Bord Gáis Energy Index
Understanding energy

January 2018

BGE/EI/UE/0218

Bord Gáis Energy

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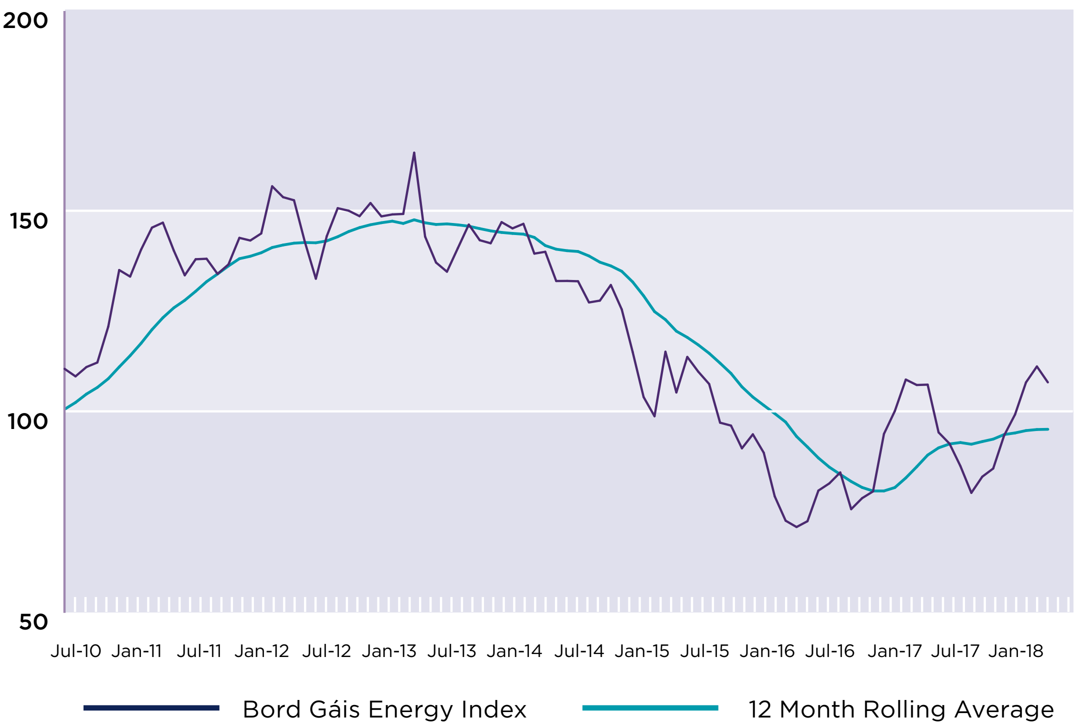
January 2018

