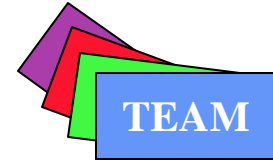


TEAM Energy Tips

“Butterfly Fundamentals”

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The concept of the “butterfly effect” first came to popularity many years ago. Based on recent natural gas price movements, we’ve coined the term “butterfly fundamentals” to explain the large impacts of small pieces of news or seemingly unrelated or non-traditional information on natural gas prices.

Let’s take a look at the butterfly fundamentals with regard to natural gas pricing.

There is general acceptance that the supply and demand balance is very tight in North America and will remain this way for several years. Based on this, prices have been quite volatile. However, there continues to be extensive volatility in the price of natural gas that seems to disregard the fact that storage levels are high.

Some believe this is due to a concern that even these high inventory levels will not be sufficient to meet a normal winter demand. They reason that the heat sensitive market has grown to a point where 3.1 Tcf is no longer a high enough target and that we need to invest in additional storage capacity.

Whether or not this is true, this doesn’t

intuitively explain the continued volatility now that winter has begun and storage levels continue to be higher than both last year and the 5-year average.

Of course, as long as natural gas is used to heat homes, office and storage space, we will have volatility in the price due to changes in the weather.



However, these days we have volatility in this market due to non-traditional factors. Some of these non-traditional factors are discussed below.

The vagaries of war and the uncertainties experienced daily during a war contribute to the fear of supply disruption which may lead to price spikes for short periods.

Even oil price movements are not showing an intuitive relationship since natural gas prices have been increasing both during periods of oil price increases as well as during oil price decreases.

In addition, we now hear a lot about hedge funds and their contributions to the volatility of natural gas prices. While these investors would not be classified as “butterflies” based on their enormous size, their influence on price levels does qualify as a butterfly fundamental since they are a non-traditional source of price volatility.

Interestingly, we should probably expect to see continued volatility and new butterfly fundamentals coming into play over the next few years and during any other times that supply and demand is in tight balance.

Investors in general reap many benefits from the sheer volatility of markets. The interrelation of many markets causes butterfly effects to create volatility across multiple markets. As long as investors continue to seek higher returns, expect to see relatively volatile markets with more butterfly fundamentals coming into play.

At TEAM we’re always on the look-out for new types of energy risk in order to help our clients make informed energy decisions. Do you know which butterflies to watch?

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Traditional Fundamentals

For the purposes of this article, traditional fundamentals include the storage level, drilling levels, production decline rates, hurricane activity and other immediately related items.

Over time, some of the items we consider butterfly fundamentals may become less relevant while others will likely move into the “traditional fundamentals” category.

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