

Bord Gáis Energy Index

Understanding energy

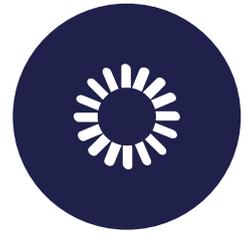
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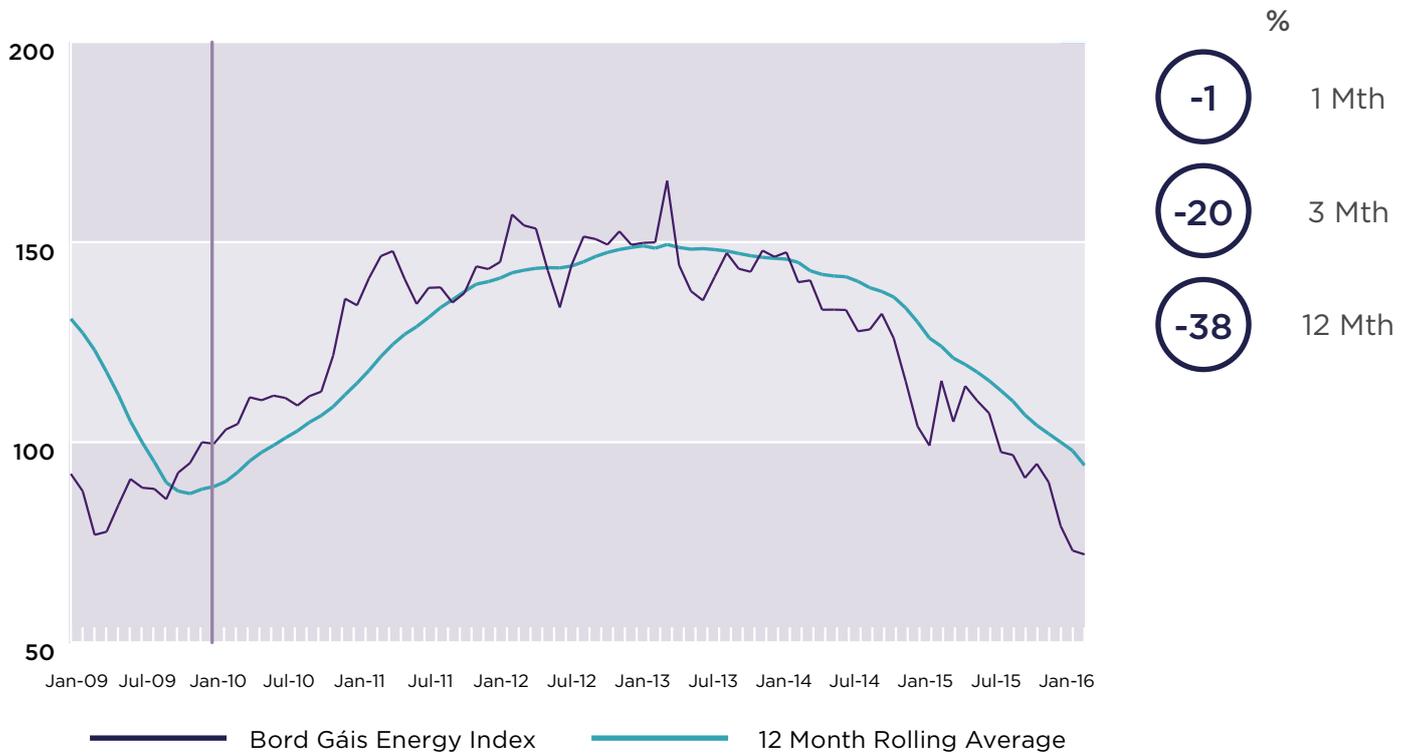


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February 2016



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



Summary

In February 2016 the Bord Gáis Energy Index fell by 1% month-on-month. Wholesale prices of Brent crude oil rose by 3%, while UK prompt wholesale gas (-10%), European coal (-3%) and Irish wholesale electricity (-5%) recorded losses month-on-month.

In February 2016 the Index stood at 72.

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Oil Index



*Index adjusted for currency movements.

Data Source: ICE

Oil

Oil prices pushed higher in February as prices responded to an agreement between OPEC & Russia on a potential production freeze. The Brent front month benchmark contract closed the month 3.5% higher at \$35.97 a barrel.

