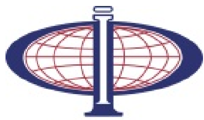

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POTEN LNG OPINION

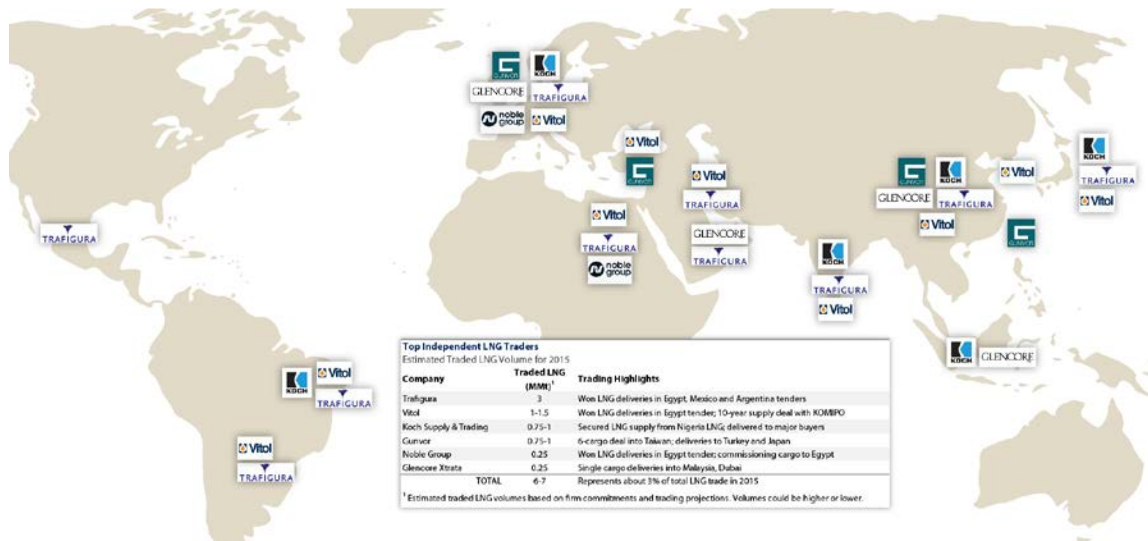
Traders Take More LNG Market Share in 2015

The LNG desks at the international trading houses have been steadily growing in importance in the LNG market as the commodity business's traditional middlemen gradually take market share and become significant suppliers. Typically these type of traders have provided liquidity in spot commodity markets and some of the biggest name energy traders have been able to establish significant positions in LNG, particularly in emerging markets. But 2015 is shaping up to be the year that the pure trader takes a more substantial role. In three of the highest profile tenders this year in Argentina, Mexico and Egypt, traders will account for the majority of the supply. At the same time, Vitol is set to begin a 10-year supply deal into Korea, an unprecedented term for an LNG trader. Total delivered volume from independent commodity traders is likely to be around 7 MMt this year, which would be around 3% of the entire market, according to Poten estimates.

Trader Trafigura burst onto the LNG scene in 2013 with a hefty supply deal into Mexico's Manzanillo with the country's electricity incumbent, Comision Federal de Electricidad (CFE). It followed that with two other major tender awards into Mexico, including the first short-term supply into the Altamira terminal on the Caribbean coast this year. The successes in Mexico surely helped Trafigura land almost half of the supply in a tender for more than 70 deliveries issued by the Egyptian Natural Gas Holding Co (Egas). Trafigura got 33 of the cargoes to be delivered in 2015 and 2016, with 16 deliveries planned for this year. This haul has launched Trafigura into the position as top independent commodity trader in the LNG market, taking the crown from Vitol (see LNGWM, June '13). With its positions in Egypt, Mexico and at least five cargoes into Argentina as well as early-2015 sales to Kuwait, Dubai and Asian buyers throughout the year could put its total traded volume close to 3 MMt in 2015. Last year, Trafigura traded 1.7 MMt and did not record any volume for 2013, according to the company's annual report. If this year's volumes materialize, Trafigura will start to challenge the smaller trading operations within large producers, such as Gazprom, which could trade as much as 3 MMt this year.

