PACE COMMS

Energy Pricing Report

16th July 2020

Energy bills are driven by both the price of energy on the wholesale market and Third-Party Costs (TPCs). TPCs include non-energy costs set by the government, network (the National Grid), policy and system costs and electricity transmission/distribution costs.

The biggest single cost on a bill is the price of the energy. The wholesale cost of the energy makes up approximately 40% of an electricity bill and 70% of a gas bill, with the remaining being TPCs, which have been continuously rising in recent years and can be volatile.

This pricing report focusses on the energy element of a bill to help you keep track and understand the wholesale energy market and the factors affecting the price of your contracts.

Overview:

Signs that demand is rising has led to OPEC members to look at their next move since imposing supply cuts in April. It is expected that the historic cuts will start to unwind and increase production by 2 million barrels a day.

British Gas also released their quarterly report, which highlights how even though the wholesale price of energy has decreased because of the coronavirus, the Non-Commodity/Third Party costs have increased (especially for electricity) which is pushing contract prices up.

Wholesale prices are still low in comparison to pre-coronavirus levels but are not likely to get lower now unless there is a second outbreak. Switching now is likely to be the best chance at locking in a low rate as demand continues to increase with more businesses returning to work, contract prices will follow suit and become more expensive.

Bullish Factors (*upward pressure*):

- OPEC and its allies expected to look at increasing their crude output.
- Global demand for oil continuing to rise, stabilising the markets and contract prices.

Bearish Factors *(downwards pressure):*

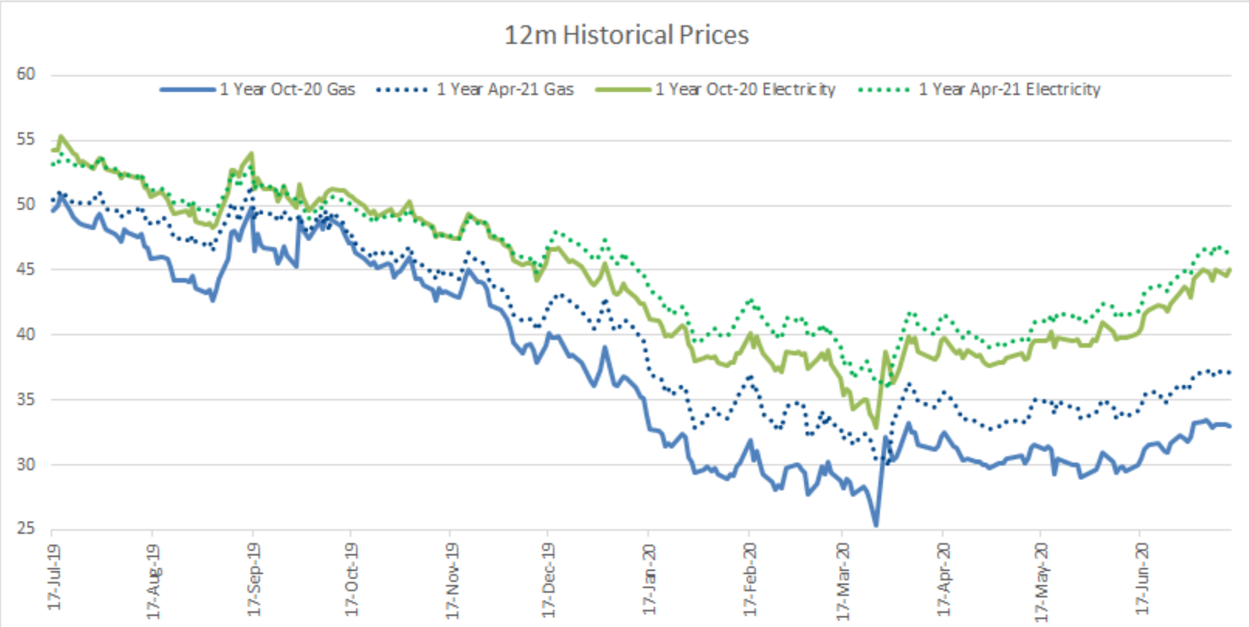
- The fear of a second wave in winter that could be worse than the first.
- Expected delivery of gas with a near-full storage inventory.

