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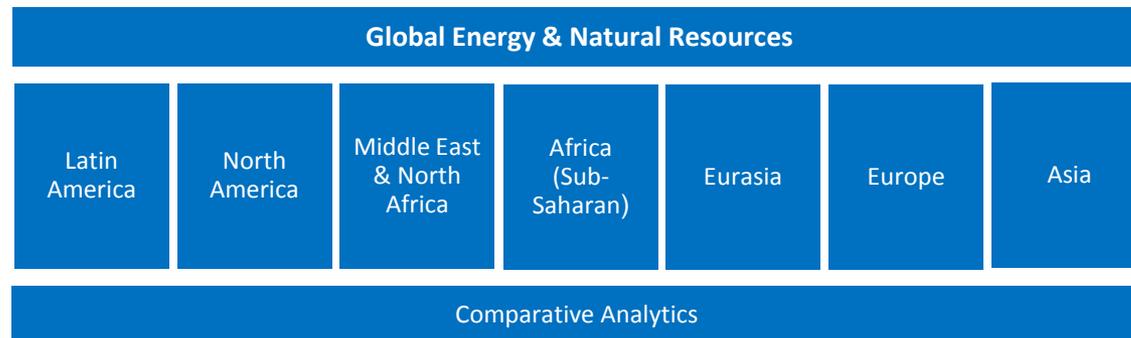
US LNG in the global gas market: risks and opportunities

August 19, 2014

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The US will impact global gas trade in 5 areas

#1: More upside for US LNG exports, positioning the **US as world's top 3rd LNG exporter by 2020**

#2: The **US pricing factor is a game-changer**, giving new pricing exposure for Asian buyers

#3: Competitive threat from **US LNG will undercut rivals, notably historical and established producers**

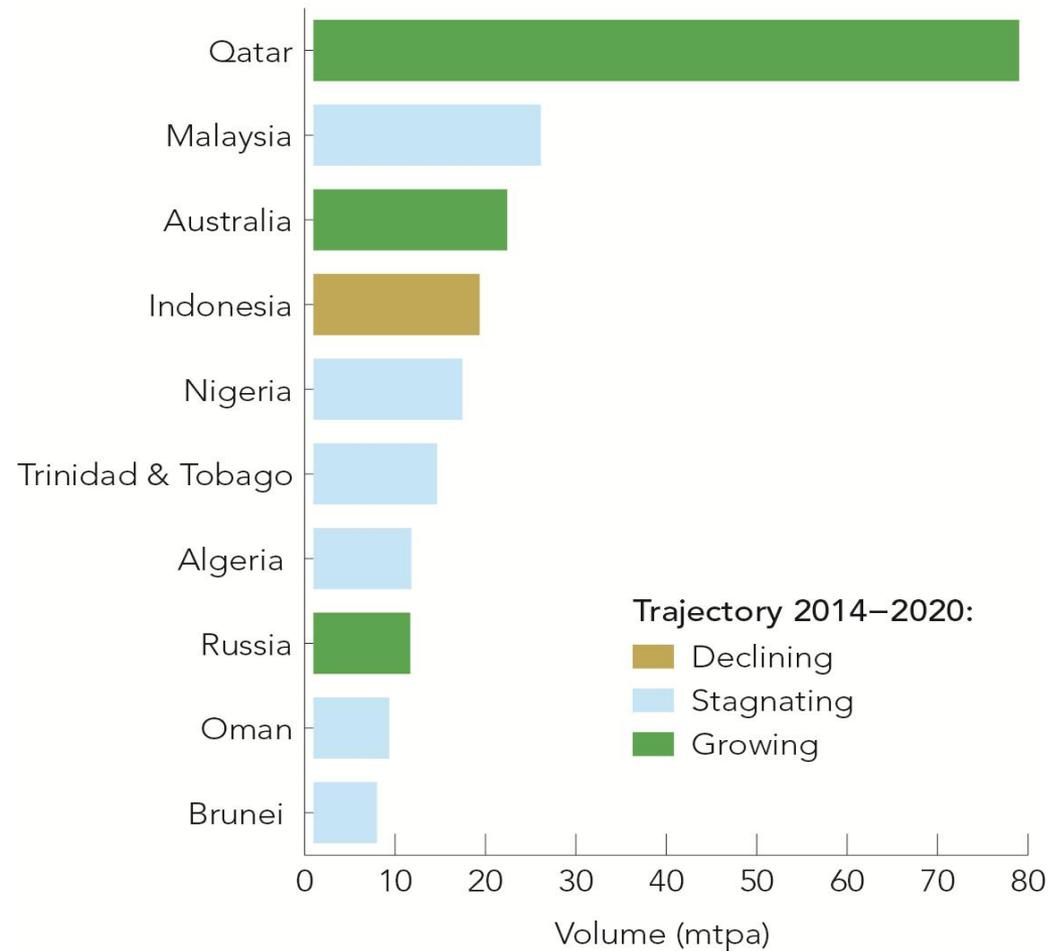
#4: **Flexibility of US LNG contracts will encourage more liquidity and interconnectedness** in the global gas market

