Blake Baxter

Subject: FW: MEP Weekly Gas Update 10-13-2016
Attachments: MEP Gas Storage Chart 2016 10 13.pdf; NG Price Curve 2016 10 13.pdf

From: Blake Baxter
Sent: Thursday, October 13, 2016 5:00 PM
Subject: MEP Weekly Gas Update 10-13-2016

Natural gas is currently trading at $3.341 per Dth

Despite a few minor setbacks the bull rally in natural gas continued again this week. It made a significant move upward last Friday after Thursday's bearish storage report and then after a pause of a few days made another jump today after what would have to be considered a bullish storage report was published. And here you probably thought that all of the excitement of late was limited to U.S. Presidential politics.

The bullish story goes something like this: Winter is Coming (I guess they are all fans of The Game of Thrones). Sorry, yes, the narrative is that winter is coming and that it is going to be colder than last year. This is a rather low bar considering how warm the U.S. was last winter. Some speculators are saying that it will in fact be colder than normal. However, so far I have not seen any forecasting to support that view. It is forecasted that the upper plains will be colder than normal, but then hardly anyone lives there so the HDD impact on consumption would be minimal in that case. The northeast is forecasted as more "stormy", but not colder.

The bulls are also proclaiming that gas is king. This narrative runs down the path that says that we have retired a lot of coal generation and that utilities will burn gas even at a premium price. However, I view this as a weak argument at best because they never mention that we still have 300 GigaWatts of coal generation in the electric generation stack. We saw this past summer that when gas prices pressed $3 /Dth, that MISO put more coal into the stack. Moreover, not only are gas prices making coal more economic, but the utilities are sitting on bigger stocks of coal. The utilities should be looking for an opportunity to shed some of that inventory and recover their coal expense. And the thing about coal units is that once they are online and purring you do everything in your power to keep them that way.

Coal stocks and average number of days of burn for non-lignite coal by region (electric power sector)

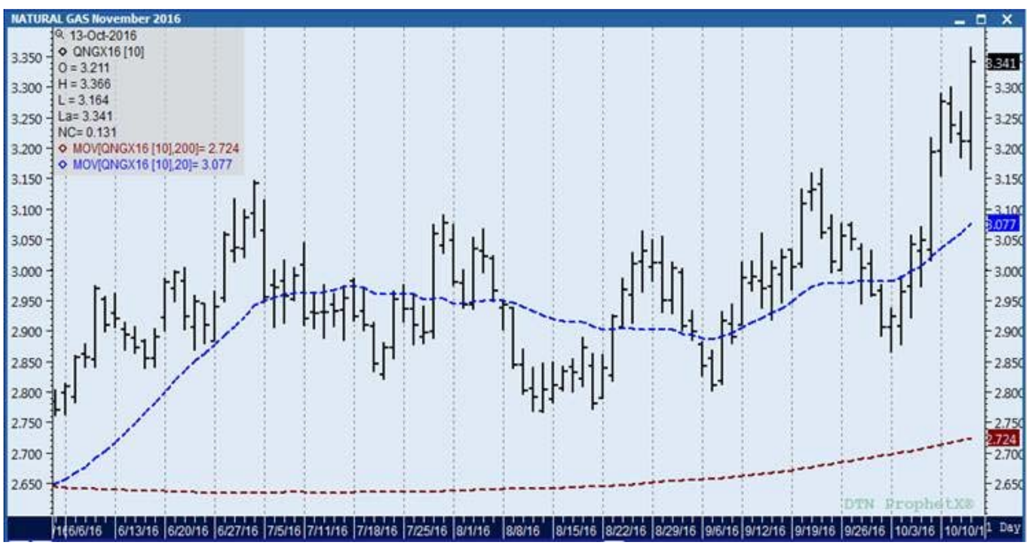
		July 2016		July 2015			June 2016		
Zone	Coal	Stocks (1000 tons)	Days of Burn	Stocks (1000 tons)	Days of Burn	% Change of Stocks	Stocks (1000 tons)	Days of Burn	% Change of Stocks
Northeast	Bituminous	6,320	115	6,735	112	-6.2%	7,043	119	-10.3%
	Subbituminous	163	134	762	217	-78.6%	171	157	-4.7%
South	Bituminous	30,996	81	30,364	72	2.1%	35,292	82	-12.2%
	Subbituminous	6,510	69	5,865	63	11.0%	7,180	74	-9.3%
Midwest	Bituminous	17,322	92	14,802	75	17.0%	18,434	91	-6.0%
	Subbituminous	42,951	78	36,809	60	16.7%	45,364	76	-5.3%
West	Bituminous	5,689	75	5,364	68	6.1%	5,862	75	-2.9%
	Subbituminous	33,520	85	31,508	76	6.4%	36,200	83	-7.4%
U.S. Total	Bituminous	60,327	87	57,265	76	5.3%	66,631	86	-9.5%
	Subbituminous	83,144	80	74,945	66	10.9%	88,915	79	-6.5%

