The Geopolitics of East Med Gas: Hyped Expectations and Hard Realities

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Rapidly Changing Regional and Global Context

- The context surrounding East Med gas has fundamentally changed since a few years ago in terms of geopolitics, gas market fundamentals, market structure, pricing structure,   & challenges facing oil & gas industry

- Discuss these in context of Europe, why Europe? East Med gas is presented as one of the ways for Europe to diversify its supply sources away from Russia.

- Often argued that East Med gas hub can bring the regional countries closer together as the gas dividends are large

- But how convincing are these arguments?

Trump team is adopting a pipeline plan to wean Europe off Russian fuel

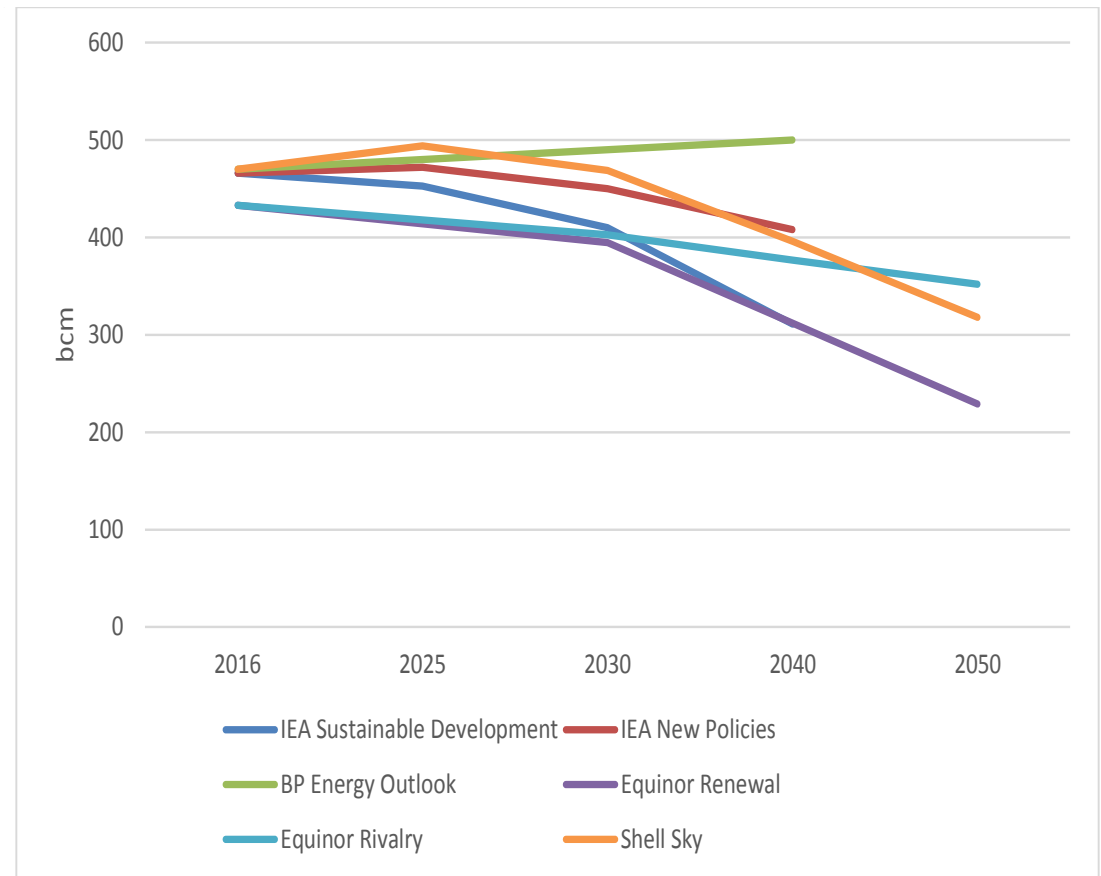BY MICHAEL WILNER
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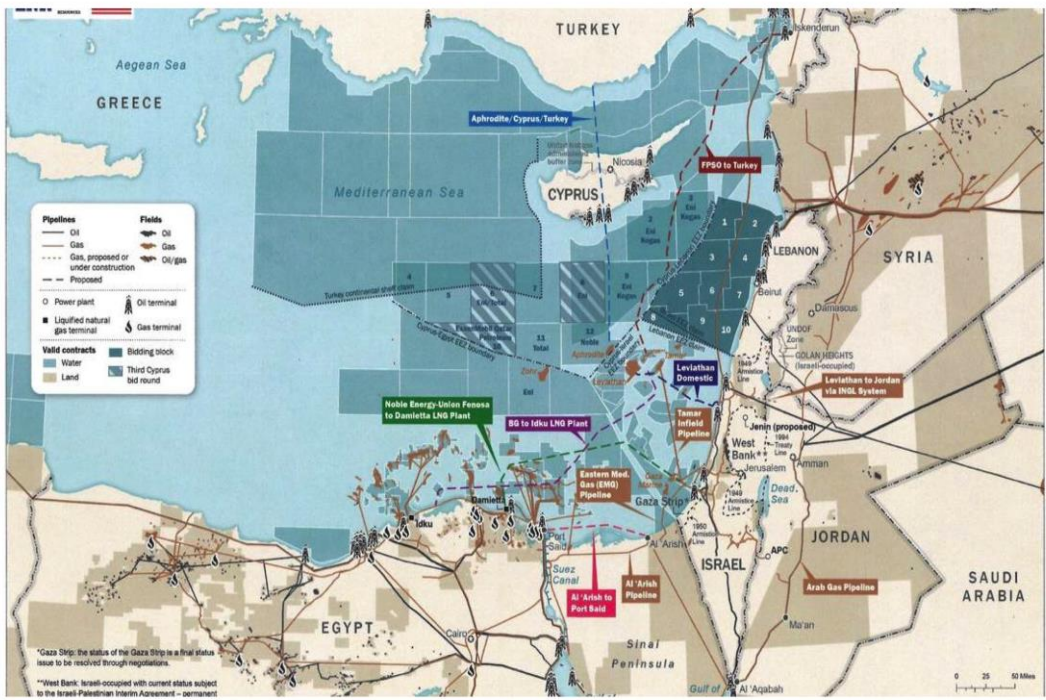
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Key Transformations in Global Gas Markets