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



%	
-4	1 Mth
8	3 Mth
1	12 Mth

Summary

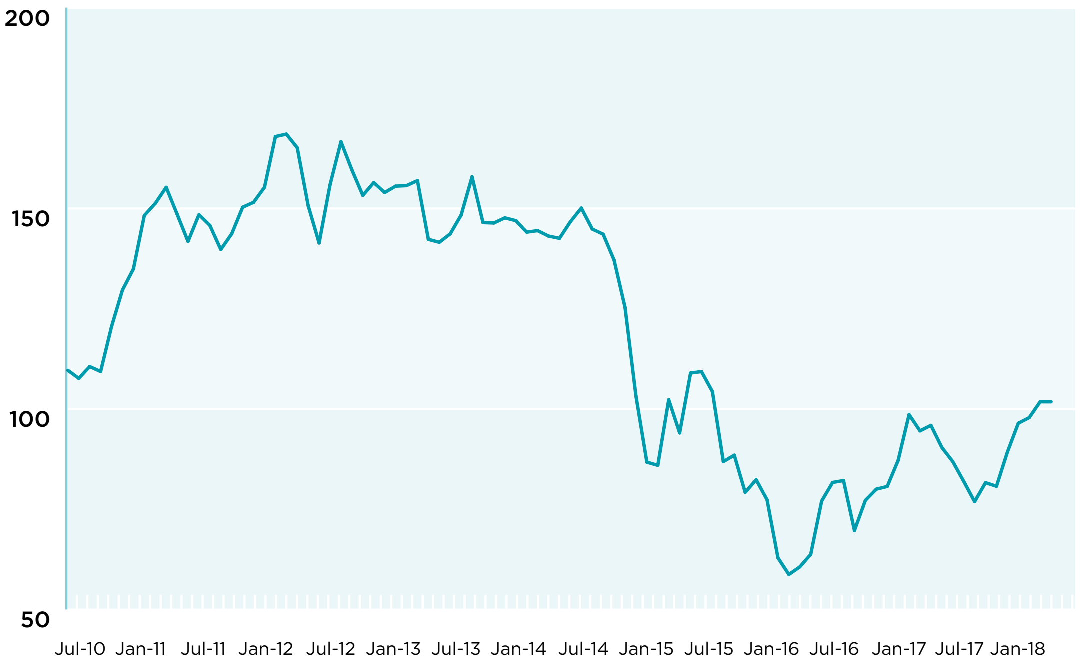
The Bord Gáis Energy Index for January is down 4%. Generally, prices were lower in January with the notable exception of oil prices which moved higher over the month. However, the increases were wiped out for euro-based users as oil is priced in US dollars. The dollar weakened significantly over the month, meaning that prices were flat in euro terms. Among the other constituents of the Energy Index wholesale gas prices fell 10% having rallied strongly in December. This was mainly due to milder than normal temperatures and the return of key gas infrastructure in North Sea. Wholesale electricity prices also fell in line with gas prices and coal also followed suit posting an 8% drop.

In January, the Bord Gáis Energy Index stood at 108 (-4%).

Bord Gáis Energy Index

January 2018

Oil Index



%	
0	1 Mth
6	3 Mth
8	12 Mth

Index adjusted for currency movements.

Data Source: ICE

Oil

Oil began 2018 on a continued bullish trend with Brent crude, the global benchmark, trading as high as $71 dollars per barrel before finishing the month at $69. Overall, prices were flat in euro terms as the weakness of the dollar meant that any gains were negated.

US crude oil production rose to more than 10 million barrels per day (bpd) during January. This is due to the remarkable recovery of shale oil since the depths of the oil price crash in early 2016. The US, along with Saudi Arabia and Russia, is now one of only three countries capable of producing more than 10 million bpd. Bearing that in mind, it is somewhat counterintuitive that oil would be trading close to three-year high prices just as the US is pumping the most oil since 1970.

However, that only tells half the story. Since hitting lows of under $30 dollars early in 2016, oil prices have more than doubled and demand has surged from 96 million bpd to almost 100 million bpd. This is more than double the rate of increase when prices were above $100 per barrel. This has also coincided with a pact by Russia and OPEC to restrict output. The final piece of the puzzle driving prices is the low levels of investment over the last three years.

