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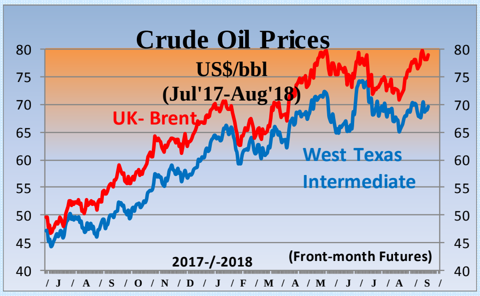
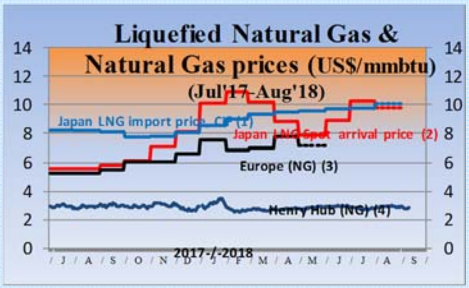
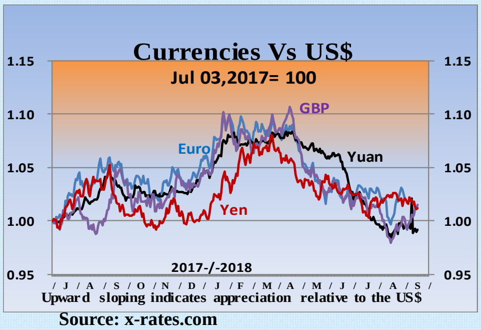


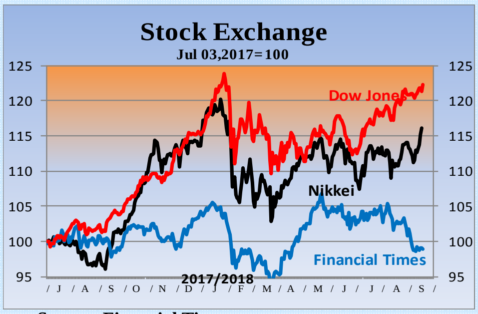
Source: DOE-EIA, Financial Times, NASDAQ



Sources:
(1) Ministry of Finance "Japan Trade Statistics"
(2) Ministry of Economy, Trade and Industry
(contract month basis)
(3) Estimated by World Bank and World Gas Intelligence
(4) DOE-EIA, NYMEX (Front-month Futures)
(5) Investing.com



Source: x-rates.com



Source: Financial Times

Contents

【World Monitoring】

Summary

【World Monitoring】

1. US: Slump in Investment Decisions for New LNG (Liquefaction) Plants

Investment in new LNG (liquefaction) projects has stalled. The reasons include the shortage of pipeline transportation capacity in the US, the increase in pure new build projects instead of converting existing plants, and the impact of the trade war.

2. EU: Energy Integration in the Iberian Peninsula

The leaders of France, Spain, Portugal, and the EU Commission met for the Second Energy Interconnection Summit and signed the Lisbon Declaration, which aims to strengthen energy integration in the Iberian Peninsula.

3. China: US-China Trade War Deepening

Since the start of August, the war of additional tariffs has escalated while the US and China have resumed trade talks. The trade war is heading into a quagmire. US LNG exports to China will decrease drastically.

4. Russia: The West's Economic Sanctions and President Putin's Approval Ratings

The United States enforced stronger sanctions against Russia on account of using a biochemical weapon. Meanwhile, Germany and Russia continue discussions on constructing Nord Stream 2. President Putin's approval rating is falling in Russia.

1. US: Slump in Investment Decisions for New LNG (Liquefaction) Plants

Yoshikazu Kobayashi, Senior Economist, Manager
Gas Group, Fossil Energies & International Cooperation Unit

In the United States where up to 70 million tonnes of new LNG production (liquefaction) capacity is scheduled to be on stream by 2020, financial investment decisions (FIDs) for liquefaction projects beyond 2020 are stalling due to the ongoing easing of LNG supply and demand. There are many promising projects awaiting an FID in the US, including the Golden Pass LNG project with a liquefaction capacity of 15.6 million tonnes per annum (mtpa) planned jointly by ExxonMobil and Qatar's QP, and Driftwood LNG (26 mtpa) of Tellurian which uses the equity model, which packages investments in various value chains such as upstream interests, pipelines, and liquefaction. However, Cheniere's Corpus Christi Train-3 (4.5 mtpa) is the only project that has received an FID this year.

Despite the apparent upturn in the investment environment for US liquefaction projects including the global expansion of the LNG market, a recovery in oil prices and an increase in domestic natural gas production, the following factors seem to be holding back FIDs for new liquefaction projects. The first is pipeline capacity bottleneck in the United States. There is currently a shortage of pipeline transportation capacity between the Permian Basin in West Texas, where natural gas production is growing rapidly, to the liquefaction plants on the Gulf of Mexico, causing serious problems. There is enough supply at the source for new liquefaction plants, but it is not clear whether enough feed gas can be secured where liquefiers are actually located. Construction of new pipelines is being planned to resolve this issue, but lack of transportation capacity is becoming a concern for FIDs as it could cause a supply crunch and send feed gas prices up.

