Gas shortage in EU – problem without short-term solution

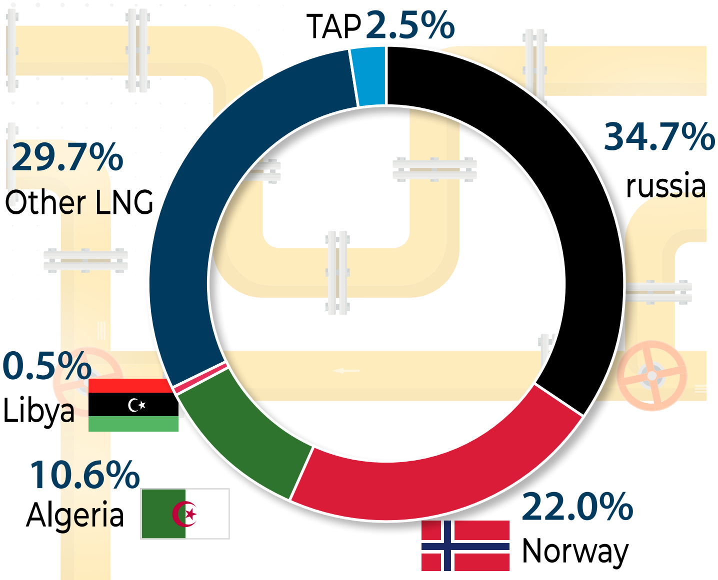
Since the beginning of the Russia-Ukraine war, gas supplies have become the big issue for the EU. In 2021, the European Union imported 155 billion cubic meters (bcm) of natural gas, including LNG, from Russia. This accounted for around 45% of total imports and close to 40% of its total gas consumption.

According to ENTSO-G data, in the first quarter of 2022 net gas imports in EU amounted to 962 TWh, of which 66% arrived through pipelines and around 34% through LNG terminals. While Russia secured almost 35% of gas imports, Russian pipeline gas for the first time over the last eight years lost its top supplier position of the EU and ensured only 28% of the EU external gas supply.

28%
share of pipeline gas imports from Russia in 1Q 2022

+72% y-o-y
LNG imports in EU in 1Q 2022

Gas imports extra-EU in 1Q 2022



Source of data: European Commission, estimation of GMK Center

According to some experts, Gazprom's gas exports to the EU could fall by around **a third** this year due to the war in Ukraine, rivalry with liquefied natural gas, and plans to switch to ruble payments. In 2021 around 140 bcm of pipeline gas arrived in the EU from Russia and based on the take-or-pay clauses of the long-term contracts, the minimum volume should be around 75-80 bcm in 2022. According to some estimations, this year EU could end up short 40 million tons of natural gas – around 10% of its annual consumption.

40 mln tons or
10% from annual consumption
potential deficit of natural gas in EU in 2022

To ensure gas supply at reasonable prices in winter European Commission proposed to fill gas storages to 80% by November 1, 2022, rising to 90% for the following years. As of July 11, 2022, EU gas storages are filled by 62.3%. Current gas volumes in storage facilities are close to the average level for 2011-2021. If gas supplies from Russia continue, there should be no problems in gas market.

