Power Foresight Monthly Outlook: May 2024

Summary

- We see broadly bearish pressure on European power prices in the short-term, driven by both power market fundamentals and expectations on the direction of gas and carbon prices.
- From a fundamental viewpoint, demand recovery remains subdued across most of Europe (except for the Nordics), while French nuclear availability is in a good position and hydropower in France and Spain remains well above the average for the time of year. This is putting bearish pressure on near-curve prices, with a significant number of negative prices expected in the next two months and deeply negative spark and dark spreads highlighting that average efficiency coal and gas plants are out of the mix.
- The latest seasonal weather forecasts suggest that May will see temperatures close to historical averages, though above-average temperatures can be expected across much of Europe in June, July, and August, leading to increased cooling demand.
- On the gas side, a key driver will be the end of maintenance at the US Freeport LNG plant in May, which is expected to provide downward pressure to European spot gas prices despite Norwegian maintenance reducing pipeline supply to Europe.
- On carbon, our analysts see scope for the Dec-24 contract to decline to a €60t-65/CO2e range and potentially test the €60t/CO2e support level if speculators were to add additional short positions and the next industrial production numbers continued to show no uptick compared to 2023.
- Weak technical indicators can be seen despite recent price increases, with April's closing price below January's open indicating a failed bullish engulfing pattern, possibly signalling weakening bullish momentum.
- Conversely, liquidity data suggests a continuation of the bullish trend, though caution is warranted due to bearish fundamentals.

Power demand outlook

- Power demand across Europe remains supressed with limited demand recovery seen so far in 2024. As we recently analysed, European consumption in Winter 23/24 was just 1.5% higher than the previous winter (though only 1% higher when adjusted for weather). Strong growth in the Nordics supported this trend, while major countries like Germany and Great Britain saw lower demand in Winter 23/24 than in the previous winter, highlighting that recovery has yet to take root.
- As we highlighted in a recent webinar, we are forecasting European power demand to increase by 2.7% year on year in 2024, meaning that a gradual recovery is expected throughout the year. The increase is forecast to stem primarily from the residential and commercial sectors as the macroeconomic situation improves, while industrial demand will be slower to recover.
- The latest seasonal weather forecasts from Copernicus suggest that temperatures across most of Europe are expected to be near to average for May, meaning there is limited price impact. However, forecasts for June, July and August are for above average temperatures in Central and Southern Europe, with France seeing a temperature deviation of 1.21 degrees Celsius in July. This leads to a €2.5/MWh price increase compared to our ‘no weather’ scenario due to additional cooling requirements. A similar price deviation is seen in Spain, though the bullish price pressure is less significant in most other European countries.

Power supply outlook

- Fundamental drivers of supply in western Europe are broadly bearish, but export restrictions on France's Eastern borders, expected to last until mid-May, have hampered the flow of electricity between markets. RTE said they may send notices to limit French-Italian NTC to between 1.6-2.8GW, while NTC on the French-Swiss border would be reduced from 2.8 to 2GW, and NTC on the Belgian and German borders may be adjusted by at least 400MW at points.
- French nuclear availability remains in a good position, with output in May expected to be around 2TWh higher than 12 months previously, with similar expectations for June and July.
- In Southern Europe, aggregated reservoir stocks are close to the maximum of the 2015-2022 range, weighing on prices for Q3. On an individual basis, French and Spanish stocks are well above the average for the time of year, while Swiss and Italian stocks are below this historic average. Both Italian and French run-of-river generation are also above normal for the time of year. However, soil moisture indexes show wide swaths of much drier than normal conditions over Italy and some scattered areas in Spain, signalling inflow to rivers could slow on the back of these dry conditions.
- Early snowmelt is thought to have led to higher than seasonal reservoir stocks and run-of-river, but this could have implications for later in the year if there is no longer sufficient snowpack to replenish rivers and reservoirs. Although the remainder of the week beginning 29 April was expected to be wetter than normal in France, Spain and Italy, the following week is expected to be much drier than normal in France and Spain and in line with seasonal norms in 2024.

