

EU Counsellor: Turkey is strategic partner for energy

AA Energy Terminal, 09.06.2016



The EU considers Turkey a strategic energy partner following on from ministerial level energy dialogue between Turkey and the EU, according to Head of Trade, Economy, Energy and Agriculture Section of the EU Delegation to Turkey.

Balazs Gargya spoke during the International Geothermal Congress Turkey 2016 in Izmir where he said that the high level meetings, which are held at least one a year, should continue. “The channel of high level communication that has been created now should be maintained. We very much look forward to continue and discuss with Turkey [on energy issues],” Gargya said.

Gargya, commenting on the EU’s position on energy cooperation with Turkey said, “In that regard, we believe that the Trans Anatolian Natural Gas Pipeline (TANAP) is a significant part of the Southern Gas Corridor. So when the Southern Gas Corridor is completed, it will be a very important step in diversifying gas supplies to Europe.”

The EU has recognized the construction of the Southern Gas Corridor as a project of ‘common interest’. Through the implementation of this project, the strategic relationship between Turkey and EU will be reinforced in a very tangible way, according to Gargya. He also signified that other potential partners for energy cooperation would be examined.

“The Southern Gas Corridor would also allow other suppliers to put their gas into TANAP to reach Europe. Of course there are a number of potential suppliers. In this regard, there are different considerations to be taken into account,” he said.

Highlighting Turkey’s goal of becoming an energy hub, Gargya said two issues are very important. “First is unbundling, so basically full separation of the transmission network operation from supply activities should be ensured. Mandating third party access to the gas networks as well as LNG and storage terminals within the country is also very important,” he added.

With regards to renewable energy developments in Turkey, Gargya said that Turkey has set ambitious but attainable objectives for 2023. “We believe that if Turkey appropriately speeds up the transformation of the regulatory framework, this target will actually be attainable,” he explained.

In order to decrease energy imports and dependency, Turkey wants to increase renewable installed capacity in the coming years. Therefore, the Turkish government has made it a priority to increase the share of renewable sources in the country’s total installed power to 30 percent by 2023. Gargya clarified some areas for assessment for Turkey to reach its renewable energy goals for 2023.

“The one important area that we have found is that the use of biofuels can certainly help Turkey attain these objectives in the renewable energy area. But in addition to that, retail price deregulation can also be a helpful feature. Finally, the administrative burdens that are associated for example with the creation of licenses and of plans for different installations that are required should also be simplified,” Gargya asserted.

Putin: Moscow will not abandon Turkish Stream gas project

AA Energy Terminal, 08.06.2016



Russia will not abandon the Turkish Stream natural gas pipeline project despite the ongoing political problems with Turkey, said Russia’s President Vladimir Putin.

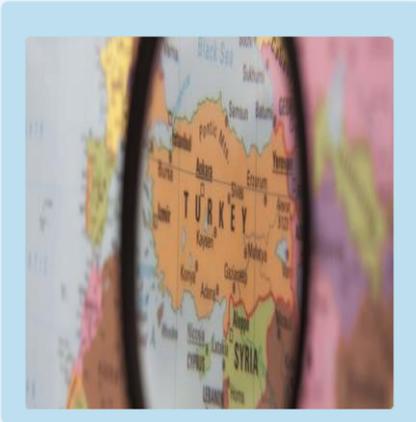
Putin met with Benjamin Netanyahu, at a press conference in the Russian capital Moscow where he said that Moscow would not give up on the Turkish Stream. “There are certain difficulties of a political nature with Turkey. Also we are waiting on a clear position of the European Commission on the project,” he said. Alexey Miller, CEO of Gazprom, announced that Putin had canceled the construction of the South Stream Natural Gas Pipeline in December 2014.

Putin laid the blame on the European Union for axing the project. After terminating the project, Putin announced that Gazprom would build a 63 billion cubic meter (bcm) capacity natural gas pipeline to Turkey, bypassing Ukraine and naming the project the Turkish Stream.

However, the Turkish Stream, which was planned to carry Russian gas to Europe through Turkey, was cancelled by Ankara. Following the downing of a Russian fighter jet after it had violated Turkish air space despite multiple warnings from the Turkish military, relations between the two countries soured rapidly, kicking off some Russian economic measures against Turkey.

Turkey's BOTAS prepares FSRU tender

Argus, 08.06.2016



Turkey's state-owned Botas has decided to build a floating LNG storage and regasification unit (FSRU) and is in the process of preparing the relevant tender documentation. The firm has started the process to obtain a licence for the construction and operation of the FSRU. The terms of the tender will be finalised when it has received the necessary permits, which could take a number of months.

The FSRU will have around 20mn m³/d of capacity and will probably be situated in Bandirma, northwest Turkey, Botas' general manager, Mehmet Konuk, previously said. The company is still working on the costs for the investment.

There is potential to raise capacity to 30mn m³/d, according to market participants. Botas will hold exclusive rights to operate the unit, although it may allow third-party access if LNG supplies exceed its needs. Turkish energy regulator EPDK in March clarified the definition of an FSRU in local legislation, subsuming it under existing definitions of LNG and storage activities in the country's gas market law, which entered into force in 2001.

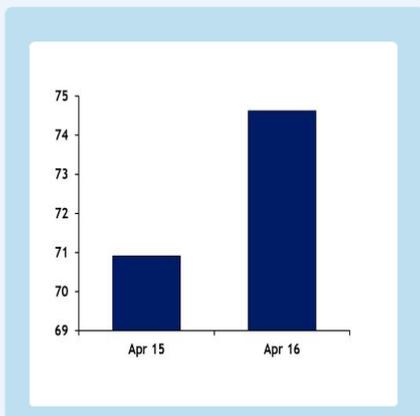
The new rules were intended to eliminate a key hurdle that blocked licence applications for FSRU projects. Turkey's total entry capacity is expected to rise to 228mn m³/d by next winter from 200mn m³/d. And it is forecast to climb to around 240mn-245mn m³/d by the start of 2018, through FSRU developments and other expansions.

The country has two LNG terminals at present — the 6mn t/yr Marmara Ereğlisi facility, near Istanbul, which Botas operates, and private-sector firm Egegaz's 4.4mn t/yr Aliaga complex, on the Aegean coast. The sites have 8.2bn m³/yr and 6bn m³/yr of sendout capacity, respectively. Entry capacity at the terminals is expected to expand in the coming years. Capacity at Marmara Ereğlisi will rise to 24mn m³/d from 16mn m³/d, Botas previously said.

Turkey's Kolin Enerji has started the licensing process for an onshore LNG terminal in Aliaga with 6.3bn m³/yr of capacity. Project costs are estimated at around \$750mn. The site will have 280,000m³ of storage and 18mn m³/d of sendout capacity. It received its environmental permit in September 2013.

Turkey's Tetas may buy lignite-fired output

Argus, 07.06.2016



Turkey's state-run trading company Tetas may start purchasing domestic coal-fired generation from independent generators in a bid to incentivise the sector and reduce dependency from foreign energy resources.

A new law will allow Tetas to purchase domestic coal-fired generation from independent power producers if the amount of power demanded by distribution companies is not met by output by its existing bilateral agreements. The volume of purchases, delivery period and price are to be defined by a council of minister, according to the final draft amendments approved by parliamentary committee responsible for energy.

These amendments were approved by the Turkish parliament last week along with other changes to energy laws, and they will take effect when published in the official journal. With the new rules, Tetas is kept exempt from the scope of the public tender law for its energy purchases from IPPs.

Current legislation does not allow the firm to sign contracts with private entities and its purchases are limited to existing concession contracts — with the so-called Tetas plants, including build-operate (BO), build-operate-transfer (BOT) and transfer-of-operating-rights (TOOR) agreements.

It is still unclear when Tetas will announce its first purchase of lignite-fired power from IPPs, but a few participants expect that it could be launched for delivery as soon as the beginning of July or August.

Tetas purchases of lignite-fired output could only have an upside impact on day-ahead prices if Tetas decides to reduce volumes of bilateral agreements with the BO, BOT and TOOR plants, which seems unlikely for the short run, some market participants said.

But Tetas might face a power deficit when the 672MW Birecik hydropower plant's concessionary contract ends in early October. The changes come as an effort by the Turkish state to support domestic coal-fired generation and reduce dependency on foreign resources.

Currently, domestic coal-fired generation is estimated at an hourly average of 4.0-4.5GW. Low spot prices this year have reduced the profitability of thermal plants. Some gas-fired capacity is left out of the merit order, reducing the share of gas in the generation mix.

And current day-ahead prices can only cover input costs of lignite-fired plants with efficiency levels at or below 38pc, one lignite-fired generator said, adding that repayment of credit taken to make investment has become more challenging amid a strong depreciation of the Turkish lira against the dollar last year.

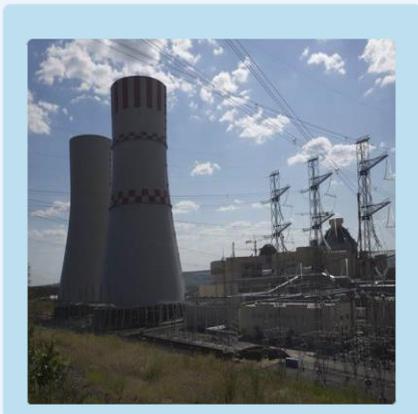
The Epias day-ahead base-load average between January and delivery for 8 June was TL120.23/MWh, down by TL8.46/MWh compared with the same period last year. Turkey's installed lignite-fired capacity rose by 430MW during January-May to 9.8GW, as a second 135MW unit at the 270MW Bolu Goy nuk, a 145MW unit at the 290MW Adularya, and a second 150MW unit at the 450MW Tufanbeyli plants started commercial operations. Tufanbeyli's third 150MW unit is running testing operations, and Adularya's second unit is expected on line this month.

