

Europe turns to North Africa in bid to replace Russian gas volumes

Italy's Prime Minister Mario Draghi is visiting Algeria on Monday where he will reportedly sign a gas agreement for an additional 9 Bcm/year of imports. Separately, EU Vice President Frans Timmermans made a visit to Cairo on Sunday in a bid to secure LNG volumes for Europe. The trips to North Africa come as Europe looks to replace Russian gas volumes, however question marks remain over Egypt's and Algeria's ability to sustain gas production at a level to underpin exports.

Italy has taken steps to wean itself of Russian gas following the war in Ukraine and the new gas deal with Algeria complements plans to install two additional floating storage and regasification units (FSRUs) over the next 12-18 months which will take the country's total number of LNG terminals to five.

As for Algeria, the country's gas production has increased in recent months, and hit a record annual high of over 100 Bcm in 2021, according to reports. However, one key question is whether Algeria will manage to maintain or let alone increase gas production to help meet Europe's rising demand for non-Russian gas.

"The conventional wisdom has been for a while that Algerian output was flat or declining, and with growing domestic demand, the scope for exports was diminishing," said one industry observer speaking to Gas Matters Today. "However, they seem to have reversed the production trend."

"Historically oil production was optimised, and gas production was constrained by the need to reinject gas, particularly into Hassi R'Mel. But with gas now more valuable than oil, I wonder if they have changed their approach," he said.

However, "several significant barriers" could impact gas exports to Europe, Justin Dargin, a MENA energy expert at the University of Oxford told Gas Matters Today.

"Algeria, like many other African countries seeking to increase gas production for export, faces capital constraints that could prevent it from making the investment needed to increase its export potential. Algeria has a somewhat large social spending budget that has eaten into its ability to funnel the investment sums needed to help it meet Europe's gas needs," Dargin said.

"Additionally, Algeria has rising domestic gas demand and little means at the moment to invest in renewable energy to any appreciable amount that would be able to unlock additional inflows for export to Europe. And, across the region, there are still clear security issues that could flare up that would potentially hinder gas production projects. Lastly, Algeria still must contend with mismanagement and corruption that are rife throughout its hydrocarbon industry," added Dargin.

Italy, which has made a commitment with G7 and EU partners to reduce imports of Russian energy, imported an estimated 29 Bcm of gas from Russia in 2021. The EU has announced that

imports of Russian coal will stop in August this year, and there are some signs that oil and even gas may be sanctioned in the longer term.

Gas consumption in Italy stood at 76 Bcm in 2021, up 7% year-on-year, according to the EC's most recent gas market report which was released this week. Italy imports almost all its gas, including around 9 Bcm of LNG in 2021, according to the report. Gas-fired power generation was up by almost 20% year-on-year reflecting lower hydro levels.

Algerian import contracts are indexed to oil and Italian importers paid an estimated EUR 20/MWh for the gas in the fourth quarter of 2021, according to the EC report. In quarter-on-quarter comparison, the import price for Algerian gas in Italy was up by 8%, and year-on-year it rose by 51% in Q4 2021. By comparison, the import price estimate for Spain in Q4'21 was EUR 26/MWh.

"For the future, the current advantage of oil-indexed contracts is likely to remain as long as spot gas prices are at current high levels, though recent high crude oil prices will filter in the oil-indexed contracts during the spring and summer of 2022," said the EC report.

The EC report also noted that Italy's gas imports from Algeria was up by 15% year-on-year in Q4'21. At the same time, the contract concerning the GME pipeline that supplied the Iberian peninsula with Algerian gas through Morocco expired on 31 October 2021. This means only the Medgaz pipeline, which is being expanded from 8 to 10.5 Bcm/y capacity, currently supplies Spain with Algerian gas.

According to the report, Algeria exported 15 Bcm of LNG in 2021, of which around 8.5 Bcm went to Europe.

Egyptian LNG

Separately, EU Vice President Frans Timmermans travelled to Egypt to discuss collaboration in energy – namely LNG and hydrogen.

Egypt's gas production is increasing and the country is tipped to supply more gas to Europe to help replace the bloc's Russian imports. As with Algeria, there are questions over Egypt's ability to keep production at current levels and how much of the gas that will go to the domestic market. But Eni, which discovered the giant Zohr gas field in 2017, will undoubtedly try to capitalise on rising prices for LNG by boosting output from its Damietta plant. The start of gas exports from Israel to Egypt via the Jordanian section of the Arab Gas Pipeline could also lend support to LNG exports.

"It does seem that Egypt, given its large gas finds over the past several years, would be able to increase gas exports to Europe. Egypt has over the past decade been able to drastically increase its domestic gas production and reduce its domestic gas/power demand rates to be able to allow it to potentially help Europe offset its Russian gas dependence," said Dargin. - AW