*e*Research

Third Party Research March 16, 2013

Five Reasons Behind the Rise in Natural Gas Prices

e*Research Corporation** is pleased to provide an article from ***Oil & Energy Investor, featuring Dr. Kent Moors.

Bottom Line: There are subtle changes occurring in the natural gas market. New market drivers are at work. An increase in supply is now well documented, in the monstrous findings of shale gas as a result of new and improving horizontal fracking techniques. But, there are also new factors involved on the demand side. Dr. Moors outlines five of them. As the natural gas market shakes itself out, this will provide new investment opportunities, a consideration for a future article by Dr. Moors.

Today's editorial begins on the next page, and is entitled:
"Five Reasons Behind the Rise in Natural Gas Prices".

Oil & Energy Investor is a leading source of investment news, research, financial opportunities and insights on global markets, with a particular emphasis on the oil and gas sector.

Dr. Kent F. Moors is an internationally-recognized expert in global risk management, oil & natural gas policy and finance, cross-border capital flows, emerging market economic and fiscal development, and political, financial, and market risk assessment.

You can learn about ***Oil & Energy Investor*** and subscribe, for FREE, to receive its e-letters and alerts at its website: http://oilandenergyinvestor.com/

***e*Research** was established in 2000 as Canada's first equity issuer-sponsored research organization. Our various research packages allow corporate management to choose the form of research coverage that best meets their company's needs. Investors benefit by having written research on a variety of under-covered companies.

Bob Weir, CFA
Director of Research

Note: All of the comments, views, opinions, suggestions, recommendations, etc., contained in this Article, and which is distributed by *e*Research Corporation, are strictly those of the Author and do not necessarily reflect those of *e*Research Corporation.

Five Reasons Behind the Rise in Natural Gas Prices

by DR. KENT MOORS | *published* MARCH 15TH, 2013

Not long ago, the market was laboring under expectations that the NYMEX futures contract for natural gas would remain at around $3.00 per 1,000 cubic feet (or million BTUs). The pundits were proclaiming that a surplus of shale gas, over production, and historic storage surpluses translated into long-term discounted pricing. Last year's historically warm winter over much of the U.S.A. had not helped the price either.

While this year the weather is more seasonal, there are other factors in the price rise. For the investor, this means there will be plays developing in specific areas that were simply non-existent six months ago. Make no mistake, we are not about to go back up to the $12 plus levels experienced a few years ago. Those days may be gone forever – one of the tangible impacts of the unconventional gas revolution (shale, tight, coal bed methane).

There will still be volatility in this sector as the ongoing balance between extraction potential and well counts works itself out. But we are likely to move into a manageable pricing dynamic. And that means for natural gas investors – with apologies to Sherlock Holmes – the game's afoot!

A Change in Market Drivers Takes Place

Natural gas pricing used to be largely about how cold were winters and hot were summers. Heating needs were the driver in the first case, electricity generation for air conditioning determining the second. These still exist, but today there are other determining factors.

The environment in which they operate has changed dramatically. Given the known extractable reserves currently available in the U.S. market, it would be possible to increase overall gas production 25% a year for the near future.

Nobody is about to do that, of course. It would destroy the market and most of the companies working in it. But that amount of available volume eliminates a concern on the supply side. In fact, it will serve to moderate and put some downward pressure on pricing whether or not it is extracted.

The key is on the demand side. Here, several factors are emerging to portend higher prices. Once again, we need to keep this in perspective. My estimate remains for an average of about $4.35 come high summer, absent any unforeseen developments, with an increase to $4.85 to $5.15 by the end of 2014. Not a major advance, but enough to kick start an entire sector. Why?

Because of five underlying reasons, all of which I have discussed in previous issues of *OEI*. Each has been enhanced by the period of reduced prices since lower prices will always encourage greater energy use. As the reliance increases with the usage levels, so will the commodity price.

Five Factors to Consider in Natural Gas Prices

First, broad based industrial use has finally returned and exceeded pre-crisis levels. This is always the last of the main traditional demand areas to return after a recession (and the most recent as the worst in seventy years).

