THE OXFORD INSTITUTE FOR ENERGY STUDIES

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

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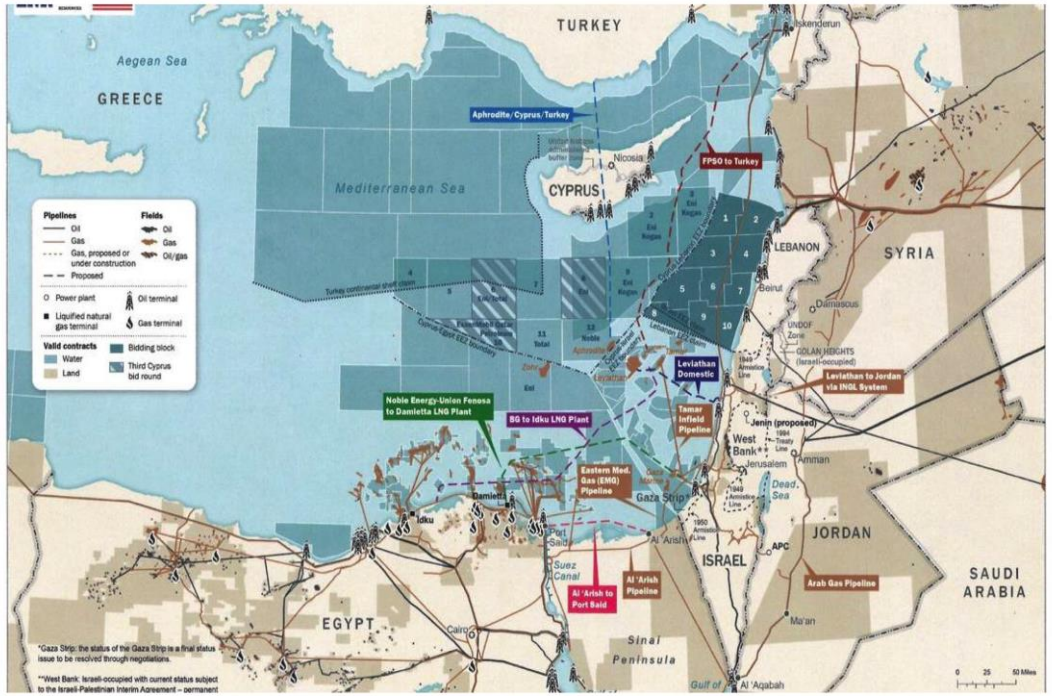
Rapidly Changing Regional and Global Context