MARKET REPORT

Gas and Power

Gas contracts dipped slightly this morning as storage inventories are near full and there is another delivery of gas (LNG) expected in the UK next week.

Overall, gas and electricity contracts have gained value when compared to last week. This is supported by an expected fall in renewable generation for gas and electricity, resulting in more reliance on oil. As trading within the oil markets has remained strong, this is supporting the increase in contract prices further.

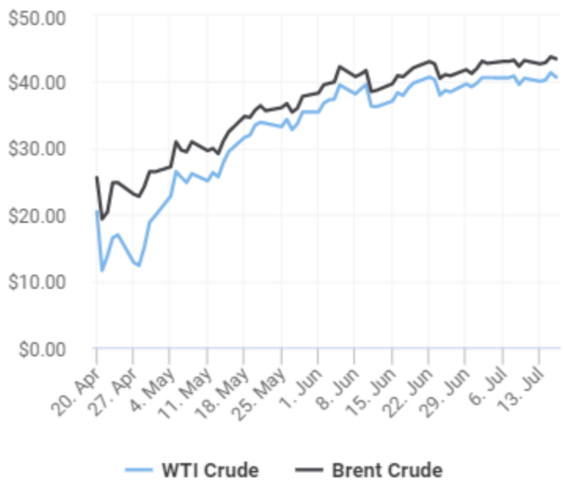


Crude

Increased confidence that OPEC members and its allies would not agree to extend the production cuts and look at increasing the output by 2 million barrels a day will keep contract prices steady.

Brent has not returned to pre-pandemic levels, where it reached $68.91/bbl in trade price in January. However, it has been trading steadily for the past month and still has not dropped below $40/bbl in trade price since the start of June, which is a huge recovery since it plummeted to $20.37/bbl on April 22nd, the lowest point in 18 years.

Current price standings:
Brent Crude = **$43.54/bbl**
WTI Crude = **$40.83/bbl**



ENERGY NEWS

Growing Energy Demand

The world's leading oil producers (OPEC and its allies, known as OPEC+) are expected to announce an increase in output, amid signs that demand is rising.

As of 2018, OPEC members accounted for an estimated 44% of global oil production, thus giving them a major influence on global oil prices. Oil prices took a plunge, reaching 18-year lows, as the pandemic crippled the global demand for oil and countries came to a halt. Due to this, historical supply cuts were imposed by OPEC and its allies in April to help ease the effects of an oil glut and stabilise prices.

Expectations are growing that from next month the cuts will be reduced, meaning that output will increase by 2 million barrels a day. The challenge for OPEC is that while they don't want to cede market share to other producers bringing production back, if they ease the cuts, they risk pushing oil prices down. Other analysts believe that because the market is technically seeing a supply deficit, there is room for the group to ease. Currently, the expectation of increasing the daily output is supporting oil prices, which is keeping contract prices higher.

As demand continues to grow, it will start to increase contract prices even more. The more optimistic outlook comes after the International Energy Agency (IEA) last week suggested that the worst of the impact caused by coronavirus lockdowns may now be over and predicted a slight improvement in global demand for crude oil this year. However, they also cautioned that much still depends on how the pandemic develops.

"Winter Wave"

A report requested by the UK's chief scientific adviser, Sir Patrick Vallance, stresses there is still a high degree of uncertainty over how the coronavirus pandemic will play out this winter. Research suggests the virus can survive longer in colder conditions and is more likely to spread when people spend more time indoors.

Experts are concerned the NHS will be under extreme pressure, not just from a resurgence of coronavirus but also from seasonal flu and a backlog of regular, non-coronavirus workload.

Keeping infection rates low as Britain emerges from lockdown will be critical in controlling the disease. So the fear of a second wave happening will continue to weigh on markets and contract prices, as the virus has not gone away and we do not have a vaccine for it yet.

