Bord Gáis Energy Index

UNDERSTANDING ENERGY

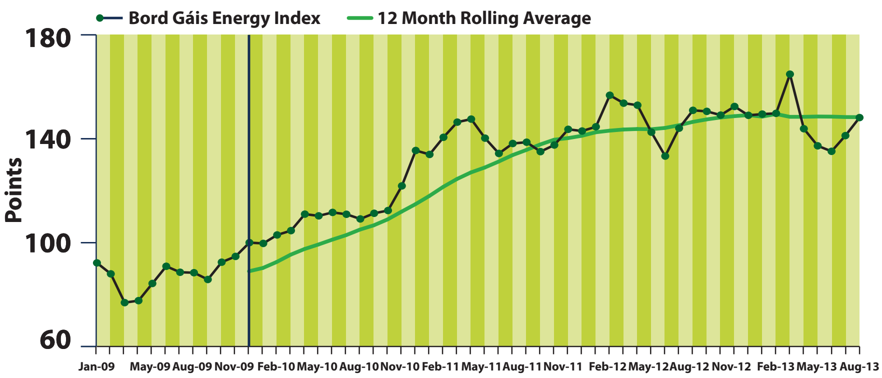
August 2013

think beyond

Bord Gáis Energy

CONCERNS ABOUT OIL SUPPLY PUSH BORD GÁIS ENERGY INDEX UP FOR SECOND CONSECUTIVE MONTH

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



1 Mth	4%	3 Mth	7%	12 Mth	-3%

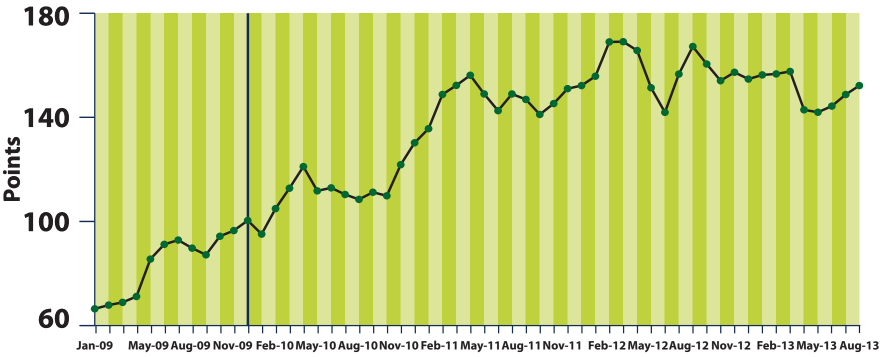
Summary:

The Bord Gáis Energy Index rose 4% month-on-month as the Brent crude oil price spiked following the suspected use of chemical weapons in Syria and an increasing likelihood that the international community will now intervene militarily in the conflict. Significant supply shortfalls in both Libya and Iraq added to traders' concerns as the oil market has turned tight at a time of low surplus production capacity.

A 2% increase in the wholesale gas price provided additional momentum to the Index's overall rise month-on-month as a relatively high historical August gas price in pence per therm has been amplified by a weakening euro. A relatively well supplied gas market over the month was not enough to apply any substantial downward pressure on prices as the market prepares itself for the beginning of winter 13/14 on 1 October.

Oil markets turned decidedly bullish in August with the increasing likelihood of an international military intervention in the conflict in Syria. Although Syria has not been an oil supplier since 2011 the market fears that the situation could evolve into a regional conflict involving some of the world's major oil producers. The price spike experienced has been supported by significant supply shortfalls in both Iraq and Libya and the ongoing potential threat to oil supplies through Egypt.

