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TPLNG Outlook

LNG’s Prisms

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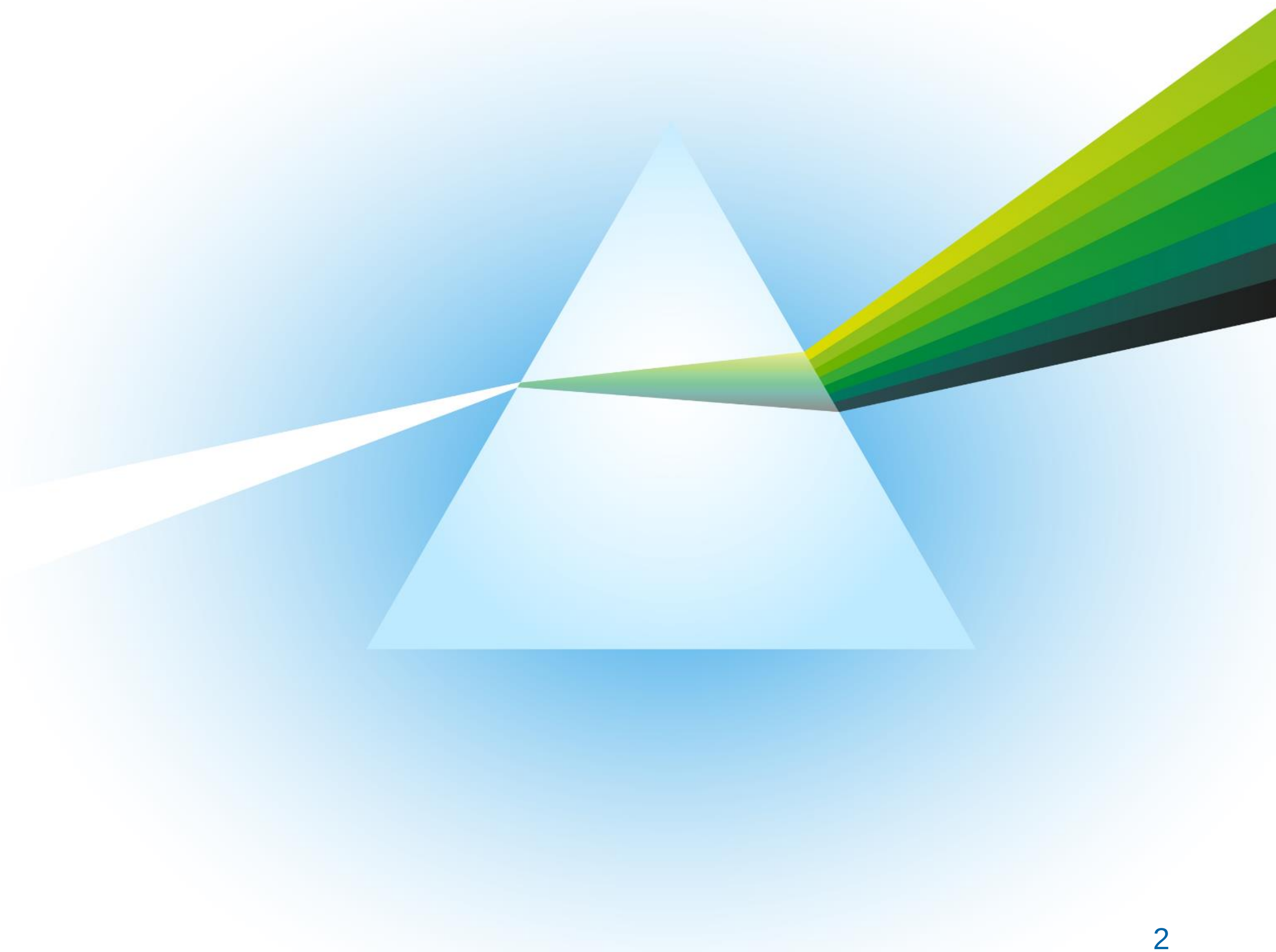
Introduction

Prisms can have many faces, they are transparent and they disperse light.

