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# Political priorities affecting the global liquified natural gas trade

BY TATIANA GOTVIG

While 2022 was a year of unprecedented volatility in global natural gas and liquified natural gas (LNG) markets, 2023 concluded with no signs of stabilisation. In fact, a few seemingly unconnected events in 2023, including announced transactions, brewing disputes and domestic regulatory developments, pointed to further volatility in the short and mid-term, with geopolitics remapping global LNG trade and investment in the long term.

## Political priorities are largely uniform, but geopolitics trump it all

At a strategic level, political priorities influencing the global LNG sector are largely uniform across the globe and are typically framed as the energy trilemma – energy security, energy sustainability and

energy affordability. A precise balance between the three strategic objectives (or a clear domination of one or more of them) in a specific region or country is determined by a combination of economic, geopolitical and climate considerations, as well as the country's position as a net importer or exporter of natural gas and its stance relative to geopolitical alliances. Geopolitical factors, on one hand, disrupt long established contractual relationships, and, on the other hand, create new forms of LNG contracting, including import financed procurement underwritten by government backed agencies tasked with securing energy supplies.

## European disarray

Fracture lines have appeared as the collective efforts to reduce dependence on Russian gas have continued across

Europe. Established on 25 March 2022, the EU-US Task Force on Energy Security declared that it aims to reduce the EU's reliance on Russian energy by diversifying its natural gas supplies in alignment with its climate objectives and by reducing its overall demand for natural gas. At a meeting held on 31 October 2023, the Task Force reviewed the diversification of Europe's natural gas supply sources. The joint statement resulting from the meeting positively assessed the progress achieved noting that the US had become the largest supplier of LNG to Europe. While the increase of the US LNG share in the European market may be a success story for some, but not all, US LNG projects, the collective European buy side has little to celebrate.

Germany, the highest natural gas consumer in Europe, best illustrates the

results of the Task Force's declared aims of alignment with climate objectives and reducing demand for natural gas. In May 2022, Germany rushed through the LNG Acceleration Act to simplify the licensing procedures for LNG receiving infrastructure and the procurement law for LNG projects. The Act initially contemplated that the operation of LNG receiving terminals can only be authorised until 31 December 2043 and that the subsequent operation only be permitted for climate-neutral hydrogen and its derivatives. In 2023, the Act was amended to ensure that the subsequent use of LNG receiving terminals for hydrogen and its derivatives is enshrined in the legislation regulating the authorisation process. As the Bundesrat fine tunes legislative measures to balance Germany's strategic objectives of weaning itself off Russian gas without jeopardising its climate ambitions, BASF announced it had broken ground on its polyethylene plant in China. Harsh statements criticising BASF's move to China are disregarding economic reality – energy intensive German industries built on cheap Russian pipeline gas are not economic to run on US LNG. As manufacturing industries heavily reliant on gas are forced either to shut or relocate to countries that offer more energy security, the Task Force's aim of reducing the EU's overall demand for natural gas is well on track.

Some European countries seem less resolute when it comes to achieving the Task Force's aims. While the supply of pipeline gas from Russia dwindled after the sabotage of the Nord Stream pipelines, European imports of Russian LNG between January and September 2023 remained steady compared with the same period in 2022. Spain and Belgium increased their imports of Russian LNG by 50 percent in 2023 compared with the previous year. Terminals in Belgium and France continue to transship Russian LNG destined for India and China. Coincidentally, two days after the Task Force's meeting held on 31 October 2023, the US Department of State added LLC Arctic LNG 2, the operator of the Arctic LNG 2 project, a flagship LNG project of Russia's Novatek, to the Office of Foreign Assets Control's (OFAC's) Specially

Designated Nationals list. This is the first set of sanctions directly targeting a Russian LNG project. The impact of designating LLC Arctic LNG 2 as a sanctioned entity remains to be seen. It appears that regulatory measures and market forces are not resulting in desired outcomes, and sanctions will remain a crutch in efforts to rid Europe of Russian molecules.