- European market fundamentals have become highly uncertain both on the supply and demand side

- Europe will be the sinking ground for gas while demand is expected to increase marginally or flat-line in the 2020s.

- In a liberalised & globalised LNG market, there is reluctance to sign 20-25 year contracts; old days of financing and shifting risks towards consumers are gone. Financing new greenfield LNG projects becomes more challenging.

- Oil price-linked contract disappearing; hub prices are the 'market price'; sellers get netback from hub and take risk.

- Pipelines have become very difficult due to geo-politics and transit costs; very few <u>major new</u> pipelines – other than Russia to Europe and Asia – are likely to go ahead any time soon. LNG projects will dominate future gas trade.

European Union: gas demand projections to 2050 (bcm)

Legend:
- IEA Sustainable Development
- IEA New Policies
- BP Energy Outlook
- Equinor Renewal
- Equinor Rivalry
- Shell Sky

Sources: IEA (2018), pp.550-551. BP (2018), p.54. Equinor (2018), p.57. Shell Sky Scenario.

What Do These Trends Mean for East Med Gas?

- New area with limited reserves and relatively higher cost of production (compared to Qatar or Russia or the US)

- Low gas prices in Europe mean that costs of new LNG projects at around ~$5-$6/Mmbtu may be too high for many markets.

- Profits could be made, but the margins will be small.

- Available gas reserves should be developed to meet local and regional domestic demand

- Benefits of utilising common infrastructure to reduce costs (LNG facilities in Egypt under-utilised; some pipeline infrastructure already built)

- Fundamental issue is commercial feasibility of gas re-exports from Egypt. Under current market conditions, highly unlikely that any third party gas supplies could be re-exported from Egypt's LNG infrastructure but this could change

Worldwide gas prices and LNG tightness

Source: OIES
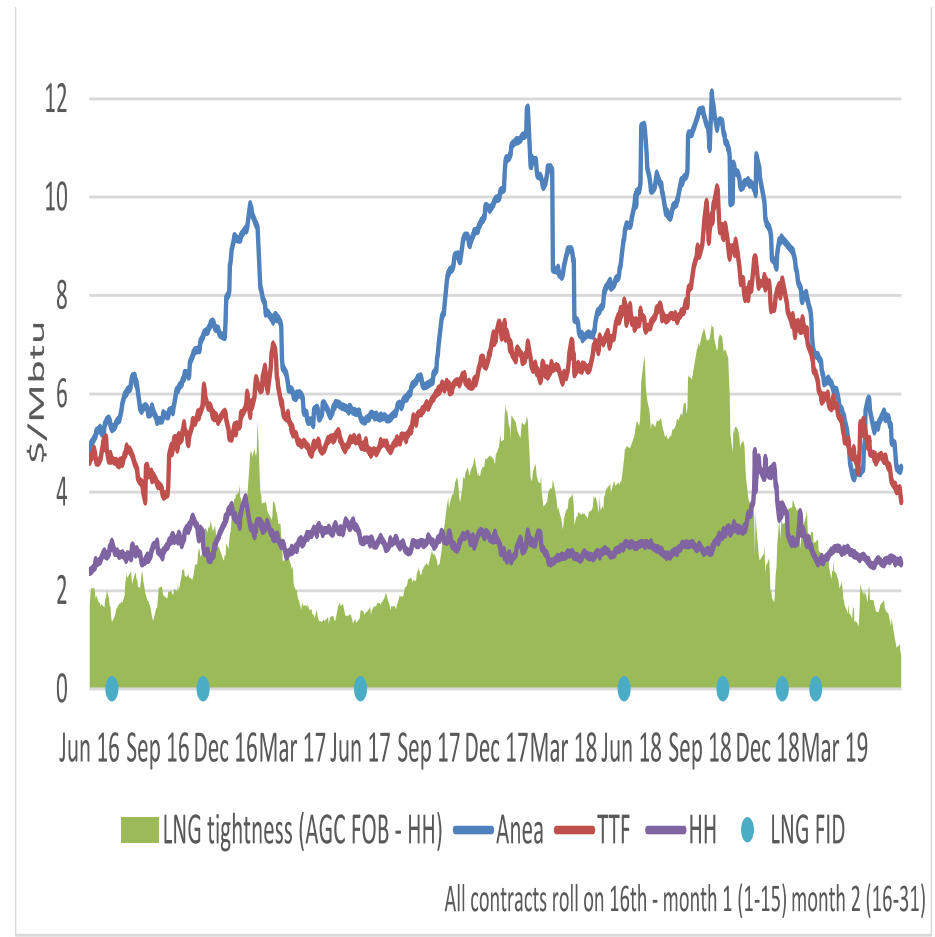
Regional Gas Trade and Hard Realities