Oil Index



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

*Index adjusted for currency movements.
Data Source: ICE

Oil

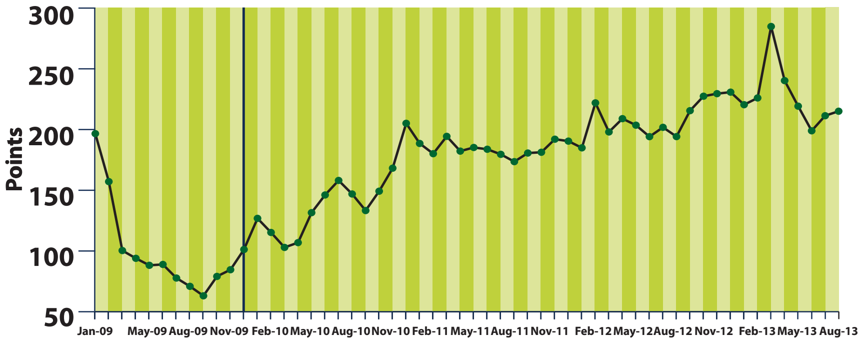
Month-on-month the front month Brent crude price rose 6% in euro terms as events in Syria, Libya and Egypt threatened global oil supplies. At one point the Brent crude price surged to a six-month high when it traded at over US$117 a barrel.

In early August violent scenes and deaths in Egypt, following a crackdown on those protesting against the overthrow of Mohammed Morsi by the powerful Egyptian military, pushed oil prices higher. Traders feared that protests and retaliation by the Muslim Brotherhood against the military could disrupt oil supplies through the Suez Canal and Sumed pipeline (the Sumed pipeline provides an alternative to the Suez Canal for transporting oil from the Persian Gulf region in the Mediterranean).

Towards the end of the month the focus shifted to Syria following an alleged chemical weapons attack by the Assad regime which killed more than 1,400 people on 21 August. This has increased the chances of a US led military strike in Syria. Syria itself has not been an oil supplier since late 2011 nor is it a transit country for oil supply, so a strike would not directly threaten global oil supplies. However, traders fear that a military strike could widen the conflict beyond the borders of Syria and potentially impact the supply of oil from some of the OPEC producing countries in the region. There is also the fear that a US strike could endanger the revival of negotiations to resolve the nuclear standoff with Iran, which has long been a source of periodic anxiety in oil markets. In addition to the prospect of reduced oil supplies, real falls in oil production in Libya and Iraq have tightened the market. Libya's oil production reportedly has fallen to as low as 400,000 b/d as strikes and protests have crippled its oil export facilities. In May Libya produced an average of 1.4million b/d of crude oil. Iraqi production is also faltering amid rising sectarian violence, regional tensions and challenges associated with building and maintaining infrastructure. Despite what the International Energy Agency describes as an adequately supplied market, the 'fear factor' dominated during the month amid a series of geopolitical tensions. Falling supplies from Libya and Iraq have been somewhat offset by rising Saudi production but this has come at the expense of spare OPEC capacity. Analysts from the bank Societe Generale suggest that the price could eventually surge to US$125 if air strikes are launched and US$150 a barrel if the military action disrupts production in the region.

A series of better than expected economic releases during the month suggest that the global economy is showing tentative signs of recovery and this in turn added to the upward momentum in oil prices. US growth in the second quarter was revised up from 1.7% to 2.5% and it was a further sign that the world's largest economy may be getting back on track. It was also revealed that the US manufacturing sector grew at its fastest pace in five years in August, with a pick-up in new orders. Following 18 months of recession, it was revealed in August that the euro zone economy grew 0.3% in the second quarter of 2013. This followed news that euro zone industrial output grew 0.7% month-on-month. It was also revealed that China's manufacturing activity picked-up speed in August as it hit a 16-month high. This helped to allay fears of a sharp slowdown in its economy. With an improving US economy, there is however a growing belief that the Fed will 'taper' or cut back their injections of cheap cash later this year. This weighed on equity prices during the month and on some emerging economies and provided some limited downward pressure on oil prices.