Can they help decipher what's happening in the Global LNG business right now?

Well it depends on which prism you look through! – ie the producer prism, the portfolio player's , the trader's , the buyer's prism etc.

In this edition we look at prisms emerging from the Japanese Producer Consumer conference held in Tokyo in October. This brought several large industry players together to discuss the outlook for imports into Japan and the wider Asian region. And we review the IEA's latest publication of their Global Gas Security review, which strives to give an objective overview of industry trends.



Executive summary

October 2020 was a month that all 'shorter term' market participants will remember for a long time to come. Record breaking price moves in both Physical and Paper markets created shock and awe as a barrage of end November and early December shorts came to market at speed and in aggressive fashion. What this did was flush out a larger pool of shorts, specifically in the Far East, who ended up clambering over each other to try and secure supply, bidding up the price and creating high levels of anxiety. It was a sight to be seen, as the paper market rallied hard day after day, from the front of the curve even out to Sum21 and bullish sentiment ran high. By the last week of October, reality struck and the market fell back down to earth…shedding 5 weeks of gains in 1 week. Thank you winter!.

TPLNG Global look back September 2020: LNG SUPPLY was UP 0.74Mt (2.7%) compared with August 2020 , mainly due to higher USLNG and Australian production (2Mt).

The USA with all its cancellations year to date is up 9.6Mt in volume (+40%) compared to last year. The largest reductions in LNG supply for Jan-Sept 2020 yoy were in Egypt and Malaysia which reduced output by 2.1Mt and 1.6Mt respectively.

LNG DEMAND: Asia imports were up 3.6Mt (+2%yoy). Japan remains the largest importer year to date at 54.7Mt. China is up 3.9Mt yoy to 47.4Mt and India is up 2.5Mt yoy at 19.5Mt. Europe's imports were up 5.9Mt (+9.4%) yoy.

All in all this is a good performance volumetrically. Margins have been impacted, particularly in Q3 for time lagged oil indexed term contracts. This is featuring in several companies' Q3 profit warnings.

TPLNG Cumulative 2020 YTD and full year outlook: Jan-Sept 2020, global sales reached 270Mt , up 6.9Mt yoy. Expect growth around 10Mt this year to about 367Mt if current trends continues.

LNG outlooks: This month we present some different perspectives from the recent **Japan Producer Consumer conference** and from the IEA's new report on the Global Gas Security review 2020. Buyers are clearly striving to control their costs and maximise flexibility that can be negotiated in new LNG supply deals. Japan, as the largest global importer is made up of several utility companies managing a deregulated competitive downstream market. Add in Covid-19 uncertainties on demand growth and also new policies to support Energy Transitions and you can see why Japanese demand forecasting is more difficult than ever. Ongoing profitability is not a given any more for Japanese utilities and it seems inevitable Japanese companies will have to re-engineer their commercial contracts and make them more market responsive.

The IEA's Global Gas Security review provides evidence that the global business is holding up in volume terms, but gives no indication as regards to the margins and the value outlook for the global business. It sets out a scenario for gas demand to rebound in 2021 supported by fast growing Asian and Middle East markets. This presumes Covid-19 is brought under control – and conceded the recovery will be drawn out if that is not the case. In 2020, it points out that LNG investments have dried up and LNG contracting activity has only been around half of 2019 levels. It states that about 1/3rd of active term contracts will expire by end 2025 – which is about ~200bcma/140Mtpa – and sees the trend of more flexible contract structures and more diverse pricing structures as likely to continue. But the report stops short of saying how much of the global LNG business it expects to be transacted spot and short term. It does state that oil indexation is losing ground in pricing LNG and that by 2025 it forecasts it will fall from 70% in 2018 to a level of just over 50% by 2025 in LNG contracts.

