

Steep rise in wholesale oil prices offsets wholesale natural gas price decline as Bord Gáis Energy Index remains unchanged

Monday, 7th July 2014: Continuing steep rises in wholesale oil prices have offset declines in wholesale natural gas prices this month leaving the Bord Gáis Energy Index unchanged month-on-month. Brent crude oil hit a yearly high in June as events in Iraq alarmed the market and raised concerns about the ability of global oil supplies to meet rising demand. The rising oil prices were however offset by a 12% drop in Day-ahead average UK natural gas price for June. The recent tension and military activity in Iraq has increased the threat to the global supplies of oil which resulted in a 2% increase in the front month Brent Crude Oil price. The drop in natural gas prices also had an effect on Irish wholesale electricity prices which fell 4% in June, as gas is the primary fuel used to generate electricity in Ireland.

The current decline in the price of wholesale natural gas is attributed to the mild UK winter which reduced the need to withdraw gas from storage facilities over the winter period. This has left storage levels quite high at 83% full compared to just 53% at the same time last year. The UK is also continuing to benefit from bumper gas supplies and this is adding further pressure on prices.

In June 2014 the Index stood at 133.

Commenting on the Bord Gáis Energy Index for June, John Heffernan, Gas & Power trader at Bord Gáis Energy said:

“The threat to Iraq's oil production capabilities and export potential following ISIL’s territorial grab in the country has had a significant impact on global oil prices in June. With global oil demand expected to increase sharply, a complete loss of Iraqi exports would have dramatic consequences for global oil prices. It would not be inconceivable for prices to surpass the record highs reached in July 2008 (above US\$145 intraday for Brent) with the world having no spare capacity anywhere. The future course of the conflict is very uncertain and the majority of Iraqi oil is reportedly safe. However, it is a concern that sect conflict in the Middle East region is spreading, intensifying and appearing intractable and these events are not positive for oil prices.”

Oil (+2%)

Month-on-month the front month Brent crude price rose 2% in euro terms as the front month Brent crude oil price hit its highest level this year, with the market alarmed by the emergence of ISIL (the Islamic State in Iraq and Levant) on the world stage. Traders were concerned by the nature of the current bout of violence in Iraq and scale of ISIL's territorial grab. Events in Iraq again demonstrate the deep sectarian divide that exists in a region that supplies vast quantities of oil to the world. Oil traders are concerned that the world has very limited extra production capacity at its disposal currently and the loss of Iraqi oil, or further supply disruptions, would result in oil price spikes. Question marks over Iraq’s ability to supply oil coupled with concerns in Libya, Iran, Syria, South Sudan, Yemen, Venezuela and Nigeria, could expose the world to oil price spikes if supply disruptions occur over the coming months.

Natural Gas (-12%)

The average Day-ahead gas price for June was 12% lower month-on-month in euro terms as weak demand and bumper supplies continued to push prices lower at present. The fullness of the UK's gas in store is a factor weighing on gas prices as the need to replenish stocks ahead of the winter is weaker this summer given the fullness of the UK gas storage facilities. In addition, the UK is currently experiencing a strong and steady supply of Qatari LNG cargoes due to softening Asian prices.

Despite a major gas transit pipeline in Ukraine carrying gas from Russia to Europe being hit by an explosion in June and the decision by Moscow to cut off supplies to its neighbour over the long-running payment dispute, wholesale gas prices in the UK continued to weaken as Russian gas supplies to Europe remain uninterrupted. The standoff between Ukraine and Gazprom continues over a disputed US\$4.5 billion gas debt Gazprom claims that the Ukraine owes. Despite the gas market's current ease with the crisis in Ukraine, if this dispute continues into autumn it raises the possibility of the Ukraine siphoning off gas bound for Western Europe, to satisfy rising domestic demand.

Coal (-2%)

In euro terms the ICE Rotterdam Monthly Coal Futures contract fell 2% month-on-month and at US\$73.20 /mt, the ICE Rotterdam Monthly Coal Futures price closed the month at its lowest level since September 2009. Barring any major supply cuts, there is nothing to support prices, with sources pointing out that supply-demand fundamentals in Europe remain bearish. Weakening European gas prices are also starting to marginally erode Europe's demand for coal.

Electricity (-4%)

In June the monthly average Irish wholesale electricity price fell 4% month-on-month as a result of softer wholesale gas prices (gas powered generation dominates the generation mix on the island of Ireland). Despite the 12% month-on-month drop in the monthly average Day-ahead wholesale gas, and softening European coal prices, the average 'clean spark' in Ireland rose by approximately €2/MWh to close to €13.50/MWh (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) and this rise supported electricity prices in the month. In a European and Irish context, and in an internationally competitive environment, €13.50/MWh remains a strong 'clean spark', particularly given that we are in the summer period when demand softens.

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