Bord Gáis Energy Index

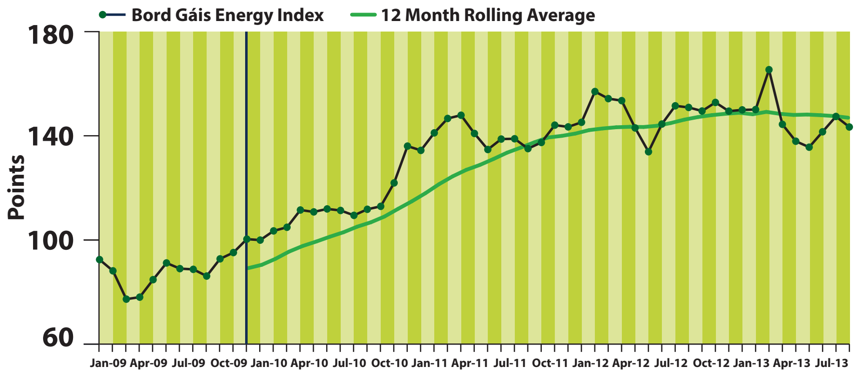
UNDERSTANDING ENERGY

September 2013

Bord Gáis Energy

BORD GÁIS ENERGY INDEX DROPS 3% DESPITE INCREASES IN WHOLESALE GAS, ELECTRICITY AND COAL PRICES

Bord Gáis Energy Index (Dec 31st 2009 = 100)



1 Mth	-3%	3 Mth	6%	12 Mth	-5%

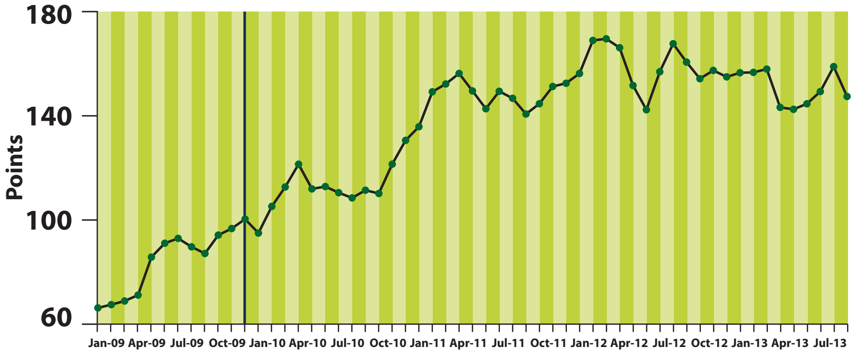
Summary:

Despite rising wholesale gas, coal and electricity prices, the Bord Gáis Energy Index fell 3% in September 2013 due to falling Brent crude oil prices.

In September 2013 the Index stood at 143 and recorded its first month-on-month drop since June 2013.

Surprisingly, UK Wholesale Day-ahead gas prices in September continued to rise and traded at levels similar to those seen during the high demand months of winter as market participants feverishly replenished depleted stocks over the summer months. As a result of the unique and evolving gas demand and supply dynamics of 2013, the average Day-ahead price this year far exceeds that of recent years. On the plus side, the risk premium associated with oil prices was partially squeezed out of the market as the real and potential threat to oil supplies eroded in September.

Oil Index



1 Mth	-7%	3 Mth	2%	12 Mth	-8%

*Index adjusted for currency movements.
Data Source: ICE

Oil

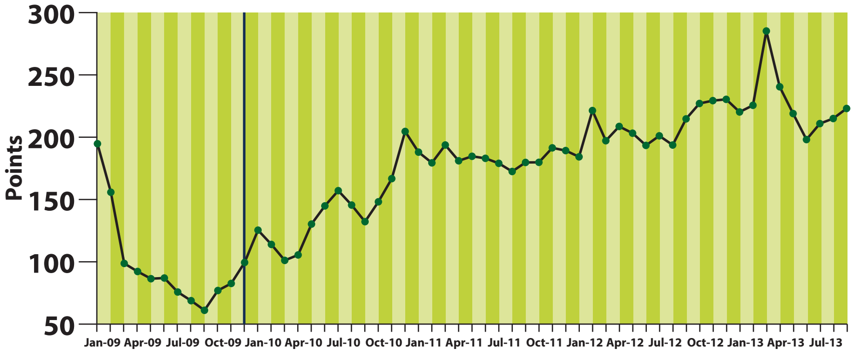
Month-on-month the front month Brent crude price fell 7% in euro terms as diplomatic progress on both Syria's chemical weapons and Iran's nuclear programme squeezed some of the risk out of the market.

