

Bord Gáis
Energy Index
Understanding energy

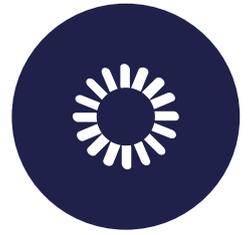
AUGUST 2016

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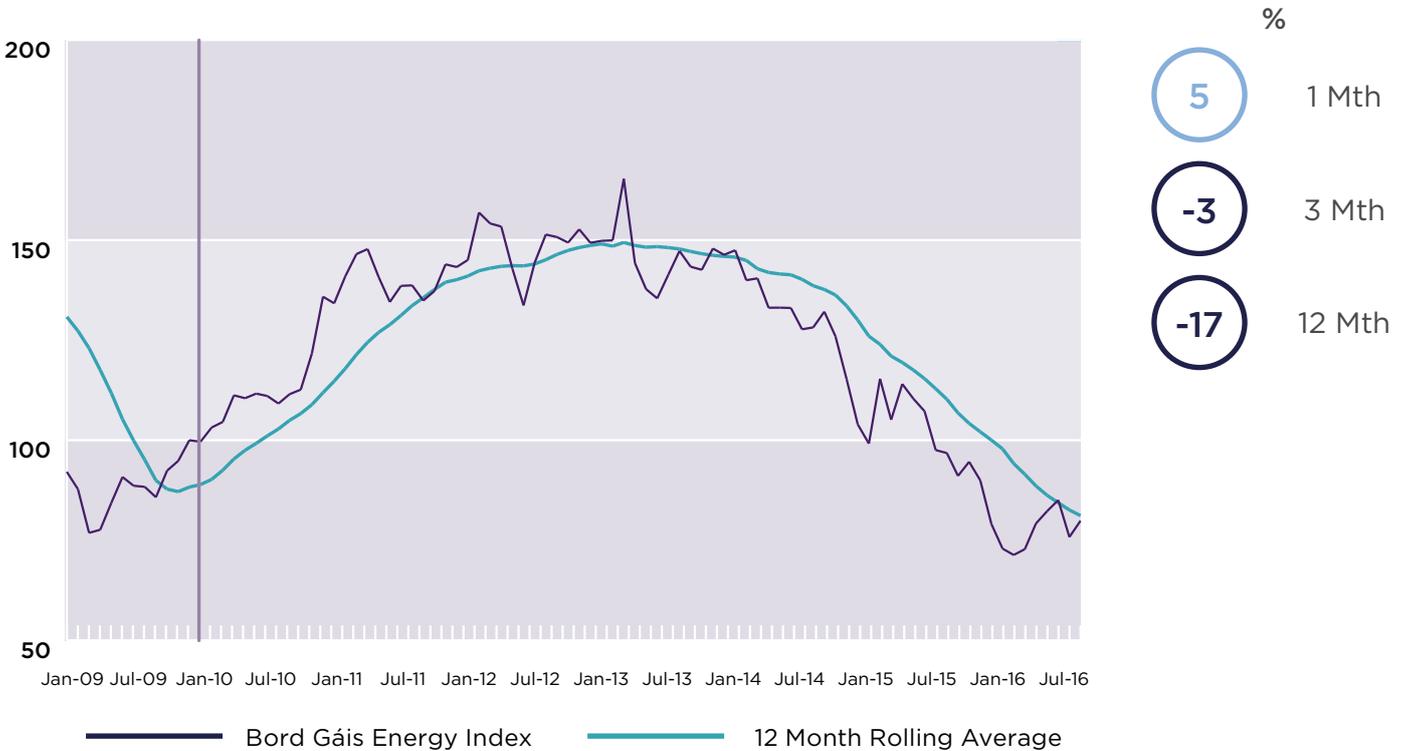


Bord Gáis Energy Index

August 2016



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



Summary

In August 2016, the Bord Gáis Energy Index was 5% higher as oil rallied 11% on renewed talks of a production freeze. Among the other components of the Index, UK prompt wholesale gas prices were 12% lower, Irish wholesale electricity prices were up 1% while coal also rallied over the month, finishing the month 7% higher in euro terms.

In August, the Index stood at 80.

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Oil Index



Index adjusted for currency movements.

Data Source: ICE

Oil

The Brent crude benchmark contract continued to fluctuate in August as the oil price closed the month 11% higher at \$47.04 a barrel having dropped 15% in the previous month.

As we entered August, the recent bearish sentiment was firmly ensconced as a deteriorating global economic outlook, a stronger US Dollar and resilient oil supply all continued to weigh on oil prices. However, sentiment shifted sharply in early August on comments from the Saudi oil minister, Khalid al-Falih, that OPEC could discuss action to stabilise markets at an informal gathering in Algeria in late September. The market took this as a signal that the perennial production freeze, to help rebalance the over-supplied market, was back on the agenda.