- 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

JUNE 05, 2019 06:00 AM



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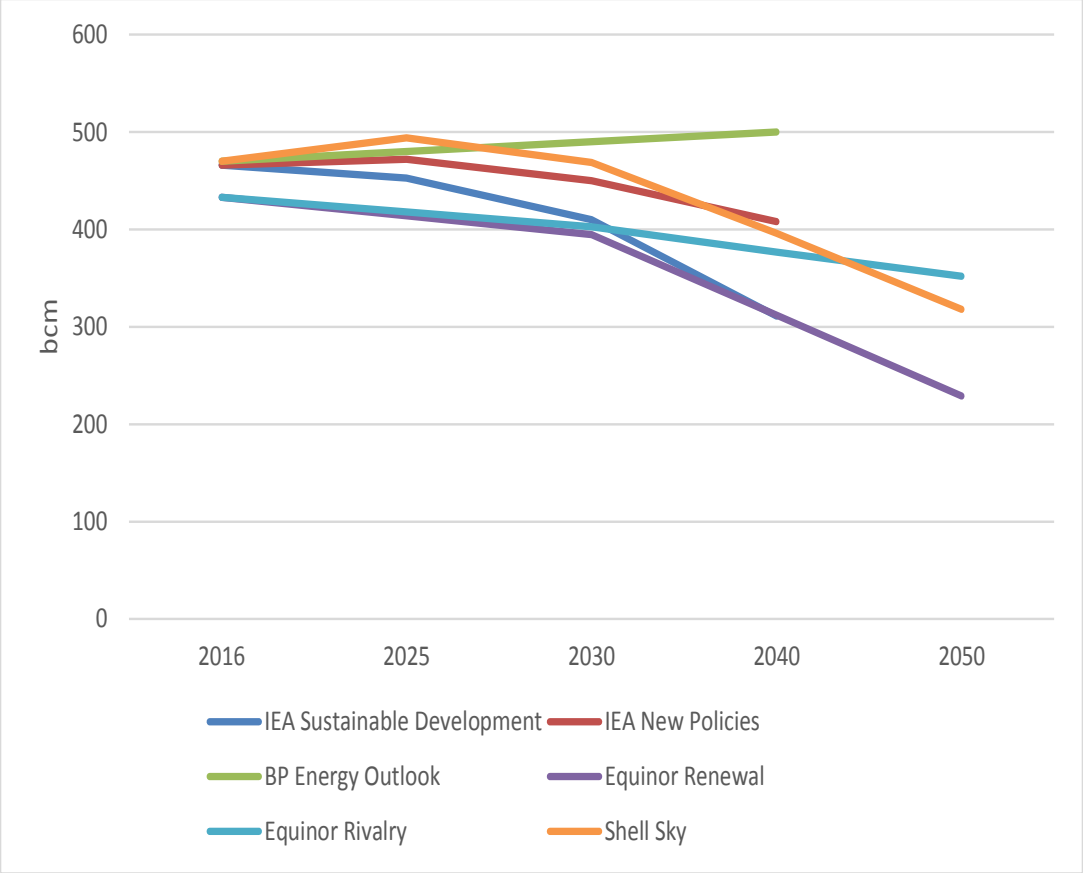
Key Transformations in Global Gas Markets

- 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 major new 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)