At the beginning of September the front month Brent crude oil price traded above US$116 a barrel due to numerous supply disruptions and heightened geopolitical tensions. According to the EIA, unplanned OPEC and non-OPEC crude and liquid disruptions hit a significant 2.7 million b/d in August. The EIA assigned the production falls to Iran (600,000 b/d due to unplanned outages), Iraq (250,000 b/d), Libya (1 million b/d due to the deterioration in the security environment and the closure of key oil exporting facilities, pipelines and fields), Nigeria (290,000 b/d), South Sudan (170,000 b/d due to the shut-ins and natural field declines), Syria (220,000 b/d), Yemen (100,000 b/d due to the repeated disruption to the Marib-Ras Isa pipeline), Brazil (50,000 b/d) and the North Sea (40,000 b/d). These outages combined with relatively low surplus production capacity, created a tight world oil market in recent months and the front month Brent crude oil price had been rising since mid-April.

By mid-September oil prices started to weaken as the supply picture began to improve and most significantly, geopolitical tensions started to ease. The potential threat from an escalation of Syria's civil war was defused following the unanimous adoption by the UN Security Council of a binding resolution on ridding Syria of chemical weapons. The resolution demands that Syria abandon its chemical weapons stockpile and for weapons experts to be given unfettered access to make sure it is dismantled by the middle of next year. Iran's so-called 'charm offensive' and a historic phone call between an American and Iranian president helped raise the prospect of a resolution to the long standing nuclear dispute between Iran and the West. Since the imposition of sanctions it is estimated that Iran's crude exports have fallen from 2.2 million b/d to less than 900,000 b/d. Bank of America said its analysis suggest that a 'positive supply shock' of 1 million b/d could push oil prices down by US$20 a barrel, although it added that Saudi Arabia could cushion the blow by reining in output from current production. However, it is estimated that it may take years to bring Iranian oil output back to pre-sanction levels and that the window for a deal on the nuclear issue is likely to be open for a relatively short time and that positions could harden if negotiations fail to produce tangible results in the next few months. The restart of some oil fields and the resumption of crude oil loadings at some export terminals in Libya following strikes and protests has helped ease the tightness seen in oil markets. Oil supplies were further bolstered by the ramping up of South Sudan's oil production following its landmark deal with its northern neighbour Sudan to ensure the transit of South Sudanese crude for export to world markets. Production also restarted at the giant Majnoon oil field in southern Iraq which is one of the world's biggest oil fields and which will support Iraq's crude oil export target of 2.6 million b/d in October. The seasonal decline in oil consumption in Middle-Eastern countries will also help alleviate the oil market tightness.

Oil prices did receive some support by the US Federal Reserve's surprise decision to delay tapering its monthly bond purchases. However, this was counter-balanced at the end of the month by the prospect of a US government shutdown and a crisis for Italy's government.

Natural Gas Index



1 Mth	4%	3 Mth	13%	12 Mth	4%

*Index adjusted for currency movements.
Data Source: Spectron Group

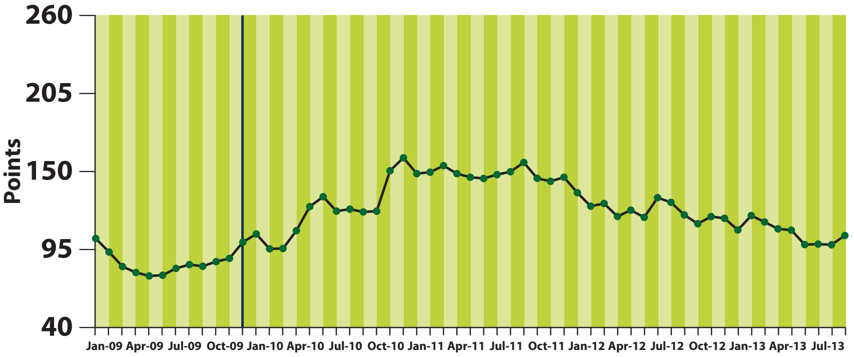
Natural Gas

In euro terms, the average Day-ahead gas price for September was 4% higher month-on-month. The month-on-month increase is significant as the August price was the strongest monthly average gas price recorded for a summer since the market was established in the late 1990s, according to Platts. Over the summer months, wholesale gas prices were in line with levels seen last December and January which is due to unprecedented demand for gas storage injections following the complete depletion of stocks in March 2013. The greater need for gas storage injections was met with very low Qatari LNG deliveries which increased the UK's dependence on Norwegian and Russian gas.