- Geopolitics: East Med is not a region; geographically it is, but countries can't be further apart politically.

- Gas will not bring the countries closer together; 'gas dividend' is not big enough to overcome the historic and long and deep rooted problems.

- Countries would be keen to diversifying their sources of supply: reluctance to be locked in by pipeline gas (security of supply issues): example of Jordan.

- Pricing issues: Would domestic bankrupt utilities be willing or capable to pay market prices? Case of Lebanon

- IOCs will continue to push for LNG as their preferred choice and push for shared facilities to reduce costs with ambition to create a gas hub

Crude Oil Prices and Subsidies to Electricité du Liban

Source: https://www.executive-magazine.com/economics-policy/lebanons-electricity-crisis
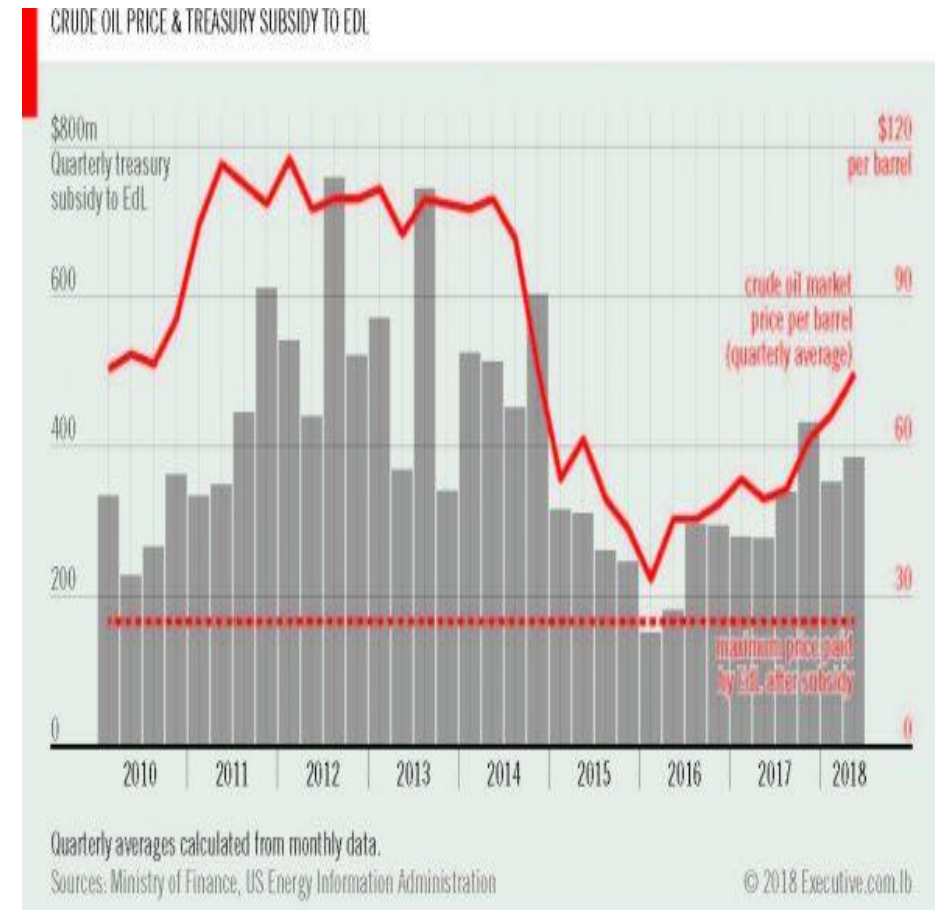
Concluding Thoughts

- East Med is not a game changer at the global level

- East Med gas would not have an impact on the European energy balance in such a way as to dent Russian market share

- The impact would be more regional but the challenges facing regional gas trade remain immense

- Most likely East Med gas would be a game changer for the individual countries if the reserves eventually get developed and monetised