ADVANTAGE UTILITIES
YOUR COMPETITIVE ADVANTAGE

Quarter 1 - 2021

ENERGY BUDGET OPTIMISATION REPORT

HELPING YOUR BUSINESS ACHIEVE COMPETITIVE ADVANTAGE

CORONAVIRUS RECOVERY

Is there light at the end of the tunnel?

WIDER COMMODITIES

What is driving oil and carbon up?

RECENT PRICE SPIKE

Cold temperatures driving demand.

CARBON NET ZERO

How can your business get ahead?

ENERGY BUDGET OPTIMISATION Q1 2021

Welcome to the Advantage Utilities Energy Budget Optimisation Report Q1, 2021

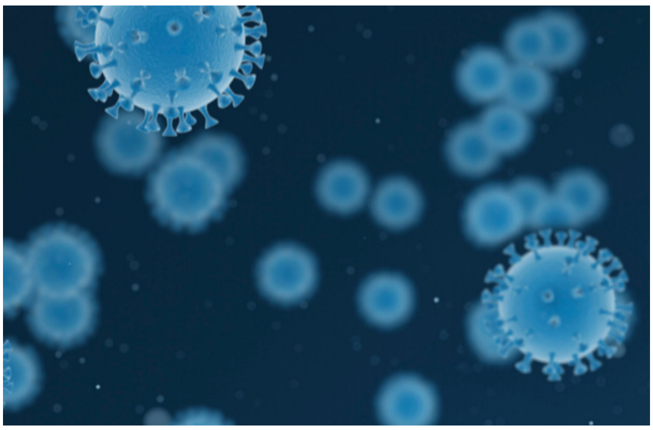
Here we take a detailed look at the current International and UK market drivers. These are the factors that will dictate the trading opportunities in 2021 and ultimately the cost of energy over the next 12 months.

Uncertainty and volatility are always present in the energy market. This means it is important to be informed about what could affect your energy budget as we like to think that more information drives smarter decisions.

ISSUES COVERED IN THIS REPORT:

1. Market Recovery From Coronavirus

What will this mean for markets?



A huge effort is underway in countries all over the world to roll out immunisation. It will likely take a bit of time to fully suppress the virus, but commodity markets have already reacted optimistically and are looking ahead, hoping that things go according to plan. During the fourth quarter of 2020 and the winter period, despite restrictions, we have actually seen demand increase as cold weather with lasting below-seasonal temperatures have driven requirements up by more people using gas and electricity for heating.

Going into the start of winter, the outlook for energy prices were bearish with lacklustre demand due to coronavirus, gas storage at healthy levels and the wider commodity complex struggling to recover. Nevertheless, our analysts did mention in the previous quarterly report that *"a harsh winter could easily see demand increase in the coming months"* and that is exactly what has happened.