Some 4.6GW of domestic coal-fired capacity was transferred to the private sector during 2013-15 and most of these plants have undergone rehabilitation works to improve efficiency (see table). They are also eligible to sell their output to Tetas under the new rules. And state-run utility Euas' lignite-fired capacity was 3.2GW by the end of 2015, counting for 15.5pc of its total generating capacity.

A new method for the privatisation of renewable and coal-fired capacity is also introduced through the recent law changes. If Euas or its affiliates decide to sell their assets for the purpose of investing in new renewable or lignite-fired power plants, buyers will not have to purchase the asset outright. Instead, buyers will compete for a guaranteed sales prices from Tetas for the plant's output through a privatization auction. Under these auctions, the initial guaranteed sales price will be set by the energy ministry and the company agreeing to receive the lowest sales price will win the tender.

Turkey to increase gas storage obligation

Argus, 08.06.2016



Gas storage obligations for private-sector gas importers in Turkey may be increased to a maximum of 20pc in the future, as the country's storage capacity expands.

Turkish private-sector companies that have imported natural gas for five years or more currently have to reserve 10pc of their contracted annual gas import volumes. But this could be extended to a maximum of 20pc by the energy regulator EPDK's board in line with the country's gas storage capacity, according to new rules approved by the parliament last week. Amendments to energy laws approved last week will take effect when published in the official journal.

Turkey's only underground storage facility, at Silivri near Istanbul, is expected to raise withdrawal capacity to 25mn m³/d from 20mn m³/d by the winter of 2016-17. Turkey also plans to increase its gas system entry capacity by 20pc to around 240mn-245mn m³/d by the start of 2018, following the planned expansion of LNG capacity through the use of floating storage and regasification units and existing sites.

ICI 500 study announces TÜPRAŞ as Turkey's biggest industrial enterprise

Daily Sabah, 07.06.2016



Istanbul Chamber of Industry (ICI) has recently announced the 2015 results for “Turkey’s Top 500 Industrial Enterprises” study, which has determined the giants of the industry sector since 1968.

TÜPRAŞ was revealed as Turkey’s biggest industrial enterprise, with sales-from-production figure of TL 35.4 billion in 2015 and holding this position for the last 10 year in a row. According to the study results announced by ICI Chairman Erdal Bahçivan, TÜPRAŞ preserved their place at the top of the industry, followed by Ford Automotive with TL 14.7 billion and Arçelik with TL 9.998 billion.

The top three corporations on the list belong to Koç Group holdings. The study reveals the current situation and problems of the real economy. Announced two months earlier than last year, one of the most specific outcomes of the study was that financing costs had increased by 75 percent compared to last year. This means industrialists lost 63.4 percent of their profits as financing costs.

According to the study, the manufacturing industry has grown under the Turkish economy as a whole for the past four years, except for 2014. In 2015, the economy and manufacturing industry grew by 4 and 3.8 percent, respectively.

In 2015, ICI 500’s export reduced from \$61.3 billion to \$53.4 billion, a decrease of 12.9 percent. By the end of 2015, ICI 500 enterprises constituted 37.2 percent of Turkey’s exports, along with 38.9 percent of industrial exports. The top five exporters among ICI 500 enterprises are Ford Automotive, Tüpraş, Oyak Renault, Tofaş and Arçelik.

ICI 500 companies’ net sales increased seven percent in 2015 reaching a total of TL 450 billion (\$155.3 billion) from TL 421 billion (\$145.3 billion) in 2014. According to ICI research, Turkey’s manufacturing industry growth was under the national economic average over the last four years, with the exception of 2014. In 2015, the Turkish economy grew four percent while the manufacturing industry’s growth was 3.8 percent. In the same year, ICI 500 companies’ exports decreased 12.9 percent, from \$61.3 billion to \$53.4 billion.

Stating that the study revealed the abnormal increase in the financing costs in 2015, ICI Chairman Erdal Bahçivan said the majority of operating profits that the industrialists had realized with great efforts went to financing costs. According to Bahçivan, financing costs increased by 75.1 percent compared to 2014. Industrialists lost TL 28 billion (\$9.65 billion) out of TL 44 billion (\$15.16 billion) in profit, or 63.4 percent, due to financing costs. This percentage is 16 percent on average for public industrial enterprises around the world. In other words, the thing that makes Turkey different from the rest of the world is not the percentage of indebtedness, but the cost of the loans.

Nearly two-thirds of revenue, which industrialists earn by great efforts, research and development and investments and by creating employment and taking risks, goes to finance. Bahçivan indicated that this was an unacceptable and unsustainable situation and it was impossible for the Turkish finance system to continue like this.

He added that while industrialists struggled with such financial burdens, the important financial institutions were also unhappy, and the wheels of industry did not seem to be spinning healthily. Stating that Turkey's growth should be backed by research and development as well as high technology, Bahçivan said: "SMEs, which we will encourage to produce high value-added productions, will help Turkey's qualified growth with their dynamism."

Will gas thaw the ice between Russia, Turkey?

AI Monitor, 08.06.2016



With a nuclear power plant project underway and a new gas pipeline on the table, Turkey and Russia were moving toward a strategic partnership in the energy realm when things changed abruptly in November after Turkey shot down a Russian warplane at the Syrian border.

President Putin was furious. He vowed that Russia would never forget the downing of the jet and the killing of the ejected pilot, that Turkey would regret its action and would not get away with a few economic sanctions and "a tomato ban." Following Putin's threats, Moscow curbed imports, put restrictions on the activities of Turkish business people.

And Moscow cut the tourist flow to Turkey, leading to a 68% drop in the number of Russian vacationers in the first four months of the year. Turkey, for its part, slowed down energy projects with Russia. The construction of the Akkuyu nuclear power plant almost ground to a halt, and a major gas pipeline project, to which Moscow attached much importance, was put on ice. The planned Turkish Stream conduit was to carry 63 billion cubic meters of Russian gas to Europe via Turkey per year.

Gokhan Yardim, the former head of Turkey's state-run gas company BOTAS, told AI-Monitor that Russia is under pressure to put in place an alternative gas route to Europe since its transit agreement with Ukraine is scheduled to expire in 2019.

One option for Russia was the South Stream pipeline, which was to run to Bulgaria through the Black Sea and from there on to Europe. The project, however, failed to win the green light from the European Union. In a surprise move in late 2014, Putin proposed an alternative — Turkish Stream — during a visit to Ankara. According to senior Russian officials, the project was to become operational in late 2017.



In January 2015, Russian Energy Minister Alexander Novak advised European clients to buy gas from Turkish Stream, reminding them that the transit agreement with Ukraine would expire in 2019. Similarly, Gazprom chief Alexey Miller said time was running out and urged interested European buyers to hurry up with arrangements to take gas from the Turkish border.

The Russian enthusiasm to replace Ukraine with Turkey was obvious, but the plane shooting snagged the project. Turkish President Recep Tayyip Erdogan denied initial reports that Moscow was the one to suspend the project, asserting it was Ankara's decision.

Soon, however, the showdown in bilateral ties began to hurt both the Turkish and Russian economies, much to the discontent of both countries' peoples. Turkey suffered major losses in tourism and exports, while Russia faced the risk of losing a strategic partner in giant energy projects. With Russia under pressure to secure an alternative to the Ukrainian route, the clock was not ticking in its favor.

That's where the might of diplomacy came into play. The old dictum of no permanent friends and enemies in international affairs appeared to be at work on May 28, when Putin conveyed a softer message to Turkey during a visit to neighboring Greece.

Stressing that Russia never thought of going to war with Turkey, he said, "I hope we never come to that point. But what is done is done. Not only was our plane shot down, but our pilot was killed, which is a war crime under international law. We have received some explanations, but an apology has never come.

We want to improve our relations, and we were not the ones to spoil this relationship. Words are not enough; action is needed. We are in contact with Turkey, and we expect certain fundamental steps. But there have been none so far." Responding to Putin's remarks, Erdogan also used a softer tone, though he claimed to be unaware of what Moscow expects.

Speaking ahead of a trip to Africa last week, he said, "I have difficulties in understanding what first step is expected from us. We are not a country sitting in the defendant's chair. We are not the ones who want to ruin relations with Russia either. It's really thought-provoking that our relations have come to this point or that he [Putin] is sacrificing a great country like Turkey over one pilot's mistake, though our ties with Mr. Putin had reached a truly different level as two good friends.

We need to make efforts to improve relations with Russia anew. I hope that this problem will be overcome as soon as possible, and that Turkey and Russia will continue to move forward as they did over the past decade."

According to Turkish journalist Nerdun Hacıoglu, a veteran Moscow correspondent for Hurriyet, Putin's remarks in Athens constituted "a wink at Ankara," which he explained with the following factors: the departure of Prime Minister Ahmet Davutoglu, whom Russia held responsible for the plane shooting, and his replacement by Binali Yildirim, who was quick to express a desire to mend fences with Russia, the negative economic impact of Turkish entrepreneurs leaving the Russian market and Moscow's desire to salvage mega projects such as the Akkuyu nuclear power plant and the Turkish Stream pipeline. It should not come as a surprise if the Turkish Stream project is taken off the shelf in the near future.

