GLOBAL LNG MARKET: RUSSIA TAKES 6% AT ONCE

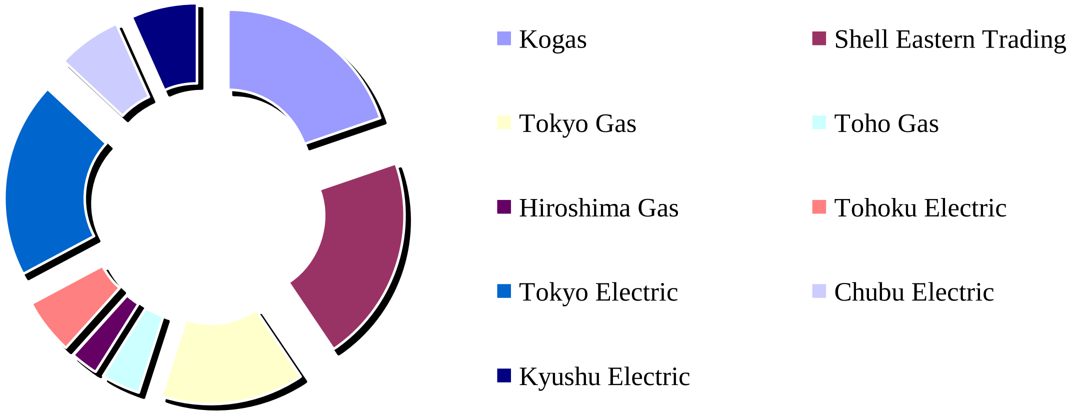
BY KIRILL LEBEDEV, IFS SENIOR ANALYST, FEBRUARY 19, 2009

Russia has entered the club of LNG exporters as the first Russian LNG plant was opened yesterday in south Sakhalin. The first production line has been put into operation, the second line will be started by the end of the year. This is a landmark event for Russia's oil and gas industry and the economy on the whole.

Construction was started in 2003, the $4 billion plant is expected to produce 9.6 million tons of liquefied natural gas a year. 3.2 million tons of liquefied methane is expected to be produced in 2009.

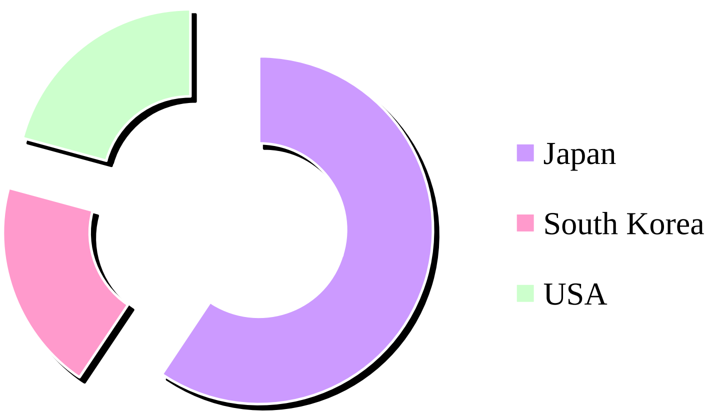
More than 80% of LNG has been already sold. Also, Korean Kogas, Japanese Toho Gas and Tokyo Gas and Shell Eastern Trading have call options.

Figure 1. Buyers of Sakhalin LNG



Almost 60% of the LNG goes to Japan's energy companies. The US and South Korea buy equal amounts of gas. The sales mix might change a bit however after the call options are sold.