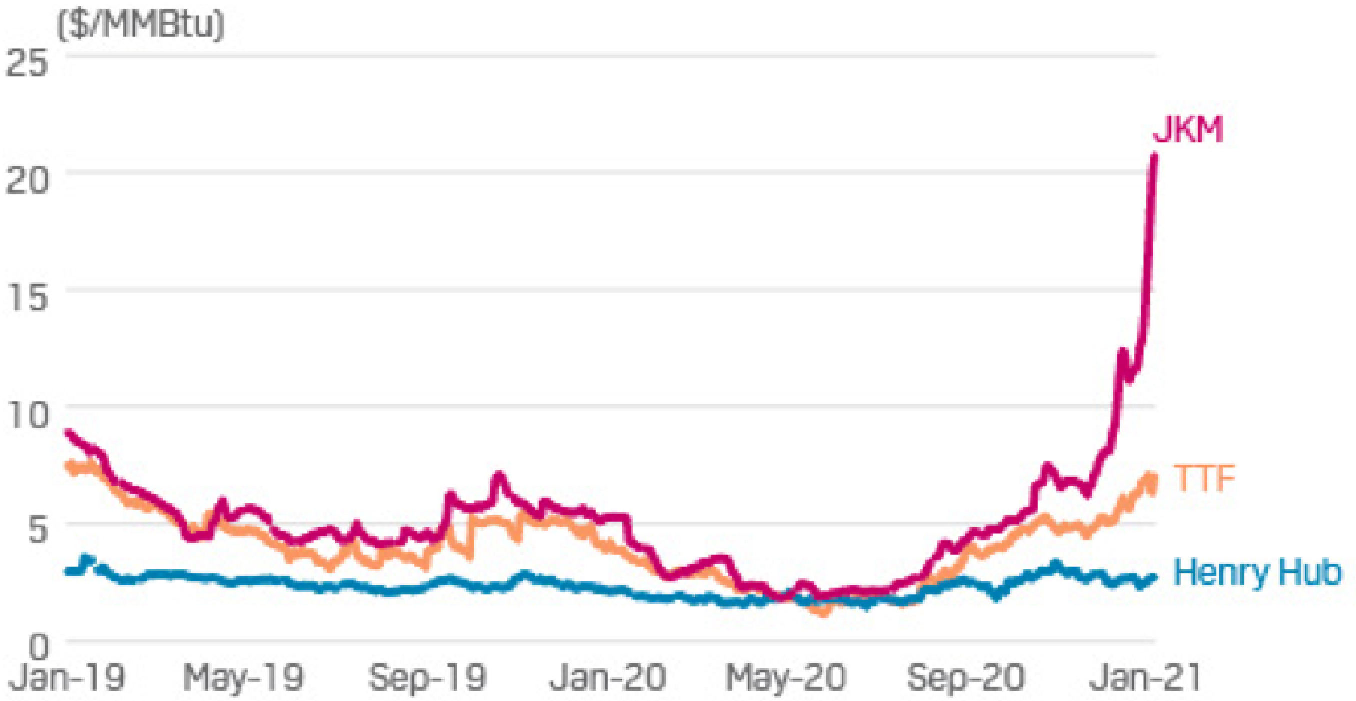
The cold weather has increased demand, which has counteracted the dive caused by lockdown restrictions and caused a spike in energy prices. Of course, with milder temperatures returning in the weeks going forward, we could again see the impact of coronavirus restrictions more prominently on-demand as cases are peaking globally and countries around the world continue to struggle with lockdowns. However, opportunities exist in unpleasant times, and by careful monitoring of energy markets coupled with analysis and forecasting of energy usage, potential gains can be achieved.

2. Recent Price Spike – Asian LNG / cold weather

The low temperatures have not been exclusive to the UK; Northeast Asia has seen freezing temperatures drive demand extremely high and this has caused JKM (Japan Korea Marker, the index for Asian LNG spot prices) to the highest level ever recorded, shooting up from record lows last year. This unprecedented rise in price has seen JKM increase some 1000% since May 2020 and is shown in the graph below.

Beijing recorded its lowest temperature since 1966 as the blast of cold weather drives up demand in China, Japan and South Korea. This vast price increase has been amplified by the fact that there are also supply disruptions in the LNG market with several LNG exporting countries including Australia, Nigeria, Malaysia and Indonesia seeing lower gas exports for this time of year, which has put more reliance on shipments coming from the United States and Russia. Adding to the problems, ships travelling to Asia from the US have been experiencing hold-ups through the Panama Canal with heavy congestion, some reports suggesting vessels are having to wait as long as seven days to get through the waterway, further inflating freight costs.