The fact that Putin delivered his message from Athens makes it even more meaningful, given that Russia and Greece have reached their own agreement on gas deliveries to Europe. Yet to bring the gas to Greece, a conduit needs to be built via Turkey.

Unit International to build \$4.2B natural gas-combined cycle plants in Iran

Daily Sabah, 06.06.2016



Turkey's Unit International, owned by former Galatasaray Chairman Ünal Aysal, has signed an agreement with the Iranian Energy Ministry to establish nearly \$4.2 billion worth of natural gas-combined cycle plants in Iran. The signing ceremony was held in the Iranian capital of Tehran.

In accordance with the agreement that will be in place for 20 years, Unit International will establish seven natural gas combined cycle plants in different parts of Iran with a total installed capacity of 6,020 megawatts. Construction of the plants, which will satisfy a large portion of Iran's energy requirements, should start in the first quarter of 2017.

Unit International CEO Aysal said the foundations of the company's new investment go back 34 years, as it has carried out energy projects in Iran since 1982. "We have completed all our work on time. We have not faced problems in any of our work. We would like to demonstrate the reliability and power of Turkey and Turkish businessmen once again through our new investment that is based on confidence and friendship," he said.

Pointing out that the current productivity of Iran's installed natural gas-combined cycle plants is 32 percent, Aysal said the plants to be established by Unit International will have more than 60 percent productivity. When construction of the plants is completed, Unit International will meet nearly 10 percent of Iran's electricity demand.

The plants will utilize the build-operate model. According to the agreement, Iran will give natural gas to Unit International for 20 years and purchase the electricity generated from that natural gas at the combined cycle plants at the agreed tariff for six years.

After the first six years, Unit International will either export the generated electricity or sell it on the Iranian free market. So far, only Iran's domestic investors could make such investments with state aid in the country. Aysal said Unit International's agreement with Iran is a first in terms of Iran opening up to foreign capital, continuing: "Our mutual confidence and friendship of many years has enabled us to create a new model that will gain acceptance in international markets and could open Iran's door to foreign capital flow. This is one of the largest investments ever made in a single package in Iran and the world."

Mohsen Tarztab, the general manager of Iran's Thermal Power Plant Holding (TPPH), which undertook the job on behalf of the Iranian Energy Ministry, spoke after the agreement was reached, stressing that the agreement indicates a revolution for Iran.

Tarztab said Iran has experienced a challenging negotiation process spanning 12 months in which more than 1,000 hours' worth of talks were held with Unit International in regard to the agreement. He noted that new natural gas-combined cycle plants will be two times more efficient than the existing ones in Iran, which have low efficiency due to their old technology.

Thus, Iran will use 50 percent less natural gas to produce electricity while saving a significant amount of natural gas. "Our agreement with Unit International sets a precedent for all other foreign investors," Tarztab stated.

Meanwhile, Unit International will start investing in an 840-megawatt natural gas-combined cycle plant for the Kurdistan Regional Government (KRG) at the end of this year. The company, which provides nearly one terawatt hour of electricity to 9,000 consumers a year, has a significant place among electricity-selling companies in Turkey and the Balkans.

Israel's Energy Ministry: Leviathan oil fields may be smaller than original estimates

Haaretz, 05.06.2016



The partners in Israel's Leviathan natural gas field on Sunday shrugged off a lower estimate of its size from the country's Energy Ministry, which said the field could be 20 percent smaller than the companies have predicted.

The ministry included the estimate in its approval of the development plan for the field. This was 17.6 tcf, lower than the companies' 21.9 tcf estimate. The ministry also said this could change after it receives more drilling data on one of the project's wells, Leviathan 5. The companies are sticking with their assessment and are pushing ahead with plans to bring the field online by the end of 2019.

"The partnership clarifies that there has been no change in the resource estimate," the Israeli partners said in a statement to the Tel Aviv Stock Exchange. Found in 2010, Leviathan was one of the world's largest offshore discoveries of the decade, expected to bring Israel a major cash windfall and export deals which are waiting to be signed with countries like Egypt, Jordan and possibly Turkey. Israeli conglomerate Delek Group, through subsidiaries Delek Drilling and Avner Oil, holds a 45.34 percent stake in Leviathan.

Texas-based Noble Energy has a 39.66 percent share, and Israel's Ratio Oil has the remaining 15 percent. The issue has had little impact on the companies' shares in Tel Aviv, which were mostly flat in Tel Aviv.

Yossi Abu, chief executive of Delek Drilling and Avner Oil, told Reuters they were satisfied with the Energy Ministry's approval, which he said included a production capacity of 21 billion cubic meters a year. "The reserves are enough to meet domestic demand and exporting contracts with neighboring countries as we plan, according to the approved development plan," he said. Both the companies and the ministry used outside energy consultants to come up with their estimates.

Iranian oil exports soar as shipping companies return to Iran

Oilprice, 08.06.2016



When Iran was desperate to start exporting the millions of barrels it was pumping each day out of the ground, it found it had an unexpected problem: not only did it not have enough spare tankers, but few if any shipping companies were willing to move the cargo. There were two key reasons for this.

The first hurdle was residual U.S. restrictions on Tehran which are still in place and prohibit any trade in dollars or the involvement of U.S. firms including banks - a major hurdle for the oil and tanker trades, which are priced in dollars. As a result, by mid-April only eight foreign tankers had shipped Iranian crude to European destinations since sanctions lifted.

That equates to only around 10 days' worth of sales at the levels of pre-2012, when European buyers were purchasing as much as 800,000 barrels per day (bpd) from the OPEC producer. Michele White, general counsel with Intertanko, an association which represents the majority of the world's tanker fleet, said: "We have witnessed a reluctance by our members generally to return to Iranian trade given the prohibition on use of the U.S. financial system - essentially no U.S. dollars."

The second and far bigger problem, were implicit Saudi Arabian threats for shippers not to transact with Iran or risk losing Saudi business. "It's seen as an unknown risk," said one shipbroker. "No one wants to disrupt their relationship with the Saudis."

Iran admitted as much. A senior Iranian government official, who declined to be named due to the sensitivity of the matter, acknowledged his country was finding it difficult to hire foreign tankers. "We are working on the problems.

There are various issues involved, financial, banking and even insurance. It has improved a little bit since the lifting of sanctions but we still face serious problems." Asked if this and the need to modernize some of the domestic fleet were holding back exports, he said:



“Of course it does.” As Reuters said at the time, Iran’s problems may not be resolved any time soon, adding that two other sources with other leading oil tanker operators echoed the above concerns and said they were not doing Iran deals at the moment. Fast forward a little over a month later, and somehow all the issues have been resolved.

According to an update from Reuters, more than 25 European and Asian-owned supertankers are shipping Iranian oil, allowing Tehran to ramp up exports much faster than analysts had expected following the lifting of sanctions in January. As noted above, “Iran was struggling as recently as April to find partners to ship its oil, but after an agreement on a temporary insurance fix more than a third of Iran’s crude shipments are now being handled by foreign vessels.”

It appears that, whether with or without outside pressure, Saudi Arabia relented. “Charterers are buying cargo from Iran and the rest of the world is OK with that,” said Odysseus Valatsas, chartering manager at Dynacom Tankers Management. Greek owner Dynacom has fixed three of its supertankers to carry Iranian crude.

And while some international ship-owners still remain reluctant to handle Iranian oil, due mainly to some U.S. restrictions on Tehran, increasingly more are discovering the necessary loopholes to buy Iran’s discounted oil and ship it onward to their end destinations, pocketing a profit spread in the process.

Reuters data shows that at least 26 foreign tankers with capacity to carry more than 25 million barrels of light and heavy crude oil, as well as fuel oil, have either loaded crude or fuel oil in the last two weeks or are about load at Iran’s Kharg Island and Bandar Mahshahr terminals.

The resumption of international shipping of Iranian oil has been made possible by an increase in interim, limited, insurance cover by “P&I clubs” - maritime mutual associations that provide “protection and indemnity” insurance to shippers.

Among the main reasons for the stalled shipping was that the International Group of P&I Clubs, which represents the world’s top 13 ship insurers, increased the amount covered by so-called “fall-back” shipping insurance from 70 million to 100 million euros (\$113.36 million) in April. “In the first days after lifting sanctions only Iranian ships were loaded in the country, mainly due to several problems in finding insurance/reinsurance,” said Luigi Bruzzzone of ship broker Banchero Costa.

And yet, despite a world glutted with oil, the discounted Iranian product led to a prompt resolution: “The strong interest of the market in these trades pushed all the stakeholders to solve all the problems ... and almost all P&I Clubs have granted their insurance.”

The “fall-back” cover is designed to offset any shortfall in payments from U.S. reinsurers, who are still not allowed to deal with Iran. “We are not surprised to see the increase in Iranian cargoes given the progress made by the P&I clubs and obviously the increase in Iranian production,” said Brian Gallagher, head of investor relations at leading Belgian tanker owner Euronav, which itself is not involved in Iran yet. “We’re interested in such trade ... (but) it will still take time for Iran to be fully integrated as there remain restrictions around dollar denominated transactions.” Indeed, while the partial lifting of sanctions means foreign tankers can now transport Iranian oil, risks remain because large accidents might not be fully covered.