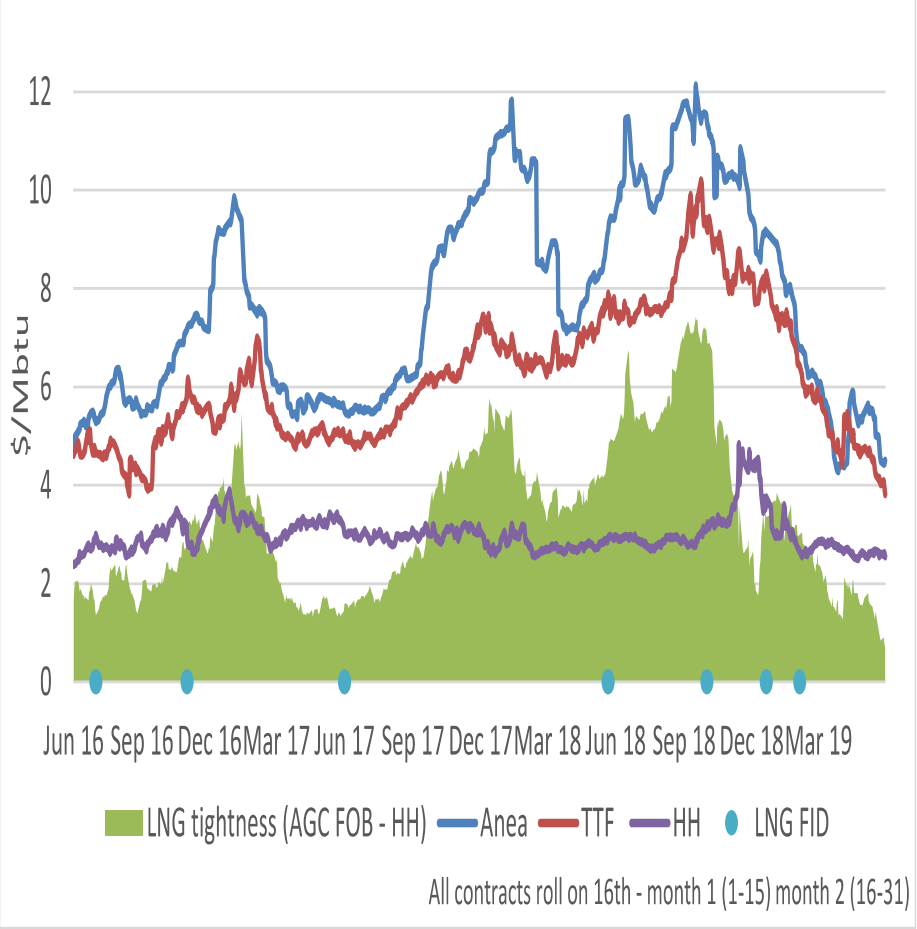


Sources: IEA (2018), pp.550-551. BP (2018), p.54. Equinor (2018), p.57. Shell Sky Scenario.

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



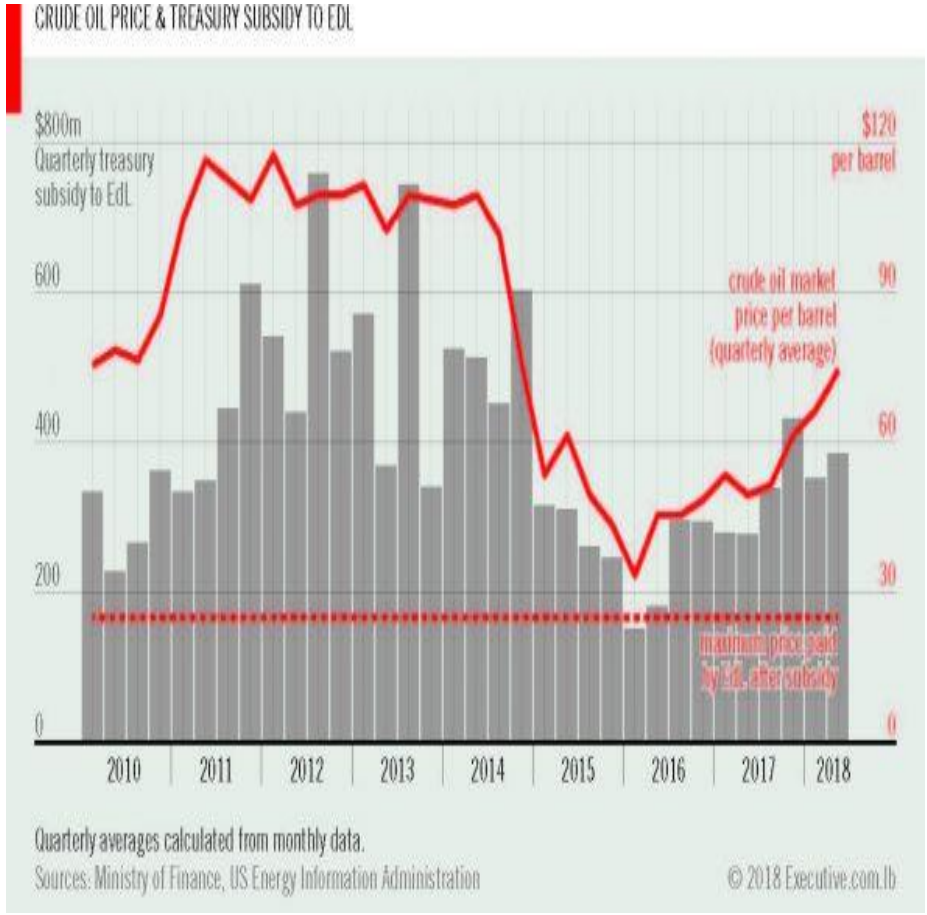
Source: OIES

Regional Gas Trade and Hard Realities

Case for East Med gas to be traded within the region is very strong but real challenges ahead

- 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