Changing World of LNG – Coronavirus play

BY AFSIR AHMAD

Lockdown measures and negative economic outlook stemming from the coronavirus pandemic took its toll on the global economy including Asia, resulting in the second consecutive year of sluggish LNG demand growth. Japan, the world's largest LNG importer, saw LNG demand decline in the first quarter of this year, and imports continued to fall through April as the coronavirus outbreak began to spread. Lockdowns across Europe were as severe as Asia, but the total impact on gas demand was proportionally less due to the smaller share of gas used in the industrial sector, the resilience of gas use in the power sector and the largely unaffected demand from residential use. Although Europe's total gas demand was down in comparison to last year, however, reductions in domestically produced gas and Russian pipeline imports created more room for LNG to be absorbed. The single largest fundamental difference from 2019 was Europe's vast gas inventories. The poor margins and consequent drop in offtake resulted in the under-utilisation of US terminals which continued in the summer months. Demand continued to drop, the global LNG industry faced its first seasonal demand contraction since 2012. **In general, a return to stronger growth is not expected until mid-2021**.

Pandemic Impact on demand

Whilst LNG supply grew globally through the first three months of 2020; however, around the same time demand started to react to the changing market conditions, much before COVID 19 was declared a pandemic by World Health Organization. The LNG market showed further weakness from April as Asian spot LNG prices fell to a record low as a result of lockdowns and lower industrial output. The average LNG price for May delivery into northeast Asia fell to $2.30 per MMBtu below the previous low recorded in February when demand dropped in China, where the coronavirus first emerged. With the lockdown in the last week of March in India, prices took a turn for the worse after top buyers in India declared force majeure on LNG imports. Together with a drop in demand from Europe, which witnessed some of the highest number of coronavirus cases in April-May, caused LNG supply to swell globally. Consequently the Asian spot prices sank further due to dampened demand. The situation also forced buyers to push back cargo deliveries. LNG trade was severely impacted.

Record Low Price

In an unusual move, Royal Dutch Shell issued a five-year strip tender offering four cargoes a year from 2021 onwards with an option to extend for another five years. Prices for spot LNG cargoes imported into Japan, the world's biggest buyer of the fuel, fell in April to their lowest since the country's trade ministry started compiling data in 2014. Demand for gas too started to erode because of the lockdowns due to coronavirus pandemic. The outbreak turned markets on their heads, with U.S. oil prices slipping into negative territory in end March. Industrial activity around the world slowed, as demand continued to be depressed, Asian spot LNG prices fell to a record low of below $2/MMBtu, with the average LNG price for June delivery into northeast Asia estimated at a new record low of around $1.85 per MMBtu. Wide scale cancellation of

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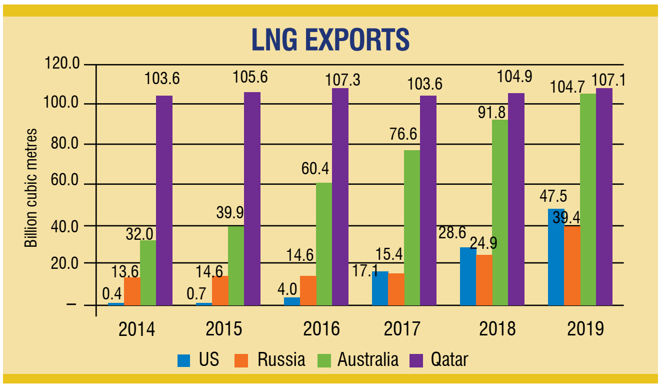

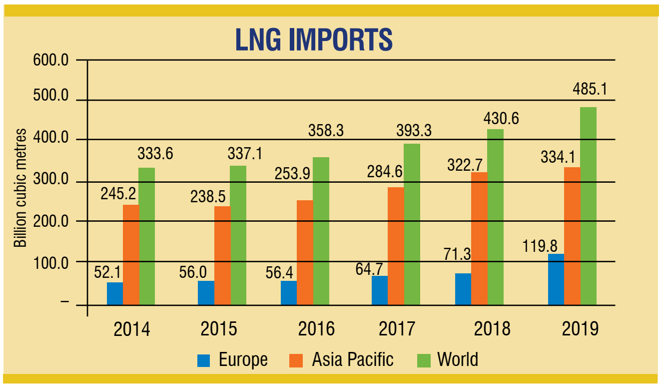

cargoes from USA was witnessed which is usually the cheapest source for gas. The average LNG price for June delivery was almost half that for June a year ago.