As a result, insurers say many first-tier oil shippers, many of them publicly listed such as Euronav, Teekay Group or Frontline, still shy away from carrying Iranian oil. If the fall-back cover is exhausted in an incident, Andrew Bardot, executive officer at the International Group of P&I Clubs, said that costs like “collision and cargo liabilities, will not be covered, and will remain with the ship-owner”. A single Very Large Crude Carrier (VLCC) supertanker costs around \$90 million, and the costs of a large oil spill can reach into the billions of dollars.

“The limitations of the ‘fall-back’ cover - together with other continuing restrictions, for example those relating to the U.S. dollar and use of the U.S. financial system - however have discouraged a number of ship-owners, and in particular the large shipping groups, from resuming trade with Iran in which they were previously engaged,” said Bardot.

So with the logistical hurdles resolved, and with international vessels supporting Iran’s own tanker fleet, traders said that its oil exports was now close to pre-sanction levels of around 2.5 million barrels per day (bpd). “Iran has ramped up harder and faster than expected,” Citi analysts said.

This means that the disrupted supply from the wildfires in Canada, and the outages from militant attacks in Nigeria, would be promptly replaced with Iran oil. This would put further pressure on Canada and Nigeria to restore full output over fears of losing long-standing customers to Iran.

Iran’s oil exports were between 2.1 and 2.3 million bpd in April and May, up from 1.3 million bpd a year ago, when Iran was shut out of the European market and dependent on limited shipments to Asian buyers. Asia is the main destination for crude shipped by foreign vessels, with India, China and Japan the biggest takers, but at least four international tankers are also heading for Europe.

India, in particular, is taking a lead role as its demand soars and refiners such as Essar Oil, Reliance Energy, Hindustan Petroleum Corp, and Bharat Petroleum Corp enjoy good ties with Iran. The non-Iranian companies currently chartered to carry its oil include Chinese state controlled shipper China Shipping Development, PetroVietnam and Japan’s Idemitsu Kosan. Greek, Turkish and Seychelles-owned tankers are also shipping Iranian crude.

As a reminder, the key catalyst for the recent ramp in crude was Goldman turning bullish on oil due to near-term supply disruptions, which at least in the case of Canada are promptly getting resolved. As such, it would not be at all surprising that with the world back to an oversupplied market, anywhere to the tune of 1-1.5 mmb/d, once the peak summer driving season ends, and as all the excess oil still scrambles to find a home, that we will see a rerun of the summer of 2015, when oil flat lined at \$60 until mid-July, at which point it proceeded to promptly crumble. That, as regular readers will recall, is also Morgan Stanley’s thesis: namely that the summer of 2016 is merely a rerun of last year, and the price action will follow suit.

Saudi Arabia cuts oil prices in Europe as Iran ramps up exports

WSJ, 05.06.2016



Saudi Arabia cut its oil prices to Europe, signaling mounting competition after OPEC failed to cap its output amid Iran's exports ramp up.

In an email sent to customers, state oil company Saudi Aramco said it had cut its light crude prices by 35 cents a barrel to northwest Europe and by 10 cents a barrel to the Mediterranean for July deliveries. The price reduction is surprising, as demand typically grows in the second half of the year as refineries return from maintenance. In addition, markets have recently been buoyed by outages in countries like Nigeria.

But Saudi Arabia's move comes after the Organization of the Petroleum Exporting Countries last Thursday failed to agree on a production ceiling. The absence of output limits effectively gives a blank check for the group's two most influential members and rivals, Saudi Arabia and Iran, to pump at will.

Geopolitical tensions helped scotch the deal on capping production, with Iran taking a firm stand late last Wednesday against any move that would limit its own production as it aims for an economic comeback following the end of Western sanctions in January. By contrast, Saudi Arabia had expressed openness for a collective output cap.

The two Persian Gulf nations, which belong to rival sects of Islam, are jockeying for political influence in hotspots such as Yemen and Syria. The the European price cut on Sunday also exemplifies their intense competition for oil markets. Iran resumed its crude exports to the European Union in February after an EU embargo on its oil was lifted and is now heavily competing there with Saudi Arabia, which had partly replaced Iran as a source of European supply during the sanctions.

Shipments from Iran to the EU have now reached 400,000 barrels a day. They are set to increase to 700,000 barrels a day in the coming months after Iran clinched deals with Greek, French and Italian refiners, according to Iranian officials. By contrast, Saudi Arabia exported 800,000 barrels a day on average to Europe last year, according to the International Energy Agency.

As a result, Saudi Arabia and Iran have been matching each other's price cuts, though they deny offering special, private discounts to individual buyers. Iran believes it will ultimately have the upper hand, as its finances are less dependent on oil. "Saudi Arabia will be big loser in the price war," Akbar Nematollahi, the head of public relations at Iran's oil ministry, wrote last month in the ministry's in-house magazine. Some European oil producers could be collateral victims of the rivalry. Northern European oil producers, mostly in the U.K. and Norway, have struggled to attract new investments amid depressed oil prices.

Competition for market share has been less intense in Asia, where Iran was always allowed to sell. On Sunday, Saudi Arabia increased its light-crude prices to the Far East by 35 cents a barrel. It also raised prices by 10 cents a barrel in the U.S., where Iran is still banned from selling.

Nord Stream 2 provides cost-effective contribution to EU climate protection target

Baltic Course, 08.06.2016



Natural gas offers versatile applications, from chemical feedstock, to heating, cooling, transportation on land and sea – to power generation. In power generation, gas emits 50% less CO₂ compared to coal, even less when transport and mining are factored in, and gas is used in more efficient combined heat and power plants.

In the EU, gas is expanding its share in the power generation mix, projected to overtake coal in about 10 years. Current CO₂ emissions in the EU stand at around 4611 Mio t. of CO₂-equivalents – which is about 19.8% below 1990 levels, likely to reach the 2020 target of a 20% reduction over 1990.

However, as for the 2030 targets of 40% reduction, the European Commission contends² that Europe is not yet on track. According to a PWC study, the EU will need to decarbonise at 3.1% per year (measured in tCO₂/GDP) to reach its 40% reduction target by 2030. This is faster than the UK's 'dash for gas' in the 1990s or Germany's restructuring after reunification. Despite the EU's existing policies to tackle climate change, it will still need to "find another gear."

Coal use in the EU28 power sector accounted for 927 Million t. of CO₂ in 2013, generating a total of 905 TWh of electricity. Producing the same amount of power with gas, the EU could save 500 Mio. tonnes of CO₂, already a long way towards the reduction goal. Switching just one percent of the overall EU's electricity generation from coal to gas cuts CO₂ emissions by about 5 million tonnes. The UK for example, increased power consumption between 1990 and 2013 by 11%. Still, emissions from power generation decreased by 29% over the same period, which the UK department of Energy and Climate Change attributes to the fuel switch from coal to gas⁶.

However, in Germany gas is under pressure from cheap coal – despite an ever growing share of renewables, emissions have even gone up recently from increased coal burning, from 315 Mio. t. of energy related CO₂-emissions in 2010 (when gas covered 14% of power generation, coal 43%) to 327 Mio. t. in 2013, reflecting that the share of gas in power generation dropped to 10.5% while coal grew to 45.5%.



Germany needs to reach a reduction down to 750 Million tonnes of CO₂-emissions by 2020 (from currently 912 Mio. t.) to stay on track with its own emission reduction targets (40% under 1990 by 2020). Currently, this goal is not in sight. Latest expert estimates put the German government's plan to retire coal plants in reserve at saving only 8 Mio. t.

Using 55 billion cubic metres of gas (nameplate capacity of Nord Stream 2) to replace coal in power generation would by itself save about 160 Mio. t., or 14% of the CO₂ from power generation overall. Fuel switching from coal to gas, even within the existing power generation capacities in the EU, can move gas demand by as much as 30 bcm in one year.

As such, renowned research institutions like the IEA and IHS CERA predict a growth in gas demand. The IEA sees gas demand, even under new policies, as largely stable (+2 bcm over current levels, EU28 New Policies Scenario for 203512) – if only current policies are accounted for, demand will grow by 98bcm (EU28 Current Policies Scenario for 204013). IHS Energy sees gas demand in the EU moderately grow to about 500 billion cubic metres, driven by the power sector recovery, which will see rising demand.

If this demand for more gas is not met or gas supplies become less competitive, coal will once again replace gas (as it happened in Germany, see above). In a well supplied market, gas can compete with coal, despite the currently record low carbon price. However, this market liquidity requires new gas deliveries in a cost-competitive and secure way, since domestic production is projected to rapidly decrease.

Nord Stream 2 will offer a secure, reliable connection to the world's biggest gas reserves in Siberia, where investments from Russian and international energy companies over the last decades have ensured that the gas fields are amongst the most cost-effective sources from which to supply Europe. At the same time, Russian gas supplies are available and deliverable at short notice, making Russian piped gas the best option for Europe's gas supply - economically and ecologically.

LNG, as often suggested, will certainly play a role in supplying the EU, yet its role in realizing a secure, affordable and sustainable gas supply are limited. Higher emissions: Liquefaction and shipping of LNG causes about a third more emissions than piped gas. By comparison, the Nord Stream 2 pipeline will need only one compressor station to propel the gas across the Baltic Sea.

