

WHY NATURAL GAS PRICES ARE SOARING AROUND THE WORLD

Relevant for: Economy | Topic: Infrastructure: Energy incl. Renewable & Non-renewable

This is supposed to be an off season. Winter is yet to set in. But natural gas prices soared over the past few months, especially in Europe. The price of natural gas in Europe is now six times higher than what it was last year. Across the continent, natural gas inventories are falling. On Wednesday, the benchmark Dutch gas futures price jumped 40% in the morning trade to touch €162.13 a megawatt-hour, an eight-year high, but reversed course after Russian President Vladimir Putin assured Europe of supplies. But even after the day's fall, gas prices in Europe remained twice as high as they were a month earlier. And on Friday, prices started rising again. What's driving up the prices?

Supply constraints

A host of reasons, from economic recovery to geopolitics, are attributed to the price rise. Global energy demand fell last year when economies slipped into COVID-induced lockdowns. When growth returned this year, especially to Asian economies, demand shot up and energy producers struggled to meet the growing demand, pushing up prices. Even in the U.S., the world's largest natural gas producer, prices rose from \$1.7 per million British thermal units on March 31 to \$6.3 per mBtu on Oct. 5. Europe, which is heavily dependent on imports to meet its energy demand, was particularly hit hard.

As part of Europe's shift towards cleaner energy, many countries had moved away from coal to gas to produce electricity. This increased Europe's reliance on gas. On the other side, the continent's natural gas production has shrunk over the years, as many countries shut down production fields over environmental concerns. If Europe's natural gas production (excluding Russia) was about 300 billion cubic metres in 2005, it fell to less than 200 bcm in 2021, according to Rystad Energy. Norway, Europe's main producer of natural gas, has seen its production shrink from 117.6 bcm in 2015 to 105.3 bcm in 2021. This has left Europe largely dependent on Russia.

Energy geopolitics

As prices shot up amid growing worldwide demand and falling production in Europe, supplies from Russia via a pipeline that passes through Ukraine and Poland also shrank, which made the situation worse. Russia has built another gas pipeline, Nord Stream 2, which will take Russian gas directly to Germany bypassing Ukraine and Poland, whose governments are critical of the Kremlin. But supplies to Europe through Nord Stream 2 are yet to start as the pipeline is awaiting approval from European authorities.

In the past when Europe's energy demand shot up, Russia had stepped up supplies. But this year, Gazprom, Russia's state-controlled energy giant that supplies about 35% of Europe's gas requirements, has booked less additional exports than the traders wanted, adding pressure on supplies. The International Energy Agency said this week Russian exports to Europe this year were lower than they were in 2019. This has fuelled speculation that Mr. Putin is using the energy crunch in Europe to get approval from the EU for the Nord Stream 2 pipeline. Several countries in Europe as well as the U.S. remain critical of the pipeline, which they say would help Russia enhance its leverage over the continent and would also allow Russia to economically punish Ukraine and Poland. U.S. National Security Adviser Jake Sullivan told the BBC on

Thursday any attempts by Russia to exploit the crisis would backfire.

Putin's assurance

The Kremlin has dismissed such criticism, saying Russia has no role in the energy crunch. On Wednesday, Mr. Putin said the amount of gas flowing through the operational pipeline is set to exceed volumes agreed under Gazprom's contract with Ukraine. He also said Russia could "reach another record of deliveries of our energy resources to Europe, including gas". This temporarily calmed the markets.

But Mr. Putin didn't say how Russia was going to step up supplies — through the existing pipeline or Nord Stream 2? Russian officials have already said Gazprom can send more gas to Europe if Nord Stream 2 comes online quickly. It is to be seen if additional supplies would be tied to a quick approval for the pipeline. Furthermore, the Russian domestic gas market also remains tight. Inventories are running low, and winter is coming, which would shoot up demand constraining Russia's export capacity. And demand is rising not only in Europe and the Americas, but also in Asia. Coal shortages in India and China could drive up prices of natural gas further.

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