

OIL & GAS

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Expert meeting takeaways

We hosted Kaushik Deb – Research Fellow at KAPSARC (King Abdullah Petroleum Studies and Research Center), Riyadh, for investor meetings in Mumbai. Key excerpts:

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Light-heavy spreads could remain under pressure: Refineries across the world are facing shortages in heavy (sour) crude oil supply due to production disruptions in Iran and Venezuela (~3mbpd). On the other hand, more volumes of the light (sweet) crude variant are increasingly becoming available owing to higher tight oil production from the US. This implies that light-heavy crude spreads may remain under pressure. An increase in oil output from Venezuela looks difficult in the near term as political uncertainty has disrupted investments in the sector.

IMO may not fuel GRM surge in immediate future: Most ports globally are likely already compliant with the upcoming IMO 2020 regulations (with some exceptions such as Indonesia and a few African countries). Nevertheless, the expected positive impact of IMO on diesel spreads could be muted in light of the slowdown in global economic growth. Over the long term, LNG is likely to emerge as the preferred fuel for shipping considering its favorable economics versus all liquid fuels, including IMO compliant ones.

LNG demand growth could slow: Over the last two years, gas consumption in China has grown substantially due to government efforts to reduce coal consumption (mostly for power generation) in the country. But China has recently allowed the use of clean coal, albeit with restrictions, for power generation – this could temper growth in LNG consumption.

Renegotiation of long-term contracts carries global precedent: Long-term gas contracts have historically been successfully renegotiated across the world. For instance, RWE – one of the largest power generation companies in Europe – had renegotiated gas prices for the period of 2005-10 with Gazprom, at a time when the latter had lost considerable market share to Norway due to lower regional spot LNG prices. Gazprom had agreed to give discounts at the end of each year (in lieu of lowering long-term prices).

To resolve the pricing differential for India's long-term LNG import contracts (e.g. RasGas, Gorgon), buyers might need to consider using a gas-linked price formula such as Henry Hub, moving away from the current oil-linked formula.



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