European gas outlook

- Maintenance at the 15mtpa three-train US Freeport LNG plant is expected to conclude in May, having last run at full capacity in mid-January. The works are expected to allow the plant to increase its nameplate output by 10%, to 16.5mtpa, from June. Signs of rising feedgas into the plant, as well as increased LNG loadings, will provide downward pressure on European spot gas prices. ICIS data shows that in 2023, of the 12.3m tonnes of LNG exported from Freeport, 54% was delivered to EU and the UK. The plant has run below one-third its usual capacity in April.
- Norwegian maintenance that will reduce pipeline supply to Europe will continue through May, having commenced in April. On average, 52mcm/day of Norwegian production will be unavailable over the month, although this falls to 48mcm/day if one-day works at the major Troll field on 21 May is discounted. Peak production from Norway is just over 350mcm/day. Unplanned outages aside, the maintenance should be priced into the market.
- Germany's newest LNG import terminal, the Stade FSRU, may receive its first cargo during May. Operator data shows one no-obligation slot was marketed for the month. No slots (either with or without obligation) were marketed for April even though the FSRU, the Energos Force, arrived back in March. Together with the new terminal at Mukran (that replaces the one at Lubmin), German LNG imports could begin to steadily rise in the coming months, which could lead ICIS TTF prices to weaken.
- A ten-day outage is expected in Libyan pipe flows into Italy during May. ICIS Gas Foresight expects this to marginally delay Italian storage stocks hitting 90% fullness, although we still predict this EU-mandated target to be reached in August, well ahead of schedule. LNG imports are unlikely to ramp-up to cover the cut in flows on the GreenStream pipe, as a major outage continues at the OLT import terminal.
- As is typical for the time of year, European demand will likely slide lower into May, from April rates. Focusing just on 12 main hubs in northern and central Europe, ICIS Gas Foresight predicts an 8% fall in consumption, month-on-month. During the first third of 2024, demand in the same region has been 19% lower than the 2017-2021 average. The falling seasonal demand should be priced in.

European carbon outlook

- In April, the EUA market once again experienced high volatility with a €16t/CO2e price range between troughs (€57t/CO2e, 3 April) and peaks (€73t/CO2e, 16 April). At the time of writing, the Dec-24 contract was consolidating at the lower end of the €65-70t/CO2e trading range.
- EUA market participants continue to face a challenging trading environment as key price drivers remain either unchanged or difficult to predict.
- For utilities, fuel switch dynamics will continue to remain relatively irrelevant in May as the lion share of average efficiency thermal power plants in Europe remain out of the money with negative forward power spreads. Stronger industry demand or a power supply shock will be needed for order for spreads to improve again.
- For industrials, confidence is slowly returning for some sectors like chemicals. However, the combination of high energy prices, low demand and tight monetary policy has hit European energy intensive sectors tremendously in 2023. This means that even a return in confidence has so far not been translating into production output recovery compared to 2023 according to our latest analysis.
- For speculators, funds have been short squeezed by geopolitical induced volatility in April. In parallel, the short positioned players also need to manage the risk of improving eurozone macro sentiment. However, considering the latest bearish industry production numbers and overall expectation for a gradual recovery rather in H2 2024, there is in our opinion room for speculators to build additional short positions in May. With that said, the closer the EUA market is getting to June for potential ECB interest rate cuts, the higher the risk for short specs to face some degree of temporary bullish reversal from a macro perspective.
- Despite the current EUA price stabilisation at time of writing, we see scope for the Dec-24 contract to easily go back to a €60t-65/CO2e range and potentially test the €60t/CO2e support level if speculators were to add additional short positions and the next industrial production numbers continued to show no uptick compared to 2023.

Technical analysis/Liquidity

- Looking at the monthly candles for the Cal-25 and Quarterly contracts, while the last two months have seen an increase in price, the technical indicators appear weak. April's closing price is below January's open, despite an earlier attempt to surpass it earlier in the month, signalling a failed bullish engulfing pattern.
- This failed bullish engulfing pattern is a sign of the bullish move lacking strength, and traders may interpret this as a warning signal that bearish momentum is returning.
- Conversely, liquidity data remains bullish. Both open interest and trade volumes have increased in successive bullish months, suggesting a continuation of the bullish move.
- However, given that fundamentals are bearish, relying solely on liquidity indicators may not be enough to suggest that the bulls will continue in May.