Vitol Takes Lead On Long-Term Business

Vitol started deliveries this year in what is the first long-term LNG supply contract from a commodity trader, sending cargoes to Korea Midland Power Co (Komipo). The 10-year, 0.4 MMt/y deal was announced April 2012 and was groundbreaking at the time for an LNG trader without dedicated access to supply to enter into a term deal. It could be a harbinger for additional opportunity for traders to take part in the medium- and long-term positions, which is where some see the most value in the LNG market. The Geneva-based trader also had a five-year contract with Kuwait Petroleum Corp (KPC) that ended in 2014. Vitol bolstered its profile by securing seven cargoes in the Egas tender and has been consistently active in the spot market. Vitol has also been successful as a supplier to Argentina, providing the country's logistically-tricky Escobar terminal



Top Independent LNG Traders
Estimated Traded LNG Volume for 2015

Company	Traded LNG (MMt)[1]	Trading Highlights
Trafigura	3	Won LNG deliveries in Egypt, Mexico and Argentina tenders
Vitol	1-1.5	Won LNG deliveries in Egypt tender; 10-year supply deal with KOMIPO
Koch Supply & Trading	0.75-1	Secured LNG supply from Nigeria LNG; delivered to major buyers
Gunvor	0.75-1	6-cargo deal into Taiwan; deliveries to Turkey and Japan
Noble Group	0.25	Won LNG deliveries in Egypt tender; commissioning cargo to Egypt
Glencore Xtrata	0.25	Single cargo deliveries into Malaysia, Dubai
TOTAL	6-7	Represents about 3% of total LNG trade in 2015

[1] Estimated traded LNG volumes based on firm commitments and trading projections. Volumes could be higher or lower.

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The company is expected to trade between 1 MMt and 1.5 MMt this year, including its deal with Komipo.

The LNG desk at Koch Supply & Trading has been developing its trading capabilities since 2013 and has become the third-largest trader in the market with an estimated traded volume this year of around 0.75 MMt. The US-headquartered energy trader has not captured the headline deals that Vitol and Trafigura have but have been steadily doing business in both basins. Its entry into the market with a strip of Nigeria LNG cargoes from Enel came in late-2013 and has gained additional supply from the Bonny Island production plant since. Koch has been able to build business around a relationship with Malaysia's Petronas as well as with Atlantic Basin consumers such as Petrobras.

Market sources expect Gunvor to challenge Koch for the third ranking in the market after hiring a short-term team last year that initiated a flurry of activity already in 2015. One of the oil market's largest oil traders, Gunvor reportedly has obligations for a strip of six cargoes into Taiwan's CPC this year and have delivered cargoes to Turkey and Japan. The Hong Kong-based commodity trader Noble Group made its mark earlier this year by poaching a team of traders from Bank of America Merrill Lynch and quickly winning cargoes for Egypt. The Egas tender provided Noble with obligations for seven deliveries to its Ain Sokhna import terminal. Noble accounted for Egypt’s commissioning cargo in March as well as its first commercial delivery in April. While the Egypt cargoes were a coup for Noble is in the early days of building its LNG trading book and could exceed an expected 0.25 MMt of traded volume this year. Glencore Xtrata is also single cargoes periodically but the LNG team is still reeling from the tragic death of its leader, Luis Lesmes, last year. Excelerate Energy continues to carve out a niche in the LNG trading business but is ultimately a shipowner with a trader business, not a pure commodity merchant.