Source: U.S. Energy Information Administration

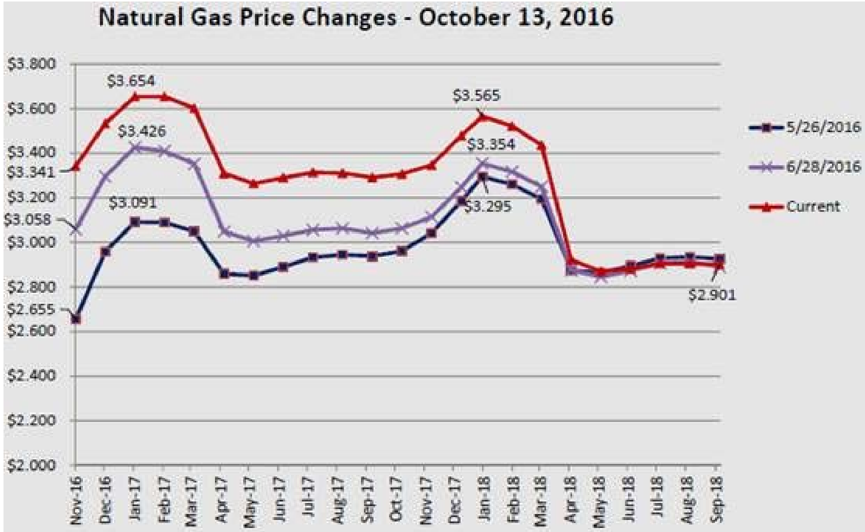
In addition, the bulls are arguing that gas production has dipped as a result of the low prices from earlier this year. And this claim we can rate as completely true. There is no question that gas supply and demand are in closer equilibrium than last year. This however sets up an interesting test of exactly how industrial the shale drilling process really is today. Drilling rigs have increased by 120 from the late May low; drilling permit requests having been increasing all summer and as we discussed last week – Wisconsin sand mines are back in production. So how soon will we see production start to increase again? That is one great question. The EIA is saying that gas production next year will increase by 4 BCF/day. The markets have assumed this as fact for quite a while as that is why 2018 gas prices continue to trade under the 2017 prices. But we are going to have to see a continued growth in the rig count before we will see substantial additions to our gas production. Right now that is not likely to occur until late winter at best the way things look.

Currently, we continue to see the forecasters calling for a warm fall. Our temperatures have dipped here today, but Wisconsin is expected to be back in the 70's again next week. That guarantees two more weeks of large storage inventory builds at a minimum. And while our year on year gas storage inventory has declined substantially (which was inevitable in any event), we will still enter this winter with near record inventory AND with record inventory in the northern market areas where gas is needed the most in winter.

Looking at the daily chart we can see the dramatic impact of today's EIA storage report. The EIA reported a +79 BCF build at 9:30 CPT and the market which had been off in morning trading quickly surged 15 cents/DTH. It continued upward, albeit slowly, and finished the day at $3.341 /DTH, up 13.1 cents.



With the bulls making another run this week all of the strips also show sizeable increases. The Winter Strip increased 25.8 cents week-on-week to $$3.556 /Dth. The 2017 Calendar Strip was up 18.6 cents to $3.401 /DTH while the 2018 Calendar Strip added 8.9 cents to $3.079 /DTH. Every month through the winter of 2017-18 has seen a substantial increase during this rally.



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We are also available on **Twitter** at **@MEPNatGas** with updates on natural gas prices as well as national & Wisconsin gas industry news.

Have a great weekend.

Blake

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