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Israeli Gas Export Options Blurred

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The failure of the ILDC Energy (Israeli Land Development Co. Energy Ltd)-led consortium to discover gas in the Sara & Myrah license areas in August and September 2012 has not only created an aura of uncertainty regarding the dynamic development of further Israeli discoveries, it has also further blurred Israel's alternative export options as Cyprus is expected to aggressively promote its own project for the construction of a 5 million metric tons LNG liquefaction plant in Vasilikos.

The empowerment of the conservationist faction within the Israeli government as a consequence of the dry wells in Sara & Myrah combined with the country's upcoming elections set for 22 January 2013, have frozen any major decision that could be taken on the recommendations of the Tzemach Committee proposals. The Tzemach Committee suggested in its final report to the Israeli cabinet published on 29 August 2012 that Israel could export by 2037 up to 500 bcm of its existing and prospective gas resources.

The Committee also proposed the establishment of a flexible quota system that would allow for the export of up to 75% of the annual production from major fields with an estimated capacity above 200 bcm as long as the owners of smaller capacity fields sell their export quotas to Israel's domestic market after acquiring a so-called *Replacement Transaction Permit.* "In other words" as the Committee's Executive Summary notes "the overall amount that will be permitted for export from a reservoir with a capacity greater than 200 BCM will not exceed 75% of the scope of gas in the reservoir".

These provisions provide the emerging Israeli gas system with the necessary flexibility to exchange export quotas in ways that would allow the market to become more competitive as medium and small-size reserves holders trade their own export quotas with the current dominant players like Noble, Avner Oil & Gas and Delek Drilling. Such market conditions would also make it easier for the Noble/Delek partners and their major allies in the Tamar (Isramco) and Leviathan (Ratio Oil) consortia to muster the necessary capital in order to construct a major underwater pipeline connection that would give the Israeli gas system an alternative "northern entry point".

So far all of Israel's offshore gas reserves are channelled to the mainland via a single underwater pipeline that links the existing fields (Yam Tetis) with a single entry point located just north of Ashdod a city close to Ashkelon and the Gaza strip. If the flow of gas through this pipeline is somehow interrupted, Israel's economy would be in grave peril and that is exactly why the country needs an alternative connection to its two recent giant discoveries which are also closer to the northern part of the country. *The problem for Israel though is that it is unwilling to build this "northern entry point" with public funds. As a result the Noble/Delek consortium has acquired another significant leverage vis-à-vis the State demanding a clear and pro-export regulatory framework in exchange for constructing the pipeline out of its own pocket.*

This trade-off is more than clear. As Gydeon Tadmor, the CEO of Avner Oil & Gas, noted on 28 October when he addressed the delegates of the *Israel Energy & Business Convention 2012,* "It is impossible to talk about a northern gas terminal if there is no project to supply the gas; in other words, Leviathan. It is impossible to talk about developing the Leviathan field without an export horizon. The key is the Tzemach Committee recommendations. I am sure that the government and the prime minister will approve these recommendations as quickly as possible, and there will be no delay, Heaven forbid, because the approval is a milestone".

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Although the will of Heaven is unclear, Mr. Tadmor's wish for speed is unlikely to be satisfied for at least six months. This protracted state of indecisiveness has only increased friction within the Leviathan partners as to the optimal export option for their gas, even though all consortium members are fully cognizant of the fact that there will be no gas to talk about unless they are able to attract a major international company "with top experience as an LNG developer" as Tadmor noted in his aforementioned address. *It should be noted though that the absence of a regulatory framework for Israeli gas exports is not the only factor blurring the options of the Leviathan partners as the consortium's protagonists are not necessarily seeing eye to eye on the optimal export choice.*

Mr. Tadmor was the only vocal proponent of the Vasilikos LNG option during the *Israel Energy & Business Convention 2012*, whereas Yigal Landau, the General Manager of the Ratio Oil Exploration Co. noted in the same conference that "the [gas export] facility should be based in Israel. Israel must have a back up. It cannot be dependent only on Cyprus". Two weeks later in an interview with *Reuters* published on 18 November Landau partly reversed himself noting that "Leviathan will be connected to both Israel and Cyprus". Lawson Freeman, Noble's VP for the Mediterranean Sea, did not express any preference for Leviathan's two principal export alternatives: (a) the Vasilikos LNG in Cyprus or (b) an onshore LNG in Israel's Mediterranean coast. Freeman sufficed to say that all export options are "meticulously studied".

From a geopolitical point of view a combined 20 bcm/y liquefaction terminal on EU soil would upgrade Israel's regional standing and would also make the most economic sense given Leviathan's proximity to Aphrodite and Cyprus. From a military point of view though, Israel's generals appear to have no doubts as to the necessity of putting the export facility firmly within Israeli sovereignty. It is has been made clear that the senior representative of Israel's National Security Council in the Tzemach Committee, Mr. Avriel Bar-Yosef, has vetoed the Vasilikos option on security grounds. It is still unclear how the amateurish "bombing" of Tel Aviv by Hamas' Fajr-5 missiles will influence Israel's decision on the construction of an Israeli based liquefaction facility.

Does the Israeli Prime Minister agree with Mr. Bar-Yosef? The answer to this question will not be finally answered before probably the summer of 2013. In the interim, apart from the likely export of some FLNG gas from Tamar circa 2018, the only realistic chance for Israeli hydrocarbons to reach Cyprus will depend on whether the Pelagic consortium strikes gas on the Ishai exploration block. Exploratory drilling started on 2 November and will continue for another 85 days. *What is important to note though is that the potential discovery of more Aphrodite-size fields in the recently awarded (31/10/2012) Cypriot Blocks may leave little room for Israeli gas in the prospective Vasilikos facility if the current impasse in Israel continues for another year*.

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