This speculation intensified later in the month after Reuters reported that Iran was sending “positive signals” that it may support joint action to bolster the oil market, citing unidentified sources in OPEC and the oil industry.

However, a healthy dose of scepticism is warranted when considering the prospects for a successful production freeze agreement. Firstly, we’ve heard all this before! Reports suggested a similar deal was in place ahead of the April OPEC meeting in Doha, before political tensions between Iran and Saudi Arabia scuppered any hope of a deal.

In recent months many OPEC members have ramped up production in an anticipation of a freeze, ensuring any freeze would simply maintain the elevated rate of production rather than reduce the supply glut which has pushed prices lower. In addition, the oil market faces a number of headwinds; inventory levels are at record highs, Iran continues to increase production in a bid to recapture market share lost during sanctions and US oil production is starting to show signs of growth at oil prices previously believed to be uneconomic for many tight oil producers.

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Natural Gas Index



Index adjusted for currency movements.

Data Source: Spectron Group

Natural Gas

The UK NBP day-ahead contract averaged 30.46 pence/therm for August, this is a drop of 12% when compared to July's day-ahead average of 34.21p/th and is 23%, or 34% in euro terms, below the comparable day-ahead average price of 39.78p/th in August 2015.

The price for day-ahead gas, the contract for gas delivered tomorrow, fell steadily over the month as supplies to the market remained healthy through the lowest demand period of the year. The system was oversupplied for most of the month as pipeline gas imports from Norway were strong and LNG cargo deliveries were steady, although somewhat below what the market was expecting with some cargoes diverted to higher priced Asian markets. Supplies of LNG to Europe are expected to rise over the next number of years as US and Australian production comes to the market. The outage at the Rough storage facility in the UK reduced demand in August as gas is normally bought on the market over the warmer summer months and injected into storage for use over the colder winter months. Higher wind levels also weighed on gas demand in the UK over the month as more wind was used for power generation.

The forward market also recorded lower prices over the month as the update from Centrica, the owner of the Rough storage facility and parent company of Bord Gáis Energy, that the facility expects 20 wells to be available for gas withdrawals from November 1st was seen as a positive for supply over the coming winter. An announcement made in July that due to technical issues Rough would have only 4 wells available for withdrawal, had caused prices to spike. The average price for the benchmark Winter 16 contract fell from 44.8p/th to 41.75p/th over August, a drop of 7% on the month.

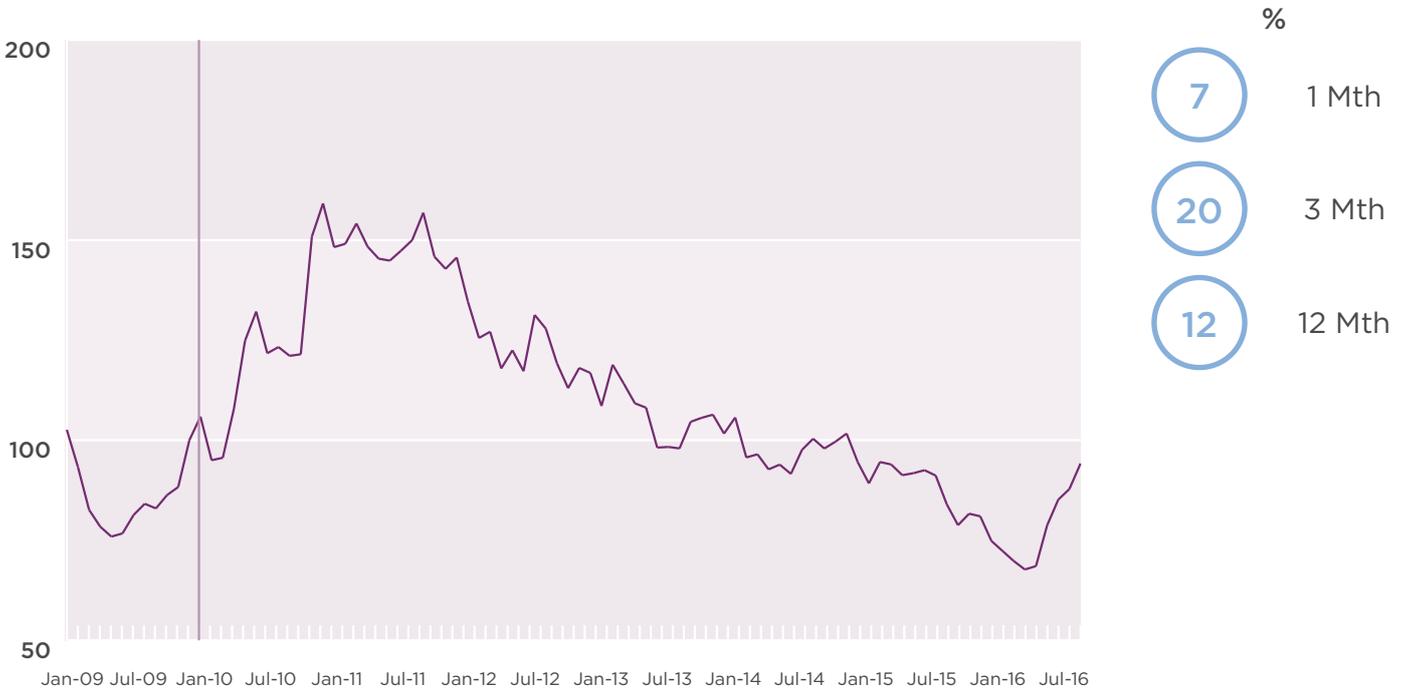
An interesting point to note was the de-linkage between oil and gas prices. Oil prices rallied over the month as exporters revived talk of a production freeze while gas prices fell, supply agreements in the UK are no longer linked to oil prices but it can act as a driver when there is no change in gas fundamentals. During August, the strong gas supply picture coupled with the positive news on Rough storage outweighed any upward pressure from rising oil prices.

