Wall Street Journal

Gas Glut Reverses Lucrative 2016 Trade

Natural-gas futures have fallen 25% in the oversupplied market, hurting plans to grow U.S. exports

Natural-gas futures have fallen sharply this year, reversing one of last year's most profitable trades. Above, a natural-gas pipeline in the U.K. Photo: Bloomberg News

By Timothy Puko
Updated March 14, 2017 9:10 p.m. ET

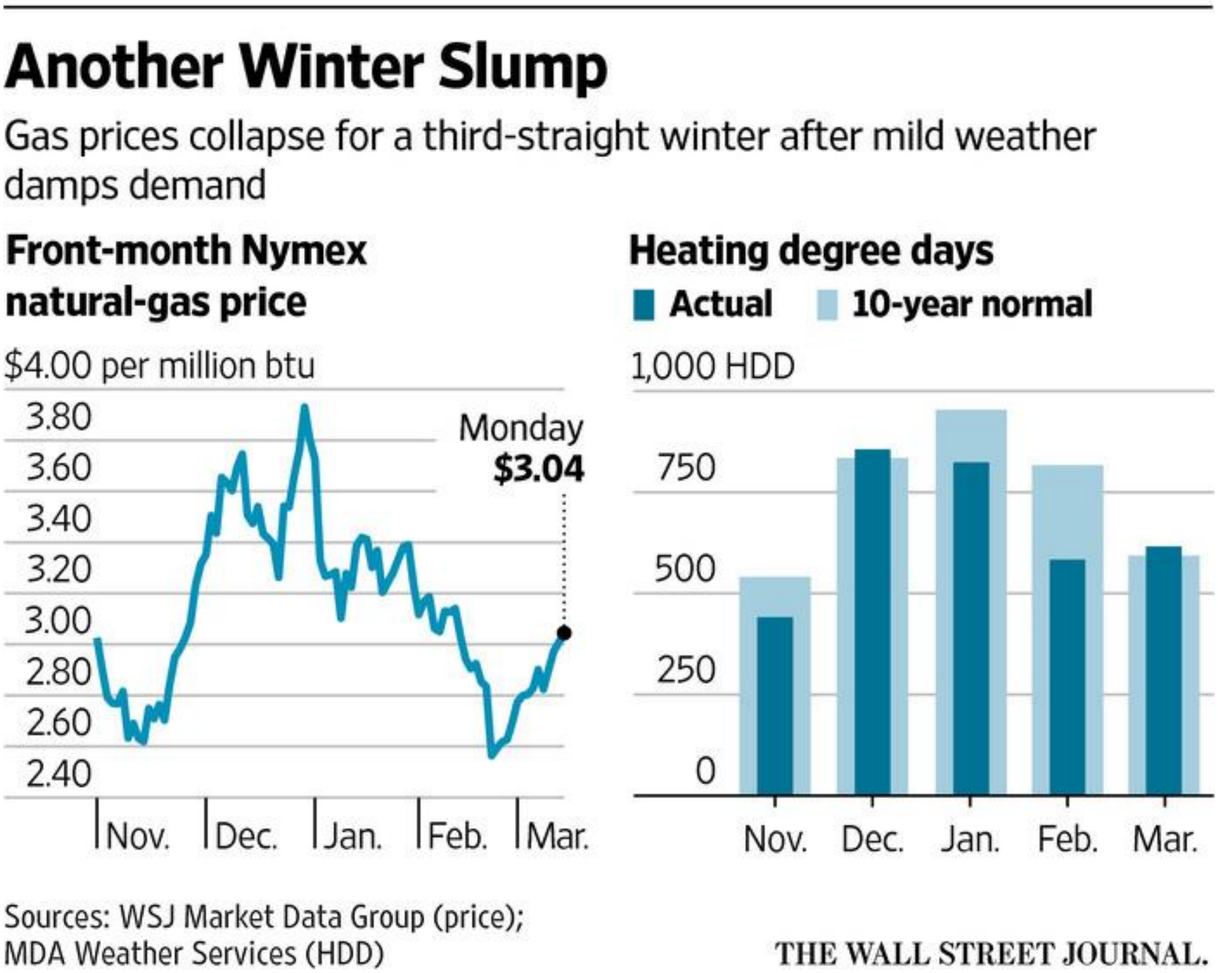
A flood of natural gas swamping the U.S. is turning into a global glut, sinking prices and dimming the hopes of American producers to export their way out of an oversupplied domestic market.