Second, natural gas is replacing oil as a feeder stock for petrochemicals – everything from ingredients used in the production of plastics to fertilizers and widely-used chemicals. This flow is actually increasing quicker than I had initially anticipated.

Third, we continue to witness a move to liquefied natural gas (LNG) and compressed natural gas (CNG) as a vehicle fuel. The transition remains primarily noticeable in higher-end trucks, with the emphasis on passenger vehicles still awaiting cost reductions. Nonetheless, heavy truck, bus, and equipment fleets are moving to natural gas.

However, the last two categories are the main stimuli.

Fourth is the move from coal to gas for the production of electricity, a development occurring most rapidly than even the rather optimistic predictions I made last year. The background is this. The U.S.A. will retire at least 90 GW of capacity by 2020, with an additional 20-30 GW likely from the imposition of EPA non-carbon emission standards (mercury, sulfurous, and nitrous oxides). Most of today's capacity is fueled by coal.

Last year, I estimated that, for each 10 GW transferred, 1 billion cubic feet of natural gas per day would be required. Well, based on the initial figures, that is coming in at 1.2 billion. It sets up this startling conclusion. If half of the transition I expect from coal to gas actually takes place, it will eat up three times the current volume in storage. Certainly, some of that will be offset by increasing production. But the operators have learned that flooding the market does not help any of them. That is another lesson taught by the shale gas age.

Finally, we have the advent of LNG exports from the U.S.A. and Canada. These are not likely to begin in earnest until late 2014, but will transform the sector. From providing none of the current global LNG trade, the U.S.A. will account for at least 9% within ten years.

For those concerned about what the exports will do to domestic end user costs, remember there is plenty of spare volume capacity waiting to be drilled. In short, this is not going to be an increase in exports at the expense of rising costs at home. There is plenty to satisfy both.

Once again, the key here is balancing production. As we move into this new gas age, remember this: *LNG exports will act as a primary outlet for excess shale gas extraction.* The greater the exports, the lower will be the volatility in pricing at home.

We are, therefore, watching a number of new investment opportunities emerging as the gas market shakes itself out. This is not a tide, but more like a series of escalating ripples, and it is not going to raise all boats. How should the individual investor play this? That will be the subject of a future *OEI*.

Sincerely, Kent

BW: See Dr. Moors' bio below.

Dr. Kent F. Moors is an internationally recognized expert in global risk management, oil/natural gas policy and finance, cross-border capital flows, emerging market economic and fiscal development, political, financial and market risk assessment. He is the executive managing partner of Risk Management Associates International LLP (RMAI), a full-service, global-management-consulting and executive training firm. Moors has been an advisor to the highest levels of the U.S., Russian, Kazakh, Bahamian, Iraqi and Kurdish governments, to the governors of several U.S. states, and to the premiers of two Canadian provinces. He's served as a consultant to private companies, financial institutions and law firms in 25 countries and has appeared more than 1,400 times as a featured radio-and-television commentator in North America, Europe and Russia, appearing on ABC, BBC, Bloomberg TV, CBS, CNN, NBC, Russian RTV and regularly on Fox Business Network.

A professor in the Graduate Center for Social and Public Policy at Duquesne University, where he also directs the Energy Policy Research Group, Moors has developed international educational programs and he runs training sessions for multiple U.S. government agencies. And until recent revisions in U.S. policy, Dr. Moors was slated to be the deputy director of the Iraq Reconstruction Management Office (IRMO) in Baghdad.

Moors is a contributing editor to the two current leading post-Soviet oil and natural gas publications (Russian Petroleum Investor and Caspian Investor), monthly digests in Middle Eastern and Eurasian market developments, as well as six previous analytical series targeting post-Soviet and emerging markets. He also directs WorldTrade Executive's Russian and Caspian Basin Special Projects Division. The effort brings together specialists from North America, Europe, the former Soviet Union and Central Asia in an integrated electronic network allowing rapid response to global energy and financial developments.