An oversupplied market driven by lower demand and record OPEC & non-OPEC production has pushed prices to 12 year lows earlier this year. Toward the middle of the month Russia, Saudi Arabia, Qatar and Venezuela agreed to freeze production at January levels, provided other OPEC members agreed to make a similar commitment. Iran, which has only recently had sanctions lifted, and Iraq both welcomed the proposed output ceiling, but crucially have not confirmed they intend to participate.

Despite widespread scepticism surrounding the proposed deal, given a history of mistrust between Russia and OPEC and the friction within OPEC, the very fact that discussions are taking place has put a bid back into oil markets with many speculators closing short positions.

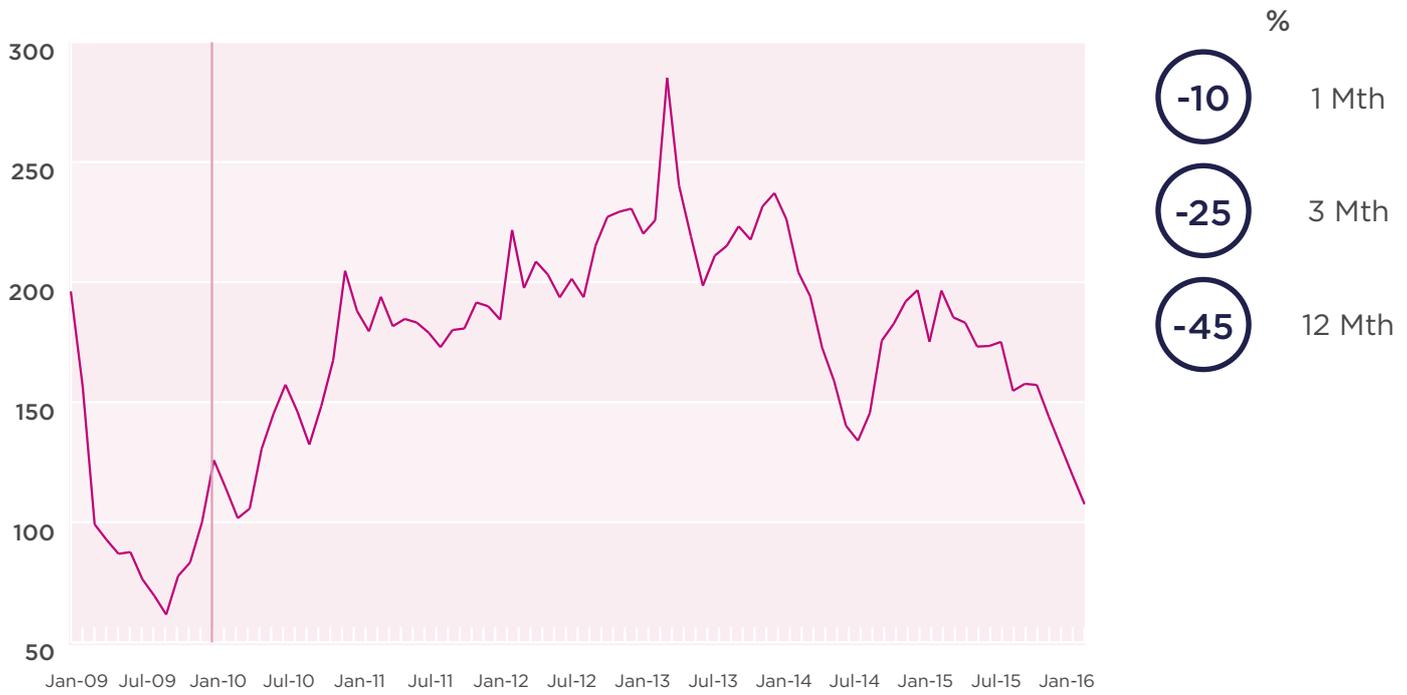
The recent rally in oil could well be sustained if we see credible evidence that the supply glut in the oil market, which has pushed prices to multi year lows, is dissipating either by way of an agreement between OPEC and non-OPEC producers or as the economics of lower prices choke supplies from higher cost producers.

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Natural Gas Index



*Index adjusted for currency movements.

