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Report

Qatar's battle for LNG market share

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Introduction

In 2005, Qatar imposed a self-moratorium on future gas developments in the North Field so a detailed study of the reservoir and impact of rapid rise of output from the field could be conducted.

The North Dome/South Pars Field is the largest non-associated natural gas field in the world shared by Qatar and Iran. It covers an area of 9,700 square kilometres of which 6,000 square kilometres lay in Qatari territorial waters.⁽¹⁾ It holds recoverable reserves of more than 900 trillion standard cubic feet or approximately 10 percent of the world's known reserves. Qatar Petroleum (QP), a national company responsible for all oil and gas industry processes in Qatar, has built 14 LNG trains with a total production capacity of 77 million tonnes per annum from the field.⁽²⁾ Until recently, RasGas and its sister company, Qatargas, had each operated seven of these LNG trains, but are now merged into a single entity known as Qatargas.

According to the chief executive of Qatar Petroleum, Saad al-Kaabi, the development in the southern section of the North Field will have a capacity of 2 billion cubic feet per day, or 400,000 barrels of oil equivalent, and increase production of the field by about 10 percent when it starts production in five to seven years.⁽³⁾

With exports of 77.2 million metric tonnes, Qatar is the largest global LNG exporter, a position it has now held for over a decade.⁽⁴⁾ But despite impressive potentials, excellent infrastructure, robust and steady production, Qatar's global market share has been declining slowly, currently standing at 29.9 percent according to International Gas Union.⁽⁵⁾ Predictions are that Qatar will likely lose its leading position in the next few years as huge new production capacities will supply the market. Australia will have the largest liquefaction capacity in the world by 2018, expected to grow to 85 million tonnes per annum (MTPA), up from 43.7 MTPA in 2016. In the United States, 57.6 MTPA is under construction.⁽⁶⁾

A bold, but calculated move

Qatar's decision to unfreeze the development of the North field caught many by surprise. Budget constraints and restrictive financial policy on one side, and development focused on colossal infrastructural projects needed for the FIFA 2022 World Cup on another, have brought some to conclusion that the country will not start large energy projects for a while. According to International Monetary Fund, the recent sustained lower oil and gas prices have adversely affected fiscal performance, as hydrocarbon exports represent on average 80 percent of the country's exports of goods and services over the past twenty years.(7)

Although Qatar is in prime position to compete with any of the established LNG exporters (as well as Russian pipeline gas), the situation on the market has drastically changed since the golden times of 2000s when profit margins were high and markets were growing. The falling prices and new volumes coming from new players such as Australia, the United States and, perhaps in the future, Iran have changed market dynamics in buyers' favour, as they are opting for shorter-term contracts. New supplies created a significant glut in the LNG market, and according to Sara Vakhshouri, President of SVB Energy International in Washington, DC, market glut had a significant downward impact on the LNG prices and the spot LNG prices in Asia in 2016, which compared to 2014, dropped by 70% and reached slightly above \$5/ mBtu.(8) Pricing arrangements have become more flexible as well and buyers, having a choice, have begun to dictate the terms and contract length. Moreover, according to Vakhshouri, the trajectory of the LNG market in the medium term and up to the early 2020s does not show any balancing of the market, and LNG production capacity is expected to remain beyond the trade volumes. In 2016, the global LNG capacity was over 300 million tonnes, while only 268 million tonnes were traded.(9)

According to Howard Rogers, Chairman of the Natural Gas Research Programme at the Oxford Institute for Energy Studies (OIES), the focus now is really on the period beyond the imminently anticipated LNG supply 'glut' i.e. when the market comes back into balance in the early to mid 2020s. "In the future, there will be fewer opportunities to sell LNG on an oil-linked basis in long term contracts and so the underlying cost base of suppliers will become increasingly important."(10)

Nevertheless, Qatar's decision to lift the moratorium according to him is "exactly the right move to make for a low cost player with plenty of resource – say it loudly to scare off the competition."(11) Also, the LNG trade is forecast to expand by 50 percent by 2020.(12)

