

## **How to View Future Asian LNG Market (2): Discussion in Malaysia**

Ken Koyama, PhD  
Chief Economist, Managing Director  
The Institute of Energy Economics, Japan

On August 29 and 30, I had an opportunity to discuss energy issues with Malaysian energy industry people, experts and government officials in Malaysia. One of the central topics there was how to view the future Asian liquefied natural gas (LNG) market. This paper deals with the same topic as the previous one (The 442<sup>nd</sup> issue of “A Japanese Perspective on the International Energy Landscape”), based on the discussion in Malaysia.

The biggest matters of interest to participants in the Malaysian discussion included slack Asian spot LNG prices and oversupply in the market. While LNG demand has been increasing since the beginning of this year, spot LNG prices have remained slack at levels far below \$5 per million British thermal units (MMBtu). This is because supply has been growing faster than demand. The LNG market has seen increasing oversupply as new LNG projects have entered the production phase one after another in such countries as Australia and the United States.

According to an outlook given by the Institute of Energy Economics, Japan, in July, global LNG demand would total 340 million tons against 350 million tons in supply in 2019 and 356 million tons against 388 million tons in 2020, indicating that supply’s excess over demand would widen further. Based on the outlook, discussion participants noted that slack spot LNG prices and oversupply could be difficult to resolve and continue in the immediate future.

As seen in winter 2017 and 2018, however, spot LNG prices could turn upward with the supply-demand balance tightening on weather conditions and unanticipated supply disruptions and other factors. In the future, we will have to closely watch developments regarding supply and demand in the global LNG market including the Asian market. While noting that the slack prices and loosening supply-demand balance would continue in the immediate future, discussion participants pointed out that present price levels would not be sustainable.

Prices below \$5/MMBtu contribute to stimulating LNG demand in emerging and developing countries where income levels are relatively lower, but they make it difficult to make final investment decision for new LNG projects. If demand continues increasing with supply growth decelerating, market may go in the direction of rebalancing to reverse the current slackness of prices. In this sense, the present spot LNG prices would not be sustainable.

In this respect, talks on the future Chinese market were interesting. While demand in the Asian LNG market has continued growing, LNG demand has been sluggish in the traditional LNG markets of Japan, South Korea and Taiwan since the beginning of this year. In contrast, demand in emerging markets including China has been expanding in a manner to support overall demand growth in the Asian market.

The problem here is the U.S.-China trade war risking an economic slowdown. As the United

States and China have exchanged retaliatory tariff hikes to escalate and bog down their trade war, concerns have grown about downside risks for the U.S. and Chinese economies. Any Chinese economic slowdown could affect LNG demand. In such case, the present oversupply feeling would grow even stronger. As far as demand in China and other emerging countries structurally supports the LNG market, the trade war and relevant economic downside risks may remain important for anticipating the future LNG market.

Amid oversupply, LNG inflow into Europe is also expanding. The deep European market has become the last resort for absorbing cheap LNG. While natural gas demand has been leveling off or rising slightly in Europe, demand for imports has been increasing due to falling regional natural gas production. Given that Europe has multiple natural gas import options including pipeline gas import from Russia, cheap spot LNG prices can increase the competitiveness of the LNG import option. This is because the liquidity of the global LNG market has increased. In this sense, we must closely watch not only the Asian market but also the European market.

At a time when spot LNG prices are slack and likely to fall further, their gap with long-term LNG procurement contract prices is attracting market participants' attention. Long-term LNG contract prices in the Asian market are mostly indexed to crude oil prices. At present, the average long-term LNG contract price is estimated at just below \$10/MMBtu, some \$5/MMBtu above the abovementioned spot prices. Depending on future crude oil and spot LNT prices, the gap could remain wide or expand further. Discussions in such market environment led me to feel that LNG buyers are increasingly hoping to revise long-term contracts and take maximum advantage of the present low-price spot market environment.

When a wide gap emerges between long-term contract and spot prices of the same good (LNG or natural gas), buyers and sellers of the good have tough negotiations on the revision of contract terms and conditions, as often seen in Europe and the United States in the past. How such negotiations would be conducted in Asia is a key point for how to view the future Asian LNG market.

Although the LNG market is still less liquid than the oil market, spot LNG transactions now account for 25% of total LNG trade. Spot and short-term contract transactions capture more than 30%. As U.S. LNG supply free from the destination clause is increasing, LNG buyers are seeking more flexible terms and conditions. As the LNG market goes in the direction of globalization and commoditization, the price affordability for the consumption side will grow even more important along with prices and mechanisms for investment in supply expansion to allow the LNG market to develop soundly.

In considering the future course of Asian LNG, we should look not only at the LNG market but also at markets for LNG's rival energy sources such as coal, renewable energy, nuclear and liquefied petroleum gas. At the same time, we must pay attention to the fact that LNG competes with domestically produced natural gas and pipeline natural gas import. In considering these points, we must take energy security and environmental problems into account. Regarding urgent air pollution in Asia among environmental problems, the growing requirement for switching from coal to gas can play a role in boosting demand for natural gas or LNG. If moves to fundamentally reduce greenhouse gas emissions in developed countries spread to Asia over a long term, however, natural gas or LNG may become subject to the impact of deep GHG emission cuts. Although Asia has yet to reach such stage, the impact of climate change countermeasures on natural gas or LNG has become a grave matter of concern in Asia, as indicated by the Malaysian discussion.

Contact: [report@tky.ieej.or.jp](mailto:report@tky.ieej.or.jp)

The back issues are available at the following URL

[http://eneken.ieej.or.jp/en/special\\_bulletin.html](http://eneken.ieej.or.jp/en/special_bulletin.html)