In this edition

Section 1: Spot

Section 2: Look back Jan – Sept 2020 and look forward full year

Section 3: TPLNG insights

Section 4: IEA's latest views on gas

Section 5: And finally…

TPLNG outlook

Sentiment: Neutral/Bullish

Can we get off this rollercoaster? The global LNG market experienced record breaking price moves in October, with Far East physical AND JKM paper prices moving in excess of 40c – 50c within a 24 hour period (16th of October) as extreme tightness in H2 NOV and H1 DEC saw a rapid jolt higher on aggressive MOC bids. As we witnessed a raft of renewed buying from Korea and China throughout the month, what became apparent was the continuation of supply shocks that have rattled the market for the past 6 weeks+ created an acute environment whereby every short over the succeeding 3 months started to rear their head. Things got messy as buyers were chasing down any offer they could get their hands on, aggravated by a backlog building in the Panama Canal and uninvited guests blocking the pathway to Cameron and Sabine terminals. These were a sunken oil rig and boat + submersible rig from the Hurricane season. The wind in the LNG sail ended abruptly as once the shorts were cleared, it took the market 5 days to erase 90c of value on the JAN JKM contract which is a 13% move. On a mark to mark basis, this is unprecedented and has proven that the old adage 'LNG can always surprise' holds true. The question we ask now is whether his has set precedence for the balance of winter or is the panic now behind us?

Supply and demand, hang on… what about the weather? It is quite remarkable how quickly the landscape of a market can change in the face of immediate prompt tightness. As counterparties appeared to remain short in the early winter driven by softer demand expectations in light of Covid-19, the market is now starting to qualify what surprises may present themselves for the balance of winter. Strong demand from all buyers across the Far East is something that took the market by surprise, as demand bounced back fast in China and hot weather / inventory draw in Japan brought out renewed interest. As Covid 19 cases have subsided in Asia (vs that in Europe), expectations for at least a partial continuation of demand across the region look to be slowly priced in. Differentials and netbacks favour the East, whilst big question marks around coal to gas switching and weather continue to imply some bidding premia. The rationalisation of this notion is also being supported by the supply challenges witnessed over the past 6-8 weeks, notably Gorgon which although is expected to bring T2 back before the end of November, can be unreliable in peak Australian summer… perhaps even more so when undergoing repairs. The counter argument to all this is the most bearish of recent news, which is the recent reinstatement of lock downs across the UK, France and Germany. There is no hiding the fact that is a significant setback for the region and will weigh on sentiment for the next month plus. However, this lock down isn't as tight as previous actions and with a significant amount of people still going to work, AND heating their homes as they work from home – optically, the profile is different.

The conversation of weather comes up around this time **every** year, and the reality is it's remarkably difficult to predict and is one of the most challenging variables to trade for / or against. La Nina is pointing to a colder Northern Hemisphere this year, with preliminary runs for Japan and Korea pointing to a slightly lower temp v average (for now). Anything at par or below, participants anticipate some underlying support for LNG. Mind you, with 2020 DQT maxed by most buyers, Q1-21 may see a limited number of incremental bids.

Macro, Macro oh Macro – when will it end.? Trump v Biden has turned into one of the most divisive elections in modern history. With expectations that we may not see a clean result for days, if not longer. Anxiety is high and volatility is abundant. Adding European lock downs, trade tensions and the hit to global earnings into the mix, we are living in a unique time in history whereby all of us will be affected in one way or another. For LNG, the most apparent impacts we see today and that will impact us into November and December is the scale back in demand from Europe, a spike in slopes from the front to the back of the curve and heightened uncertainty on how the demand profile will re emerge post pandemic. What is becoming clear is that the LNG growth story remains intact, however most supply and demand forecasts have been turned on their heads, therefore Winter, 2021 and beyond is looking hazier than we've seen previously.