LNG Market Road To Recovery

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The Abdullah Bin Hamad Al-Attiyah International Foundation for Energy & Sustainable Development

INTRODUCTION

LNG MARKET
ROAD TO RECOVERY

The Abdullah Bin Hamad Al-Attiyah Foundation for Energy and Sustainable Development provides robust and practical knowledge and insights on global energy and sustainable development topics, communicating these for the benefit of the Foundation's members and community.

In 2020, the Foundation hosted a webinar series, in partnership with Refinitiv, to explore key trends and insights as the coronavirus pandemic impacts the energy industry and hastens the transition to renewables. The most recent webinar in the series explored the road to recovery for the global liquefied natural gas (LNG) industry.

Webinar Series

H.E. Abdullah Bin Hamad Al-Attiyah founded the Webinar Series as a platform for knowledge exchange and support for the global community in the quest towards a sustainable energy future. The quarterly events, which have been hosted in Qatar for three years, are a crucial networking and learning opportunity in the calendar of industry CEOs.

The LNG market has endured a turbulent 2020, with gas consumption forecast to decline 3% this year and prices of key LNG benchmarks—JKM, TTF, and Henry Hub—slumping to all-time lows.

Yet the industry now appears to be over the worst despite the ongoing pandemic. LNG demand will average annual growth of 3.4% to 2040, according to Cheniere Marketing, a subsidiary of LNG company Cheniere Energy.

That will require additional supply in the long term, despite the LNG industry suffering from oversupply at the start of 2020, a phenomenon that Covid-19 exacerbated.

Demand is already showing signs of recovery, and stalled projects are starting to resume as lockdowns are lifted. In the last four months, Total signed a $14.9 billion financing agreement from 28 entities for its massive LNG project in Mozambique—the country's first onshore LNG development. South Korea's Posco International also won a tender to supply LNG to Pakistan, while Vietnam approved a $5 billion LNG-to-power project slated to be developed by ExxonMobil.

Other promising developments include new US energy department policies allowing for LNG exports to non-free trade agreement countries to be extended through to 2050 and Japan's coal phaseout, which should create more opportunities for LNG. Additionally, the growing participation of LNG traders, alongside traditional buyers and sellers, should bring significant benefits to the sector, enhancing its ability to optimise flows and increasing liquidity in both the physical and derivatives market, according to energy and commodities trader Vitol.

In light of these developments, how robust will the LNG industry's recovery be and what forces will shape the global gas market in the coming years?

It's been a turbulent six months for the LNG market, but positive developments are already emerging. While total global gas demand is forecast to decline by around 3% in 2020, it is expected to make a quick and robust recovery, growing by an average 3.4% a year to 2040, according to Cheniere Marketing, a subsidiary of LNG company Cheniere Energy.

In the last four months, Total signed a $14.9 billion financing agreement from 28 entities for its massive LNG project in Mozambique–the country's first onshore LNG development. South Korea's Posco International also won a tender to supply LNG to Pakistan, Vietnam has approved a $5 billion LNG-to-power project that is expected to be developed by ExxonMobil, and Mitsui-Beach joint venture said it was finalising an agreement to process gas at the North West Shelf LNG facility in Australia.

In light of these developments, how resilient will the recovery of the LNG industry be, and what forces will shape the global gas market in the coming years?

KEY HIGHLIGHTS

- Amid the tumult of 2020, price convergence across LNG's three main benchmarks showed the beginnings of an efficient, well-functioning global gas market
- East Asia will remain LNG's most important market due to the region's large population and state moves to switch from coal to less polluting energy sources
- Oil majors are more cautious about investing in LNG but are still committed to the industry

Oversupply will probably persist in the LNG sector until at least late 2021. Still, prices are unlikely to retest this year's record lows, and a wariness among investors to commit to large-scale projects should lead to the market tightening in the long term.

Giles Farrer, Director, Head of Gas & LNG Asset Research, Wood Mackenzie

Around $100 billion of investments in LNG projects have been deferred this year, noted Patricia Roberts, Managing Director of LNG Worldwide Ltd. These include delays to developments in the likes of Mozambique, Qatar, Russia, and the United States.

Such hesitance is understandable considering the unprecedented economic disruptions caused by the coronavirus pandemic, which has had a huge impact on LNG sales. Yet, overall, 2020 LNG volumes may be higher than those of 2019, said Ms. Roberts, albeit at thinner margins as tumbling prices helped LNG outcompete pipeline gas and displace coal in some Asian markets.

"Gas demand has held up much better than oil demand in light of the pandemic," said Giles Farrer, Wood Mackenzie's Director of Gas & LNG Asset Research. "Market oversupply this year was almost inevitable—Covid has made an already bad situation worse."

He believes LNG oversupply will persist for at least the next year. "The market has rallied recently, but that's likely to be short-lived ... long term, the outlook for LNG demand is robust," said Mr. Farrer, predicting a 4%

Jan Bruil, Senior Consultant LNG and Natural Gas Advisors, Poten & Partners

increase in demand over the long term. "LNG is a strong commodity."