The UK Day-ahead gas price traded as high as 67.25p a therm in the middle of the month to a closing low of 63.30p at the end of the month. Prices in early to mid-September were supported by a spell of cooler weather in Britain which coincided with maintenance. The planned maintenance work at Norway's Kaarstoe gas processing plant reduced gas production by 55 million cubic metres per day for most of the month. Norwegian gas production capacity is set to remain curtailed by 34 million cubic metres through to September next year amid continuing compressor problems at the Troll swing field. Mild weather, healthy gas supplies and storage entry restrictions at the end of the month meant that Day-ahead prices fell 4p a therm amid a well supplied market. Despite a return to milder weather at the back-end of the month, the average monthly demand for gas in the UK was 154 million cubic metres, a month-on-month increase of 15 million cubic metres. As at the end of September, the UK's storage facilities were 87% full heading into winter 13/14 which commenced on 1 October 2013. As the UK's storage facilities came close to empty in March and wholesale gas prices soared, a debate commenced on whether or not the UK needed to invest in more seasonal storage. The small spread between summer and winter contracts has made new build storage projects uneconomical. Following the UK government's announcement in September not to intervene in the market to encourage additional gas storage capacity, UK utility Centrica decided not to proceed with their projects. Disappointingly, only three LNG cargoes arrived at British shores in September.

Looking ahead, the front seasons (winter 13/14 and summer 14) both weakened during the month. The winter price weakened on a combination of mild weather at the back-end of September and a sense of readiness for the months ahead. Summer 2014 weakened in harmony with weaker oil prices.

Coal Index



1 Mth	7%	3 Mth	6%	12 Mth	-12%

*Index adjusted for currency movements.
Data Source: ICE

Coal

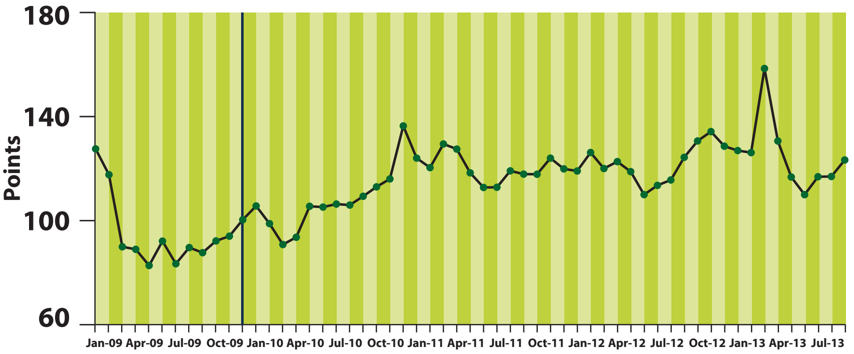
In euro terms the ICE Rotterdam Monthly Coal Futures contract was 7% higher month-on-month.

Throughout the month there was an upward momentum to prices despite a number of bearish factors such as healthy stocks in Amsterdam-Rotterdam-Antwerp, the ending of a 53-day strike at Drummond's Colombian coal mine and port operations and the successful and unexpected aversion of another strike at the rail company that operates the line connecting Colombian thermal coal mines with export terminals.

Higher coal prices have been attributed to: short-covering as prices rise, rising capesize freight rates between Puerto Bolivar and Rotterdam, market certainty and renewed buying following the end of Drummond workers' strike, utilities taking advantage of high German clean sparks spreads and a growing belief among traders that the coal market will be tighter than expected following the delayed return of Drummond's coal cargoes to Europe. It is estimated that 3.4 million m/t of thermal coal had been lost due to the 53-day dispute and that the slower than expected normalization of loading operations could tighten the European coal market in the last three months of the year. Other contributory factors include a weaker US Dollar vis-à-vis the euro, a slight escalation in traders' anxieties as the high demand months of winter 13/14 approach, a single large buyer forcing the market upward, and reduced Russian coal exports due to relatively low European prices.

