

Market Update: Oil & Gas – February 2015

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Oil markets – monthly round up

Volatility remained the watchword in the oil markets as the ICE Brent contract registered a seventh consecutive monthly fall in January, slumping to a low of United States Dollars (USD) 46.40/barrel, before rallying to a 5-week high in early February, fetching US\$60.08/b. The NYMEX WTI contract tracked a similar path, hitting a low of US\$43.58/b – before changing hands at US\$54.24/b in the first week of February.

Oil fundamentals, and the long-term health of the industry, remained hot topics throughout January and early February. Significant builds in US crude oil stocks were seemingly offset by a sharp fall in the numbers of US rigs, and cuts to capital expenditure among major oil players, raising the possibility of non-OPEC supplies falling in the medium- to long-term. For now, oil benchmarks continue to sit firm within the US\$40-65/b range.

Storage play

The contango structure on the ICE Brent and NYMEX WTI forward curves continued to entice barrels into storage facilities in January. Data released by the Energy Information Administration (EIA) reveals that US crude oil stocks

hit 413.06 million barrels (m/b) – an 80-year high for this time of year. At these levels, US inventories are the equivalent of 45-days' worth of domestic oil production.

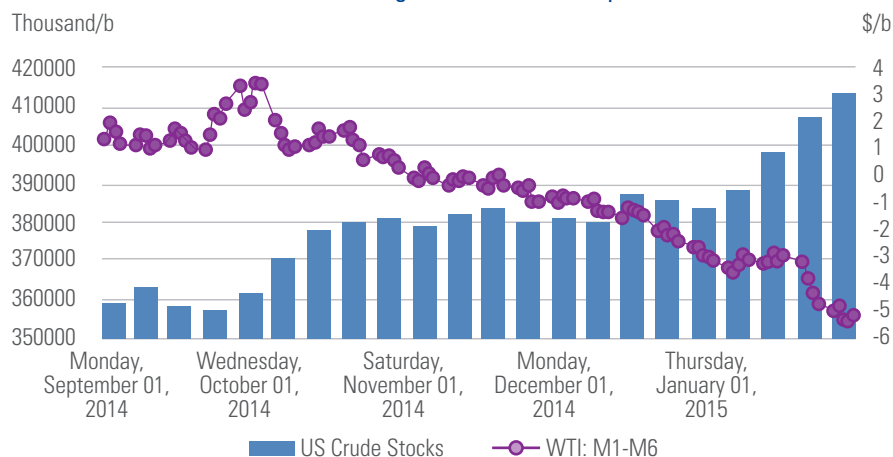
The EIA stocks data indicates that the cash-and-carry trading strategy

continues to offer a home for barrels in the short-term. The entrenched contango in the WTI market, combined with ample storage capacity at strategic locations (e.g. Cushing, Oklahoma, which is approximately 50 percent unutilized), suggests that US stocks could see further builds in the coming weeks.

Price at the pump

The short-term rally in crude oil futures was sufficient to buck an 18-week trend of falling US gasoline retail prices – the longest such slide for 15 years. However, the EIA predicts that this drop is unlikely to stoke any significant increase in end user gasoline demand. A recent EIA study reveals that the short-term price elasticity for motor gasoline is estimated to be in the range of -0.02 to -0.04. Therefore a 25-50 percent decrease in gasoline prices would raise gasoline consumption by just 1 percent.

US crude storage vs. M1-M6 WTI spread



Data source: EIA

Contacts

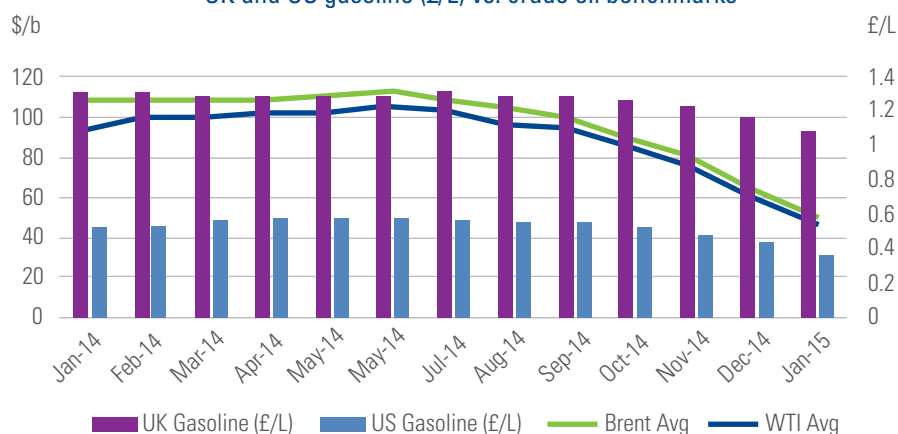
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UK and US gasoline (£/L) vs. crude oil benchmarks



Data sources: AA, EIA, ICE, NYMEX

According to data compiled by the AA, US Gasoline pump prices have fallen 36 percent since June 2014. In the UK, meanwhile, prices have been less responsive, declining by just 16.5 percent. The UK gasoline market, however, is less responsive to big swings in the price of oil, as a significant portion of the pump price is comprised of duties and tax. The drop in crude oil prices has seen this contribution increase further, with approximately 70 percent of the per-liter price made up of tax and duties, a 6-year high. (Source: RAC)

Supply side headlines

- US crude stockpiles rose by 6.3 million barrels to 413.1 million in the last week of January – the highest since the EIA started keeping records in August 1982. (Source: EIA)
- The IEA has lowered its Russian oil output projections, as the crisis over Ukraine and resulting sanctions limit Russia's access to capital and technology. (Source: IEA)