Global Gas Prices Dislocate: JKM Prices Sky-Rocket

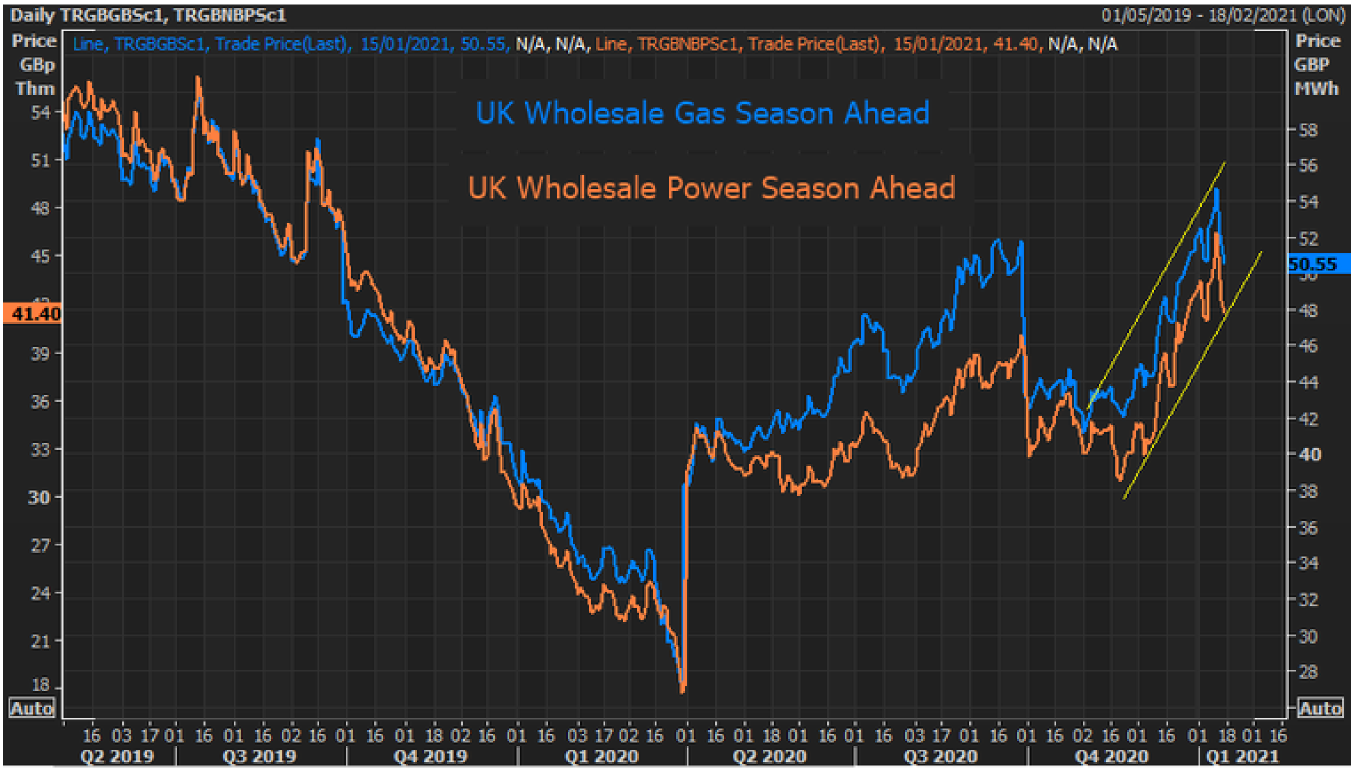


Source: S&P Global Platts

This spike in Asian demand has had a knock-on effect on gas prices in Europe and the UK as the higher premiums in Asia draw LNG shipments away from our continent in search of higher profits. This has meant fewer ships arriving on UK shores at a time when temperatures were already below the average for this time of year. Qatar was the biggest supplier of LNG to the UK in 2020, but cargoes from the middle eastern country are now being attracted by higher prices in Asia and this has meant that domestic gas storage has had to fill the shortfall, as well as less frequent LNG shipments from the US and Russia.

Wind levels have also dropped off in recent weeks putting more pressure on the power stack to use natural gas burn to generate electricity, as well as coal, with the latter now regularly making up the shortfall, having been virtually non-existent in the power stack last summer. Both supply constraints in the LNG market, as well as demand increases due to cold weather and lower renewables coupled together, have driven gas and power prices higher as illustrated by the yellow lines in the graph below. The graph also shows that energy prices are still below what they were before the pandemic started so we haven't seen a full recovery just yet and prices could still fall before this pandemic is controlled as things get worse before they get better.