Natural Gas Index



1 Mth 2% **3 Mth** -2% **12 Mth** 11%

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

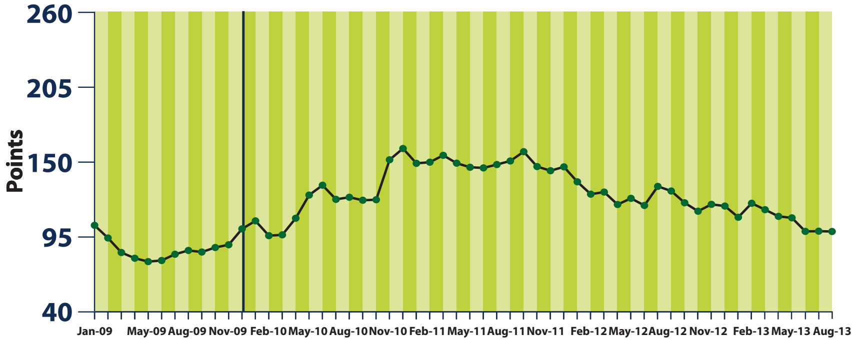
Natural gas

In euro terms, the average Day-ahead gas price for August was 2% higher month-on-month. A weaker euro versus the British Pound ensured that the slight month-on-month fall in the average Day-ahead gas price was not replicated in euro terms. However, at 64.72p a therm, the average Day-ahead gas price for August 2013 is high when compared to previous years (the comparable historical prices in pence per therm are: 2012 54.06p, 2011 53.80p, 2010 42.46p & 2009 21.50p).

With a swath of planned maintenance outages expected in August, traders were anxious that reduced gas supplies during the month could push prices higher if the market struggled to meet demand. The yearly maintenance of the Easington terminal (which cuts all flows across the key Norwegian supply pipeline to the UK) and works at the Norwegian Kollsnes processing plant were scheduled to occur in August. However, despite reduced Norwegian supplies the UK gas market coped well and prices remained steady for much of the month. Supplies were bolstered by withdrawals from medium range storage, reduced UK exports to the Continent and unseasonably low demand. Bearish European gas prices due to warm weather, low demand for storage injections and a jump in Russian supplies into Continental Europe contributed toward the steady nature of the UK market in the month. Russia's state-owned gas giant Gazprom said its exports beyond CIS in July hit a 5-year high and rose 29% year-on-year. Amid healthy gas supplies and the completion of scheduled maintenance, prices in sterling terms could have fallen lower but for a number of unplanned shutdowns and maintenance work toward the end of the month.

Looking ahead, the winter 13/14 gas price softened during August as total UK gas storage levels reached close to 90% full. Rising stock levels in the UK but also in Germany and France helped to alleviate traders' concern about gas supplies ahead of winter. However, Asian LNG demand is expected to remain strong as Japan will have zero nuclear capacity in operation by mid-September and South Korea deals with the loss of six of its nuclear reactors. As a result of rising Asian LNG demand, in the first half of this year Qatar reduced exports to Europe by 42% year-on-year, with Libya reducing exports by 13% and Algeria 10%. Summer 14 gas prices held firm as the influence of rising oil prices was being felt and news that a Norwegian maintenance outage that was due to conclude at the end of the winter is being extended into summer 2014.

Coal Index



1 Mth 0% **3 Mth** -9% **12 Mth** -23%

*Index adjusted for currency movements.
Data Source: ICE

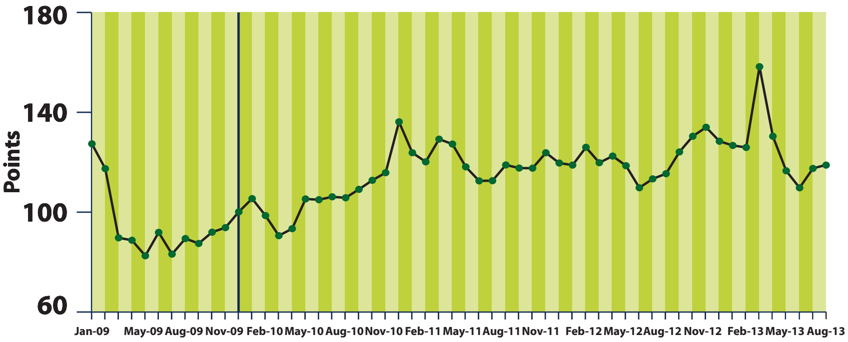
Coal

In euro terms the ICE Rotterdam Monthly Coal Futures contract was unchanged month-on-month as the European market appears to have grappled with an abundance of coal for sale, eliminating any upward price effect of an ongoing miners' strike in Colombia.