- OPEC's oil supply increase is a result of larger Angolan exports and steady-to-higher output in Saudi Arabia and other Gulf producers. (Source: Bloomberg)
- Global oil inventories increased by almost 0.8 million barrels per day (bbl/d) in 2014, the largest build since 2008. (Source: EIA)
- In 2015, non-OPEC oil supply is projected to grow by 1.28 million barrels per day (mb/d), representing a downward revision of 80,000 barrels per day (tb/d). (Source: OPEC)

Demand side headlines

- Storage companies in China are set to boost commercial oil tank capacity by more than 10 percent this year. (Source: American Journal of Transportation (AJOT))
- Energy consumption by one of the largest consumers of the world, the US government, fell to 0.96 quadrillion British Thermal Units (Btu) in financial year (FY) 2013 – the lowest level since 1975. (Source: EIA)
- Macroeconomic weakness continues to restrain global oil demand growth, with 4Q14 deliveries estimated at just 0.6 million mb/d above previous year's levels. (Source: IEA)
- Global refinery crude throughputs surged to a new record high of 78.9 mb/d in December, lifting the 4Q14 estimate to 78.2 mb/d. (Source: IEA)

Analyst estimates – Oil

Price forecasts taken throughout January show downside revisions across the board. OPEC's firm stance on production, lackluster demand growth and a strengthening US dollar were key factors behind the downward revisions, with many anticipating a U-shaped oil price recovery.

Brent	2015*	2016**	2017***
December average	75.9	82.1	87.8
January average	68.1	75.9	82.3
December median	73.3	83.0	90.0
January median	69.9	75.0	80.0

*20 estimates ** 15 estimates *** 11 estimates

Source: Based on a poll of 20 external energy market analysts

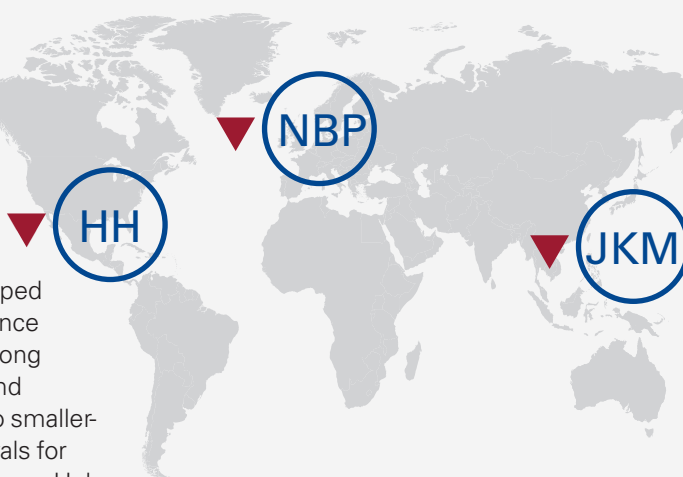


Gas markets – Monthly round up

Industry benchmarks

US

Natural gas prices dropped to their lowest levels since September 2012 on strong domestic production and inventory builds, due to smaller-than-average withdrawals for this time of year. The Henry Hub spot price averaged US\$2.99/million Btu (MMBtu) for January. (Source: EIA)



UK

Low temperatures and a series of unplanned outages in the Norwegian shelf were insufficient to stem the recent price slide in the UK gas market. The front month National Balancing Point (NBP) contract averaged 46.23p/th, for the month of January, a 14.6 percent month-on-month fall. (Source: ICE)

JAPAN

The Platts' Japan Korea Marker (JKM) LNG spot price assessment slumped to a 4-year low averaging US\$9.91/MMBtu for February delivery, a 47.3 percent year-on-year fall. Limited end-user demand, high inventories and fuel-switching were factors driving a depressed price environment not seen since before the Fukushima nuclear disaster. (Source: Platts)

Analyst estimates – Gas

Henry Hub price forecasts were moved lower by analysts in January on robust production growth in the US. Analysts predict a demand-supply imbalance over the long term under normal weather condition scenarios.

Henry Hub	2015*	2016**	2017***
December average	3.9	4.2	4.3
January average	3.7	4.1	4.4
December median	3.9	4.2	4.3
January median	3.8	4.0	4.3

*17 estimates ** 14 estimates *** 6 estimates

Source: Based on a poll of 17 external energy market analysts



A global insight

After months of successive falls, oil price benchmarks have staged a brief rally, trading at levels above the psychological support price of US\$50/b. Our global industry experts give their views on the market.

Oil: Oil supply



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"In the last few weeks we've seen significant cuts to exploration and production budgets among some of the big oil and gas players. This will undoubtedly have an impact on long-term oil supply. However, in the immediate term, the market remains over-supplied with little evidence of production abating anytime soon. The contango structure will add further pressure to the supply overhang as traders seek to hoard inventory both inland and at sea."

Oil: Storage Play



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"With more capital than attractive deals available, traders are looking to take advantage of the forward curve. Those with storage will look to lock in the most attractive storage play since 2008. Those without are looking at the trade-off between available storage prices, contango, and return-on capital hurdle rates. With low funding rates in place, there is a strong chance that the storage trade will take barrels out of the market and alleviate some of the supply-demand imbalance that has depressed global oil prices these past few months."

Oil: Asian Market Dynamics



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"An oil price below \$50/bbl inevitably leads to demand creation, particularly within the energy-hungry markets of Asia. In combination with a global crude oil supply glut – stimulated by the unconventional boom in North America – an environment has formed that perpetuates sharp volatility in oil prices. Price fluctuation is specifically acute in developing product markets, such as LNG; a trend that will be embraced by traders with strong risk appetites."

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