Finally, since Qatar's goal is to claim (at least) 20 bcma of anticipated 'gap' for new LNG supply from the mid-2020s, the North Field comeback is an inherently sensible move for the owner of a huge, undeveloped, low-cost resource to proclaim loudly its intention to

re-engage in the LNG business. In response, competing higher cost projects will either defer or cancel – especially if buyers are less likely to agree to the required (higher) break-even prices in the anticipation of getting a better deal from Qatar.(13) Another reason for the Qatar's bold move could be attributed to awareness that future Asian plans rely on energy mix including coal and renewables. Although there is no shortage of gas, there is however a shortage of supply that can be developed and transported long distances to market, either via LNG or the pipeline, for less than say \$7-8/mBtu.(14)

Battle for the market share

In some way, Qatar faces a challenge similar to the one of Saudi Arabia in the oil market, as competitors are increasing their market shares while driving down prices. Qatar will fight for its market share as most profitable LNG seller, taking advantage of the industry's lowest production costs and, through control over supply routes, exploiting opportunities while increasing pressure on more expensive producers.

Qatar's LNG delivery cost is about \$5.20/mBtu, which is close to the Russian pipeline gas breakeven price but \$2 to \$3 below full-cycle price for US LNG at today's Henry Hub prices of about \$3/mBtu. This means that at current prices, US LNG producers could cover their marginal costs but not long-term breakeven costs.(15) "With its impressive track record of LNG project execution and the co-production of condensate and LPG from the North Field, Qatar is the lowest cost LNG producer on the planet. Iran could potentially share that position depending on whether condensate yield in the South Pars field is comparable or not. But it will probably take at least 10 years before Iran develops an appropriate upstream investment framework to match that of Qatar," Rogers points out.(16)

Last but not least, QP is trying to increase its international investment in the LNG industry in order to diversify its portfolio, have higher impact and role in the natural gas and LNG industry and supply chain, and secure its market share and demand. Moreover, the merger of RasGas and Qatargas into a single entity will improve efficiency, cut costs and free up capital to fund international expansion. Currently, QP owns a 30% share in Chevron's deepwater licenses in Morocco, a 70% of US Gold Pass Project in Texas and a 40% share in Block 10 in Cyprus as partner with ExxonMobil. It also teamed up with Glencore to purchase a 19.5% share of the Russian Rosneft. QP additionally bids for Mozambique's onshore LNG project along with ExxonMobil.(17)

However, it is believed that Qatar will not dominate the next LNG wave as it did in the 2000s; that role will probably fall to the US. But as the lowest cost producer, it will benefit hugely from new low cost production exploiting opportunities on the markets where hub prices are determined by international arbitrage between higher variable cost

US producers and Russia's strategy of price vs. volume of pipeline gas on the level of European hub prices.(18)

Geopolitical concerns

However, Qatar's new LNG strategy may be seriously interrupted due to the current diplomatic rift with Saudi Arabia, Egypt, the United Arab Emirates and Bahrain, which all severed relations with Qatar. These states closed off air, sea and land routes, hitting container shipments to Qatar; but so far, there was little sign of LNG supply being hit by this. Despite concerns about disruptions to crucial supplies, the LNG market is currently calm.(19) Vakhshouri does not expect Qatar's LNG supply to non-Arab consumers to be interrupted, but the change of trade flow and replacement of natural gas exports to UAE could have impact on the LNG prices. The United Arab Emirates imports about 1.8 billion cubic feet/day of gas from Qatar via the Dolphin pipeline. "This is a significant volume and even though the LNG market is in no shortage, replacing such an amount with non-Qatari LNG could have impact on the LNG prices."(20)

In the case of Egypt, Qatar's tankers and other ships are not banned from crossing the Suez Canal despite Cairo's move to cut relations with Doha. But despite Egypt's heavy dependence on LNG imports from Qatar, it does not have direct deals with Qatar. Traders like Glencore, Vitol and Trafigura deliver Qatari LNG to Egypt but the ownership of cargos belongs to the traders from Qatar's port until they are delivered to Egypt. Traders could also replace Qatar's LNG with other supplier's cargos to Egypt.(21) If Qatar loses its access to the Suez Canal, the LNG traders will have to re-direct the cargos and use other routes which could cause a delay in delivery of the LNG cargoes to the European Union and increase their transportation cost.

If the current rift between Arab countries deepens, disrupting LNG supplies from Qatar, this may have severe consequences for the country. In order to prevent this, it is time for Doha to monetise its cleverly built ties with East and West and, with the help of its allies, try to alleviate the situation that could endanger the stability of the entire region.

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