Despite six weeks of industrial action which has reportedly paralyzed the production and shipping capabilities in the second largest thermal coal exporter in Colombia and a supplier of the fuel to Europe, European coal prices delivered into Amsterdam-Rotterdam-Antwerp failed to move significantly. The impact of the strike appears to have been offset by bearish summer sentiment amid low demand, comfortable stock levels and the availability of material from other producers in Colombia, the US, South Africa and Russia. Given the muted reaction to the strike in Colombia, analysts are of the opinion that it would take at least another month of a disruption to supplies before the market would tighten and for an impact to be felt on prices. Coal miners are set to vote in early September on whether to return to work.

Weakness in the seaborne thermal coal market as a whole also helped mitigate the impact of the Colombian strike on European prices. With further price cuts by Chinese coal producers in August, it has become more difficult to sell cargoes into China. Furthermore, with a continued slowdown in India's economy and a weaker rupee against the Dollar (during the month the rupee hit a record low against the Dollar and has fallen more than 20% this year), Indian buyers of imported thermal coal have reportedly backed away from the market as prices for Indian buyers escalated. The rupee's weakness has been associated with developments in the US, where the economy is improving and officials at the Fed have started to talk about cutting back on its stimulus measures. The prospect of the Fed's 'tapering' has seen the reversal of capital flows out of emerging economies and back to the core. It is estimated that in the past four years since the global financial crisis, nearly US$4 trillion has poured into emerging economies. The economies most at risk are those with large external deficits and India is seen as being vulnerable with a current account deficit of nearly 5% of GDP.

Electricity Index



Data Source: SEMO

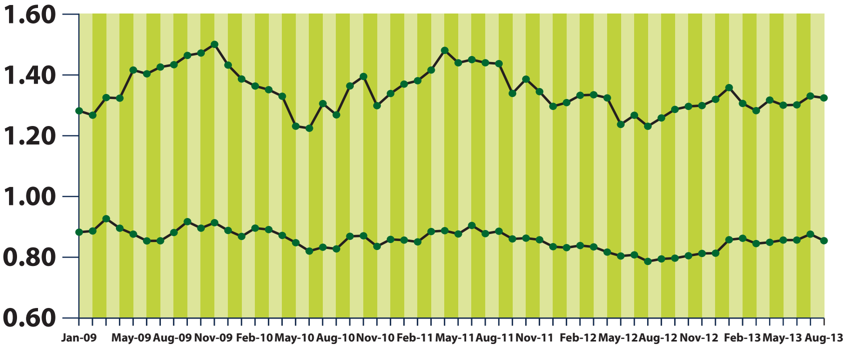
1 Mth 1% **3 Mth** 1% **12 Mth** 2%

Electricity

In July the monthly average Irish wholesale electricity price rose 1% month-on-month.

Modest upward pressure on the wholesale electricity price in August occurred throughout the month. Firstly, as the wholesale electricity price is highly correlated to the Day-ahead price of wholesale gas in the UK, the 2% rise recorded in August applied some upward pressure. Secondly, a modest rise in the cost to abate the carbon emitted in the process of producing a unit of electricity by burning gas or coal applied some additional upward price pressure. Maintenance and outages also contributed to higher wholesale prices as more expensive producers of electricity were called upon to replace lost volume. During the month the market suffered from the temporary loss of an efficient gas plant, reduced output from coal plants and falling imports of relatively cheap power from the UK. In addition, as alternative providers competed to replace lost volume, the system experienced a larger number of plant starts and stops which increased the overall system cost and applied some further upward pressure to prices.

FX Rates



1 Mth	-1%	3 Mth	2%	12 Mth	5%	EURUSD
1 Mth	-2%	3 Mth	0%	12 Mth	8%	EURGBP

FX rates

Month-on-month the euro lost ground against the US Dollar and British Pound.