In November 2023, the EC decided to refer Poland to the Court of Justice of the European Union (CJEU) for imposing restrictive requirements on cross-border traders of natural gas under Poland's national gas storage regulation, known as the Stocks Act. The Stocks Act was enacted in 2016 and was a mechanism premised on imports of natural gas from Russia. The timing of the EC's move on the Polish storage legislation raises the question of whether this is an isolated instance or a sign of enhanced scrutiny of legislative mechanisms to ensure efficient operation of gas infrastructure across Europe in the context of the EU diversification policy to prevent potential supply disruptions in the EU responding to such disruptions in a spirit of solidarity, the latter seems more likely. Landlocked European countries seeking to procure LNG, a seaborne commodity, have most at stake when it comes to ensuring that European gas infrastructure, including new receiving terminals, are operated and regulated in a spirit of solidarity. To diversify away from Russian pipeline gas, in addition to increased costs of procuring the commodity, their political priorities are sharply focused on securing access to gas receiving infrastructure.

#### Chinese LNG ambitions

China became the largest LNG importer in the world in 2023. Not handicapped by domestic politics, the Chinese government's political priorities are easier to discern.

In 2023, we saw a string of yuan-settled LNG transactions. In March 2023, China National Offshore Oil Corporation (CNOOC) completed China's first yuan-settled, cross-border LNG transaction with France's TotalEnergies. The deal involved approximately 65,000 tonnes of LNG originating from the United

Arab Emirates (UAE) exported to China and was settled through the Shanghai Petroleum and Natural Gas Exchange (SHPGX). After this, a unit of China's state-owned PetroChina and a Middle Eastern counterparty also completed a cross-border LNG trade settled in yuan. In October, CNOOC completed two more yuan-denominated trades with France's Engie and Singapore's Pavilion Energy, for 65,000 tonnes of LNG each, also through SHPGX. In public commentary on these transactions, a CNOOC representative said that yuan settlement can promote energy trade globalisation and build a diversified ecosystem for LNG trading. China appears determined to turn the SHPGX into the third global gas trading hub (in addition to the US Henry Hub and Dutch TTF) and to continue the internationalisation of the yuan.

#### Australian paralysis

Australian political declarations of priorities in respect of its gas industry have limited impact on the state of affairs in the industry due to the significant roles various non-government stakeholders (such as workers unions and native title holders) play in the industry. There were several illustrations of this point in 2023. The threat of industrial actions at LNG facilities in Western Australia raised supply fears. A traditional landowner obtained a court injunction that halted the pipeline near Tiwi Islands and put the Barossa gas project in jeopardy. These events, together with the domestic gas market intervention earlier this year, instil little optimism in LNG buyers and investors.

#### US newcomers vs LNG 'old guard'

Lawyers and negotiators involved in long term LNG sale and purchase agreements (SPAs) 20 or so years ago would recall theories on reconciling a Western transactional approach and Asian relationship-based approach. A classic 25-year LNG SPA between an international oil company (IOC) as the seller and a Japanese utility as the buyer, linked on each side to costly and operationally complex liquefaction and power generation projects, relies on cooperation between the parties over a significant period. Concepts like

good faith, reasonableness and adaptation for hardship were used to make these contracts work as time passes, and the industry, markets and other circumstances change. These concepts, while arguably somewhat 'fuzzy' and, in some cases, potentially undermining the certainty of contractual terms, worked when LNG business was a small club. Fast forward to 2023, and we may be witnessing a turning point in LNG contracting attitudes. A recent dispute between a US seller and its long-term offtakers has, uncharacteristically for LNG disputes, spilled over into the public domain and reached a point where the offtakers sought that the EU-US Task Force on Energy Security intervene and require the seller to 'immediately begin to perform' its supply obligations under their long term LNG SPAs, asserting that the seller's behaviour has shaken confidence

in the trustworthiness of American LNG suppliers. The question is whether the relationship-based approach is becoming a thing of the past in the growing LNG market with more diverse players and a sharper focus on optimising trading.

While geopolitics and sanctions are giving an additional tailwind to US LNG projects, not all US project proponents are able to capitalise on this. An example is the proponent of the Driftwood LNG project, which stated in regulatory filings that there is substantial doubt about its ability to continue as a going concern.

### Conclusion

The global LNG trade hit a record high in 2022, propelled by the Ukrainian conflict. The US and China dominated the global LNG trade in 2023 as the world's top exporter and importer, respectively.

Geopolitics will remap global LNG trade flows and investment, with sanctions leading to the fragmentation of LNG trade flows and dashing hopes that LNG will become a globally traded commodity. New forms of LNG contracting are emerging, driven by energy security concerns. ■

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