Another factor is that while many soon-to-start liquefaction projects convert existing LNG terminals into liquefaction plants, many of the new projects thereafter are completely new build projects. Inevitably requiring larger investments than conversions, new build projects require long-term contracts to secure stable sales like traditional liquefaction projects. However, the number of buyers with high creditworthiness suited for long-term contracts has not grown despite a jump in the number of LNG importing countries, placing another constraint on investment decisions for new projects.

The US-China trade war is also casting a dark shadow on the investment environment for liquefaction projects. The tariffs on steel products imposed by the Trump administration is pushing up the price of steel for building liquefaction plants, making it necessary to re-calculate investment costs. Further, China's mention of raising tariffs on American LNG imports threatens their export to China and the securing of buyers for new liquefaction projects.

New investments are essential to maintain a stable supply-demand balance of LNG in the medium to long term. It is strongly hoped that the constraints will be resolved soon to allow new investments decisions to be made.

2. EU: Energy Integration in the Iberian Peninsula

Kei Shimogori, Researcher
Global Energy Group 1, Strategy Research Unit

On July 27, the leaders of France, Spain, Portugal, and the EU Commission met in Lisbon for the Second Energy Interconnection Summit and signed the Lisbon Declaration. The Declaration aims to strengthen regional cooperation among the member states concerned within the framework of the EU's Energy Union and to better integrate the Iberian Peninsula into the internal energy market of the EU. It builds upon the Madrid Declaration of March 2015 which launched the integration process.

In October 2014, the European Council agreed on the 2030 Climate and Energy Framework and pledged, as one of the targets, to "support the completion of the internal energy market by achieving the existing electricity interconnection target of 10% by 2020, with a view to reaching 15% by 2030." This requires each member state to own power lines that can send at least 10% of its domestic electricity to neighboring countries. According to the Communication on Strengthening Europe's Energy Networks released by the European Commission in November 2017, 17 member states have already achieved the 2020 target and seven more are on the path to reaching it. However, it also stressed that additional efforts are needed to integrate in particular the Iberian Peninsula (interconnecting Portugal-Spain and Spain-France).

To establish an integrated internal energy market, the European Commission has adopted a list of projects of common interest (PCIs) and in November 2017, the third PCI list containing 173 projects was released. The list includes north-south interconnection (electricity and gas) in Western Europe and infrastructure construction in the Iberian Peninsula. At the time of the Lisbon Declaration, France, Spain, and Portugal signed a grant agreement for constructing an electricity line (280 km) crossing the Bay of Biscay connecting France and Spain. The project is scheduled to receive a grant of €578 million, the largest contribution made by the Connecting Europe Facility (CEF) to any PCI project to date. The electricity line will double the transmission capacity between France and Spain by 2025 and is expected to help Spain approach the 2030 interconnection target.

As for the interconnection of gas, the construction of pipelines between France and Spain and between Spain and Portugal has been selected as PCIs. However, according to a European Commission survey, it has been shown that the France-Spain pipeline is not economically feasible considering that European countries already have many LNG plants which are not in full operation. Though the feasibility will depend on the outlook for gas demand in Europe and the region, President Emanuel Macron is cautious about constructing the pipeline; future developments must be followed.

3. China: US-China Trade War Deepening

Li Zhidong, Visiting Researcher
Professor at Graduate School, Nagaoka University of Technology

The US-China trade war which broke out on July 6 has intensified since the start of August: the tariff war is escalating even though trade talks have resumed after being suspended for more than two months.

On August 16, China's Ministry of Commerce unusually released a statement regarding restarting the trade talks. The statement said that: (1) the trade talks are being restarted at the request of the US, which China accepted, (2) the talks will be at the vice-ministerial level, between Chinese Commerce Vice Minister Wang Shouwen and the US Treasury Under Secretary David Malpass, and (3) the Chinese side reiterates "that it opposes unilateralism and trade protectionism practices and does not accept any unilateral trade restriction measures" and "welcomes dialogue and communication on the basis of reciprocity, equality, integrity, and trust."

The trade friction is hurting both countries. In China, as of August 20, share prices have dropped by approximately 18% and the Chinese currency, the renminbi, by about 5% against the dollar since the year-end. In the United States, the price of agricultural exports in July fell by 5.3% month-on-month. As the war of attrition continues, the National Development and Reform Commission of China stressed that the impact of the trade friction is controllable and stable growth can be achieved by boosting infrastructure investment and other domestic demand. The statement implied that it was America who, despite starting the fight, had weakened first. It also implied that the talks will not be at the ministerial level like the three previous times, but will be a working-level negotiation rather than a political one. Meanwhile, in an interview with Reuters on the 20th, President Donald Trump said that he "is not expecting much" from the meeting. The talks, held on the 22nd and 23rd in Washington D.C., were generally well received by Chinese experts who recognized the importance of resuming the talks and confirming their continuation, rather than any achievements.