A series of positive economic releases in the UK strengthened the Pound during the month. A gauge measuring managers' purchasing plans in the service sector surged and industrial production hit a 10 month high. This was followed by releases showing that the UK exports are rising and that the trade deficit is falling. Rising house prices, retail sales and GDP growth added to the positive momentum. The upward revision to Q2 GDP showed that growth in the UK is occurring across the major sectors of the economy. Lending to the corporate sector is also increasing but still critically remains below its 2008 peak. Following this series of positive releases, markets have started to price in a rate increase in Q1 2015 which has helped to stimulate sterling. However, the Bank of England's new head, Mark Carney, in his first speech as Governor reiterated his pledge to keep rates low. The Bank of England is attempting to send a clear signal to businesses and consumers that a low rate environment is assured. The Bank of England may be disappointed with the initial reactions to its 'forward guidance' as it has not succeeded in stopping forward rates from steepening and the Pound has appreciated.

Falling inflation and record high unemployment in the euro zone may encourage the ECB to cut rates. This expectation weakened the euro in the month. However, after 18 months of recession the euro zone recorded economic growth in the second quarter of 0.3% quarter-on-quarter and a survey of private sector activity across the monetary block rose to its highest level in over 2 years.

The US Dollar gained versus the euro month-on-month with a growing expectation that the Fed will start reducing its quantitative easing programme later this year. This momentum will continue to build if future data, particularly jobs data, shows that the US economy is recovering. If the Fed conclude that the economy is strong enough to allow them to pare its monthly purchases of US$85 billion in Treasuries and mortgage debt, the US Dollar is expected to strengthen and the markets have begun to price this in.

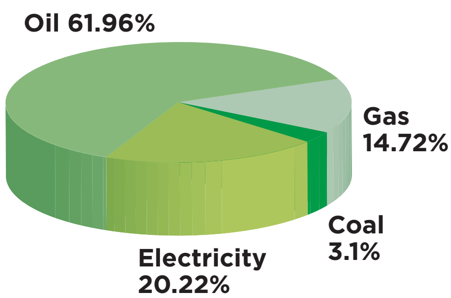
Market Outlook

How the international community responds to the suspected use of chemical weapons in Syria will determine the direction of Brent crude oil prices. Any military intervention by the international community has the potential to draw countries in the region further into the conflict and this could threaten vital oil supplies. As the global oil market is already suffering from reduced supplies from Libya and Iraq any further disruptions will push prices higher. Saudi Arabia has helped to alleviate lost supplies as its production has increased to 10million b/d from 9.15 million b/d in March but this has come at the expense of spare capacity. It has been estimated that the world's spare capacity has dipped into the 2 - 2.5 million b/d range from an estimated annual average spare capacity of 4 million b/d in 2010 - 12. A decline in spare capacity increases the vulnerability of the oil market to supply shocks and the risk of this occurring has increased with the likelihood of the international community directly involving itself in the conflict in Syria. The International Energy Agency has tried to manage the market's concern by stating that the global crude oil market is adequately supplied but such a statement reveals that they are concerned about the harmful effects of high oil prices on the global economy. The agency is reportedly ready to respond if there is a major supply disruption. In 2011 it coordinated the release of 60 million barrels of crude oil products to offset lost supplies from Libya where the uprising almost halted the country's oil exports. At the time Brent crude prices fell 8% in the 2 days after the announcement of that intervention.

Beyond the pressing issue of supply disruptions, there is a growing expectation that the Fed will start to cut back on its injection of cheap cash in the months ahead. In response, money has started to leave emerging economies who in the past looked attractive because they were growing faster than sluggish economies in the West. As western economies make tepid steps toward recovery, growth has slowed dramatically across emerging economies that benefited from a commodity boom and a lot of US consumption. With OECD countries in the 'post-peak' demand region since 2005, emerging economies have been responsible for the growth in oil demand. Stuttering growth coupled with growing non-OPEC oil supplies could, in the absence of supply disruptions, push oil prices lower.

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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