Over the last two years global thermal coal prices have been on a sustained downward trajectory due to a chronic oversupply of coal. According to Societe Generale, a sustained recovery in prices is unlikely before the first half of 2014 and that price increases would only be supported by continued discipline on the supply side. It is expected that Chinese and Indian thermal coal demand will support prices in 2014 and that the floor price will be determined by the marginal cost of production from expensive production sources such as Russia and the US east coast.

Electricity Index



Data Source: SEMO

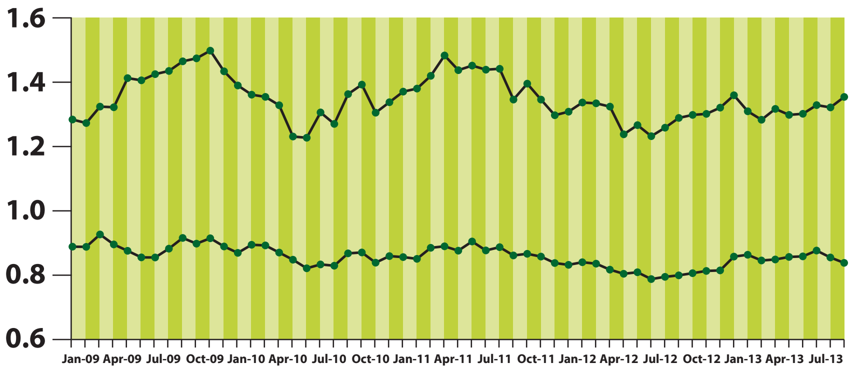
1 Mth	5%	3 Mth	12%	12 Mth	-1%

Electricity

In September the monthly average Irish wholesale electricity price rose 5% month-on-month with the combination of rising wholesale gas and carbon prices and higher 'clean sparks' (the 'clean spark' is the theoretical gross margin of a gas-fired power plant from selling a unit of electricity, having bought the fuel required to produce this unit of electricity and the cost of abating the carbon emitted).

As the Irish wholesale electricity price is highly correlated to the Day-ahead price of wholesale gas in the UK, the 4% rise recorded in the September gas price applied upward pressure. Secondly, carbon allowances rallied in September, driven by strength in the German power price which caused a short-squeeze in the carbon market. On the 17 September, the 2013 carbon price closed at €5.68 per m/t. This was the highest closing price since January 2013. The price increase has been associated with higher German power prices. Higher power prices were in turn driven by a lack of rainfall in Europe, denting hydroelectric power availability, and unplanned outages in German thermal power and French nuclear availability. Irish 'clean sparks' were supported by an increasing number of thermal generator starts (which increased the overall system cost and applied some further upward pressure to prices), the loss of a number of efficient plants and relatively cheap UK imports due to maintenance and outages, and the relatively rare use of expensive distillate units to provide short bursts of power to balance the system in the month.

FX Rates



1 Mth	2%	3 Mth	4%	12 Mth	5%	EURUSD
1 Mth	-2%	3 Mth	-2%	12 Mth	5%	EURGBP

FX Rates

Month-on-month the euro continued to strengthen versus the US Dollar.

The negative market sentiment toward the US Dollar during the month has been stimulated by three factors. Firstly, some key economic data releases in September were on the soft side. The August non-farm payrolls rose less than expected and the unemployment rate fell for the wrong reasons as people exited the labour market, having given up trying to find work. This was followed by poor retail sales numbers and evidence that US consumer confidence is weakening. Secondly the unexpected decision by the Fed to maintain its bond-buying programme at US$85 billion a month weighed on the currency as it means that freshly printed US Dollars will continue to flood the system and that there are question marks over the strength of the economy. The Fed's decision reveals that it is worried that any tightening in financial conditions could dampen the economic growth and the labour market. Thirdly, the partial shutdown of the US government after the two houses of Congress failed to agree a new budget could impact economic growth and this uncertainty weighed on the Dollar. The outcome of the upcoming Congress vote to allow the government to borrow more than its current US$16.7 trillion so-called debt ceiling will be watched closely by currency traders in the weeks ahead.

