Energy Brief

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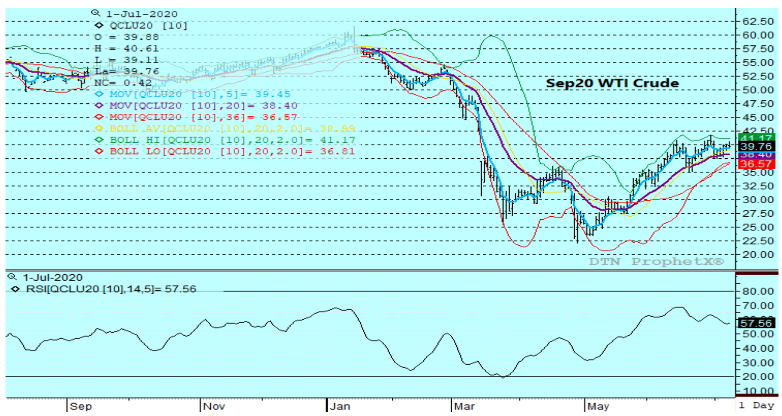
Price Overview



The petroleum complex traded cautiously higher as underlying support emerged in response to the sharper than expected decline in crude inventories and on signs that demand is beginning to stabilize outside the US, where the progress in fighting the pandemic is showing signs of success. Some caution was apparent on the upside over 40.00 in the nearby contracts as profit taking emerged, reflecting unconfirmed reports that OPEC was leaning toward easing production cuts after July from the current target level of 9.7 mb down to 7.7. The possible reduction will likely come into clearer focus as we move closer to the OPEC Price Monitoring meeting at mid-month.

The DOE report showed a decline in crude inventories of 5.5 mb with an addition of 1.7 to the SPR. Production levels at 11 mb/d remained stable. Cushing inventories, which had been falling sharply in recent weeks, were off .2 mb at 45.6. Refinery utilization remained low at 75.5 percent compared to 94.2 percent last year. Gasoline inventories increased 1.2 mb while distillate inventories declined by .6. Product supplied of gasoline at 8.6 mb was stable against last week but was 9.5 percent below year ago levels. With some major metropolitan areas seeing a pickup in COVID-19 cases and reverting back to lockdowns, some retrenchment in gasoline demand might occur over the next few weeks. Distillate supplied totaled 3.8 mb an increase of .3 from last week and stable against last year. The increase likely reflected a pickup in freight movement. Total product supplied was 17.4 mb against 18.4 last week and 16 percent below a year ago. Net imports of crude and products continue to fall at .07 mb reflecting a pickup in export levels as a recovery in overseas economies occurs.

Ideas that OPEC+ and particularly Russia, is content with values near current levels and might remain a headwind for values. Although it is encouraging that an improvement in global manufacturing activity is occurring, maintaining production restraint will be key to drawing down excess inventories. To some extent this has occurred with afloat storage levels of crude and products falling over the past month. Nevertheless with the possibility that the blockade on Libya will be lifted, demand will need to show improvement in order to allow a more normal stock situation to occur.

For now we are unconvinced that the pace of recovery from the pandemic and OPEC's commitment to keeping production low is enough to avoid a further build in stocks, particularly if OPEC production rises after July, with valuations much above 41.00 unsustainable.

Natural Gas

The market gave back some of its recent gains as the move had gotten ahead of itself after the perfect storm of extremely oversold conditions followed by short term demand improvements ignited the rapid bounce. The main catalyst of today's pullback was poor LNG numbers, as feedgas demand was off 1.3 bcf compared to yesterday. Exports to Mexico also showed a large drop, down .9 bcf from the previous day. With weather unchanged but still well above normal and production slightly lower, the negatives outweighted the positives for the moment. With lower 48 dry production hovering near 87 bcf/d, a sustained move below that level would go a long way toward confirming that a bottom is in. With Chesabeake Energy in bankruptcy that eventually seems likely. The biggest headwinds remain the large storage overhang and recent spike in COVID-19 cases. With the potential for some very large power burns in the coming weeks we believe the 1.65 area holds and the market eventually breaks out of the downtrend channel to find initial resistance in the 1.80 area, with potential to test 1.87, which represents a 38 percent retracement of the break from early May.