Traders use existing relationships to build business

The traders that have been able to pull off major LNG deals were able to gain clout into new markets because of existing relationships in other commodities, particularly in coal. In 2013, when Trafigura swooped into the CFE tender to take nearly all of the LNG delivery windows that were tendered out, the Switzerland-based trader were also working on finalizing a 3.8 MMt coal contract with CFE. In Egypt, Trafigura is a fuels supplier and the trading company’s executive chairman said last year that it would invest in Egypt’s nascent coal industry, which has more than 15 GW of coal-fired power planned. Vitol will start sending LNG volumes to Komipo this year but is already selling the Korean power company coal through the Boryeong terminal in the country’s northwest region. Komipo has the largest coal-fired power plant in Boryeong as well as a 1,350 combined cycle plant fired by LNG. Vitol also gained access to KPC when it started importing LNG in 2010 because of the trader's foothold there in crude oil.

Trafigura tackles risk with optionality

Breakthroughs for traders have largely been in emerging markets where the credit risk, particularly in the case of Argentina and Egypt, is too high for more risk-averse suppliers like the international oil companies while the importers are less stringent in pre-qualifying suppliers. “It is not so easy to make a big breakthrough in Japan unless you show you have access to significant supply,” a trader explained. “In one of these new markets, if you want to go short, you go short and you can do it without too many inquiries.” Trafigura has created an LNG risk mitigation strategy around storage availability and shipping optionality. A 15-month storage deal at Petronet’s underutilized Kochi import terminal in India has allowed Trafigura to assure buyers, especially those concerned with security of supply, that the trader is not going short when it can offer to sell storage already in-tank.

Storage also limits the risk of unforeseen interruptions, such as cargo cancellations, payment problems and operational risk at import terminals. It also allows traders to de-risk an open-ended bid in a supply tender. If the delivered, ex-ship (DES) side of a free on board (FOB) to DES back-to-back deal does not arise, Trafigura can still bid on a competitive FOB cargo knowing that storage is an option for the volumes, which can be then sold on at a later date. Brazil's Petrobras has used a similar strategy by taking firm storage capacity at Galp's Sines terminal in Portugal, although its ultimate goal is supply certainty for its erratic power market, and other traders have entered into put and call agreements, mostly at European import terminals, to reduce trading risk. However, taking a dedicated storage deal, like Trafigura has done at Kochi, is expensive and can only be profitable if it is used as a tool in a larger LNG portfolio.

Traders turn to well-worn playbook

Traders are turning to a well-worn playbook to guide their entry to the LNG markets. Traditionally, traders like Vitol, Trafigura and others have sought to secure cheap freight and access to storage as well as key infrastructure in order to give them the operational flexibility they need to take advantage of opportunities they believe they have spotted before other competitors. Vitol, for example, has used its 350,000 barrel per day of refining capacity around the world and its petroleum terminals and other infrastructure in 14 countries to support its trading activities. It is widely known as an aggressive and skillful LPG trader in Asia with a specialty in delivering large cargoes to needy clients on short notice, a specialty that can be risky, but also frequently yields premiums from clients caught short. Trafigura, Koch and other traders have made similar investments in infrastructure intended to give them an edge.

Trafigura has been able to take advantage of the overhang of shipping tonnage in the LNG market, especially by chartering Golar vessels that are not under long-term commitments. Some suggest that Trafigura and Golar have a preferential option deal that allows

the trader to charter its ships but it is more likely that the two come together so often because Trafigura is arguably the company with the largest need for shipping and Golar is long on tonnage. Golar has seven newbuilds that came out of shipbuilding yards over the last two years that are without a dedicated charter agreement. caused a collapse in the daily charter rate, which is enticing some commodity traders not yet in the LNG market to enter the market . Charter rates were $100,000 per day higher two years ago and stagnating risk taking in the market that traders thrive on. The capital risk for cargoes is also less now that LNG prices are more than half of what they were in the first half of 2014. An average-sized cargo cost nearly $60 million last year when spot prices were more than $18/MMBtu versus cargoes costing around $20 million today with prices just over $7/MMBtu.