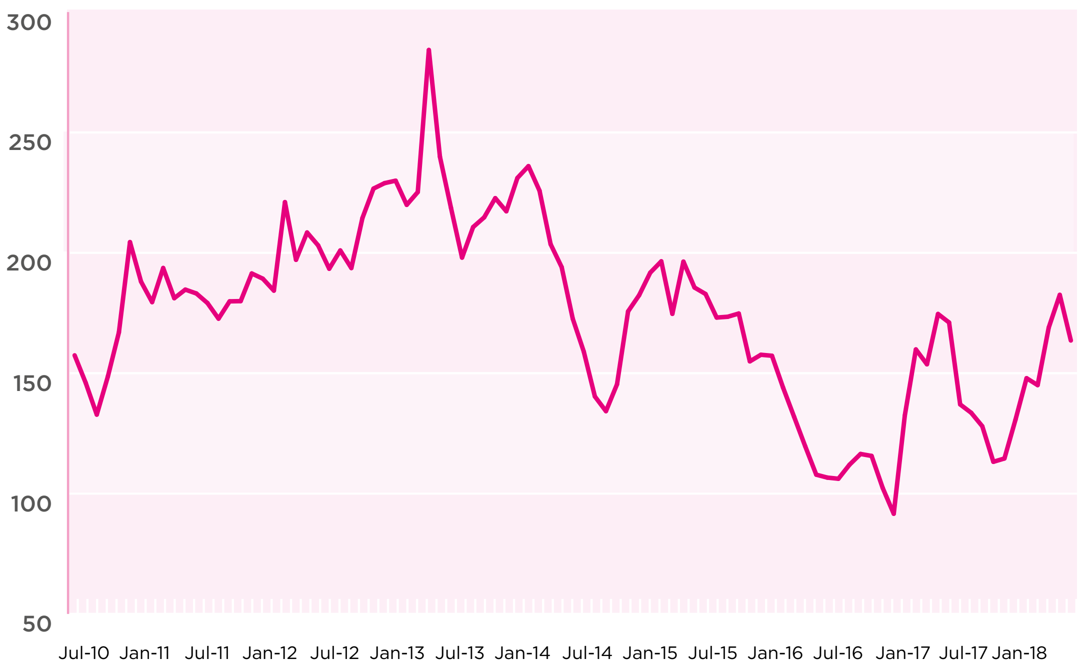
Oil consumption is expected to rise by around 1.7 million bpd this year. US shale production growth is expected to meet around 800k of the demand growth. Older exploration projects, sanctioned during the over $100 a barrel era and which are due to come on stream this year, should satisfy the rest of global demand growth. Should the pace of global demand continue to expand then the market will be more tightly balanced in 2019.

One of the key drivers of future prices is how quickly the US shale producers can expand their production. This is not certain, given that shale production is still a relatively new industry. However, one thing we do know is that those producers have significantly cut their costs since 2014, with some generating more cash now than when crude was above $100 per barrel.

Bord Gáis Energy Index

January 2018

Natural Gas Index



%	
-10	1 Mth
13	3 Mth
-6	12 Mth

Index adjusted for currency movements.

Data Source: Spectron Group

Natural Gas

The NBP day-ahead contract, the price for gas delivered tomorrow, averaged 50.38p/th in January. This was a decrease of over 10%, in euro terms, on the December average of 57.14p/th and 2.3p below the comparable period last year.

Cold weather and outages to key infrastructure supported prices in December. However, in January, prices retreated on milder weather and strong pipeline flows into the UK system. January temperatures averaged over 1.5°c above the seasonal norm resulting in reduced heating demand for gas. In addition, the return of the Forties pipeline system, which brings gas and oil from key North Sea fields into the UK network, saw UK gas domestic production return to normal levels having fallen by as much as 40mcm in the second half of December.

The UK remains more reliant than ever on imported gas supplies given the closure of the Rough facility. This winter we have seen a dearth of LNG supplies into Europe as tankers head east in search of higher priced Asian markets. However, in January, this shortage of LNG was more than offset by very strong pipeline imports from Europe.

Further out the curve, prices also retreated as prompt weakness and the return of supply infrastructure weighed on prices. The Summer '18 contract fell over 3p/th or 8% to 42.18p/th, while the Winter '18 contract settled at 50.91p/th, a drop of 2.18p/th.

There were some concerns around production at Europe's largest gas field, Groningen in the Netherlands. Production at the gas field has been reduced significantly in recent years following increasing seismic activity in the area. It is widely accepted that the increased seismic activity is a result of gas extraction from the Groningen region.

In early January, the largest earthquake since 2012 hit the region, leading to calls for further reductions in gas extraction. The Dutch Economy Minister, Eric Wiebes, stated that gas extraction should be brought down as quickly as possible. The government is expected to announce its plans for reductions in March this year.

