

## LNG to remain under pressure

The liquified natural gas market has been under pressure this year as a ramping up of export capacity and slower demand growth in Asia led to a surplus environment. For 2020, we expect a similar picture, with a further increase in supply projects



### The state of the market

The market is still struggling to digest the glut of LNG that we are currently experiencing. Asian LNG prices have been weak for much of 2019, as we continue to see a ramp up in supply from the US, Australia and Russia. The autumn rally that we have seen has been short-lived, with the market under pressure once again even as we move into winter. The pressure on Asian prices has also had an impact on hubs in other regions, with record volumes of LNG making their way into Europe this year. We expect much of the same for next year, with supply expected to ramp up further while there will still be questions about the demand outlook, particularly given concerns over slowing growth and contracting factory activity.

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*Pressure on Asian prices is impacting hubs in other regions*

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The gap between LNG supply and demand growth has widened in 2019, with demand unable to match the pace of supply we are seeing at the moment. Global LNG supply has increased by around 30-35mt in 2019 with most of this coming from the US, Australia and Russia. We believe that another 30mt of LNG supply could be available to the market in 2020 as capacity start-ups in 2019 (including Cameron T1, Elba island and Freeport T1) continue to ramp up while new projects (including Freeport T2-3 and Cameron T2-3) come online over the course of 2020.

## Weaker demand prospects possible in the short term

China's LNG imports have increased by 14% year-on-year to 47.74mt over the first 10 months of 2019, healthy growth by any standard. However, this masks some concerns. This level of demand growth is much lower than the 30%+ seen in recent years. In addition, LNG imports in the month of October fell 11% YoY- which is the first YoY decline in LNG imports since July 2016. There are a number of reasons why growth has slowed. Previous growth rates were unsustainable and largely reflected the coal to gas switch for home heating. We've also seen a slowdown in manufacturing activity in the country, which has likely weighed on demand.

There are two lingering concerns we have over Chinese LNG demand in 2020:

- If manufacturing activity does not pick up, this could continue to weigh on import demand. Manufacturing activity is going to depend largely on whether we see a convincing trade deal between the US and China.
- Recently, the Power of Siberia pipeline from Russia to China has started up, and we are likely to see increased flows of piped gas into China, which could weigh on LNG flows. While the pipeline is expected to transport as much as 38bcm annually, this will take some time, and over 2020, minimum flows via the pipeline are expected to be 5bcm.

The largest LNG buyer has also disappointed this year. Japanese LNG imports have fallen by 8% YoY over the first ten months of the year, following a 2% YoY decline for full-year 2018. A key driver behind this decline has been the restarting of nuclear capacity in the country. As we see further reactors coming online, this has the potential to weigh on import demand even further over 2020.

## Europe & LNG

With another surplus year expected for the LNG market, and assuming similar trends in the Asian market once again in 2020, it appears that we'll continue to see sizeable LNG inflows into Europe. As things stand at the moment, this supply is likely to keep the pressure on European hub prices. However, negotiations around the Ukrainian transit deal for Russian gas, which is set to expire in January, present a key upside risk for the European market.

Failing to come to a new deal will be a bullish development for the European market. The Russians are reluctant to provide another 10-year transit deal, with new pipelines set to connect with European hubs- including the 55bcm/year Nord Stream 2 pipeline, which could start operations in early 2020.

## Bullish in the longer term

The scale of supply growth we have seen in LNG has led to the market evolving fairly quickly, with an increasing shift towards short term and spot supply contracts. As supply grows, we would

expect this trend to continue. However, a low price environment and more uncertainty with spot contract pricing create longer-term issues for the global LNG market. The current low price environment means that investors may think twice before looking at new supply projects whilst the trend towards spot contracts may also mean that projects struggle to get the financing as easily as they have in the past.

This leaves the longer-term outlook for LNG constructive, particularly with a constructive demand outlook for natural gas, given its role in energy transition. However, before the market reflects this more constructive environment, it will have to deal with the current mismatch in supply and demand for the next couple of years.

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