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Changing Patterns During 2017 Give Reasons for Optimism for Development of More LNG Projects

By Andreas Silcher

There have been significant new developments in the liquefied natural gas sector, which support the view that we are about to enter a golden era for liquefication projects.

First, global demand is supported by continuously low LNG prices and high availability. Around fifteen new projects are expected to come online worldwide in the next four years, and existing supply is returning to market following planned or unplanned downtimes.

Output

Global production is forecast to reach 292 million tonnes in 2017, marking a significant increase of 34MT compared with 2016.

Secondly, there is huge potential for gas in markets such as China, the world's largest consumer of energy, with the Chinese government targeting 15 percent of all energy use from gas (currently the number stands at 6 percent) by the end of the next decade.

China is also forecast to overtake Korea as the world's second largest LNG import country. Meanwhile, Africa has already seen its first final investment decision (FID) of 2017 with Italy's ENI agreeing to develop a floating LNG unit in the Coral South gasfield offshore Mozambique with 3.4 million tonnes per annum of capacity.

ENI's Coral joint venture is billed as the world's first ultra-deepwater floating LNG project.

The Fortuna floating LNG in Equatorial Guinea, whose investors include companies such as Ophir Energy of the UK and Golar LNG, was also set to announce a positive FID.

Imports

Europe will also increasingly look to import LNG to help meet the growing gap caused by the decline in domestic gas production.

Other markets in the spotlight are India and Singapore, the latter aiming to become Asia's LNG trading and bunkering hub where large cargos can arrive and be broken up for regional distribution by smaller vessels.

All this is of course good news for the LNG carrier market, which has suffered under painfully low rates for the past two years.

The clear expectation here is that new LNG production Trains will help improve fixture activity and reduce idle time, which should result in more sustainable rates in the spot market.

Another significant development for the LNG shipping sector is the severance of diplomatic relations between Qatar, which last year produced nearly one third of the world's total LNG, and its neighbours.

Impacts

While it is still difficult to predict with certainty what impact this might have on LNG shipping, it is likely that inefficiencies caused by cargo diversions due to the blockade may soak up some of the tonnage oversupply in the spot market, which should have a positive impact on rates.

New projects and a tightening spot market should also help end the current dry spell for LNG carrier orders, which would bring some relief to the battered Korean shipyards.

Recently there have been plenty of “firsts” in the LNG ship sphere: the “Engie Zebrugge”, the world’s first LNG bunkering ship, delivered its first LNG bunkers when it completed a ship-to-ship transfer, loading gas as marine fuel on two car carriers.

Additionally, the “Christophe de Margerie”, the world’s first icebreaking LNG carrier, has been delivered to its owners Sovcomflot of Russia to work on the Yamal LNG project being completed by Novatek and its partners.

Hyundai Samho Heavy Industries has, meanwhile, received an order to build the world’s first four LNG-fueled Aframax tankers, scheduled for delivery in the third quarter of 2018.

Malaysia

And finally, the world’s first floating LNG (FLNG) production project is now live with the first commercial cargo having been loaded from the “PFLNG Satu” offshore Sarawak for Malaysia’s Petronas.

However, the current buzz is largely about smaller (import) markets and how to penetrate them.

Smaller-scale projects appear increasingly attractive to many observers in light of the pressure which low LNG prices have put on the profitability of large projects.

Peter Coleman, Chief Executive of Woodside Petroleum, the operator of two export plants in Western Australia, said that emerging market demand this year would increase from 5 percent of total LNG demand today to more than a quarter of the total by 2025.

This is leading to the development of a functioning relationship between large and small-scale LNG projects, an interface that will be an increasingly important aspect going forward.

Emissions

It is further helped by tighter regulations for emissions from ships, which make LNG an important alternative choice of fuel as it contains virtually zero sulphur.

Marine bunker solutions have the potential to soak up significant supply. In addition, policymakers globally are choosing gas for its critical role in reducing pollution.

Other small-scale opportunities include LNG fuelled buses (the first service has been launched in India) and “retail” ideas such as selling LNG in small mobile containers to commercial or even large domestic customers who currently rely on diesel in regions with poor power infrastructure.

Finally, Jamaica, which joined the growing group of LNG importers recently, is set to brew its iconic Red Stripe beer using LNG, after its brewer concluded a gas-supply agreement with a US-based supplier.

Another interesting development is the numerous gas-to-power projects with regasification on site under consideration in Africa.

In particular in West Africa, several power plants are running below capacity or are idle due to either insufficient supply of gas through pipelines, or because the diesel with which they are fuelled is too expensive.

Incentives

These come with risks, but there are large financial incentives and these projects are interesting customers for companies with existing gas interests in West Africa.

For this new era of LNG to be truly successful, the interplay between small and large-scale LNG is becoming ever more important, and solutions will need to be found.

The big names in LNG will have to do everything they can to develop sufficient supply infrastructure on a smaller scale, e.g. in the bunker market to support the growing number of LNG-fuelled ships and price gas as competitively as possible to support this new demand.

As is often the case when existing markets enter a stage of further development, established contractual terms are likely to be put to the test.

In the context of the situation in Qatar for example, ship owners will want to establish whether their charter parties include provisions specifically addressing blockades.

The numerous developing LNG markets might mean contractual counterparties which are not as sound as the traditional oil major-backed LNG project.

Guarantees

In light of this, performance guarantees and contractual default provisions should be very carefully drafted to ensure they provide the innocent party with appropriate remedies should the other party no longer be willing or able to fulfil its obligations.

Looking even further into the future, one wonders how the steadily increasing LNG demand will be met post 2020.

What cannot be in any doubt is that significant investment will be needed.

Moody’s Investor Service, on the other hand, forecasts in 2017 is that strong LNG demand growth from China, India and new markets would not be enough to absorb the fresh supply capacity coming online.

They forecast that the market would not rebalance until the early years of the next decade, when global demand and LNG import infrastructure catch up with supply.

The caution noted post 202 for the growth in the LNG market is a prudent one. Until then, the LNG industry should be cautiously optimistic, as globally the increasing demand for LNG as a more sustainable form of energy looks set to continue with the development of smaller markets.