LNG is cyclical in terms of investments, said Jan Bruil, a Senior Consultant for LNG and Natural Gas at Poten & Partners. Postponements of final investment decisions (FID) for many LNG liquefaction projects should lead to a tighter market in 3-4 years, he predicts—a view shared by other panellists.

International oil companies (IOCs) are re-thinking their strategies as an increasing determination among governments to transition from fossil fuels to renewable energy calls into question the viability of long-term hydrocarbon investments. Yet despite these concerns, IOCs are still willing to commit to LNG and will remain major investors in LNG projects—albeit with greater caution.

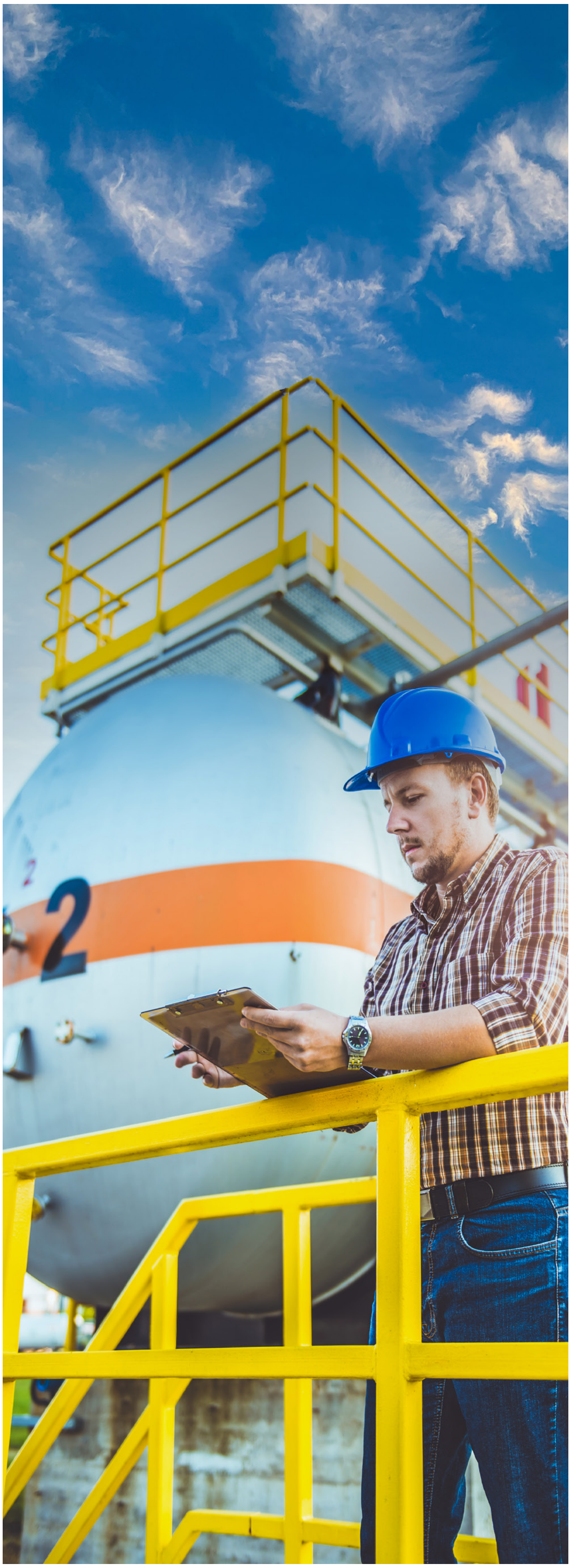
"Shell, Total, BP, are re-evaluating their portfolios and what weight they want to give natural gas, oil, and renewables. We're seeing a decrease in risk appetite to invest in these very long-term, high Capex LNG liquefaction projects," said Luke Cottell, EMEA LNG Analyst at S&P Global Platts Analytics.

Luke Cottell, LNG Analyst, EMEA, S&P Global Platts Analytics

In the webinar's first poll, 26% of attendees said LNG players should focus on capital efficiency during the coming months, while 26% argued for downstream market development. Supply chain optimisation attracted 14% of votes, decarbonisation received 11%, and digital and advanced analytics drew 9%.

"How you vote on this depends on where you sit in the LNG business," said Ms. Roberts. "If we ask Qatar Petroleum to vote in this, they would say this is a real opportunity to grow the market and go into creating demand security. If you go to an IOC, capital efficiency and use of Capex and Opex [operating expenditure] is critical."

While a tumultuous 2020 has hurt LNG producers' margins, it has already brought about some unintended benefits such as a convergence of prices across the three main hubs—Asia's JKM, Europe's TTF, and North America's Henry Hub. "There was evidence for the first time of an efficient, well-functioning global gas market," said Mr. Cottell.