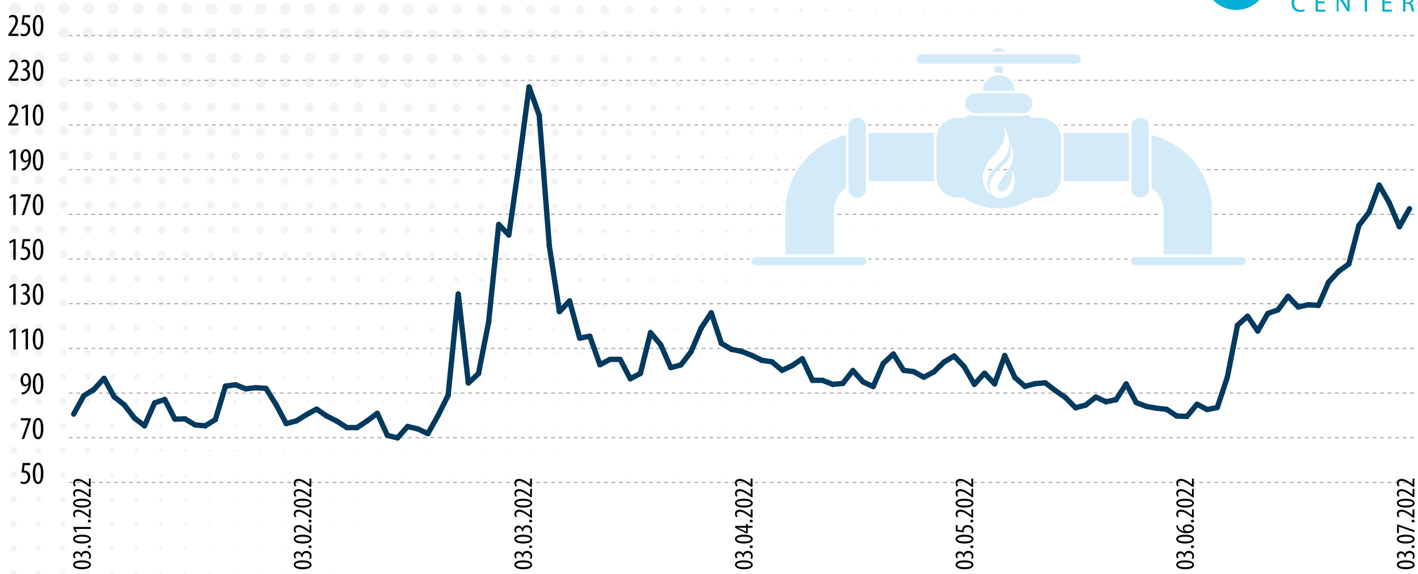
However, Russia may reduce or completely stop gas supplies. From June 16 Gazprom has reduced gas supplies via Nord Stream pipeline by 40%. The company explained this decision by delays in returning the turbine, which was sent for maintenance to Canada. Some experts estimate that if this year Nord Stream continues operating at current level of capacities, EU will fulfill no more that 70% storage for the winter.

To secure gas supplies, the EU also sharply increases LNG imports. Europe become the premium market for LNG due to a sustained TTF premium over Asian spot LNG prices. According to IEA, European LNG imports will increase by 50% (51 bcm) in 2022.

There are no surplus LNG capacities in the world, so LNG supplies will be the subject of a struggle between Europe and Asia. Rystad Energy estimated that global LNG demand will hit 436 million tons in 2022, outpacing 410 million tons of available supply. Most additional supply from new LNG projects will be available after 2024.

Possible interruptions in gas supplies affect the gas

Dutch TTF Gas Futures, €/MWh



Source of data: investing.com

price. Since the beginning of the war, TTF price almost doubled and reached 164.5 €/MWh on July 11, 2022.

Further price growth expectations are reflected in the shift of forward curve. If in March German manufacturer could lock in gas prices for all of 2023 at about 80 €/MWh, now it has to pay 145 €/MWh to hedge the same risk.

Current situation at EU gas market creates serious challenges for industrial enterprises, especially steel plants. High gas prices mean rise in electricity prices and energy costs as a whole. So, costs of steel production increase. Against the backdrop of falling steel prices increased energy costs are quizzing margins of steel producers.

Some manufacturers are trying to pass on rising energy costs to clients. For example, ArcelorMittal increased prices of long steel products by €60/t in Europe. Company linked this increase with rebound of scrap prices and surging energy costs. However, price growth opportunities are limited due to weak demand.

Rising energy prices led to a surge in inflation, which worsens economic growth and reduces demand for steel. Low steel prices and weak demand are already causing shutdown of mills. ArcelorMittal halted Dunkirk blast furnace on July 12. Acciaierie d'Italia and HBIS Serbia have announced other blast furnace closures in recent days.

In general, the current level of gas supply to EU does not cause big concern. However, the further situation is difficult to predict. There is a risk of suspending gas supplies from Russia. This risk will keep gas prices high until at least spring 2023.

+85%

TTF gas price from 23.02.2022 to 11.07.2022

High energy prices mean:

1. Rising inflation and risks of tightening monetary policy
2. Deterioration of steel demand
3. Squeezing margins of steelmakers
4. Pressure on the prices of raw materials (especially scrap)
5. Risks of capacity shutdowns and supply disruptions
6. Slowing decarbonization (especially based on DRI and EAF)

More detailed information can be provided upon your request:

- alternative gas suppliers;
- forecast scenarios for the situation on the EU gas market;
- other information on your request.

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