#5: **The “gas weapon” will be less relevant**, notably in European geopolitics

#1: The US has the potential to become world's top 3rd LNG exporters by 2020

- The approval of non-FTA LNG export projects is becoming largely depoliticized allowing more upside for US LNG exports
- Recent DOE changes to do away with pre-approvals will streamline approvals to the benefit of more serious projects
- Risk of a pause in approvals is lower – political momentum behind LNG exports to counter Russian aggression in Ukraine
- Market conditions will be main limiting factor for US export capacity, but possible upside beyond 6-8 bcf/d scenario early next decade
- In the context of global gas markets, this level of exports places the US third in terms of export volume, with Australia and Qatar set to remain the world's two largest exporters of LNG.
- 73 million tons of US LNG are already committed, and nearly a third of these bound to Japanese buyers.

Top ten LNG exporters in 2013



Source: Eurasia Group research, GIIGNL

#2: The North American pricing factor is a game-changer

- For Asian buyers, US LNG will diversify their pricing exposure and maybe reduce their fuel import bills
- The prospect of US LNG exports, has improved the bargaining position of European and Asian importers
- Prospects of US gas exports are already putting pressure on the pricing formula of several existing long-term contracts, and also shaping the pricing for new projects that will come on line later this decade
- But the evolution of global gas prices away from oil indexation will be slow-moving and achieved only in incremental steps, especially In Asia

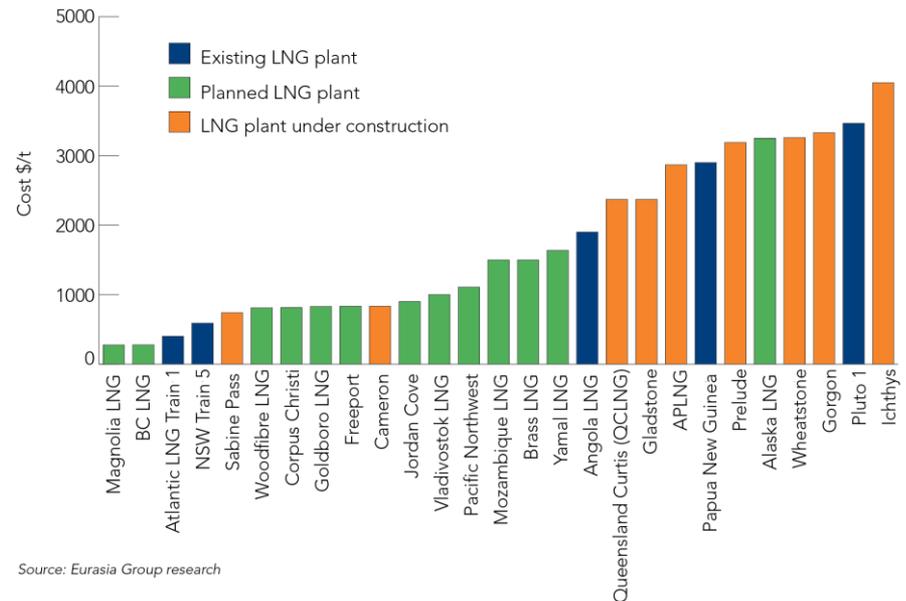
Milestone events illustrating pricing evolution worldwide (timeline)