Natural-gas futures have fallen 25% over the past 2½ months. The declines continued Tuesday, with April futures dropping 3.45% to $2.938 a million British thermal units on the New York Mercantile Exchange. Shares of gas-production companies are among this year's worst performers.

"Investors right now across the board just hate natural gas," said Pearce Hammond, an analyst at Simmons & Co. International in Houston.

The recent declines reverse one of last year's most profitable trades: Gas futures rose 59% in 2016, and shares of producers including Chesapeake Energy Corp. and Rice Energy Inc. doubled between March's lows and year-end.

Many investors wagered that new gas-fired power plants and record exports would help burn off much of the excess supply in the U.S. But a historic level of exports hasn't been enough to transform a market dominated by unpredictable weather and massive new supplies from fracking.



One issue for U.S. producers is their own growing influence: More gas for sale world-wide—often floating on ships—eases bottlenecks that once drove big local price spikes. Global prices for natural gas have plummeted, down by half in some places in recent years.

Mild U.S. weather in February also has reduced demand. Warm winter temperatures sapped about 2.9 billion cubic feet a day of demand from the market this season, compared with just the 2.3 billion cubic feet a day of new exports added, according to Platts Analytics, a unit of S&P Global Platts.

“Exports are the infant,” said J. Alexander Blackman, an executive at Standard DeltaCo., a commodities-trading firm. “Until they grow meaningfully larger..prices will be heavily influenced by mother weather.”

Bernstein Research, [Macquarie Group](#) Ltd. and energy investment bank Tudor, Pickering, Holt & Co. all are warning that oversupply may weigh on the market for years.

The trend could allay some of the biggest fears about exporting the country’s newfound bounty of gas. Major industrial consumers publicly lobbied against export approvals in recent years, warning of higher prices. Instead, U.S. prices for consumers of all types are holding around decade lows even as exports take off, according to the U.S. Energy Information Administration.

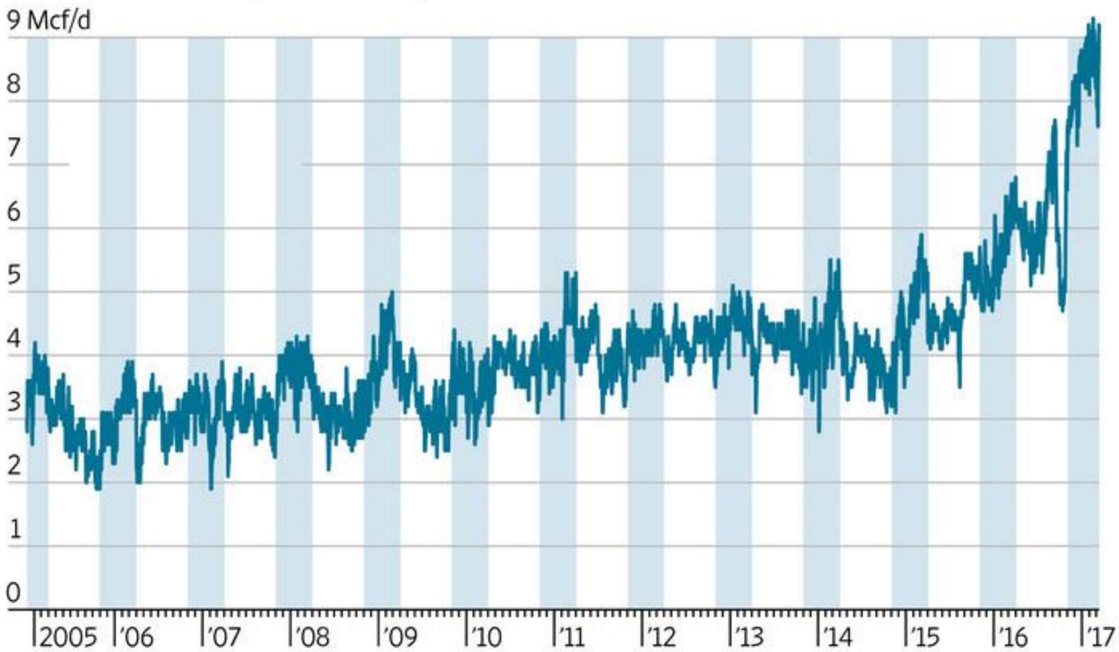
Many see sales of U.S. gas to overseas buyers as the biggest shift in the market. A mix of global oil companies, energy traders and startups have proposed around two dozen new coastal export terminals. One terminal is already open in Louisiana, and up to five more are expected to open soon.