UK Wholesale Gas & Power Prices: April 2019 – Current



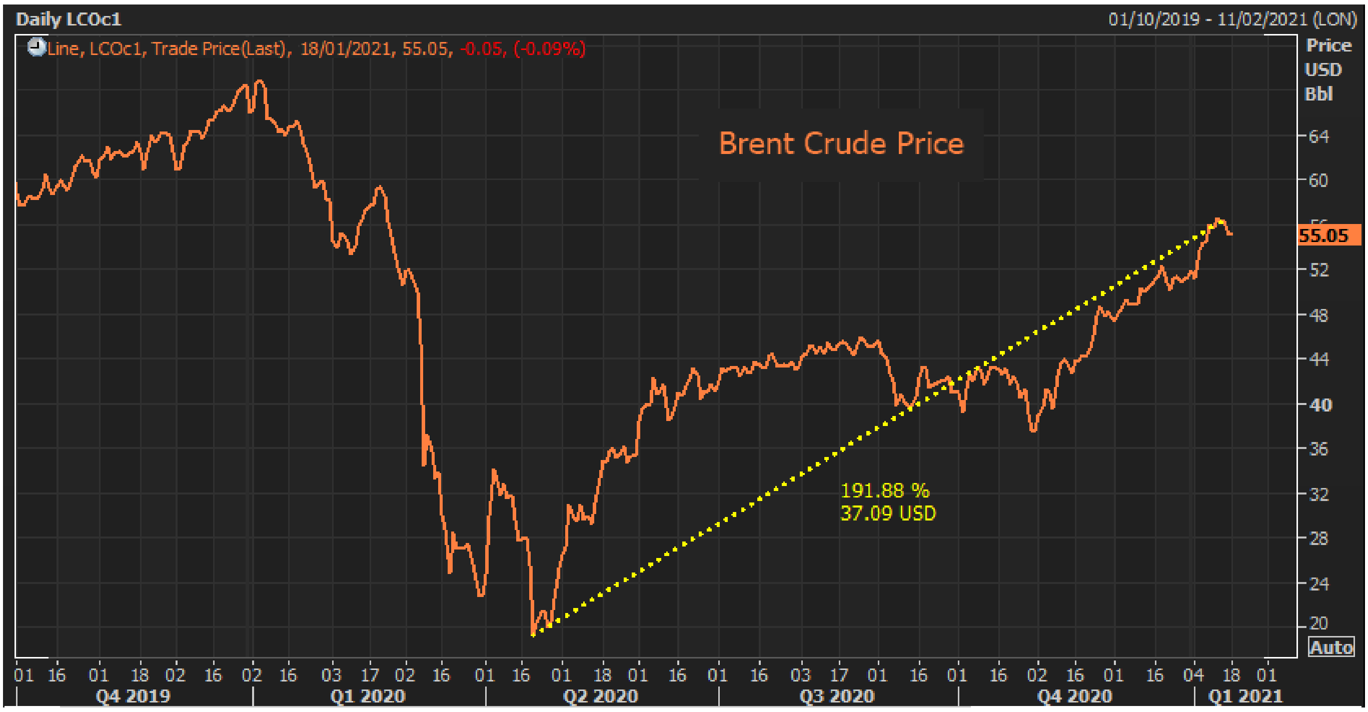
*Source: Reuters

Medium range gas storage in the UK has dipped below levels seen in the previous five years for the same time of year in order to deal with the increase in demand. Since the Rough gas storage facility, that had made up 70% of the UK's storage capacity, shut its doors in 2017, we have been used to abundant LNG arrivals to cope with periods of high demand particularly during winter.

Now that LNG arrivals are few and far between and a supply glut not expected anytime soon, gas storage plays a crucial role in filling the gap and to keep supply meeting demand. As it stands, most predictions point towards milder temperatures returning, which would ease the pressure on gas storage and, should supply disruptions also disappear with more projects going back online, we could well see a retracement in energy prices. Considering that as a result of coronavirus demand is not likely to fully recover until later in the year, once milder weather makes a comeback, we could see demand drop once again. As always, however, this is not a forgone conclusion and further cold spells coupled with continued supply issues could bring more volatility with gas storage levels dropping significantly.

