers is to woo buyers with fresh pricing strategies, flexible attitude, and new investments.

On the supply side, the US has done away with the famous destination clause, making its business contract much more attractive and freer. A pain point for most buyers, a destination clause in the LNG supply contract restricts the buyer from reselling LNG outside of a designated market, which is usually the buyer's home market. This restricts customers from taking advantage of spot prices should the right infrastructure be available on home turf.

Additionally, US supply contracts are priced against the Henry Hub. This creates a more pragmatic pricing structure reflective of the ongoing supply and demand in the gas markets as opposed to simple price fluctuations related to oil price movements. Simply put, it gives a fairer LNG price. LNG buyers see Henry Hub as a stable and affordable benchmark. According to Spencer Dale, chief economist of BP, the economics suggests that US gas prices will act as a natural anchor. On the other hand, this new pricing structure also signals growing influence for the US, shifting away from the Middle East, as a gas market hegemon via the Henry Hub benchmark. In Aug 2017, WSJ reported Anadarko Petroleum has signed deals to sell LNG from Mozambique's coast at Henry Hub prices according to Mitch Ingram, executive vice president.

Spurred by the new winds of change, Japan's JERA saw this as an opportunity for arbitration when their long-term supply came to an end in 2017.

Against this back drop of a growing buyer's market, it would do well for traditional producers from the Middle East to take a leaf out of the US' book.

FSRUS

On the investment side, FSRUs or Floating Regasification Units are the clear winners in the pipeline versus shipping debate. Instead of planning new pipelines, the need of the hour is to dive into the high seas with FSRUs. FSRUs are sea vessels that can provide gas on spot basis to customers and are a low investment option for producers such as in Egypt. They also don't require much commitment, so customers are increasingly favouring purchasing from short term suppliers with less commitment. To be fair, piped gas will not be obsolete – certainly countries like China will require a full cost basis of 20 years, it would be practical to dig pipelines but for some and uncertain markets FSRUs make most economic sense.

Another advantage of employing FSRUs is that they don't need to go through political or technical process to achieve documentation like onshore permits and neither does the customer need storage facilities. This allows countries with strong red tape culture like Pakistan to import LNG quicker.

The global dynamics of the LNG playbook are shifting, and the Middle East needs to up its game to deal with new kids on the block. Forecasts put the US right on top as one of the top three exporters of LNG by 2020, and traditional Middle East suppliers will need to use much more than their influence to keep market share in the changed LNG playground.