Gas Strategies
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Lifting US LNG ‘may become the exception, cancellations the norm’ – Gas Strategies

With European gas hubs languishing below US benchmark Henry Hub and Asian LNG spot prices offering only a tiny margin, lifting US LNG cargoes could become the exception and cancellations the norm, according to a stark assessment of today’s topsy-turvy gas market by Gas Strategies.

The remarkable shift [1] in gas prices on either side of the Atlantic is giving a new, unintended purpose to tolling contracts and sales and purchase agreements (SPAs) with US liquefaction plants, the consultancy said in a blog post [2] this week.

Thanks to their flexibility, these contracts are inadvertently becoming the go-to means of balancing the extremely oversupplied global LNG market – but at huge cost for the contract holders.

“What if we have entered a world where, during sustained periods of oversupply such as we are seeing at present, prices dictate that cargo cancellations from the US become the norm and lifting cargoes the exception?

“US LNG tollers and buyers may be left holding an extremely expensive de facto market balancing mechanism which was never planned to be the case,” the blog states. “US offtakers have effectively found themselves holding extremely expensive call options.”

Prices may rebound with seasonal demand over the winter, but this is still months away. In the meantime, those lifting US LNG are facing a USD 500 million bill [3] for cancelling a wave of cargoes – estimated to total 45 in number – that were due for lifting in July.

The blog raised doubts about “future appetite” of companies to commit to US LNG based on Henry Hub pricing “now that the reality of potentially large capacity payment losses has been seen”. This has clear implications for greenfield LNG export projects that need to pre-sell volumes under long-term binding commitments in order to leverage construction finance.

Numerous US LNG projects have been delayed in recent weeks and there is a growing risk that, without more clarity over the pace and sustainability of the global economic recovery and renewed interest in buying LNG from the US Gulf, they could be shelved indefinitely or even quietly abandoned.

The situation also raises serious considerations for how LNG market players manage US contracts, “both on a standalone basis and in the context of a wider portfolio”. Gas Strategies questioned whether a “mindset change” would be necessary to view US capacity as a viable option “only in a high demand, high price market”.

“Would this view, at least in the short-term, require a change in approach to hedging and risk management? A traditional US hedging approach has been to buy Henry Hub and sell Brent. However, as JKM and LNG spot prices in general continue to decouple from oil, is this the correct approach?” the blog asserts.

Many US offtakers chartered vessels on a long-term basis to lift free on-board (FOB) volumes. These charter holders will be asking themselves what to do with this shipping length. “Do organisations have the capability to monetise vessels via the spot market, and does the reward exist to do so?” the blog asks.

Gas Strategies sees decisions not to lift cargos from US liquefaction capacity and “other available mechanisms” as being a mainstay for the LNG industry for the remainder of 2020.

Beyond that, there are more optimistic signs, namely a recovery in Chinese LNG imports, coal-to-gas switching in South Korea spurred by low oil-indexed LNG prices, and buoyant LNG imports in India, Bangladesh and Thailand, again drive by low prices, it adds. - SK

Read in full Gas Strategies’ latest blog: Swing state: Flexible US LNG squeezed out to save the market [2]
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Photo: GAIL lifting its first LNG cargo from Sabine Pass in 2018 (credit: Cheniere)

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