Energy Brief

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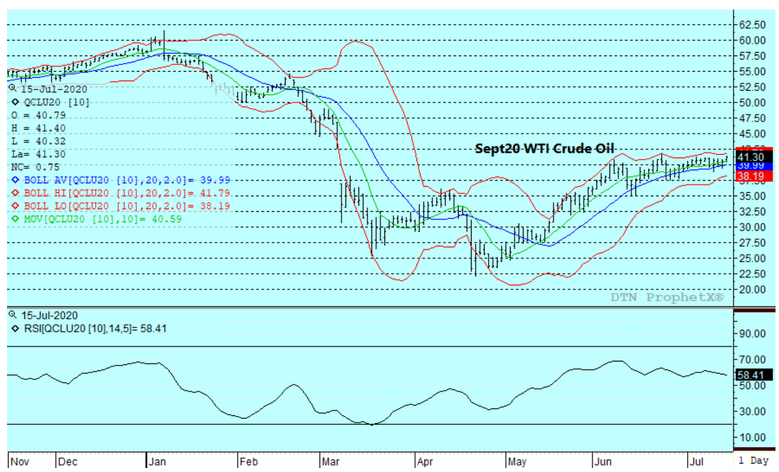
Price Overview



The petroleum complex attracted buying interest following the DOE report which showed a sharper than expected decline in crude inventories. Additional buying emerged in response to reports of progress on a vaccine for COVID along with the conclusion of the OPEC Price Monitoring Committee meeting. The appearance that the current agreement will be scaled back from the 9.7 mb/d level to 7.7 mb/d was expected, but the actual cut is likely to be higher at 8.54 mb/d as countries who had overproduced the past few months, such as Iraq, compensate for their shortfalls. In addition Saudi Arabia indicated that their export levels would not increase in August as domestic electric generation is maintained at a seasonally high level. The agreement appears to be in force through September.

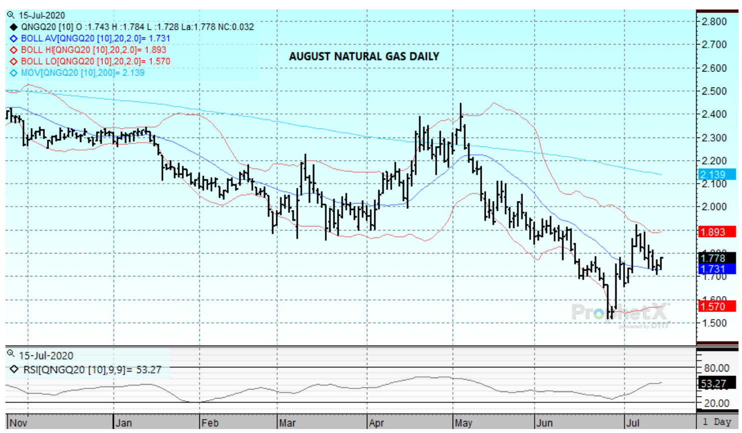
At this juncture the market is dealing with considerable uncertainty. Optimism over prospects for demand continue to circulate suggesting that the global economy will expand by as much as 4.7 percent in 2021 compared to a forecast of a decline of 3.7 percent this year. The expected increase in demand is anticipated to allow OPEC supplies to expand by as much as 6 mb/d in 2021. The possibility that the inventory overhang will begin to be reduced late this year is also helping underpin values despite the appearance that the US might lag other industrialized countries in their movement out of lockdowns.

Today's DOE report gave the market some optimism that underlying supply/demand might be moving toward a more balanced position and that excess inventories are being drawn down. US crude inventories declined by 7.4 mb as imports fell from 7.4 mb to 5.6. Refinery utilization rose to 78.1 percent with inputs of crude steady at 14.3 mb against 17.3 mb last year, a decline of 17 percent.

Despite the decline, Cushing stocks rose by .9 mb to 48.7. Product stocks also fell, with gasoline inventories declining by 3.1 mb and distillate off by .5 mb. Total stocks were lower by 9.2 mb at 2,108.5 mb compared to 1,955.7 last year. Gasoline product supplied appears to be stagnating as COVID infections surge in some areas as demand might suffer if schools and businesses delay reopening and commuter traffic remains restrained due to continued work from home. In distillate, product supplied recovered from the weak showing last week at 3.7 mb and compared to last year's rate of 3.6. Total product supplied at 18.5 mb was 8.7 percent below year ago levels.

Although the fundamentals have shown improvement, the ongoing injection of liquidity into the global economy and fiscal support will remain a key consideration as we move forward. Despite the OPEC agreement, which has helped stabilize values, it appears producers remain cognizant of the impact of higher prices on production levels, particularly in the US where additional cuts are being delayed given the recovery in prices. In addition, the global economic recovery will need to show a steady improvement in order to move inventories down to more normal levels. 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, suggesting that valuations much above 41.00 to 42.40 basis Sept WTI are likely unsustainable.

Natural Gas



Prices traded on both sides of unchanged today before finding support late in the session, with the August settling higher by just over 3 cents at 1.778. Volume was anemic as trade seemed to signal a level of uncertainty regarding the current mixed bag of price drivers. Production levels remain a barrier to rallies, remaining near the 88 bcf/d area, and LNG exports continue to struggle with worldwide demand issues. Weather continues to offer underlying support as temperature expectations remain well above normal for the second half of July. The spike in viral infections in some areas has also created an air of caution as uncertainties abound on the demand side. Tomorrow's storage report is estimated to show a 47 bcf build compared to the five year average of 63. After five straight sessions of lower lows, the 1.70 area held up yesterday and we managed to avoid a sixth consecutive step down today. With another string of warm temperatures approaching we look for the market to find support that could build momentum to possibly test the 2.00 level, which would surpass a 50 percent retracement of the May to June break.