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15-Year Fixed Refi	2.93%	2.88%
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Analysis: East Africa risks missing LNG boom

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By Agnieszka Flak

JOHANNESBURG | Wed Sep 19, 2012 8:29am EDT

(Reuters) - Bad timing may defeat East Africa's plan to become a major liquefied natural gas exporter if plants are delayed and the region is overtaken by a global gas glut.

A singleminded focus on LNG may also see Tanzania and Mozambique compromise on developing the region through gas-fired power stations and plants converting gas to fuel.

The region's geology has already delivered a jackpot in discoveries of 150 trillion cubic feet - enough to supply Germany, Britain, [France](#) and Italy for fifteen years - and consortia busy scouting wells claim there may be potential to double that.

The size of the discoveries, their location en route to Asia and buyers' desire to diversify away from big suppliers Qatar and [Australia](#) have made East Africa an attractive prospect for LNG. But the clock is ticking.

"We don't know what the market is going to be post 2020. We need to get there before then," John Pepper, managing director of Anadarko Petroleum Mozambique ([APC.N](#)) told an energy conference in Maputo. "We need to progress quickly."

Research firm Wood Mackenzie estimates global supply of LNG will reach 472 million metric tons (520.29 millions tons) by 2020, against demand of 369 million tonnes. The expected oversupply has already fuelled a global race for customers in growing markets in Asia.

Some 100 million tonnes of new LNG supply is expected to be added after 2015 alone. Officials in Mozambique are already worried about the future gas price outlook.

The stakes are high. Oil majors including Royal Dutch Shell ([RDSA.L](#)), U.S.-listed Anadarko, Britain's BG Group ([BG.L](#)) and Italy's Eni ([ENI.MI](#)) are rushing to lock in deals, putting pressure on governments ill-equipped to win favorable deals.

Yet forecasts of first gas from Mozambique by 2018 and Tanzania within a decade seem ambitious, with most global LNG plants delayed, some even scrapped, and more hurdles likely in getting a frontier gas market like East Africa off the ground.

"In my estimates, I don't have LNG from those countries by 2020. It's impossible to do it in those time frames," said Thierry Bros, an analyst at French bank Societe Generale and author of the book "After the U.S. shale gas revolution".

"Mozambique and Tanzania should focus on the development of a combination of projects, not just LNG, to supply both the regional and export markets."

East African gas, while seen competitive in price, will compete with existing producers keen to expand, and newly emerging ones, especially from North America.

The big variable is the supply coming out of the United States on the back of its shale gas ambitions and possible restrictions the world's biggest economy may place on exports.

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Even if other plants get delayed, developing gas in frontier Africa means tackling a dilapidated infrastructure, unskilled staff, maritime piracy and regulatory uncertainty, putting the region's ability to compete in LNG this decade at risk.

REGIONAL MARKET

LNG plants, which cool gas into liquid form for shipment on tankers, are capital intensive, rely heavily on debt and finding bank appetite for a project over \$10 billion will be difficult.

Current estimates put Mozambique's resources at five times those in Tanzania, but firms involved in the Tanzania consortia boast more expertise in getting LNG plants off the ground.

This would change if Shell, which dropped its bid for Cove Energy and the gas explorer's stake in the Anadarko-led consortium, found another way to buy into the Mozambican blocks.

Companies need to find credible buyers for gas to convince funders that their projects will be viable over a long-term.

"That's probably the biggest challenge all of the players have got," said Frank Harris, head of LNG consulting at Wood Mackenzie in Edinburgh.

The presence of Asian firms in both Mozambican consortia should help them find takers in gas-hungry East.

"Korea Gas is the world's biggest buyer of LNG, so you've got one of the best LNG customers as an investor in your project," Harris said, referring to KOGAS' stake in the Eni-operated Area 4 offshore Mozambique.

Cooperation between players within each country or between the two states would increase economies of scale, cut construction costs, ease labor shortages and reduce the risk for investors, but little has been mooted on that front.

The promise of high returns is tempting, but large revenues from an LNG plant only filter through when the 7-year building period ends, and with the gas price outlook post-2020 uncertain the benefits for east Africa may remain elusive for longer.

Another challenge will be to transfer the gains to transform and diversify entire economies. With 7,000 workers used to construct an LNG plant, only 200 are needed to run it.

Both countries want to see a regional gas market developed, but critics fear too much will be left to negotiable contracts.

"Domestic offtake should be very clearly spelled out in any contracts that are being signed now," said Anne Fruhauf, an analyst at Eurasia Group. She doubted this was happening.

Mozambique, a net importer of fuel, hopes to use some gas to build gas-to-liquids plants and also as a cheap source of electricity. Four-fifths of its 23 million people still have no access to power.

Tanzania said gas-fired plants will cut its reliance on hydro power, often hit by prolonged droughts. Some members of parliament have suggested it should focus on becoming an exporter of electricity rather than pursue LNG.

Both nations also hope to share their gas riches with neighbors. The continent's top economy South Africa is already lobbying to secure Mozambican gas to replace coal-fired plants.

However, their track record of using gas in their backyard is not convincing:

Tanzania is often plunged into darkness despite the Songo Songo fields, run by a unit of Toronto-listed Orca Exploration ([ORCb.V](#)), producing gas since 2004, and the two parties have long been battling over costs and control.

Mozambique only this year signed a deal with South African Sasol ([SOLJ.J](#)) to buy gas the petrochemicals group has been producing since 2004.

"Clearly, Mozambicans have learned," said Andre de Ruyter, a Sasol senior group executive. "They understand now that exporting all of your primary natural resources is not a great idea."

(Additional reporting by Marina Lopes and William Mapote in Maputo and Fumbuka Ng'wanakilala in Dar es Salaam, editing by William Hardy)

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