Energy Index maintains decline on foot of lower wholesale prices but rebound could be starting

The January Bord Gáis Energy Index fell 5% due to lower wholesale oil, gas, coal and electricity prices and in January 2015 the Index reached 99.

US tight oil has had an impact on the world oil market that would have not been imagined even 12 months ago. However, if prices remain at current levels, it is likely that production will decline in 2016. In January, the Brent crude price appears to have hit a floor of around US$50 per barrel and this level is appearing to look like a key psychological support. However with prices rebounding in early February on the news that 90 US oil rigs were idled, the largest number to be wound down in a single day since the mid-1980s, the market appears to be poised to rise on bullish news which suggests that the recent sell-off has found a bottom.

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

"Despite stabilising oil prices, there are serious concerns about the state of the global economy as evidenced by 11 central banks taking the decision to cut rates in recent months and others, such as the US and the UK, appearing to put their rate hikes on hold. China's economic growth continues to disappoint and its debt continues to rise. The combined impact of these factors will continue to be closely monitored by both consumers and producers seeking a sustainable price for energy."

OIL

Brent crude prices closed the month at US$52.99 per barrel and prices stabilised at around US$50 per barrel during the month. Some price rises at the end of the month have continued in early February and some investors may be speculating that the current period of falling Brent prices may have ended.

This speculation arose on the news that US demand for leasing oil rigs was slowing, suggesting that producers might be preparing to cut production. Today American production is almost where it was in 1970 when it reached its high point of 9.6 million barrels per day. By the end of 2014 oil production in the US was 80% higher than it had been in 2008 due to hydraulic fracturing and horizontal drilling.

Growing concern about China's slowing economic performance is raising question marks about global demand growth as Asia has become the primary source of growth. Concerns about the euro zone economy will also be a factor weighing on demand growth expectations.

On the supply side it is expected that the world will produce an extra 2 million barrels per day in 2015 with demand only increasing by 1.25 million barrels per day leading to an increase in surplus oil globally.

Natural gas

Despite an increase in demand of 7% month-on-month, ample supplies meant that prompt prices remained stable with the highest closing price being recorded in January at 49.27p/th despite some cold weather spells.

UK storage levels remained well stocked at 2.77bcm in storage at the end of January according to Gas Infrastructure Europe. 2.77bcm represents about 60% of UK storage and while this is less than this time last year when stocks were over 75% full, it still leaves plenty of gas available for the remainder of the winter period which finishes at the end of March.

Over the month of January, Summer 15 fell 3.59p/th while Winter 15/16 weakened by over 4p/th. Along with softer prompt prices, weak Brent crude prices and a possible reduction in the need to replenish winter stocks over the summer months weighed on forward contract prices.

However, despite the softening in prices, the market will continue to be concerned about developments in Ukraine and the possible effect on prices.

Coal

The ICE Rotterdam Monthly Coal Futures contract closed the month at US$66.75/mt,

With low European coal prices the market appears to be trying to find direction amid several issues that could potentially hinder supply in the Atlantic. Market participants have also pointed to uncertainty over the effects of a Colombian court's ban on night-time coal transport and its potential impact on Colombian exports in 2015.

In addition, South African physical thermal coal prices rose toward the end of the month to over three-week highs on the news that Glencore may idle its South African Optimum mine, potentially taking out about 5 million mt/year from the market.

Based on price behaviour there are no immediate concerns over Russian coal supplies being shipped to Europe. The extent of European coal stocks were revealed toward the end of January when it was reported that combined coal stocks at three delivery terminals in western Europe's Amsterdam-Rotterdam-Antwerp trading hub were around 5.722 million mt, 15.6% higher than the same week last year and the highest since late November.

Electricity

Month-on-month the Irish wholesale electricity price fell from an average of €56.23/MWh in December to €51.91/MWh in January. Weaker UK prompt gas prices in January compared to December were the main reason for softer wholesale Irish electricity prices.

A common feature of the island's electricity system is the volume of electricity produced by the numerous wind turbines which has an influence on wholesale prices. During the month of January wind turbines collectively met a sizeable 22% of demand. High wind volumes typically force more expensive thermal plant off the system and this reduces the revenues to traditional plant which now have to spread fixed costs over a far lower volumetric output, placing further question on their commercial viability in the current market structure.

FX Rates

In the past three months no fewer than 11 central banks have cut interest rates though, similar to the US, the Bank of England does not appear to be in any rush to raise rates anytime soon. The January meeting of the Monetary Policy Committee (MPC) brought no change to interest rates. However, with falling oil prices and reduced inflationary pressure, the entire MPC voted to keep rates at 0.5%. A unanimous vote pushes into the future the much anticipated move toward higher and more normal interest rates that had been gathering momentum in 2014. Expectations of low rates were copper fastened on the news that UK economic output in Q4 came in slightly lower than what was expected by the Bank of England.

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