2009	 Exporter: Statoil, Gastera Buyer: European customers	Statoil and Gas Terra introduced up to 30% spot indexation
2010	 Exporter: Gazprom Buyer: Germany, France, Austria	Gazprom accepted 15-20% spot indexation
Feb 2010	 Exporter: GDF Suez Buyer: Pakistan	Pakistan signed a six-year contract with GDF Suez incorporating linkage to HH alongside oil indexation but Pakistan's Supreme Court canceled the deal
Apr 2010	 Exporter: Stream Buyer: India	India's GSPC signed a contract for nine cargoes which was the first multicargo deal based on HH benchmark signed by an Indian buyer
Oct-Dec 2010	 Exporter: Cheniere Buyer: BG, Gas, Natural, Gail, Kogas	The volumes of Sabine Pass liquefaction plant are linked to HH prices plus a fixed premium
2012	 Exporter: BG Buyer: CNOOC	The deal has a hybrid pricing structure with 70% oil-linked and the rest tied to HH
2012	 Exporter: Gazprom, Sonatrach Buyer: European customers	Various arbitration cases in Europe turned in favor of the gas utilities as oil-linked gas prices are too high
Oct 2013	 Exporter: Novatek Buyer: CNOPC	Yamal LNG sold 3 mtpa at an estimated slope of 12.2% plus a high fixed premium
Nov 2013	 Exporter: Novatek Buyer: Gas Natural Fenosa	Yamal LNG sold 2.5 mtpa linking supply to prices at the UK's NBP gas hub and Brent crude oil at a 12% slope
Nov 2013	 Exporter: Qatar Buyer: Asian buyers	Qatari are offering medium-term deals priced at 13.5% slope, while their long-term price is more around 14.6%

#3: Competitive threat from US LNG will undercut rival projects

- Competition to build new projects is becoming tougher
- The more bullish prospect for US LNG will test the prospects for projects in other jurisdictions
- 2014-2015 will be an important year for final investment decisions (FID)
- High costs will come up against growing consumer pressure for more competitive pricing as US Henry-Hub linked LNG shakes up traditional oil-linked price structures
- Suppliers that show willingness to adjust prices will be better placed to capture market share as more abundant supply options come on line
- **TIMING IS CRUCIAL**

Global LNG construction cost comparison



Source: Eurasia Group research

#4: Flexibility of US LNG contracts will encourage more interconnectedness in the global gas market

- The destination of US LNG will be the highest-paid market, not necessarily Asia
- The nature of US LNG, clause-free supply, makes it very flexible, easily sold on the spot market, and easy to trade bringing more liquidity into the market
- The arbitrage between regional markets will subsist but will be reduced from the current spread of \$6 between Asian and European prices and \$13 between Asia and US prices
- The gas market is heading toward a normalization of prices in Asia, which are recovering to pre-Fukushima levels based on structural demand and supply changes

#5: The “gas weapon” will be less relevant, notably in European geopolitics

- US LNG will improve Europe’s security of supply. Europe will rely more on US LNG as a supply option, especially during emergency crisis.
- European utilities are more likely to match Asian premiums only in the event of crisis or supply-side disruptions from Russia, Algeria and other suppliers.
- For now, Qatar remains the world’s favored swing supplier, go-to-emergency supplier, shipping 10%-15% of its volumes under spot transactions. But the US will likely assume this role and in a more transparent manner, within a few years.

TAKEAWAYS

- The shift in gas geopolitics would have happened eventually, but it could have taken a long time without the US energy revolution.
- Recent changes in global gas trade flow, pricing, and the influence of gas on politics confirm that the gas market will be very different from the one that has existed in recent decades.
- The US's gas advantage has created new foreign policy opportunities for Washington, with implications for both allies and adversaries.
- The US ultimately has the potential to become the world's swing producer, while US Henry Hub–linked contracts could have a transformative impact on global gas pricing.
- There is potential for gas to become more like oil, which can disrupt national economies when resource rent falls, or positively transformative such as when it generates development and economic growth. And the US will be a big part of this unfolding story.

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