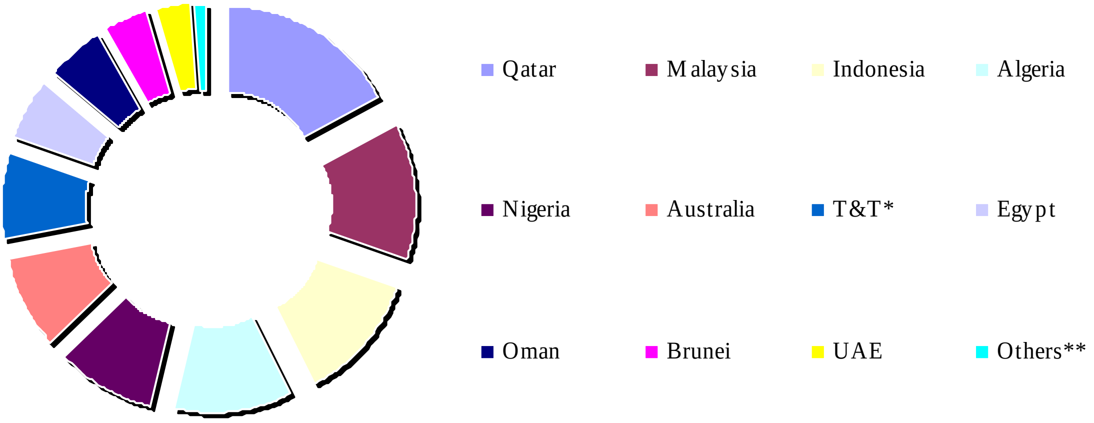
Figure 2. Countries that buy Sakhalin-produced LNG



The plant's long-term economic efficiency is proved by contracts whose term exceeds 15 years. The new LNG plant opens a whole new era in Russia's gas industry.

First, Russia has become a player at the booming LNG market. With this plant, the country will hold 5.8% of the global LNG market[1]. Based on 2007 performance, Russia could have taken the 9th place among LNG exporters.

Figure 3. LNG exporters in 2007



* Trinidad and Tobago
** USA, Norway, Equatorial Guinea

Source: British Petroleum

Second, Gazprom is mastering the Asian Pacific region with its 'tigers' that require huge amounts of energy. The region is unlikely to face a lack of demand even in the crisis for two reasons: an island country, Japan cannot use gas pumped via pipelines; India's and China's economies grow robustly, and the countries use increasingly more resources.

Third, Gazprom has closer approached to technologies of continental shelf drilling and methane liquefying. The Russian gas giant uses technologies of the British-Dutch company Royal Dutch/Shell.

At the same time, it is too early to talk about export diversification, i.e. market and industry risk minimization because LNG prices are as volatile as crude oil prices.

[1] Estimates were based on LNG market size in 2007 (226.41 billion cubic meters)

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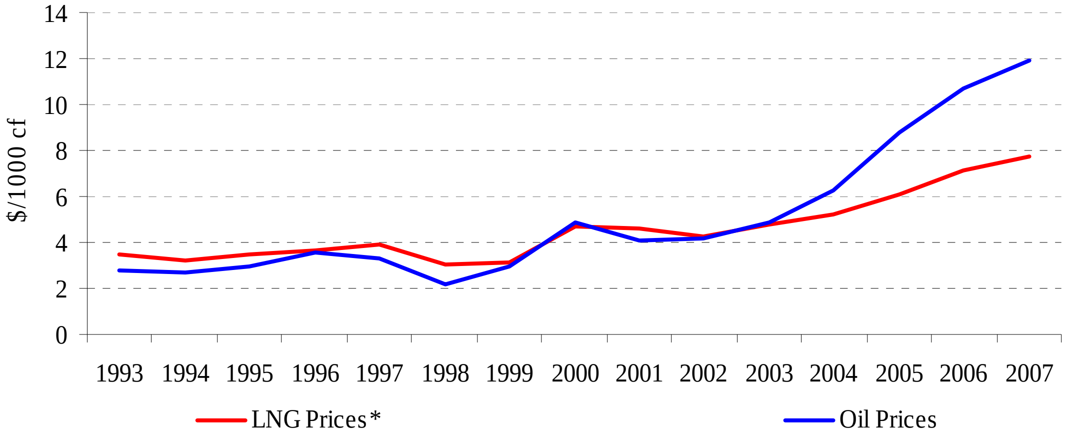
Figure 4. Oil and LNG price movements



*as Japan is a primary market for the Sakhalin plant, the listed prices are for Japan.
Source: British Petroleum