Bord Gáis Energy Index

January 2018

Coal Index

%	
-8	1 Mth
-11	3 Mth
-9	12 Mth

Index adjusted for currency movements.

Data Source: ICE

Coal

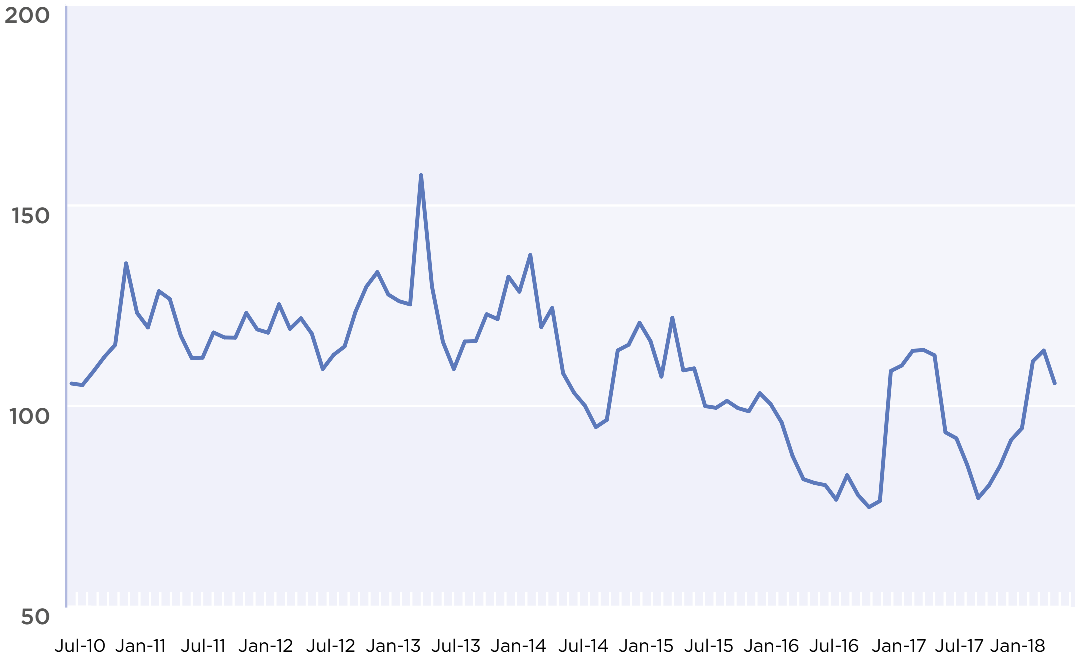
Coal prices fell by 8% in January, in euro terms, to settle at $89.60. Prices retreated despite expectations that China would import almost 21 million tonnes of coal in January, both thermal and coking, which would be an increase from 17 million tonnes in December. There were also reports that Japan, Asia's third largest coal importer, is also ramping up imports. Almost 18 million tonnes is expected to have arrived in January. Exports to Asia are primarily from Australia and Indonesia.

Prices of coal tend to decline on a seasonal basis after January as the cold Asian winter temperatures fade but this is not always the case as in 2016 prices rallied throughout the year. Despite the attempts to phase out coal in Europe on environmental grounds, it is still making up 40 percent of energy consumption in emerging markets. China's ongoing battle against air pollution is likely to result in continued curbs on coal use, and demand for imported coal may suffer as domestic production increases. In 2017, domestic Chinese miners produced 3.45 billion tonnes of coal, a rise of over 3% from 2016.