Late April and early May, while some countries were starting to ease lockdowns, secondary outbreaks in South Korea and China raised fears that the pandemic may be protracted, putting further pressure on commodity prices. And as lockdown restrictions reduced industrial demand prompted buyers to reschedule long-term LNG deliveries, sellers were left with excess volumes, flooding the market. April also witnessed the worst week for producers/sellers of LNG; a cargo from Australia was available for loading in May at $1.70-$1.75 per MMBtu on a delivered ex-ship basis. Nigeria Liquefied Natural Gas awarded a tender for two June cargoes to U.S. producer Cheniere and German's Uniper; the prices were between $1.10 and $1.50 per MMBtu on an FOB basis. Global demand for LNG remained low, with only few buyers seeking cargoes. Europe became the epicentre of vessels used as floating storage as the coronavirus pandemic severely disrupted gas demand, leading to delays in tanker discharges. Tankers started to pile up off the shores of Europe. Asian spot prices for LNG were dragged further down by a sharp drop in European gas prices and global oversupply. The Dutch market dropped by almost 30%, trading close to $1.00 per MMBtu. The low price globally forced buyers of U.S. LNG to cancel up to 45 cargoes for July loading as delivery became unprofitable, after at least 20 June cargoes were cancelled last month. However, demand from some Asian buyers began to see some recovery.

Signs of Recovery

End May witnessed a slight recovery in Asian spot prices amid easing of lockdown measures in some countries and expectations of reduced exports from the United States this month. The average LNG price for July delivery into northeast Asia increased to an estimated at $2.10 per MMBtu. There were also signs that Indian LNG demand was picking up as the government eased lockdown measures. Moving into summer, China faced with the daunting task of economic recovery.

The average LNG price for July delivery into northeast Asia increased to between $1.85 and $2.00 per MMBtu. The low prices forced buyers of U.S. LNG to cancel up to 45 cargoes for July loading; this was after at least 20 June cargoes being cancelled in the previous month. Since demand from some Asian buyers was recovering, buyers in Asia were taking advantage of low prices and were looking for cargoes for delivery from July onwards. The hot weather in the third quarter drove demand. Prices stayed stable for four continuous weeks with an average of $2.20per MMBtu. Quite a few of the demand drivers came from the Turkey, Pakistan, Argentina and India. In the first week of August, Asian spot LNG prices jumped to a more than four-month high on the back of firmer gas prices in Europe and the United States and with the onset of warmer-than-usual weather in Asia. With an improving market, Asian spot LNG prices rose to more than a six-month high. Consequent to supply concerns, the average LNG price for September delivery into northeast Asia went up substantially to between $3.60 and $3.80 per MMBtu and for October delivery price was between $3.80 and $4.00 per MMBtu. This was for the first time since end-January when prices increased to levels close to $4.00 per MMBtu. Asian spot LNG prices jumped to a multi-month high in late August, although they eased slightly towards the end of the week on expectations of more supply from the United States. The average LNG price for October delivery into northeast Asia rose to about $4.10 per MMBtu.

Supply side Issues

The facility at Australia's second-largest LNG plant was shut since May. In the United States, hurricane Laura halted loadings at export facilities at Sabine Pass, Cameron and Louisiana. And the world's largest floating LNG factory, Prelude of Shell, continued to be shut since February. The recovery in prices since June of this year seems to be largely built on the idling of some LNG output in the United States, which cut the flow of U.S cargoes to Asia. On the Australian front, there have also been maintenance-related shutdowns. In Gorgon, one of the trains had to be

Asian LNG Imports

The Asian Refinitiv data showed 161.8 MMT of LNG was delivered in the first eight months of 2020, up slightly on the 159.6 MMT for the same period in 2019. Since the price recovery started from June onwards, it's worth looking at whether imports increased in July and August, and here the evidence is not convincing.

