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For US LNG Export Industry, Price Shock Serves as Stress Test

While last week's gas market surge created some unease among proponents of US LNG exports -- which rely on sustained price discounts to European and Asian markets -- the immediate implications on LNG trade and investment appear minimal. But that could change if the spikes and volatility continue.

The recent gyrations are sure to give some pause to the several US LNG project developers whose final investment decisions (FID) are expected next year. And it has already raised concern among domestic gas users about the Trump administration's stepped-up campaign to find foreign buyers for US LNG.

Combined with other potential factors that could delay some FIDs -- including the ongoing tariff war between the US and China -- a winter of high US gas prices certainly won't speed up the decision-making process.

But while short-term price movements always inject new information for project developers and policymakers to consider, they won't do much in isolation to slow the second wave, said Kenneth Medlock, energy and resource economics fellow at the Baker Institute at Rice University.

Even if higher prices and volatility were to become the new normal, it doesn't mean LNG export capacity doesn't get built, Medlock said. Rather, it sets up a scenario in which gas may be released back into the US market when domestic prices jump instead of being loaded on an LNG vessel, acting like a storage withdrawal to meet short-term demand.

"Moreover, the argument that LNG exports will raise volatility only holds if one assumes export volumes are fixed and new domestic supply is not price-responsive, which is not the case currently, nor will it be as long as there are profitable opportunities to sell gas in the US market," Medlock said.

Tellurian President and CEO Meg Gentle, whose company is planning a large export facility on the Gulf Coast, also did not appear concerned.

"US natural gas prices are highly dependent on weather and local supply and demand," Gentle said in a statement provided to Energy Intelligence. "LNG buyers will experience price spikes from the US unless they own the reserves and can manage their own cost of supply."

She noted that Tellurian's proposed 3.9 billion cubic foot per day Driftwood LNG project "will own reserves and eliminate exposure to weather-driven Henry Hub settlements."

A cold US winter also serves as a useful stress test to assure LNG buyers of the likely maximum US gas price they might encounter over a 20-year supply contract -- a point Morgan Stanley highlighted in a report last week.

US LNG exports are expected to continue, despite near-term natural gas pricing headwinds," the investment firm said. "We see limited risk that higher near-term Henry Hub prices [will] impact US LNG exports since offtakes are highly contracted, liquefaction fees are viewed as sunk costs, and shipping capacity has already been secured."

Morgan Stanley did note, however, that a sustained Henry Hub price of about $4 per million Btu would narrow export economics to Europe, although arbitrage to Asia would still be workable at that price.

Another industry participant told Energy Intelligence that everyone should stay calm as early-season cold snaps and dramatic market reactions to them are not a new phenomenon.

"This price spike is very short-term, only impacting Henry Hub pricing and LNG export economics in the next few winter months," said Akos Losz, senior research associate at the Center for Global Energy Policy at Columbia University. "I don't think it will have any implications beyond this winter."

The arbitrage window for selling LNG overseas "would have to be closed for some time" before export projects or cargo shipments were halted, he said.

Losz is more interested in whether US gas destined for LNG exports "can be redirected back into the domestic market on short notice, if the economics would justify." US LNG market participants are going to find out "how flexible the system actually is."

Similarly, Medlock said historical analysis indicates that volatility accompanies cold weather, and lower-than-average gas storage inventories like the US is seeing today heighten the severity of those episodes. But myopia tends to creep into these matters, he added, saying such fluctuations are needed to send proper signals to the market for investment planning and decision-making.

But alarms continue to come from domestic gas users who have been warning of a price shock like the market has seen this month. "Spiking prices are symbolic of troubles ahead for US consumers," said Paul Cicio, president of the Industrial Energy Consumers of America.

"National inventories at 16% below the five-year average and over 15% below a year ago," he told Energy Intelligence, means producers can't keep up with existing US and export demand. And that is with only two export terminals operating.

"It raises enormous concerns by manufacturers as to what will happen to prices of natural gas and gas-fired electricity this time next year when four more LNG export terminals are operating," said Cicio, whose group has long advocated for the federal government to limit gas exports.

"The major LNG importing countries have winter when we do. They pull down our gas inventories when we need it most, potentially causing price spikes," he continued. "At large, this is bad news for want-to-be exporters. Financial risk and the potential for government regulatory intervention just went up."

Michael Sultan and Bridget DiCosmo, Washington