Data Source: Spectron Group

Natural Gas

The UK's NBP day-ahead contract averaged 29.55 pence/th in February. This was down 2.47p/th on January's day-ahead average of 32.02p/th and significantly lower than the comparable month average of 50.15p/th in 2015.

We saw average daily demand exceed seasonal norms for February by about 8mcm a day. However, the system balanced comfortably without pushing prompt prices higher. Stable supplies, both UKCS and imports, and storage withdrawals were utilised to comfortably balance the system and prompt prices traded lower over the month.

Further out the curve, there was a slight divergence in seasonal contracts. The Summer 16 contract continued to weaken, falling approximately half a penny to 27.6p/th, on the back of benign weather forecasts, high storage levels and continued strong LNG cargo arrivals. In contrast, the Winter 16 contract traded higher, on the back of strength in oil, trading .3p/th higher at 33.3p/th.

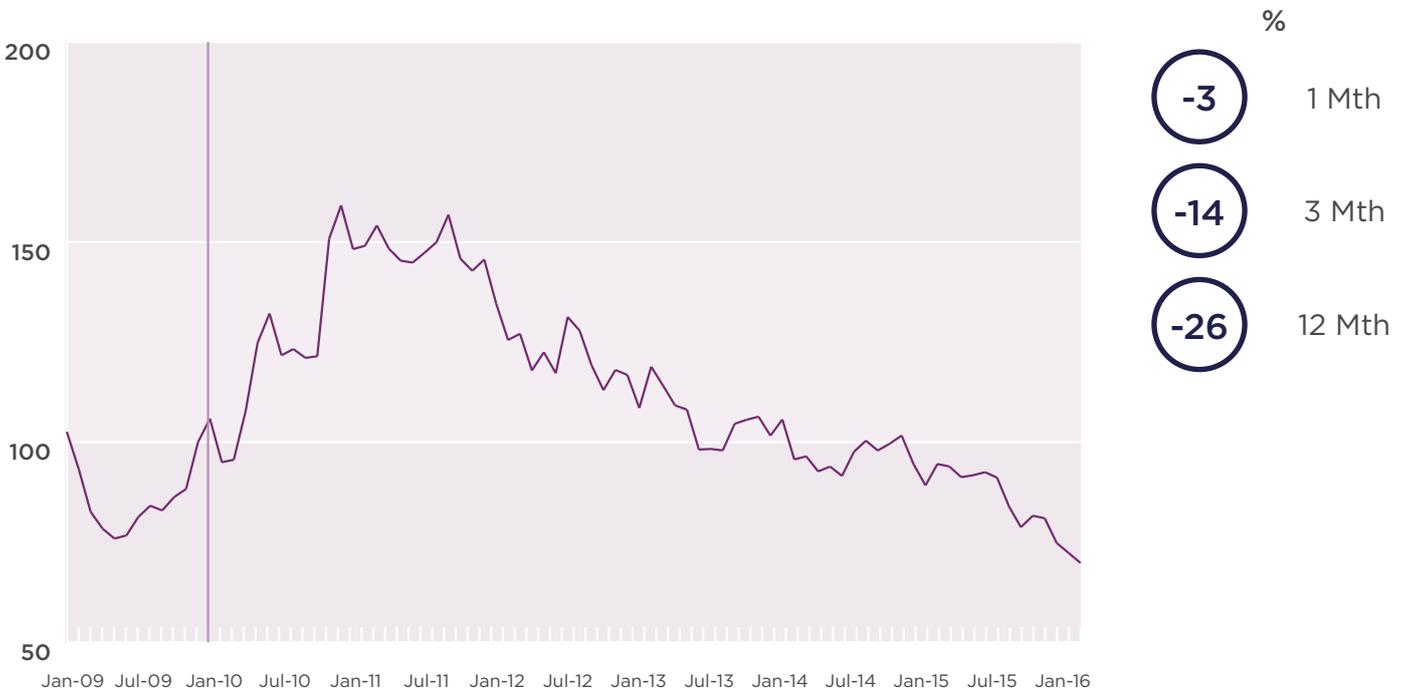
In recent days, the first US LNG cargo left Sabine Pass destined for Brazil marking the arrival of a key LNG supplier into an oversupplied global LNG market. Sabine Pass, located in Cameron Parish, Louisiana, has completed construction of the first two of its six liquefaction trains. Three other trains at Sabine Pass are currently under construction and are scheduled to come online in the next two years.