Asia's LNG imports in August were 19.78 MMT, down from 20.34 million in the same month last year, while July's were 19.33 million, down from 20.29 million in July 2019.

However, two of Asia's main buyers that purchase a greater percentage of their cargoes on a spot basis have been increasing imports. China imported 5.91 MMT in August, up from 5.14 MMT in the same month last year, while its July imports were 5.27 MMT, up from 4.63 MMT in July 2019.

India's imports were 2.19 MMT in August, up from 1.88 MMT a year earlier, while its July purchases were 2.42 MMT, up from 2.04 MMT.

Asia's biggest LNG buyer, Japan, has been relatively steady in its imports, with Refinitiv data showing 6.26 MMT in August, virtually unchanged from 6.29 MMT a year earlier, and July's 6.0 MMT down a tad from 6.4 MMT in July last year.

South Korea, the third-ranked buyer, saw a marked drop in August cargoes to 2.20 MMT from 3.2 MMT a year ago, while July imports were 2.21 MMT, down from 2.96 MMT in the same month in 2019.

However, South Korea's January-August imports are only slightly down at 25.9 MMT from 26.1 MMT in the first eight months of 2019.

Source: LNG Global

shutdown. Supply from Australia and USA was severely impacted, and with an encouraging outlook from buyers, the Asian spot LNG prices rose. The average LNG price for October delivery into northeast Asia increased to about $4.5 per MMBtu in the week ended September 4, an eight-month high and some 143% above the record low of $1.85, reached in two separate weeks at the beginning and end of May.

Asian Markets outperformed:

In Asia, despite the pandemic, volumes have held up, according to Refinitiv data, Asia's imports in the first eight months of 2020 was 161.8 MMT which was slightly up from 159.6 MMT for the same period last year. However, the modest 1.4% rise in the first eight months of 2020 indicates that demand was unlikely to have been the major driver of spot LNG's volatile price movement, rather supply factors too have been driving prices. The commissioning of new LNG trains in Australia, the United States and elsewhere had pushed the market into a supply surplus in 2019, and the coronavirus pandemic clearly destroyed the hopes of a rapid demand growth.

Financing of new projects – A victim of the Pandemic

After the COVID-19 pandemic drove down energy demand and knocked prices to all-time lows, it became difficult to procure financing for new projects. We are yet to see financing of new LNG liquefaction approved this year for the first time in at least two decades. In stark contrast to last year's record level of approvals for LNG production plants, 2020's dramatic oil and gas price drop forced companies to delay decisions on new projects. However, there is still hope that one or two LNG export projects may get the final investment decisions (FIDs). Given the current scenario, the only project with a chance of receiving an FID this year is the Costa Azul export plant in Mexico, developed by US-based Sempra Energy . The outlook elsewhere in North America is not at all encouraging. In 2019 over 21 MMTPA of new US LNG capacity came on-stream and this year more than 16 MMTPA, the huge additional capacity contributed to the global glut. We also saw Shell exiting the 16.45 MMTPA Lake Charles project in the USA.

Hope for the Future

So far COVID-19 pandemic is seen as a short term setback to the LNG demand. The fundamentals of the long term demand remains strong supported by a growing population and energy demand. The economic growth in Asian developing economies is expected to see a steady increase in demand for LNG in the coming several decades. On the supply side, US LNG exports have begun to come on line and continue to increase. The coming winter season (2020-21) could see a modest improvement in global LNG demand compared to the previous winter season. However, the possibility of a second wave of the pandemic could dent the gas demand again.

With the world seeking cleaner energy sources to reduce pollution and CO2 emissions, gas and LNG are expected to provide the impetus for a cleaner and clearer environment. LNG is and will remain a high-growth industry based on a growing economy worldwide driven particularly by Asia. The LNG industry is forecasted to grow in the next two decades. As the demand for natural gas grows and more LNG comes on-stream, traditional LNG trade flows and pricing will continue to be challenged. More importantly, the increasing appetite for spot LNG and transitions in pricing structures are likely to have significant positive impact on global LNG markets.

Acknowledgements:

1. LNG Global/RefinitivData

2. energy.economictimes.indiatimes.com

3. www.hellenicshippingnews.com