Lack in capacity: 55bcm of gas would require around 600-700 LNG tanker shipments in the Baltic Sea. Currently, in the whole world only 30 tankers are available for spot trading, meaning that the rest of vessels is tied up in long-term shipping contracts, mostly in Asia.

LNG follows the markets: Due to the prevailing market dynamics, LNG Imports in the EU dropped from around 80 bcm in 2011 to about 44 bcm in 2013, as suppliers directed their shipments to Asia because of the higher market prices in that region. Despite sufficient upstream facilities and many LNG regasification sites in Europe, which on average are only used at 25%, LNG cannot competitively replace piped gas in the European markets. Nord Stream 2 also compares favourably to onshore pipelines, which require significant land usage, longer construction times and burn more gas for interim compression. Over the pipeline's lifetime of at least 50 years, the Nord Stream 2 pipeline system will save 200 Mio.t. of CO₂ due to the higher average pressure and the lower number of compressor stations required to transit gas, compared to onshore transport.

Extensive Environmental and Social Monitoring Programmes have demonstrated that construction of the existing Nord Stream lines did not cause any significant environmental impact in the Baltic Sea, confirming the positive trend in environmental recovery after construction. So far, all monitoring results have confirmed that construction-related impacts were minor, locally limited and predominantly shortterm.

Nord Stream 2 will add a new and highly reliable supply route from Russia to the EU internal market, ensuring that gas remains affordable. By making more gas available to replace coal in power generation Nord Stream 2 will provide a cost-effective contribution to emissions reduction.

Nord Stream 2: Trust in Europe

ETH Zurich, 06.06.2016



The prospect of building the Nord Stream 2 pipeline between Russia and Germany is dividing the EU into two camps. By following geopolitical considerations, both sides are neglecting the concept of a liberalized natural gas market and are overlooking Europe's favorable position in current international gas trade.

When Russia's Gazprom and its five European partners (BASF, E.ON, Engie, OMV and Shell) signed a declaration to build two new pipelines through the Baltic Sea ('Nord Stream 2') in September 2015, this came as a real surprise for most observers.

The project would increase existing capacity from 55 to 110 billion cubic meters (bcm) a year by 2019. Gazprom would act as the main shareholder with a stake of 50 per-cent in the Swiss-based pipeline company. Nord Stream 2 will follow a similar route along the seabed as the first pipe-line project that started deliveries in 2011.

The project is completely financed by its shareholders and does not receive financial support from public sources of the EU or a Member State. It is clear that from the Russian side, not only the aspect of defending and maybe even the possibility of enlarging market shares in Europe, but also the geopolitical motivation of circumventing Ukrainian territory and reducing payments for Ukrainian transit play an important role in the project.

After the Black Sea pipeline project 'South Stream' to Bulgaria was cancelled in 2014 and considerations to involve Turkey in the transit business have been put on hold, the Baltic Sea seems to be Gazprom's most reliable and secure route to retain a hold on its most important market: Europe.

Immediately after the new pipeline project was launched, a controversial debate started among EU Member State governments and within EU institutions. Even the European Council meeting of December 2015 was dealing with the topic – an impressive record for a single infrastructure project.



So far, Germany is the most outspoken supporter of Nord Stream 2. The official position, also referred to by Chancellor Angela Merkel during the European Council meeting, recognizes the nature of the pipeline project as a commercial activity of economic actors involved in gas trading.

Following this argument, the role of politics should be restricted to ensuring the fulfilment of legal obligations. This line of argumentation is consistent with a tradition in German approaches to new infrastructure projects over recent decades, despite the fact, that the continuation of Russian-German natural gas trade has always received strong political support in the country.

Economics minister Sigmar Gabriel even added that building the pipeline would serve European energy security purposes by increasing direct links between producer and consumer. While most government officials in Germany's grand coalition support this view, more skeptical voices can be heard in the German parliament and even among leading party members of CDU and SPD as well as among foreign policy experts.

While in Germany and Austria, the promoters of Nord Stream 2 are quite outspoken, in the Netherlands and France, there is recognizable, but more silent support in government circles. Here, as well, the main line of argumentation is based on the added value of infrastructure diversification and the neutrality of political actors on economic activity in the market.

While support for Nord Stream 2 is mainly concentrated within a relatively small but powerful group of actors, the range of opponents is broader and more diverse. They all challenge the project as not being compatible with the goals and aims of the EU's new rhetoric about building an Energy Union.

First, political and geopolitical considerations are most prominent here. Not just Poland and other Central-Eastern European governments, but also actors from the transatlantic community are fiercely arguing against Nord Stream 2.

They point out that there is an ongoing war in Ukraine, and that sanctions remain in place against Russia – although they are not directed at natural gas trading. In their view, building a new pipeline and dealing with this difficult political situation at the same time would contradict each other.

This culminated in a common letter of seven prime ministers to the Commission, asking for a cancellation of the project, since it would create additional dependency for Germany and the EU, therefore influencing the political standpoint vis-à-vis Russia negatively. In addition, avoiding transit routes would weaken the political status of Ukraine as transit country and could deprive it of transit fees to the tune of USD 2 billion a year.

Although less openly stated, the same argument applies to Slovakia, Hungary and Poland, who would also potentially lose transit fees. A second line of opposition concentrates on regulatory questions. These focus mainly on intergovernmental agreements, third party access to the pipeline system and the effects on competition in the gas market. Regulatory arguments already stopped Gazprom from building South Stream in the past, when intergovernmental agreements were signed, that most likely did not comply with EU law. Therefore it doesn't come as a surprise that the Italian government as a disappointed supporter of the Black Sea pipeline is now trying to stop Nord Stream 2 for comparable reasons. Also, some EU Commission officials are cautiously trying to play this card against the project.

Third, a new aspect to the debate is mainly brought up by environmental groups and interestingly adapted by a broad range of other actors. It focusses on the future role of natural gas in the European energy mix.

In this context, antipathy against Gazprom is mixed with energy scenarios suggesting that the EU would not need the proposed additional quantities of gas imports, if it follows decarbonization policies strictly. Improved energy efficiency and the increase in the share of renewables would most likely lead to less natural gas consumption in the EU, although the plausibility of these scenarios depends on a whole range of different factors and policy frameworks.

All three lines of arguments against Nord Stream 2 tend to refer to the project as not being compatible with the EU's political project of building an Energy Union. Depending on the personal standpoint, it either runs against energy security considerations (looking at diversifying away from Russian imports as an aim in itself) or against its internal market policies by offering a single actor (Gazprom) too much power on the market, or against the environmental objectives of Europe's low-carbon-economy as part of the Energy Union.

There is a surprisingly broad consensus in Brussels, strongly supported by actors from the foreign, security and environmental policy communities, that Nord Stream 2 should be stopped by political actions rather sooner than later. What becomes clear by following the debate about Nord Stream 2 is a growing divergence between the categories under which different policy communities assess an infrastructure project.

The competitive market reality of private energy companies faces the geopolitically oriented mindset of foreign and security policy actors, with little understanding for the internal policy dynamics of each other. However, both dimensions are important. Without grasping each other's world, it is hard to develop criteria under which one could analyze projects such as Nord Stream 2.

First of all, it is important to understand the changes that natural gas markets have seen in Europe lately. With the beginning of the liberalization process in the 1990s, the role of governments and state actors in gas trading has been transformed fundamentally. Today, private companies are the main market players with a high degree of freedom to take their economic decisions based on cost-benefit considerations.

The EU Commission has gained power as the ultimate regulatory authority, guaranteeing access to infrastructure, but also guaranteeing free competition between different models of gas-trading, between different supply routes and between different fuels in the market. Still, infrastructure bottlenecks, insufficient competition and political influence by national governments are every day phenomena in many parts of Europe.

Although this market is certainly not functioning in a perfect way, the improvements during the last couple of years are impressive. What has changed, however, is the desperate dependency of single national or regional markets on one source and one supplier, as the growing number of terminals for the import of liquefied natural gas (LNG) and reserve-flow investments in pipelines show clearly. The increasing natural gas import from non-EU markets and the growing trade in flexible gas hubs with spot-markets have changed the context of the debate significantly. Under these framework conditions, Gazprom's former business model is under stress.



The possibility to use political influence or coercion on single state actors is fading. At the same time, the role of long-term contracts and 'take-or-pay' provisions is less prominent. Today, Gazprom and its economic partners are under pressure from market dynamics in every single region in the EU.

Meanwhile, Gazprom is adapting to this new situation by changing its business model, accepting spot-trading and the Commission's regulatory oversight. One could conclude: The European liberal market model has silently prevailed against the geopolitically motivated Russian model of creating one-sided dependencies.

Comparing this situation with most of the arguments against Nord Stream 2, it becomes obvious, that we are rhetorically returning to 20th century energy geopolitics, moving away from the reality of a modern energy market.

The new geopolitical frontier between the EU and Russia shows a spill-over effect in the world of natural gas markets and one should ask the question, whether the EU has to allow that to happen. The project's opponents call for the state to intervene and for strong command-and-control policies that do not fit into the picture of a liberalized gas market.

Asking a national government 'to dump' a pipeline project just appears to be outdated. For good reasons, one can deny public financial support for a project – as is happening in the Nord Stream 2 case. In order to stop a privately financed endeavor in a market environment, there must be more than just uncomfortable feelings on the side of regulators.

