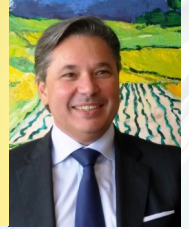


WEEKLY ANALYSIS

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RISING ENERGY PRICES AFFECT PRODUCTION, INFLATION AND PURCHASING POWER

Energy prices literally explode in Q3 2021. Inventory reductions driven by rising global demand. Indirect effects of the energy transition on the energy market. Risk of recession after a supply shock?

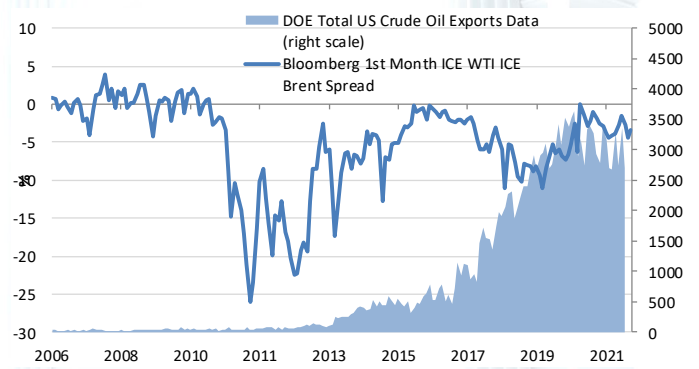
Key Points

- Energy prices literally explode in Q3 2021
- Inventory reductions driven by rising global demand
- Indirect effects of the energy transition on the energy market
- Risk of recession after a supply shock?

Energy prices literally explode in Q3 2021

The price of West Texas Intermediate (WTI) crude oil has jumped by nearly 73% in 2021 and has exceeded USD 80 per barrel for several days now. Its European equivalent, North Sea Brent, is up 67% and approaching USD 85 per barrel. Half of this increase (+32% and +33%) took place in the last eight weeks alone—a period that coincides with the extraordinary +75% rise in natural gas prices from USD 3.7 to 6.5. Tensions are rising and affecting other energy sources, including coal. The post-pandemic world is waking up to the fact that our economies are still extremely dependent on fossil fuels and gas, especially as all economies are emerging together from the health crisis and competing for the energy needed to achieve their development goals. Coal prices have soared by over 300% in Australia. Reserves are dwindling everywhere, and China is recommending that its companies store as much energy as possible in anticipation of likely bottlenecks and shortages. In India, too, preparations are likely to be made for power outages, as the economy is largely dependent on energy from coal-fired power stations. The rise in energy prices is the result of producers' failure to anticipate the rise in various countries' demand caused by the post-pandemic economic rebound. It is probably also a symptom of the current global clash between a still cautious supply struggling to meet a revitalised consumer demand, as the former has already drawn heavily on inventories and cannot adjust production.

WTI-Brent Differential and US Crude Exports



Sources: Bloomberg, BBGI Group SA

The gas factor

The rise in natural gas prices is not all that surprising and is rooted partly in the rather radical change in the US market. The overproduction of gas due to the shale industry over the last ten years had reached extreme levels, to the point where it was no longer possible to store output, until the recent development of LNG export capacity. The situation is different in the post-pandemic era, with production remaining well below its previous level while demand is increasing with the global move towards reducing carbon emissions. The explosion in demand for natural gas as a result of the reduction in targets is a logical consequence occurring just as inventory levels are reduced before the start of the cold season. Modelling of the flows between supply, demand and inventory levels suggests there is a risk of near-zero stock in the event of a cold snap.

In addition, deliveries of Russian gas to Europe declined sharply, suggesting that this was a move by the Kremlin to pressure Germany into quickly approving the certification of the newly completed Nord Stream 2 (NS2) pipeline. This pipeline remains at the centre of geopolitical tensions between the US, Ukraine and Russia.