Exporting the U.S. Glut

As shale-drilling led to record U.S. production, more U.S. gas went abroad, weighing on international prices

Total exports

Canada, Mexico and liquefied natural gas



Note: November to March, the winter heating season, is shaded
Source: Platts analytics' Bentek Energy (exports)

THE WALL STREET JOURNAL.

As recently as a few years ago, U.S. exports amounted to nothing. Now, new pipelines to Mexico and a terminal on the Gulf Coast send about 8% of U.S. output abroad. That could climb to nearly 18% in five years, Platts Analytics said.

Cheniere Energy Inc. opened the Sabine Pass export terminal in Texas a year ago, and the nearly 2 billion cubic feet it ships abroad each day could grow fivefold as four to five new terminals ramp up through 2020, according to analysts' estimates. Exports from the U.S. to Mexico could grow from nearly 4 billion cubic feet a day today to nearly 6 billion in the same period, Platts Analytics said.

Overall, the U.S. is expected to be a net exporter by 2018, according to the U.S. Energy Information Administration. It has been nearly 60 years since the U.S. last shipped out more natural gas than it brought in annually.

But the impact of that export growth could be canceled out by new supply. U.S. gas producers have nearly doubled their number of rigs from a historic low last year. Oil rigs also have nearly doubled, and they produce gas as a byproduct. Macquarie estimates that 9 billion cubic feet a day of new gas from oil wells alone between 2017 and 2021 will completely cover all new demand from exports.

Global supply is likely to increase by 44% in 2020 from 2015 levels and outpace new demand through the end of this decade, according to Moody's Investors Service.

Some investors think growth projections for U.S. exports look a little too rosy.

Pipeline delays in Mexico and President Donald Trump's pledge to change trade terms with that country could undermine sales to the most important export market for U.S. producers. Mexico last year received nearly 60% of U.S. gas exports, according to EIA.

Australia and the Middle East put so much gas on the global market that it leaves little room for more U.S. export terminals that could help erase the domestic glut, said Robin Wehbé, portfolio director at Boston Company Asset Management. He spent 2016 buying shares of oil, metal and other commodity-producing companies, but not producers of natural gas.

"It's too easy to find," said Mr. Wehbé, whose company is a unit of Bank of New York Mellon Corp. "We've got plenty of it coming out of our ears."

Not everyone is that bearish: Mr. Hammond at Simmons & Co. notes that many U.S. exporters have long-term contracts guaranteeing buyers for their gas.

Mexico also doesn't have a good alternative to U.S. gas. It would probably need higher prices and years to build new infrastructure to replace U.S. gas with new domestic production, according to Simmons.

Write to Timothy Puko at tim.puko@wsj.com

Appeared in the Mar. 15, 2017, print edition as 'Natural-Gas Glut Deepens.'