The British Pound gained versus the euro month-on-month on the back of a number of positive economic releases. 'Red-hot' business surveys, falling unemployment, rising productivity, an expanding service sector and a strong and confident housing market all suggest the UK economy is improving. Indeed, the final estimates of UK Q2 GDP confirmed that almost all the boxes required for a recovery are in place. This positivity is raising the market's expectation of higher rates and this in turn is supporting the Pound. The ECB's decision to keep interest rates at present or lower levels for an extended period of time weighed on the currency in September as did the ECB's forecast of a slow and gradual recovery in 2014. Speculation that the ECB will pump liquidity into the financial system also weighed on the currency. With inflation at a three year low of 1.1% in September, there are not many indicators pointing to an imminent rate rise either. The potential collapse of the Italian government at the end of the month added to the potential risks to the euro zone's recovery. Investors are relying on the current Prime Minister to guarantee Italy's deficit targets and deliver the stimulus needed to end the country's recession. The euro has surged this year as the currency bloc emerged from its longest-ever recession but this strength is a problem for the region's global competitiveness.

Market Outlook

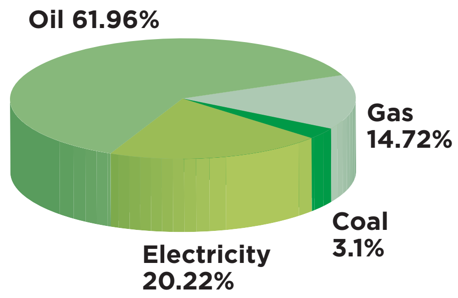
With the winter 13/14 gas season commencing on 1 October there will be an increasing focus on future gas supplies and prices. As always Mother Nature will be the primary driver of wholesale gas prices during the peak demand winter heating season. A key concern for traders is the fact that Norwegian gas production capacity is set to remain curtailed by 34 million cubic metres through to September 2014 amid continuing compressor problems at the Troll swing field. According to Reuters, the Troll outage significantly limits flexibility to ramp-up Norwegian production to meet peak demand in severe weather conditions. In 2012/13 Norwegian exports to the UK were 16% higher than the previous year. Should Norwegian supplies not meet demand in case of a cold British winter, UK customers could begin importing increasing volumes of gas from continental Europe, which receives most of its gas from Russia. However, this switch could come at a cost as it could inflate wholesale UK prices to attract flows into Britain. Russia sells most of its gas under long-term contracts linked to the price of oil. Russian gas exports to Europe rose by 14% during January - August. Falling supplies of LNG from supplies such as Qatar due to the price premiums being offered by Japan and South Korea further restricts the UK's gas supply sources. On this point in September Japan shutdown its last functioning nuclear reactor, with no timetable for a restart. On a positive note, the outlook for LNG delivery to the UK may improve from January 2014, with the news that Petronas has signed a 5 year deal with Qatargas, to supply gas to the Dragon LNG facility in the UK.

Future oil prices will be linked to diplomatic progress on Syria and Iran with the signs being positive in September. However, Israeli Prime Minister Benjamin Netanyahu has warned against working with the Iranian government and has described Iran's President as a 'wolf in sheep's clothing' in a speech to the UN General Assembly. Iran is due to take part in what has been described as 'substantive negotiations' on its nuclear programme in Geneva on 15 October with a group of nations known as the P5+1, which include the US, Russia, China, the UK, France and Germany. A removal of the geopolitical 'fear premium' could take US$10 or more off the price of Brent crude oil.

Other factors that could potentially weigh on the price of oil in the months ahead include: the impact of tapering on the 'Fragile Five' (being the loss of the cheap cash injections on those emerging economies with large current account deficits - Indonesia, South Africa, Brazil, Turkey and India) given that the expected growth in oil demand is associated with emerging economies; the economic impact of a failure by the US Government not to raise the debt ceiling; and a forecast growth in non-OPEC supply by over 1 million b/d in 2014.

Re-weighting of Bord Gáis Energy index

Following the SEAI's 2011 review of energy consumption in Ireland, there was a 6.4% drop in overall energy consumption. Oil continues to be the dominant energy source with most of the oil used in transport and the remainder being used for thermal energy. For the purposes of the Bord Gáis Energy Index, the total final energy consumption in Ireland fell 1,089 ktoe (toe: a tonne of oil equivalent is a unit of energy, roughly equivalent to the energy content of one tonne of crude oil) between 2009 and 2011. This fall was made up of a 1,022 ktoe drop in oil consumption (down 13.5%), a 20 ktoe drop in natural gas (down 12.6%), a 7 ktoe drop in electricity (down 0.3%) and a 40 ktoe drop in coal (down 10.98%). The Bord Gáis Energy Index has been re-weighted in January 2013 to reflect the latest consumption data. The impact has been minimal and has resulted in slight reductions in the share of oil and gas and a slight increase in the weighting of electricity in the overall Index.



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