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Uncertain future of Skulte LNG terminal project

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There have been efforts in Latvia to build an LNG terminal in Skulte since 2016, but recent decisions by the government in Riga make the realisation of the investment uncertain. Even the damage in early October 2023 to the Balticconnector pipeline, which connects the gas system of Estonia and Finland, has not changed the Latvian government's approach to the Skulte LNG terminal. Latvia is counting on existing import capacity in the region to ensure the availability of natural gas for the country's customers as well.

Importance of natural gas in the economy. In Latvia, natural gas plays an important role in the economy because it is the only fossil fuel used to generate electricity (36.4%), with renewables accounting for the remainder. This commodity is used in power plants and thermal power plants, most notably in Riga (the CHPP-1 and CHPP-2 power plants owned by Latvenergo)[1]. There is no natural gas production in Latvia, which means that it is entirely imported, and supplies over the years have been primarily from the Russian Federation (Luhamaa point in southeastern Estonia). The cancellation of natural gas supplies from Russia ("IEŚ Commentaries", no. 587), due to the ongoing Russian-Ukrainian war, has meant that natural gas is now supplied from the direction of Lithuania (Kiemenai point) and Estonia (Karksi point).

Latvia plays an important role in ensuring the energy security of the Baltic States, as the region's only underground natural gas storage facility in Inčukalns is located on its territory (storage capacity is 2.3 bcm per year). This storage facility is used by all the Baltic states and Finland.

Project characteristics. The project to build an LNG terminal in the port of Skulte, Latvia, has a short history having been initiated in 2016. The project envisages the construction of an FSRU-type LNG terminal and a pipeline of about 34 km connecting to the tanker on which the regasification process would take place, and on to the underground natural gas storage facility in Inčukalns, located inland. The terminal is ultimately expected to have an import capacity of 4.1 bcm per year, with investment costs estimated at USD 120 million. A key aspect of this project is the direct connection between the terminal and the storage facility, which significantly reduces the cost of the investment (construction of the tanks consumes about 60-80% of the total project cost). The investment is being carried out by AS Skulte LNG Terminal, owned by the National Gas Terminal Society and Peter Ragauss[2] (a total of 80%), and AS Virši (20%). AS Virši acquired a stake in the terminal in May 2022. According to the intention of the shareholders, the project was to be completed in 2023-2024, but the situation was complicated by the Latvian government's position, which changed significantly in 2023.

Problems with the project. The project to build an LNG terminal in Skulte has been viewed differently by the Latvian government since 2016, for at least three reasons. First – the investment is planned by private investors, which means that the state would have limited influence on its operation (the government did not agree to the terms of cooperation presented by the initiator of the investment). Second – from the government's perspective, the existing natural gas import capacity in the Baltic Sea region provides sufficient imports for Latvia as well. There are already three LNG terminals in the region: Klaipeda in Lithuania and Inkoo and Hamina in Finland.

[1] A. Kuczyńska-Zonik, *Republika Łotewska*, [in:] *Raport. Bezpieczeństwo energetyczne państw Europy Środkowej i Wschodniej*, red. B. Surmacz, M. Paszkowski, Lublin 2023, pp. 120-121.
[2] American entrepreneur with Latvian roots, active in the energy market, among other fields.

As a result, the import capacity in the Baltic States alone currently stands at almost 13 bcm against the demand for natural gas in 2022 at 2.8 bcm (Lithuania, Latvia, Estonia combined), and 3.9 bcm jointly with Finland. Third – Latvia is guaranteed the possibility of importing natural gas through the LNG terminal in Klaipeda, Lithuania, as Latvenergo has reserved adequate unloading capacity at the terminal for the next 10 years.

The Latvian government's position has changed dramatically in the last two years. Originally, the authorities were sceptical about the legitimacy of the terminal's construction, despite the fact that the investment was on the Three Seas Initiative's list of projects of common interest. The Russian-Ukrainian war changed attitudes toward the investment, which was reflected in the project's status as a "project of strategic importance for state security" on 30 August 2022, followed by the adoption of a law supporting the investment by the Latvian Parliament (Saeima) on 19 September 2022. The law indicated that the terminal would be put into operation by 15 September 2024, and thus, before the next autumn-winter season. However, as early as 11 April 2023, the government withdrew its support for the investment, communicating that the terminal was still likely to be built, but on a commercial basis. Subsequently, on 19 October 2023, the parliament supported a bill submitted by the ruling parties (New Unity, the Greens and Farmers Union, and the Progressives) to repeal the law of 19 September 2022 (85 out of 100 deputies voted in favour).

Balticconnector pipeline damage. The damage to the Balticconnector pipeline on October 8, 2023, did not significantly affect the discussion of renewed support for the construction of the Skulte LNG terminal. The debate that took place did not lead to a revision of the government's position on the investment. Importantly, the damage to the pipeline itself is not expected to have a major impact on the level of energy security of either the Baltic States or Finland, as companies in the region use the natural gas stored in the Inčukalns storage facility and other available import channels. At the end of October 2023, the filling level of the storage facility was the highest ever (around 96%), which is partly due to the low level of demand for natural gas in the region and the high level of supply through LNG terminals operating in Lithuania and Finland.

Conclusions

- The Skulte LNG terminal, due to the recent decision of the Latvian Parliament, will not be implemented as a project that has political support from the authorities. The vote showed that there is currently no support for the implementation of the investment (85 out of 100 parliamentarians voted against the introduction of the bill, all of them parliamentarians from the government coalition). Importantly, the terminal was not to be built with public funds. However, the lack of political support does not mean that the terminal has no chance of being built in the future, but its launch will depend solely on the decisions of private investors.

- Given the import capacity in the region – there are already existing LNG terminals for natural gas supply – as well as a much lower level of consumption than in the past, attracting investors will be difficult. It was primarily the economic factors that influenced the decision to withdraw support for investment. At the same time, the priority of the new Latvian government will be to work on reducing the role of fossil fuel resources in favour of renewables ("IEŚ Commentaries", no. 953).

- The government's position in the context of terminal construction is based on an assessment of the regional situation, including existing import capacity. In addition, there have been indications that the terminal in Lithuania may be expanded, which means that import capacity will be high in the region and will fully cover the demand for natural gas in Lithuania, Latvia, and Estonia. The Baltic States also have the possibility of importing natural gas from Poland through the GIPL pipeline (Poland-Lithuania interconnector), which was put into operation in May 2022, with a capacity of 2.4 bcm per year from Poland to Lithuania ("IEŚ Commentaries", no. 357). In addition, in this situation, it is possible that Baltic companies will be interested in reserving import capacity at Poland's planned LNG terminal in Gdansk (two FSRU-type terminals are to be operated as part of the investment, the second of which, with a capacity of 4.5 bcm, is to be used for non-Polish customers).