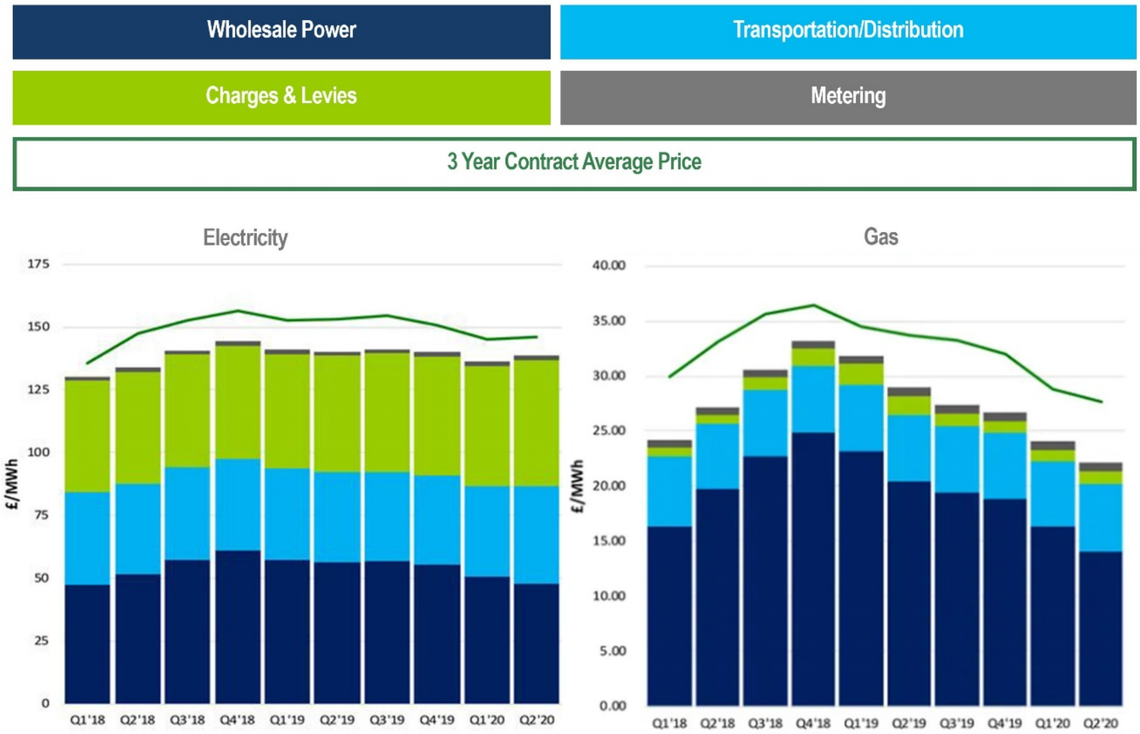
Rise of Non-Commodity/Third Party Costs

British Gas released their quarterly report, with an update of exactly what goes into the prices suppliers charge. During the second quarter of 2020 the UK economy experienced the full impact of the coronavirus lockdown. In the energy market, the lockdown has resulted in a significant decline in energy demand and a fall in wholesale prices. These two effects combined with an increase in renewable generation has forced the Electricity System Operator (ESO), National Grid ESO, to take more actions to keep the system stable at additional cost. Since these costs are shared with industry participants based on consumption, lower demand has resulted in a smaller charging base and in turn a higher balancing charge.

With non-energy costs accounting for around 62% and 32% of businesses' electricity and gas bills respectively, these rising costs are pushing energy prices upwards, particularly electricity prices. Gas demand has been less severely impacted than electricity and with storage at its highest levels since 2017, both wholesale and retail prices remain subdued.

Several measures have been put in place to soften the impact of this sharp rise in non-energy costs on customers' bills. However, the combination of all the costs together means the increase will be felt by many.

As we enter the second half of the year, there are encouraging signs that economic activity is gradually starting to recover. Higher electricity consumption is likely to stabilise some of the more volatile charges such as BSUoS (Balancing Services Use of System) and RO (Renewables Obligation).



As you can see from the charts, business energy prices for both electricity and gas have been falling since the end of last summer, reflecting a general decline in wholesale or commodity prices (dark blue area on chart).

This decline in energy prices accelerated during the coronavirus lockdown. However, by the end of the quarter, electricity prices have started to rise again driven by the impact of Non-Commodity/Third Party costs (see above) as well as rising wholesale prices.

Pace Comms Ltd

5 Castle Court
The Cartway
Bridgnorth
WV16 4BG, UK

info@pace-comms.co.uk

01384 898260