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Coal Index



Index adjusted for currency movements.

Data Source: ICE

Coal

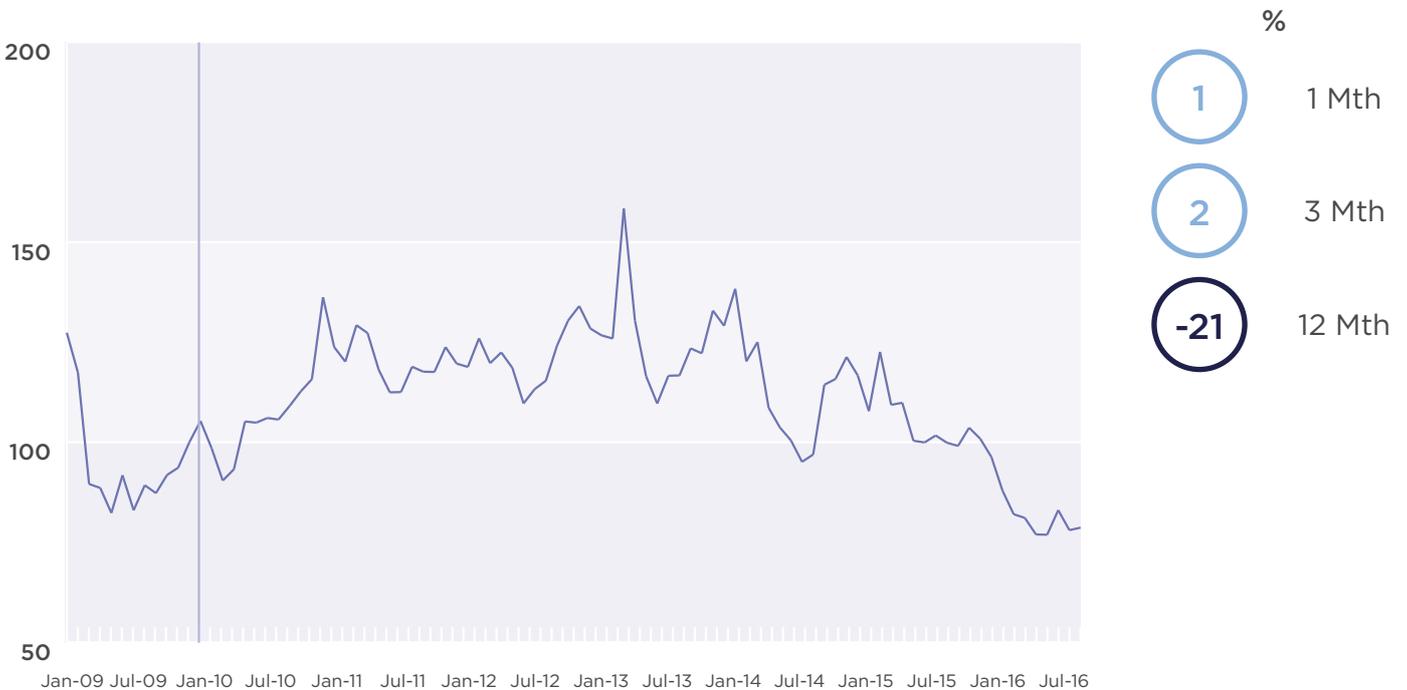
Coal prices closed the month at \$61.3 per metric tonne, an increase of over \$4 from August's close of \$57.15. The remarkable turnaround in coal prices, following years of constant price declines, has seen prices rally over 41% from the February lows of \$44.30 as a combination of supply contraction, demand growth from China and a broad commodity rally have all helped push prices higher.