Also the second line of arguments against Nord Stream 2 – 'Europe doesn't need more gas' – is flawed. Since the nature of a market economy is to be found in actors' taking risk and chasing opportunities, the claim that political actors should intervene and stop a project because there will be 'no need' for gas in the next 20 years, stems from a time of centrally-planned and state-controlled energy markets.

Natural gas will compete against other fuels in the heating, transport and electricity sector, while the restrictions of climate policy can be met by many different mitigation options. The idea of a market economy implies, that every actor should have the right to take risks and dump money, as long as this is not public money.

One of the main aims of the liberalization process in gas markets was to Europeanize regulatory practices, to introduce competition and to put the consumer at the center of political action. Most of the arguments around Nord Stream 2 are – on purpose or not – trying either to re-nationalize the debate, to avoid a competition-friendly environment with Gazprom as one among several actors or to put geopolitics before consumer interests.

If we follow these arguments, this would mean a 180 degree turn-around from a policy approach that has been successfully followed during the last 15 years in the EU's internal gas market. Instead, the EU should be more self-confident about its market policy, allowing competition to pick winners and trusting in the Commission's regulatory control. To readjust the debate, three important aspects need to be considered for future dealing with the Nord Stream 2 case:

First, the EU Commission has to be in the regulatory driver seat, expecting an unbiased assessment of realistic compatibility options of the project with unbundling, third party access and competition provisions under the internal market laws. Following these criteria, the Commission has to analyze the project and decide how to deal with the investors' approach. This should be done without taking gas demand scenarios or geopolitical considerations into account.

Second, for good reasons, the German government has lost a lot of political credit on Nord Stream 2. Not because the project is wrong from an energy point of view, but because the rules of good diplomacy and the perspective on geopolitics were absent in dealing with the proposal.

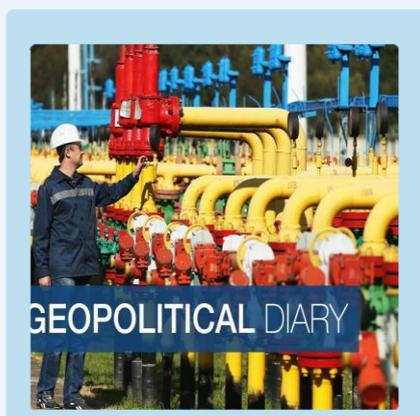
Consulting the Russian government before talking to Central-Eastern European member states or the Commission was a major fault and discredited the commercial nature of the project. In an integrated European gas market, the time of national energy infrastructure politics should be over. Therefore, it would be wise to end engagement with the project on the side of German politics.

Third, in a community that is based on the rule of law, the rule of law should apply to all actors in the same way. In the end, this means, that economic activities in the range of the legally defined framework should be assessed under the existing regulatory criteria, but not under normative categories of good or bad.

It is a question of self-confidence of Europe's liberal market approach to handle a project such as Nord Stream 2. If there is a desire to change the way politics and markets interact in the EU, this would need a more fundamental debate for which Nord Stream 2 is certainly not the right point of departure.

For Russia, natural gas is losing its potency as a political weapon

Strafor, 09.06.2016



There was a time when Russia could manipulate other countries with its natural gas supplies. It still can, but the threat is less effective than it once was. Ukraine's national natural gas company, Naftogaz, confirmed that it will consider negotiating direct natural gas purchases with Russian natural gas giant Gazprom without mediation from the European Union.

Ukraine's willingness to deal directly is a sign of growing assertiveness and also of how much Kiev — with help from Brussels — has been able to chip away at Moscow's ability to use gas supplies as a political weapon.



Moscow's use of energy to affect policy in not only Ukraine but also other countries in Central and Eastern Europe that import Russian gas almost exclusively was a constant theme of the 2000s and early 2010s. In response, the European Union enacted a number of initiatives designed to depoliticize natural gas.

Legal architecture was created, such as the Third Energy Package, which split the ownership of natural gas transiting a pipeline from the owners of the pipeline, and physical infrastructure, such as gas interconnectors and pipelines, was built up so that gas could move more freely through Europe.

Ukraine, which is not a member of the European Union, had been slower to develop this legal and physical infrastructure but now it largely has. There are now enough interconnections between Ukraine and its western neighbors — Slovakia, Poland and Hungary — that Ukraine can import up to 20 billion to 25 billion cubic meters of natural gas annually from Eastern Europe.

Though most of the natural gas that Ukraine buys still originates in Russia, its ability to import from its neighbors means that Russia can no longer charge Ukraine a much higher price than it charges them because Ukraine could just buy the gas at a lower price from those countries. And, importantly, Brussels is breaking down an element of Russia's contract with natural gas importers that prohibits them from exporting or selling gas to others.

Moreover, the European Union has included Ukraine (and the Balkans) in its broader Energy Union initiative, which Brussels established to extend its common energy market initiatives to neighbors not in the European Union. Ukraine has been gradually adopting Third Energy Package principles and legislation.

In addition to building up its physical infrastructure, Kiev has also implemented measures to limit natural gas consumption, including increasing efficiency in winter heating and using more coal for power generation.

In 2011, Ukraine consumed 53.7 billion cubic meters of natural gas. In 2015, it consumed just 28.8 bcm, consequently reducing natural gas imports to 16.2 bcm in 2015, of which only 7 bcm was directly purchased from Russia. (Ukraine imported 9.2 bcm via Europe.) This trend even continued over the entire course of 2015. Ukraine has not directly purchased gas from Russia since November 2015 and did not during the worst of the 2015-16 winter even though it had negotiated a winter package with Gazprom through the trilateral negotiating framework.

Now that these changes are largely in place, negotiations between Naftogaz and Gazprom will mostly be financially motivated, even pragmatic, although the political relationship between Moscow and Kiev remains extremely tense. Naftogaz may even have the upper hand because it does not need a gas deal, it merely prefers it. But negotiations are not necessarily going to be smooth. The two companies have a number of outstanding claims, counterclaims, lawsuits and countersuits pending against one another over past dealings. These include most recently Gazprom's threats to sue Naftogaz over increasing natural gas transit fees in January 2016.

Though Europe is entirely on board with initiatives promoting one common energy market, Russia's proposed Nord Stream II pipeline project is driving a wedge between its supporters (Germany being the strongest) and its Eastern European detractors, such as Poland and Slovakia.



The project envisions routing a 55 bcm natural gas pipeline through the Baltic Sea directly from Russia to Germany, circumventing Ukraine and Eastern Europe. Germany has chosen to view the project in purely economic and business terms, while the project's detractors regard it as Berlin selling out on the Energy Union concept and directly negotiating deals with Russia — possibly allowing Russia to still politicize natural gas supplies.

From the point of view of Eastern Europe, Nord Stream II makes it more likely for Russia to implement natural gas cutoffs again than without the pipeline. Historically, most Russian natural gas flowed through Eastern European countries such as Poland or Ukraine to Central European markets such as Germany, and despite this, Russia was twice willing to cut off natural gas to all of Europe to punish Ukraine for going against its wishes.

To the project's detractors, adding even more infrastructure to directly deliver natural gas to Germany eases the constraints on Moscow's ability to cut off supplies to Eastern Europe, specifically. Previously, cutting off gas to Eastern Europe also meant cutting off gas to Germany. Though these Eastern European countries have built up considerable infrastructure for trading, it is not perfect, and they would still feel considerable shortages in the event of a substantial cutoff.

It is for this reason that Eastern European officials, including Slovakia's Maros Sefcovic, the European commissioner for the Energy Union, have been strong advocates of aggressive interpretations of EU law if the pipeline is built.

EU law, however, is not clear on this particular pipeline. Germany has taken the view that key aspects of the offshore part of the pipeline do not need to adhere to all of the Third Energy Package, whereas Sefcovic has argued that the Third Energy Package should extend to the exclusive economic zone of Europe, not just its territories.

The European Commission has not officially ruled on the issue, but it is currently discussing an interpretation. Should Brussels interpret the application of the Third Energy Package offshore, the pipeline project may be in jeopardy over its economic viability. Such a ruling would require the stripping of the pipeline's ownership — which is now supposed to be more than 50 percent Gazprom's — from the supplier of the gas, which is of course Gazprom.

In the midst of this process, Germany has been trying to ease the concerns of its neighbors, and Wednesday, German Economy Minister Sigmar Gabriel outlined three conditions for Berlin's approval. Those are that the pipeline must adhere to German regulations, must not affect Ukraine's pipelines and must not limit Eastern European natural gas supplies. Though Berlin may be trying to ease tension over the divisive pipeline, the problem from the perspective of Eastern Europe is that enforcing the latter two conditions once the pipeline is built would be difficult.

Though the concerns over pipelines and natural gas supplies have eased, the issues remain at the center of most political debate in Europe over energy security and will continue to do so. Despite the European Union's single market policy, Russia will inevitably remain the region's most significant natural gas supplier. In 2015, Russia exported 160 bcm of natural gas to Europe in addition to the 24 bcm it exported to Belarus and Ukraine. Only five countries — none in Europe — produced that much natural gas that year. The best Europe can do is limit Russia's ability to manipulate gas supplies for political aims.

None of this, however, detracts from the reality that the utility of using natural gas as a political lever is far less potent and that Ukraine and others have made significant progress in developing natural gas supply options. Indeed, Russia's increased pragmatism and its business-minded approach to its energy negotiations with Europe — and now Ukraine — are indicative of the shift in Moscow's thinking on the relationship between energy exports and its foreign policy.