Patricia Roberts, Managing Director, LNG Worldwide Ltd

Mr. Farrer described how his clients in North America were now interested in what was happening in Asia-Pacific "because it's actually having a direct impact on the Henry Hub forward curve... because of that, the focus on advanced analytics is becoming more prevalent within the trading space".

Declining US LNG exports have been the biggest supply-side response to falling prices and oversupply, said Mr. Cottell. Yet as the northern hemisphere winter approaches, US exports have nearly recovered to nameplate level.

"The story next summer becomes a challenging one again because we have all this global supply, which was turned in the summer of 2020 in response to record low prices, and that will look to come back into the market as we move into a higher price environment," said Mr. Cottell.

"[There's] a massive amount [of] supply to ask the market to absorb. Once again next summer we'll be in a state of oversupply, and we expect to see a convergence of global gas prices and also a likely situation of further US curtailments."

LNG GROWTH & DEMAND

Despite these pressures, Henry Hub prices will have a higher floor due to a substantial drop in natural gas production following this year's oil price slump, Mr. Cottell predicts.

Asia remains the most important gas market, accounting for more than two-thirds of LNG consumption.

"Growth will be centred on South East Asia," said Mr. Bruil. "The major Far East Asian countries are reacting to Covid probably better than the much of the West and demand hasn't been affected as much. We're confident that Asian demand will continue to grow, driven by countries like India and China."

The LNG industry is keenly watching government policy changes in Asia-Pacific, said Mr. Farrer, highlighting South Korea's measures to limit coal-fired powerplant output to improve air quality. Similarly, Japan has announced a review of its coal retiral policy, while India is mulling introducing a clean air programme.

"That raises the prospects of gas stepping in to meet some of that demand," said Mr. Farrer. "At the same time, we're also watching whether carbon taxes will be introduced, particularly in the advanced countries and how that will play into gas." Mr. Bruil agreed, noting "the future [of LNG] is to replace coal in Asia".

Ms. Roberts described China as Asia's pivotal market, predicting the world's second-largest economy could become a 100 million tonne LNG market by 2030. "We will depend more and more on China," she said.

It is not only the power sector driving gas demand in Asia. Mr. Cottell noted India's use of LNG to produce fertilisers, plus the commodity's use in other countries' industrial sectors, and as a direct energy source in some residential markets.

WEBINAR SPEAKERS:

Moderator:

Axel Threlfall,
Editor-at-Large,
Reuters

Speaker:

Giles Farrer,
Director, Head of Gas & LNG Asset Research,
Wood Mackenzie

Speaker:

Jan Bruil,
Senior Consultant LNG and Natural Gas Advisors,
Poten & Partners

Speaker:

Luke Cottell,
LNG Analyst, EMEA,
S&P Global Platts Analytics

Speaker:

Patricia Roberts,
Managing Director,
LNG Worldwide Ltd

"Across the region, we see slow liberalisation of markets, [while] buildout of infrastructure is supporting gas demand across [the] Asia Pacific—it remains the growth engine for the global gas market," said Mr. Cottell. "With the right mixture of competitive pricing, liberalisation, and policy support, we can see those sectors grow their use of gas."

A second poll asked attendees about the biggest driver of LNG demand next year. Among respondents, 34% said it would be coal-to-gas and oil-to-gas switching, 23% said an increase in industrial consumption, 17% said accelerated demand growth in Asia. A smaller proportion of 11% said lower wholesale gas prices, and 6% said recent investments in terminals and pipelines to connect gas to consumers.

Yet Mr. Farrer played down the likely impact of oil-to-gas and coal-to-gas switching, citing high LNG prices versus coal and Europe's significant progress in already substituting gas for coal.

China has around 250,000 trucks and 100,000 buses running on LNG, supported by about 2,500 refuelling stations, said Ms. Roberts. Progress has been slower in Europe, but she expects the transportation sector's switch to gas from diesel to accelerate over the next five years as the supporting infrastructure is built.

A third poll sought to establish the biggest challenges facing the gas sector. Among viewers, 37% said the declining role of gas in baseload power generation, 22% said pressure from new technologies such as hydrogen, 15% said the rapidly declining cost of batteries, and 12% cited increasing electrification which will diminish the use of gas for heating and cooking.

"Gas is being hit by rising renewables penetration, but at the same time gas is finding market share as coal retirals are moved forwards," added Mr. Farrer. "That will sustain gas and LNG demand through the 2020s and into the early 2030s."

Although less polluting than coal, gas is still a major source of carbon dioxide and noxious substances, and its status as a less malign alternative has been questioned. To remain in the energy mix for decades to come, LNG must clean up its supply chain—no matter the cost—and displace coal wherever possible so that humanity can slow the rate of climate change and secure our planet's future.

OUR MEMBERS

Currently, the Foundation has over 15 corporate members from Qatar's energy, insurance, and banking industries as well as several partnership agreements with business and academia.

Our partners collaborate with us on various projects and research within the themes of energy and sustainable development.

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