On August 23, while the talks were under way, the trade war entered its second phase when both countries invoked an additional 25% tariff on $16 billion worth of goods of the other country. Combined with the first phase of taxes on $34 billion worth of goods, additional tariffs are now imposed on $50 billion worth of goods. According to US statistics, this accounts for about 10% of Chinese exports to the US and about 38% of US exports to China. The US intends to impose a 25% tariff on a further $200 billion of goods in September and China a 5-25% tariff on a further $60 billion of US exports. China remains adamant that it is not afraid of the trade war and will continue both the trade talks and tariff wars with the US.

As yet, energy is not a direct target of the trade war. US crude oil was initially included in the $16 billion of goods subject to the second phase of China's retaliatory tariffs but was removed from the final list released on August 8. Instead, automobile-related items which have a stronger effect on jobs were added. Meanwhile, US LNG is on the list for the third phase of China's 25% additional tariffs. This is meant to deliver a blow to President Trump for whom expanding LNG exports to the world market is a priority. If invoked, the tariffs will significantly reduce US LNG exports to China. This would inevitably hurt the import business of China's state-owned oil major CNPC in the US, but national interest was put ahead of one company. It will be interesting to see from which country China imports LNG and gas to replace US LNG.

4. Russia: The West's Economic Sanctions and President Putin's Approval Ratings

Sanae Kurita, Senior Researcher
Global Energy Group 2, Strategy Research Unit

On August 8, the US State Department announced that it will impose additional economic sanctions on Russia for the attempted murder of British national Sergei Skripal and his daughter Yulia using the nerve agent Novichok. Based on the US law that prohibits the use of biochemical weapons (CBW Act), the sanctions will be introduced on August 22 and will ban the export of national security-related goods and technologies. Contrary to President Trump's soft stance toward Russia at the July summit, the US Congress is acting tough against Russia with several bills related to harsher economic sanctions being submitted, including from the Republican Party. Additional sanctions could be invoked as early as November.

Russia's Kommersant has reported that one of these bills, the Defending American Security from Kremlin Aggression Act (DASKAA), may require the United States to gradually reduce low-enriched uranium imports from Russia by 2031. In 1993, for the purpose of nuclear disarmament and non-proliferation of nuclear weapons, the two governments signed the United States-Russia Highly Enriched Uranium Purchase Agreement and had been implementing the Megatons to Megawatts Program (US purchases of low-enriched uranium from dismantled Russian nuclear weapons for use in power generation) since 1995. Imports continued after the program was closed in 2014 albeit in progressively smaller quantities. If DASKAA becomes effective, Russia's state-run nuclear company Rosatom may lose exports to the US, which accounts for about 40% of its income from low-enriched uranium exports ($700 million as of 2017). There are also bills on stricter sanctions on the energy and financial sectors and mandatory sanctions on export pipelines; the development of such discussions must be closely monitored.

On July 5, the Council of the European Union extended economic sanctions targeting specific sectors of the Russian economy, which had been due to expire at the end of July, by six months. This is an extension of existing sanctions and Europe is not making any moves to tighten sanctions. On August 14, Russia's consortium Nord Stream 2 AG announced that it has now obtained all licenses from the Russian government for constructing the Nord Stream 2 gas pipeline. The company has already finished receiving necessary construction licenses from Germany, Finland, and Sweden, and the only remaining country is Denmark where the licensing process is under way. On August 18, Russian President Vladimir Putin met with German Chancellor Angela Merkel to discuss Syria, Ukraine, and Nord Stream 2. Regarding Nord Stream 2 which is being targeted by the US, President Putin repeated his previous words that the project is "purely economic" while admitting that "the transit of gas through Ukraine may be economically efficient." Chancellor Merkel also stressed the position of Ukraine on the natural gas route to Europe and urged Russia and Ukraine to come to the table.

In Russia, the approval rating of President Putin and the Medvedev Cabinet has collapsed, with growing disapproval after the government announced a pension reform which includes raising the pension age. According to the Russian Public Opinion Research Center, the percentage of those who answered that they "support President Putin's activities" fell from 80% after inauguration to 63%, while those who "do not support" rose to 26% from 12%. As US-Russia relations worsen, the developments in the Russian government which is struggling to deal with the situation in and outside the country must be closely monitored.

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Energy and Economy Indicators of Japan

IEEJ Homepage Top

Back Numbers of *IEEJ e-Newsletter*

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IEEJ e-Newsletter Editor: Yukari Yamashita, Director
IEEJ Newsletter Editor: Ken Koyama, Managing Director
Inui Bldg. Kachidoki, 13-1 Kachidoki 1-chome, Chuo-ku, Tokyo 104-0054
Tel: +81-3-5547-0211 Fax: +81-3-5547-0223