EU countries agree on mandate over scrutiny of Russian gas deals

Bloomberg, 06.06.2016



European Union governments agreed on a mandate for talks on a draft law to strengthen scrutiny of natural-gas contracts with Russia and other external suppliers. The draft law on intergovernmental energy agreements was proposed by the European Commission in February as part of a package to improve energy security in the region.

Energy ministers representing the bloc's 28 member states meeting in Luxembourg on Monday endorsed a provision to introduce a mandatory EU-law compatibility check before governmental agreements on gas with third countries are signed.

Under a compromise crafted by the Netherlands, the holder of the EU presidency in the first half of this year, representatives of EU nations agreed to apply the ex-ante checks to intergovernmental gas deals while excluding oil contracts from the assessment.

They also softened the proposed provisions on ex-post assessment of non-legally binding commitments. Member states will not have to notify the commission about such commitments, which include joint political declarations or memoranda of understanding, unless they want to do so.

To enter into force, the proposed law on governmental agreements needs weighted-majority approval by member states in the EU Council of governments and majority backing from the European Parliament. The two institutions have the right to propose amendments and their positions are reconciled in negotiations known as trilogue, which also involve the Brussels-based commission.

IEA sees tighter markets next decade

Natural Gas Europe, 09.06.2016



The IEA sees the present length in the global gas market – as evidenced by spot prices lower than oil-indexed prices would be – continuing, with “heavy oversupply” until 2018. But upstream investments will remain low, setting the course for higher prices by the early to mid-2020s, its latest Medium-Term Market Report for gas says.

“We see massive quantities of LNG exports coming on line while, despite lower gas prices, demand continues to soften in traditional markets,” said IEA CEO Fatih Birol. These contradictory trends will both impact trade and keep spot gas prices under pressure.”

He added that the combined factors of cheaper coal and continued strong renewables growth were blocking gas from expanding more rapidly in the power sector. Net imports to Europe are projected to increase by roughly 40bn m³/yr over the next five years as demand growth, albeit very slow, and falling production push import requirements to record highs.

Some of this will come as LNG, as Japan, China and Korea move from short to long positions; although Europe’s ability to absorb additional LNG is limited by cheap coal and increasingly competitive Russian supplies.

The report also dwells on how Russian gas will reach Europe, in particular the relative merits of Ukraine and Nord Stream. Ukraine now transits 63bn m³ – or 40% of total Russian pipeline exports to Europe (including Moldova).

Gazprom is determined to minimise flows through Ukraine – although the report says that flows have been very reliable for a few years, especially given all the problems the country has to deal with – and yet expanding Nord Stream is also problematic contractually and physically, not to mention politically. This last is an area the report steers clear of.

Gazprom is the major stakeholder of the project, with a 50% share, while the remaining stake is split among Engie, BASF, Shell, E.ON and OMV, who do not own any capacity but collect on transit fees. If this 55bn m³/yr expansion is realised, total transit capacity through Nord Stream would be 110bn m³/yr, more than enough to displace all gas transiting Ukraine to the EU.

But gas flows would need some reconfiguring. Gas today is contracted to delivery to Eni, Austrian Eongas and generally south/south-east companies at Baumgarten – the border point from Slovakia into Austria. But shifting the contractual delivery point for all that gas, as Gazprom has proposed, to the Nord Stream landfall at Greifswald instead would require complex capacity bookings between north Germany and Baumgarten, leading to price renegotiations, and more pipeline links having to be built, it says.



Given the above bottlenecks, even with an expansion of Nord Stream, it is likely that Turkey's fast growing Istanbul region, Moldova and probably Hungary, Bulgaria, Greece, the Balkans and parts of Italy would still need to be supplied via Ukraine. This could amount to about 40-45bn m³/yr, about 25bn m³/yr less than was shipped through Ukraine in 2015.

It is also questionable if 110bn m³/yr supplied via one route would improve gas transportation security. Disruption of any serious kind to the Nord Stream pipeline system could affect up to 60% of Russian gas exports to Europe if the Yamal route, Nord Stream 1's, precursor, is full. If Ukraine transit falls significantly, today's large and flexible capacity is unlikely to be kept in working order.

For Ukraine, Russian gas transit is worth about \$1.6bn/yr, used not only are used to cover the operational and investment costs of the system, but also help reduce Naftogaz's deficit. Operating the Ukrainian gas transmission system effectively is significantly different depending on whether it handles 70bn m³/yr or 30bn m³/yr.

Gazprom's success in launching Nord Stream 2 remains subject to resolution of a number of issues, the IEA says, including new supply terms with its European buyers such as outspoken opponent Eni; and how will Gazprom address the regulatory issues related to third-party access and the current limitations on the use of OPAL.

Overall, global projected demand growth of around 140bn m³/yr is not enough to absorb the 190bn m³/yr of new liquefaction capacity projected to come on stream between 2015 and 2021 and the supply side will need to do its part to keep the market in balance, including low use of export facilities.

However by 2021, the report expects demand and supply to have returned more into alignment. For new projects in particular, this suggests that returns on investments will be low for some years. Similarly, the sharp compression of price differential among regions reflects a tendency for prices to move towards (and in some cases below) marginal costs of transportation – a natural development in an oversupplied market with no region needing to attract extra cargoes.

Slower demand and converging prices have resulted in a trading environment less conducive to growth in spot and short-term transactions. It is not surprising, therefore, that after a long period of growth, spot and short-term transactions as a share of total trade declined last year.

But while persistent oversupply and compressed regional spreads are set to remain a drag on the growth in spot trading, there are more sellers and buyers entering the LNG market, meaning a longer chain of potential transactions. And the more flexible contract model governing US exports will naturally trigger growth in short-term and spot trading. How lucrative those transactions are seems to be the key question rather than whether they will occur at all.

In aggregate, the three top Asian LNG importers are likely to see their imports-to-contract ratio moving from a short position of around 40bn m³/yr in 2011 to a long position of around 20bn m³/yr in 2017-18. Korea, Japan and China all tapped heavily into the spot market until last year, to meet robust demand growth. The outlook for 2015-18 is remarkably different, as all three countries will likely have to enter the spot market on the selling side. Sellers will therefore be forced to chase new markets and new buyers.

Potential customers previously shunned as too risky or too challenging to trade with, often due to their low credit-worthiness or their small volume requirements, are now attracting the attention of LNG sellers. Lower prices make purchases financially more accessible thus lowering counterparty risks while sellers who sit on long-unsold positions are happy to take on more risk.

Pressure to renegotiate contracts will intensify and the sellers look likely to lose. Petronet took only about 70% of its contracted 10bn m³/yr from Qatar over a period of time, falling below minimal contractual obligations. But anxious to retain business, last year Qatar waived \$1bn of penalties and they rewrote the formula to bring contract prices more in line with the level of spot prices. The IEA expects the trend to continue towards shorter contract duration, full destination flexibility and, particularly as oil prices start recovering, lower oil slopes.

IEA: LNG players to seek new markets

WSJ, 08.06.2016



Major traders and sellers of liquefied natural gas will begin to look to new markets over the next five years as demand from traditional centers wanes, the International Energy Agency said in a report.

In parallel, global supply is set to grow exponentially, putting pressure on prices in the spot market. Cheaper prices for alternative fuels, such as coal, will also soften gas prices, while more carbon-efficient technologies could push demand away from natural gas and toward renewables. The market will likely find strength in China, India and Southeast Asia as Japan and South Korea buy fewer volumes, the IEA said.

Chinese gas demand slowed to around 4% in 2015, leading to fewer purchases on the spot market. But demand is likely to recover, as the country diversifies its energy sources away from dirtier fuels, such as coal, to work toward improving air quality.

Chinese demand remains the largest downside risk to overall gas demand growth, the IEA said. The extent to which efforts are made to improve environmental policy and the speed at which industrial activity picks up will determine the rate at which demand grows.

Indian gas demand will rise to around 6% each year until 2021, the body said. India is a price-sensitive LNG buyer, and as international prices fall, demand is set to encourage buyers to import gas. But in the short term, sellers will focus on Europe as a market for their excess volumes of LNG.

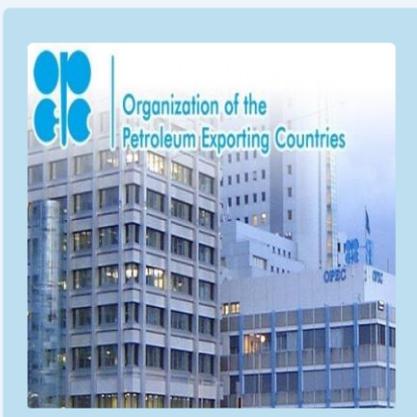
“We are at the start of a new chapter in European gas markets,” IEA Executive Director Fatih Birol said. But there is a question mark over how much natural gas Europe can actually absorb. The IEA projects European gas demand to increase only modestly over the medium term. As Russia competes with volumes from the U.S., Gazprom is likely to adopt a more competitive and flexible approach to gas pricing, possibly reducing demand for LNG volumes in the region.

The body has dropped its global demand forecast figures from 2% to 1.5% each year until 2021, to reach 3.9 trillion cubic meters. A slowing global economy is reducing demand for fossil fuels. Global liquefaction supply will increase by 45% between 2015 and 2021, according to the IEA. Volumes will mostly increase from Australia and the U.S. Qatar's position as the world's largest exporter of natural gas will be challenged by Australia. Qatar's gas is exported from the super-major 77 million tons a year Ras Laffan export facility.