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Electricity Index



Data Source: SEMO

Electricity

Including capacity payments, the average Irish wholesale electricity price increased by 1% over the month.

Excluding supplier capacity payments, the average wholesale price for August was 5% lower at €36.2/MWh compared to €38.12/MWh in July, a decrease of €1.92/MWh on the average monthly wholesale price.

The average wholesale cost of imported gas from the UK decreased by 12% in sterling terms. Irish wholesale power prices typically tend to track the cost of imported gas as it is the most significant cost in the production of electricity.

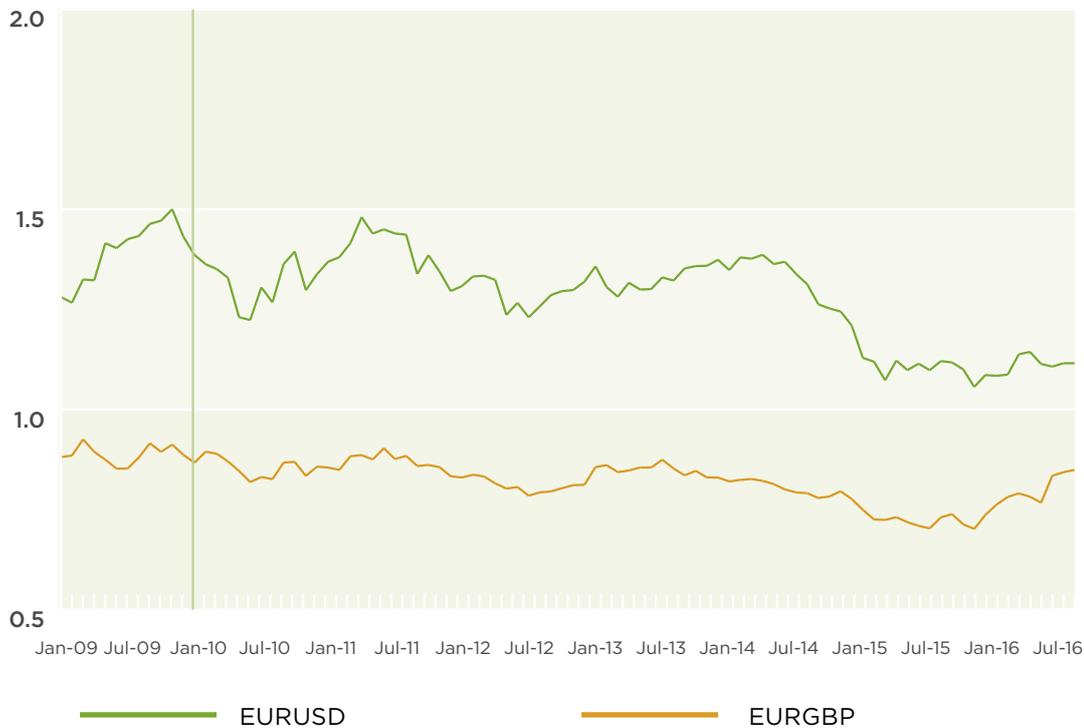
An average monthly clean spark of approximately €9.51/MWh was recorded in the month, which is up from the €7.98/MWh observed in July (an increase of 19.2%). The proportion of demand met by wind in August increased to 19.78% from 13.4% in July. Although the proportion of wind on the system increased during the month, there were a number of plant outages which, along with some volatility in the wind, contributed to the higher sparks.

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FX Rates



EURUSD %

- 0 1 Mth
- 0 3 Mth
- 0 12 Mth

EURGBP %

- 1 1 Mth
- 11 3 Mth
- 16 12 Mth

FX Rates

In August, the euro gained in value marginally versus the British pound and was flat versus the US Dollar. The euro was 1% higher against the pound, finishing the month at 0.8491p and flat against the dollar at \$1.1158.

The euro traded at almost 87 pence sterling at one point during the month as the Bank of England surprised markets by announcing a larger stimulus package than had been expected. Base rates were cut from 0.5% to 0.25% and a new round of quantitative easing was announced. The Bank will buy £60 billion of government bonds per month over 6 months and it will also buy corporate bonds for the first time at a rate of £10 billion per month. This package is to help the British economy counter any post Brexit weakness.

The euro was flat versus the dollar over the month even as speculation grew that a rate hike was likely before the end of the year from the US Federal Reserve. This came after minutes of the previous Fed meeting were slightly more hawkish than had been expected by the markets. Markets were pricing about a 55% chance of a rate hike at the end of August but the pace of any hiking cycle is likely to be slow as futures markets don't fully price a hike until middle of 2017 and no additional increase after that until June 2019.

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