Bord Gáis Energy Index

January 2018

Electricity Index



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

Data Source: SEMO

Electricity

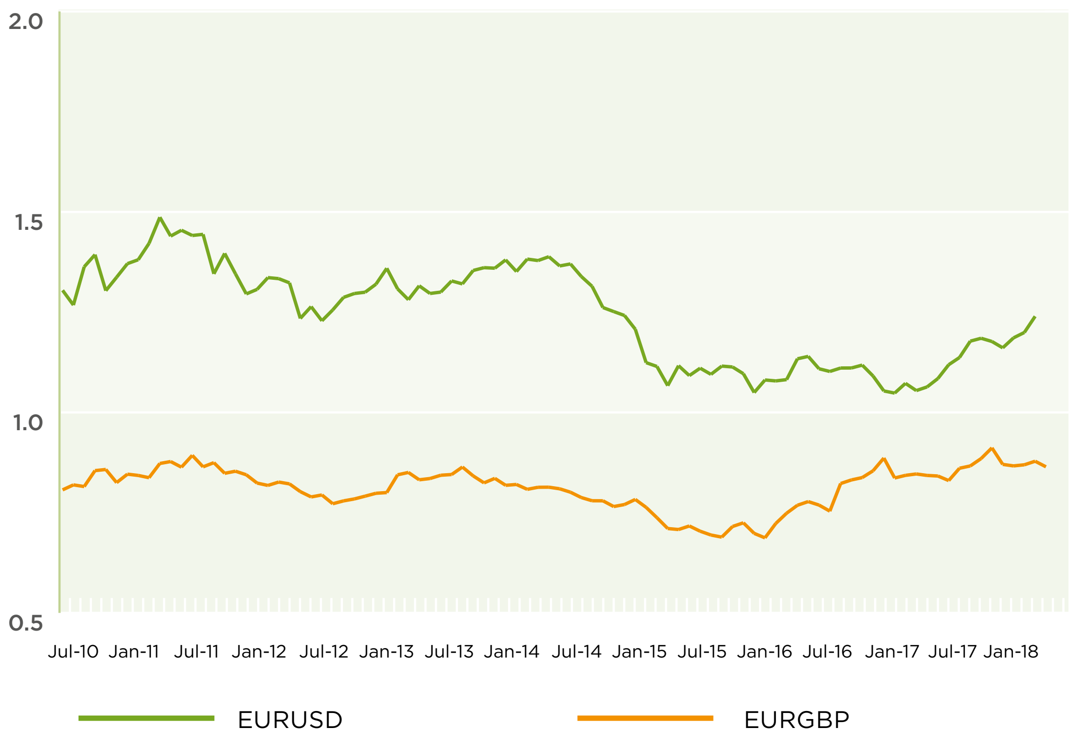
Excluding supplier capacity payments, the average wholesale price for January, was €50.65/MWh compared to 56.88/MWh in December – a decrease of €6.23/MWh. When supplier capacity payments are included, wholesale electricity costs fell by 7% over the month. Wholesale electricity prices typically track the cost of imported gas as it is the most significant cost in the production of electricity. However, this can vary on a month-to-month basis.

The clean spark decreased from €11.88 in November to €8.72 in December. The price of gas was 10% lower over the month, while wind output also increased month on month from an hourly average of 1373GW up to 1863GW – an increase of 36%. The proportion of demand met by wind in January was 43%.

Bord Gáis Energy Index

January 2018

FX Rates



EURUSD %

3 1 Mth

7 3 Mth

15 12 Mth

EURGBP %

-2 1 Mth

0 3 Mth

2 12 Mth

FX Rates

The weak dollar remained the dominant story in foreign exchange markets in January. The single currency finished January at $1.2415 versus the Greenback, a gain of 4 cents over the month!

Despite rising US bond yields and the prospect of a continuing Federal Reserve tightening, the dollar remained under pressure. The market grappled with increasingly harsh trade rhetoric and conflicting dollar policy messages out of the Trump administration. At the January close the dollar Index, which measures the dollar against a basket of currencies, was trading at levels not seen since 2014.

The market has long anticipated normalisation in rates in the United States. However, better than expected economic data out of the euro-zone has seen a shift in market expectations for normalisation of rates sooner than previously expected.

Against sterling, the euro was 1.5% lower closing the month at £0.8753 from December's close of £0.8889 as sterling sentiment was lifted by rising confidence that the UK would achieve a softer Brexit.

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