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Coal Index



*Index adjusted for currency movements.

Data Source: ICE

Coal

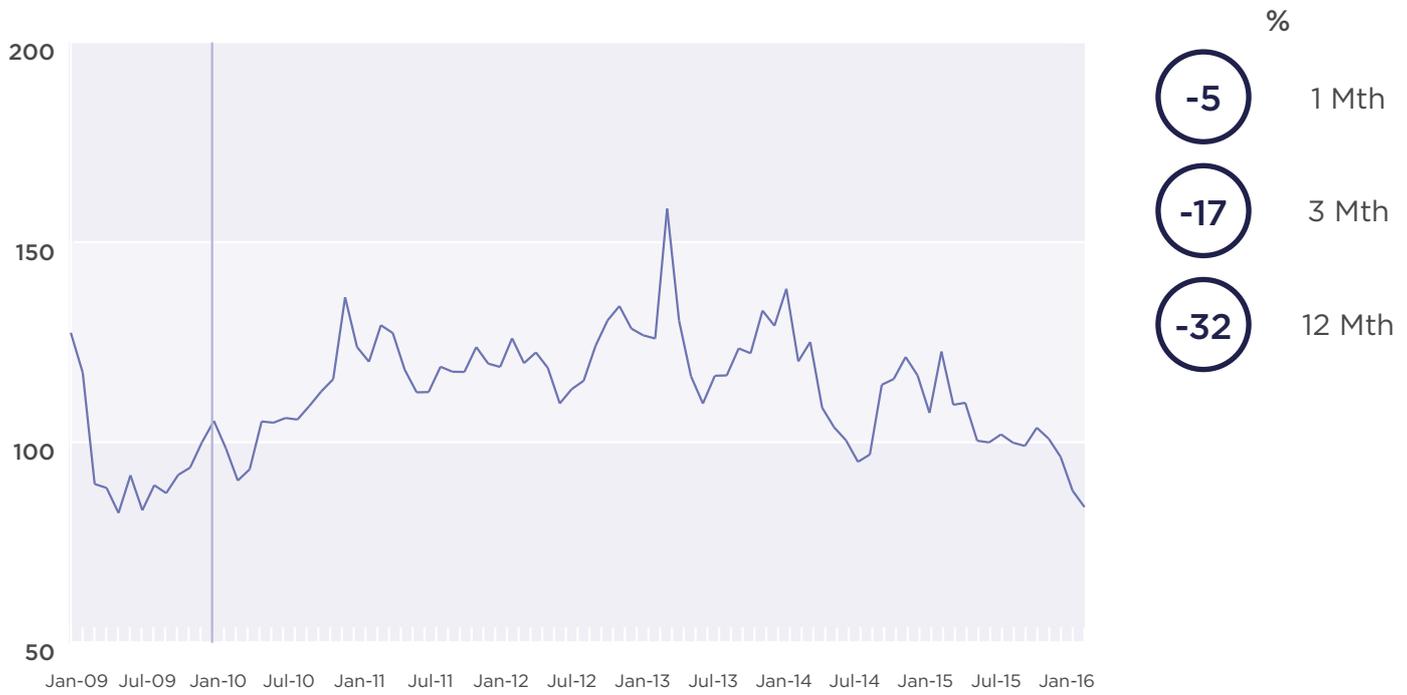
Coal prices traded 3% lower on the month at \$44.30 per m/t. The price reached an intra-month low of \$43.40 per m/t before recovering toward month end. In China, up to 1.3 million workers in the coal sector are expected to lose their jobs as parts of an effort to reduce industrial overcapacity in the country. The coal industry continues to face difficulties such as weakening demand, global overcapacity, increasing environmental legislation and falling prices for substitute commodities such as natural gas.

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Electricity Index



Data Source: SEMO

Electricity

In line with falling UK prompt gas prices, Irish wholesale prices dropped month-on-month in spite of increasing spark levels.

Month-on-month the average wholesale price of electricity fell by just over 7.6% in February. The average wholesale price for February was €36.95 compared to €39.99 in January, a fall of €3.05/MWh. This drop was partially offset by an increase in supplier capacity payments bringing the overall drop in electricity to 5%.