LNG contracts are also set to become more flexible as trading dynamics change. Traditional oil-linked pricing is likely to be replaced or mixed with natural gas hub pricing. Some producers have already moved toward hub pricing. U.S. Sabine Pass volumes are linked to prices at Henry Hub.

Oil supply disruptions highest since 2011

AA Energy Terminal, 10.06.2016



Disruptions in crude oil supplies worldwide were at their highest monthly level in May since January 2011, the U.S., EIA said. “Unplanned global oil supply disruptions averaged more than 3.6 mbpd in May 2016,” the EIA said.

The administration pointed out to surge of production cuts in Canada, Nigeria, Iraq and Libya, and mentioned outages in Kuwait, Brazil and Ghana, noting that disruptions in the latter group of countries were offset by the supply cuts in the former group. The EIA said wildfires in Canada's oil rich province Alberta led to a supply disruption of an average 0.8 mbpd in May.

In Nigeria, militant attacks on oil and gas infrastructure caused supply disruptions in May to increase to 0.8 mbpd, while “Nigeria's crude oil production fell to an average of 1.4 mbpd in May, its lowest monthly level since the late 1980s,” the administration noted.

While power outages and unfavorable weather conditions in Iraq's Basra Gulf region led to a supply cut of 50,000 barrels a day, issues with oil exports from Libya added another 50,000 barrels per day to disruptions. Coupled with domestic production decline in the U.S., “the rise in disruptions contributed to a month-over-month \$5 per barrel increase in Brent crude oil spot prices in May,” the EIA said.

With unforeseen supply cuts around the world and global oil demand picking up slowly, Brent price rose from below \$30 a barrel in late January to almost \$53 per barrel early Thursday -- its highest level since October. The EIA expects global supply outages to decrease in June since most are subsiding, such as the wildfires in Canada and poor weather conditions in Iraq's Basra. But, it warns that supply disruptions due to political conflicts, such as the ones in Libya, Nigeria, northern Iraq, South Sudan, and Yemen can also last for years.

No new Australian LNG projects doesn't mean no new LNG

Reuters, 09.06.2016



Conventional wisdom in the liquefied natural gas (LNG) sector is that no new projects will be built for several years, given the vast cost can't be reconciled with the current low prices. This view has led some in the industry to predict that the market will flip back to a structural shortage sometime in the early to mid-2020s, once again sending prices soaring as new supply takes so long to be built and become operational.

The cancellation or deferment several projects in Australia, Canada, the United States and elsewhere seems to perfectly illustrate the view that no new LNG will be coming to market once the plants currently under construction are completed.

The wave of LNG building in recent years has seen eight projects being built in Australia, with five now operating and the remaining three nearing completion, and five in the United States, the first of which has starting shipping cargoes. This has helped drive LNG from a structural deficit to a surplus, with the attendant decline in Asia spot prices from a high of \$20.50 per million British thermal units (mmBtu) to a record low of just \$4 in April this year.

Long-term contract prices linked to crude oil have also suffered as Brent has slumped, further undermining the economics of new plants. Australia's biggest LNG operator, Woodside Petroleum, shelved plans to build the \$30 billion Browse LNG project in Western Australia state in March, citing oversupply and low prices.

Royal Dutch Shell and Malaysia's Petronas have also pushed back final investment decisions on greenfield LNG developments on Canada's west coast, and progress has slowed on planned U.S. projects and those in frontier countries such as Mozambique and Tanzania. The era of mega-LNG projects appears to be over, at least for now.

This point was underscored by Saul Kavonic, a senior analyst at consultants Wood Mackenzie, who told the Australian Petroleum Production and Exploration Association conference in Brisbane this week that the country's wave of recent LNG projects had failed to meet hurdle rates.

The average breakeven cost for the recent projects, which will see Australia overtake Qatar as the world's biggest supplier of the super-chilled fuel, is \$12.60 per mmBtu, a price well above the current spot level and also most long-term oil-linked contracts. However, while Kavonic said that building new projects is unviable in the current situation, Australian LNG producers can boost volumes if demand warrants increased supply. The first way to do this is through de-bottlenecking existing plants, a process Kavonic said delivered an average 14 percent boost in capacity at LNG plants that have implemented the efficiency measures in the past.



An additional 4 million tonnes per annum of LNG is probable and a further 6 million possible from de-bottlenecking, Kavonic told the conference. These are fairly significant numbers, as 10 million tonnes would represent an 11 percent increase in Australia's eventual capacity and is just under half of Chinese annual demand. The second way to boost capacity is through brownfield expansions, which Kavonic said typically cost about 30 percent less than building projects from scratch.

This could add more than 10 million tonnes in Australia, but Kavonic estimates that brownfield developments would require a price above \$8 per mmBtu to be economically feasible. A third way to boost capacity is backfill, which involves committing new gas to existing projects to allow them to continue operating beyond their expected and planned life.

While this doesn't add new capacity, it prevents volumes from leaving the market, and Kavonic estimates that 15 million tonnes of capacity could be maintained by 2030 if companies adopt backfill policies. What becomes clear is that there are substantial volumes of LNG that can come to the market in the coming years at considerably lower prices when compared to the huge cost of developing new plants and natural gas fields to supply them.

There are of course some fairly significant hurdles, the main one being the need for the various companies in the industry to put aside rivalries and work together to share infrastructure and establish joint ventures to supply natural gas to LNG trains. "Boys and girls don't like to share their train sets," was how Kavonic put it, a jest that rings true when looking at the three adjacent coal-seam gas to LNG plants recently built at Gladstone, on Australia's east coast.

These plants don't share infrastructure even though it would have been more cost-effective for all concerned if they had jointly developed facilities such as pipelines, storage, jetties and power supply. Perhaps the expected period of low prices in the next few years will encourage the sort of innovation and cooperation that would allow LNG producers to increase output at competitive costs should demand grow strongly in the 2020s.



Announcements & Reports

▶ *BP Statistical Review of World Energy June 2016*

Source : BP

Weblink : <http://www.bp.com/content/dam/bp/pdf/energy-economics/statistical-review-2016/bp-statistical-review-of-world-energy-2016-full-report.pdf>

▶ *The New Japanese LNG Strategy: A Major Step Towards Hub-Based Gas Pricing in Asia*

Source : OIES

Weblink : <https://www.oxfordenergy.org/publications/new-japanese-lng-strategy-major-step-towards-hub-based-gas-pricing-asia/>

▶ *Natural Gas Weekly Update*

Source : EIA

Weblink : <http://www.eia.gov/naturalgas/weekly/>

▶ *This Week in Petroleum*

Source : EIA

Weblink : <http://www.eia.gov/petroleum/weekly/>

Upcoming Events

▶ *7th International Energy Forum*

Date : 10 June 2016

Place : Istanbul, Turkey

Website : www.iicec.sabanciuniv.edu

▶ *Energy Systems Conference 2016*

Date : 14 - 15 June 2016

Place : London, UK

Website : www.energysystemsconference.com

▶ *World National Oil Companies Congress*

Date : 15 - 16 June 2016

Place : London, UK

Website : <http://www.terrapinn.com>



► *Energy Trading Central and South Eastern Europe 2016*

Date : 15 – 16 June 2016
Place : Bucharest – Romania
Website : <http://www.energytradingcsee.com/>

► *Eurasian Natural Gas Infrastructure*

Date : 22 – 23 June 2016
Place : Athens – Greece
Website : <http://www.engi-conference.com/>

► *ERRA Summer School: Introduction to Energy Regulation*

Date : 20 - 24 June 2016
Place : Budapest, Hungary
Website : <http://erranet.org>

► *FLNG World Congress 2016*

Date : 28 - 29 June 2016
Place : One Farrer Hotel, Singapore
Website : <http://www.flngworldcongress.com/>

► *9th SE Europe Energy Dialogue*

Date : 29 – 30 June 2016
Place : Thessaloniki, Greece
Website : www.iene.eu

► *FSRU Asia Summit*

Date : 06 – 07 September 2016
Place : Amara Sanctuary Resort Sentosa, Singapore
Website : <http://www.fsrusummit.com/>

► *Operational Excellence in Oil and Gas Europe*

Date : 19 – 21 September 2016
Place : London, UK
Website : <http://www.opexinoilandgasemea.com/>

► *Global Oil & Gas - Black Sea and Mediterranean*

Date : 22 – 23 September 2016
Place : Athens, Greece
Website : www.iene.eu



► *23rd World Energy Congress*

Date : 09 - 13 October 2016
Place : Istanbul, Turkey
Website : <http://wec2016istanbul.org.tr/>

► *15th ERRA Energy Investment & Regulation Conference*

Date : 17 - 18 October 2016
Place : Budapest, Hungary
Website : <http://erranet.org/InvestmentConferences/2016>

► *21st IENE National Conference “Energy and Development 2016”*

Date : 24 - 25 October 2016
Place : Athens, Greece
Website : www.iene.eu

► *European Autumn Gas Conference 2016*

Date : 15 – 17 November 2016
Place : Hague, Netherlands
Website : <http://www.theeagc.com/>

► *5th Greek Cyprus Energy Symposium*

Date : 29 - 30 November 2016
Place : Nicosia, Greek Cyprus
Website : www.iene.eu