3. Wider Commodity Markets: Oil Recovery & Carbon All-Time High

Brent Crude Price: October 2019 – Current

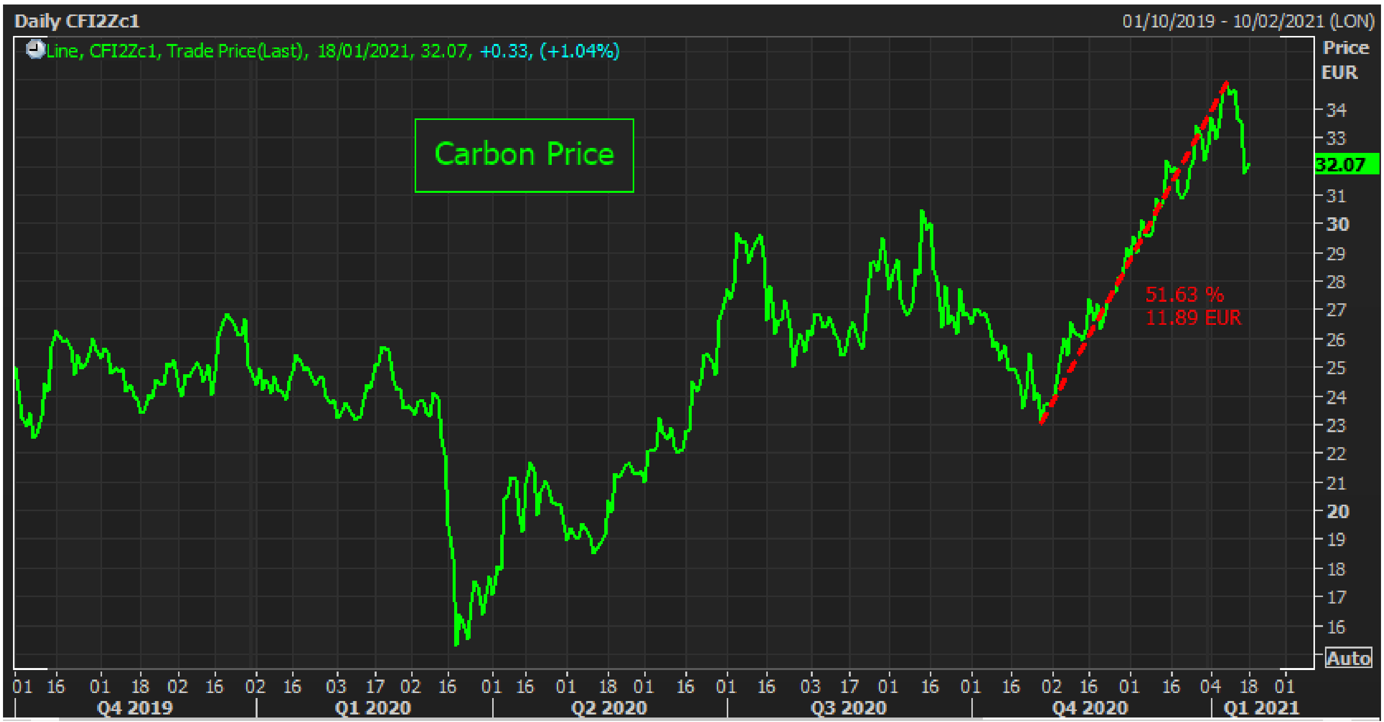


*Source: Reuters

The wider commodity complex has also seen notable gains of late, which has provided volatility to the far curve energy contracts and helped drive price. Since June, up until the middle of November last year, oil prices were trading rangebound with little turbulence as shown by the Brent Crude graph above. But since November, we can see that volatility has returned and an upward move in price has broken through the $46 barrier. This uptick is in part thanks to the promising coronavirus vaccine news and the hopes that global demand will start returning to normal as infection numbers reduce and the pandemic is better controlled. However, perhaps the biggest factor driving oil price recently was the highly anticipated OPEC+ meeting where oil-producing nations reviewed global output cuts to deal with the demand lulls seen globally as a result of Covid-19 restrictions. Although the meeting did not go particularly well, Saudi Arabia unexpectedly volunteered to reduce their output by 1,000,000bpd, allowing Russia to increase production by 100,000bpd, whilst the net global supply is further reduced. This curtailment on supply has supported prices and ensured that we don't see supply outstrip demand as we saw back in April of last year. In addition to this, political events of late have provided some stability to markets. In the UK, a Brexit deal was finally reached and is now done and dusted, we hope.

In the US, Joe Biden won the presidential race with vows to re-enter the Paris climate change agreement and plans to revisit the Iranian nuclear deal, whilst more recently the Democrats won control of the Senate after election wins in the state of Georgia, granting them legislative power. This has removed some of the lingering political uncertainty and helped support prices. As the graph above shows, although prices have increased recently, they are still below pre-pandemic levels and we could see further volatility in the coming months as we all search for a ‘new normal’.

Carbon Price: October 2019 – Current.



*Source: Reuters

The European carbon market has had a volatile last twelve months or so with the coronavirus pandemic causing prices to tumble in March, whilst reaching all-time highs in recent weeks. The latest spike should be attributed to short-term market volatility with a delay in January carbon permit auctions causing a shortage in supply. But there has also been plenty of other support for the carbon price with the European Union putting into law their new carbon target of cutting 55% of emissions by 2030, causing fewer permits set to be available in the coming years. The cold weather and increased usage of fossil fuels including coal have recently added to the short-term volatility.