In general the wholesale price of electricity can be assessed by examining three components:

- The UK wholesale cost of gas
- The European-wide price of emitting one tonne of carbon
- The clean spark (which is what in general terms a gas powered generator receives in energy payments from the market once the cost of producing a unit of electricity is deducted)

The wholesale cost of imported gas from the UK decreased month-on-month by just over 7.5% in sterling terms. Irish wholesale power prices typically tend to fall with the cost of imported gas as it is the most significant cost in the production of electricity. The cost of emitting one tonne of carbon also fell from €7.02 in January to €5.23 in February.

A monthly clean spark of approximately €8.46/MWh was recorded in the month, which is up from the €7.76/MWh observed in January (an increase of 8.9%). The average spark year-to-date is approximately €8.11/MWh. The increasing spark can be linked to the reduction in wind levels. Demand levels remained steady month-on-month, however wind levels fell. In February, 22.4% of the island of Ireland's demand was met by wind (down almost 4% month-on-month). Less wind on the system results in increased running for coal and gas fired power plants, putting upward pressure on spark levels.

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FX Rates



EURUSD %



EURGBP %



FX Rates

In February, the euro strengthened marginally versus the US dollar and it also gained ground against the British pound.

February proved to be another volatile month for global markets, particularly for developed market equities which ended the month down but off the lows. In the bond market, perceived safe havens rallied for the second consecutive month with US Treasury, UK Gilt and German Bund yields declining. The euro strengthened marginally versus the dollar over the month. However, this small gain disguises the significant volatility that we saw in the pair with the rate reaching a high of almost EUR 1.14 before finishing the month close to EUR 1.09. US economic data was mixed and generally softer in early February although releases improved somewhat later in the month. Q4 GDP was revised higher to 1% from 0.7% annualised due to upward revisions to inventories and net trade. There was no Fed policy meeting in February. The minutes of the January meeting were interpreted as having a dovish slant by the market and the current consensus expectation is that there will only be one US interest rate hike between now and the end of 2017.

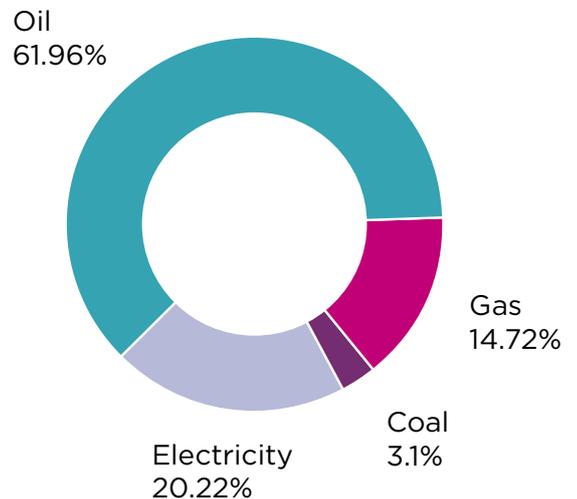
In Europe, political headwinds increased as the UK Prime Minister David Cameron announced a referendum on the country's membership of the European Union (EU) to be held on the 23 June. The pound fell 2.7% versus the euro over the month as polls imply that the vote will be close. 'Brexit' fears intensified as several key cabinet ministers and the mayor of London Boris Johnson, joined the Leave camp. In its February meeting, the Bank of England unanimously agreed to leave policy unchanged from an 8:1 vote previously. Growth and inflation targets were revised lower; inflation forecast to be at 0.9% in 2016, much lower than the 2% target. Market expectations for the first UK interest rate rise have been pushed out further with the first rate rise now expected in 2017.

European data was generally disappointing in February, headline inflation fell -0.2% while core inflation fell to 0.7%. The softer read on inflation has ratcheted up pressure on the European Central Bank (ECB) to unleash another round of monetary policy easing at its meeting on March 10. After the ECB's January meeting, ECB president Mario Draghi assured markets that additional monetary policy action was imminent. The market consensus is that the ECB will increase its asset purchase programme, which currently stands at EUR 60 billion per month, and to cut its deposit rate by a further 20 basis points to -0.5%.



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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