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China gas demand becomes more feasible at low LNG prices but challenges persist

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HIGHLIGHTS

Buying interest picks up for forward deliveries in recent tenders

Price advantage of pipeline gas over spot LNG starting to erode

Spot LNG still not a guaranteed money making business in China: analyst

China's natural gas demand is becoming more feasible with Asian LNG spot prices dropping below the key $9/MMBtu level this week, but a steeper drop may be needed for any substantial demand to emerge amid challenging economic conditions.

As a result of lower Asian LNG prices, buying interest was seen picking up for forward deliveries, especially in North Asia.

China's Shenzhen Energy closed a buy tender on May 30 seeking an August-delivery cargo, and the tender was awarded in the low $9s/MMBtu, according to several sources.

Prior to this, China's Guanghui Energy was heard to have partially awarded a buy tender for certain cargoes delivering from July 2023 to January 2024, S&P Global Commodity Insights reported earlier.

The prices of pipeline gas in China, which reflect crude prices 9-12 months ago, have been rising this year, with the average net import price above $8.5/MMBtu in April, showed calculations based on customs data.

This means that the price advantage of pipeline gas over spot LNG is fading, which is expected to stimulate buying interest from importers who do not have sufficient long-term contracts in hand, market sources said.

"Rising prices of domestic pipeline gas in China could provide some incentive for downstream industries to switch to LNG," a Chinese importer said, adding that the current LNG prices were quite competitive and second-tier buyers could be more likely to come out to buy spot cargoes.

At the same time, a second Chinese importer said that lower prices of LNG had stimulated some industrial demand. "We are monitoring prices for any opportunity to buy," the person said.

Platts assessed the July JKM at $8.862/MMBtu on June 1, the lowest level in over two years, due to ample supply and persistently weak downstream demand in markets across the region.

"A declining price is always a good thing for buyers, especially for those who can blend spot purchases into their existing portfolio of domestic production and term supply. However, so far this year, spot LNG has not made money in China's domestic market," said Jenny Yang, senior director at S&P Global.

Yang, who leads market analysis on Greater China natural gases, said trucked LNG prices, which are typically higher than the regulated piped gas supply, have been declining too.

"By the time volumes priced at $9/MMBtu now finally get delivered, trucked LNG may have fallen below it (taking into consideration value-added tax and terminal fee), therefore buying spot is not a guaranteed money making business," she said.

She said that the economic condition was not so great, with high inventory levels reported at terminals, and $9/MMBtu is still more expensive than coal for both industrial and power generation, even as coal prices continue to decline.

Downstream demand

Meanwhile, natural gas-fired power plants in China increased power generation on the back of more power demand due to a combination of high temperatures since late May and lower gas prices, market sources said.

Several regions in China, including Sichuan, Yunnan and Guangdong provinces, recorded high temperatures of 40 C or above in recent days, setting a record for the hottest May, according to local media reports.

In addition, the natural gas procurement cost of many gas-fired power plants dropped to around Yuan 3-3.5/cu m recently, roughly reaching the breakeven level for term power supply or even below the breakeven point for spot electricity, a power plant source in southern China said.

This means that gas-fired power plants can now be marginally profitable, a big improvement from last year's steep losses, which is believed to have encouraged them to ramp up power generation to meet demand growth recently, industrial sources said.

The gas consumption and gas-based power generation of Guangdong Energy's gas-fired plants both increased by about 35% month on month in May, according to a company source.

Guangdong province had around 30.55 GW of gas-fired power capacity at the end of 2021, accounting for about 28% of China's total gas-fired capacity of 108.59 GW in 2021, official data showed. It plans to increase gas-fired capacity to about 55 GW by 2025, according to a provincial development and reform commission notice dated May 24.

Many ceramics companies in Guangdong have also restarted more production lines since mid-May due to lower gas procurement costs, Ceramics Information, a Foshan government-backed information provider said May 24.

The LNG procurement price in many ceramics production areas in Guangdong dropped to around Yuan 3.2-3.3/cu m recently, the lowest in two years, CI noted, adding that the average LNG price was above Yuan

5/cu m in 2022 when many firms were forced to shut production lines.

Ceramic factories in Guangdong, about 85% of which use natural gas as fuel, had slashed operating rates to around 40% due to high gas prices, CI said previously. Almost 30% of natural gas in China was used in the building and sanitary ceramics industry, according to data from the China Building and Sanitary Ceramics Association in 2021.