France has faced nuclear power plant outages, Germany has been ramping up coal burn and the UK sees increased coal usage to generate power to make up for reduced natural gas and wind. Furthermore, now that the Brexit transition period has ended, the UK is likely to have its own carbon pricing mechanism as it moves away from the European index. Details on how the new system will work are sparse and very much up in the air - providing some uncertainty. Despite these record highs, it seems as this is just short-term turbulence and we can already see prices starting to reverse some of the gains made. Fundamentals such as milder temperatures returning alongside reduced demand from lockdown restrictions in Spain, Germany, Italy etc., should see prices retract and settle lower.

4. Carbon Net Zero: Government Energy White Paper

Last year, the UK became the first major economy to pass net-zero emissions legislation requiring all greenhouse gas emissions to be net-zero by 2050. This was obviously a huge step in the right direction and now that the government have released the Energy White Paper, there are more details on how this can be achieved and what policy will drive us towards this target. The paper plans for more nuclear power generation in the UK electricity mix, with one large scale nuclear project planned before 2024 in addition to the Hinkley Point C project which is already under construction. Of course, more emphasis is put on increasing renewable energy projects, with a target of 40gw offshore wind power by 2030, up from current levels of 10gw. The government have also pledged to phase out diesel and petrol-only vehicles by 2030 with hybrid vehicles being phased out five years later by 2035. On top of this, £1.3 billion has been put aside for electric vehicle recharging infrastructure to ensure a smooth transition.

Now that the plan is in place and the government have made clear what the targets are, it's time for everyone to get on board and do their bit to make sure we achieve them. Although we are in a very difficult economic period, the government has committed huge investment to ensure the targets are met, but for the UK to succeed, all businesses will have to adapt and work towards the common goal. There are many ways your business's carbon footprint can be reduced, including securing green energy contracts, as well as installing electric vehicle charging points, solar, combined heat and power units (CHP) and LED lighting, all of which make long term financial sense on top of lowering emissions and getting closer to carbon net-zero. The push towards net-zero is not going away and we will all have to do our bit sooner or later, so if you want to get ahead of the curve and future proof your business, get in touch with our team and find out how we can help.

5. SUMMARY

WHAT COULD THIS MEAN FOR YOUR BUSINESS?

Despite the Covid-19 pandemic continuing to dominate the state of affairs at the start of 2021, energy prices have spiked recently with short term volatility returning to markets. Prices haven't sunk to significant lows as cold temperatures and a bleak supply picture has diminished the effect of lockdown restrictions. Now that warmer weather is expected going forward and some of the short term drivers start to have less of an impact, the current situation points towards a bearish outlook for the next couple of months. In particular, reduced demand as a result of lockdowns is likely to continue to spoil demand before the vaccination programme is completed and things start to return to some form of normality. Although prices have seen an uptick recently, they are still below pre-pandemic levels and it wouldn't be ill-advised to start thinking about renewing energy contracts at the moment as prices start to come off. However, despite the current picture being bearish, more cold spells and any unexpected supply disruptions could cause short term volatility and could see prices rise once again.

As Carbon Net-Zero and reducing carbon emissions gains more mainstream media attention and becomes an integral part of business going forward in the UK, now is the time to start familiarising yourself with some of the changes we will all have to make as individual businesses. The earlier you identify and act upon reducing your emissions, the easier it will be in the long run whilst also saving your business money at the same time.

BULLISH

- U.S Stimulus Package
- OPEC
- Vaccine Hopes/Success
- LNG Restrictions
- Unforeseen Cold Snaps
- Carbon

RANGEBOUND

- Oil
- Weather
- Coal

BEARISH

- COVID-19 infections
- Lockdowns & Restrictions
- Supply/Demand Scenario
- Return to pre-spike LNG arrivals

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Should you have any questions or queries regarding energy contracts, renewable energy products and services, energy management or water, waste and telecoms then please do not hesitate to contact your account manager or a member of our team on 0207 371 5360.

We wish all of our clients and prospects a healthy and speedy return to normality during this difficult time, and rest assured we are here to serve your accounts with business as usual.

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ABOUT US:

Advantage Utilities is the consultative partner that considers every technology and finance option to help its clients achieve their goals. Backed by our simple motto – Procure, Reduce, Manage – Advantage Utilities is a one-stop shop that helps businesses to achieve their sustainable energy ambitions while adding value, reducing costs and meeting legislative compliance.

Advantage Utilities champions a consultative, customer-centric approach. We get to know our clients inside out - their needs, priorities and goals, so that we can develop, implement and manage a tailored solution to match.

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