

## Coal merely a band-aid for Europe

- Europe's continuing reluctance to enter into long-term contracts for LNG highlights its resolve to green up its energy sources
- Despite falling back on coal usage amid the Russia-Ukraine war, the EU is unlikely to accept coal as a long-term energy source
- We remain cautious on emitting sectors such as coal; expect oil price to stay high during US summer months while gas may see another spike in winter

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**Carbon emission likely to exceed COP's target for CY22:** Given the sudden reduction in Russian oil & gas volumes and the high price of LNG cargo, many European countries have silently restarted their coal plants – this is partly reflected in all-time-high coal prices at US\$ 300/mt, nearly 3x higher than mid-cycle prices. China too has been steadily ramping up coal production due to elevated LNG prices over the last one year. Given significantly higher coal usage in CY22, carbon emission during the year is likely to materially exceed COP's implied 2°C warming trajectory, in our view.

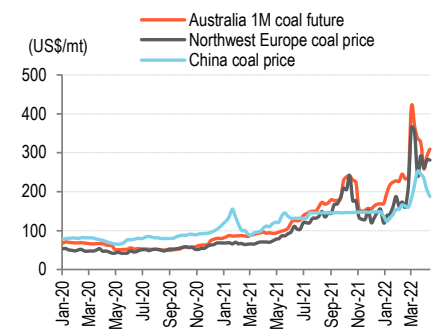
**EU expected to double down on climate targets:** We note the EU's reluctance to enter into long-term contracts for LNG to set off lower Russian gas volumes, with the region instead continuing its search for short-to-medium-term cargo. Note that long-term contracts are much cheaper than spot prices. Even at current elevated oil prices, most long-term contracts, which are typically oil-linked, would likely cost US\$ 12-14/ mmbtu against the current spot price of US\$ 30-35/mmbtu. We, therefore, believe that once the Russia-Ukraine situation eases and the EU is able to diversify its energy sources, it will likely double down on climate targets.

**Plans to diversify away from Russia gas:** The EU's plan to replace Russian gas includes a combination of higher use of renewables, an increase in energy efficiency and diversification of supply sources.

**Summer oil & winter gas:** Oil consumption usually rises in June-August, in part due to the summer driving season in the US and demand for oil-fired power in Asia and the Middle East. Lower Russian volumes are likely to put further pressure on oil prices during the summer season despite releases from strategic storage. Peak gas demand, on the other hand, occurs in winter months (Dec-Feb) due to heating requirements. Given the visible reduction in Russian oil and gas volumes, we expect oil prices to remain elevated in summer months while gas prices could rise even further in winter.

**Cautious on emitters:** We continue to maintain that high carbon-emitting sectors, in particular coal-based companies, will face headwinds. Please refer to our note [Climate Action: Taking the bull by the horns](#) of 2 November 2021 for details.

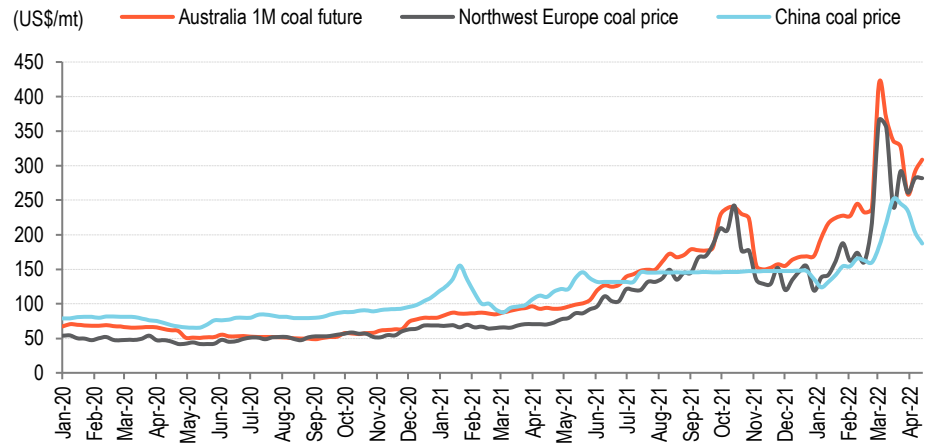
## Coal price at significant premium to mid-cycle level



Source: Bloomberg, BOBCAPS Research

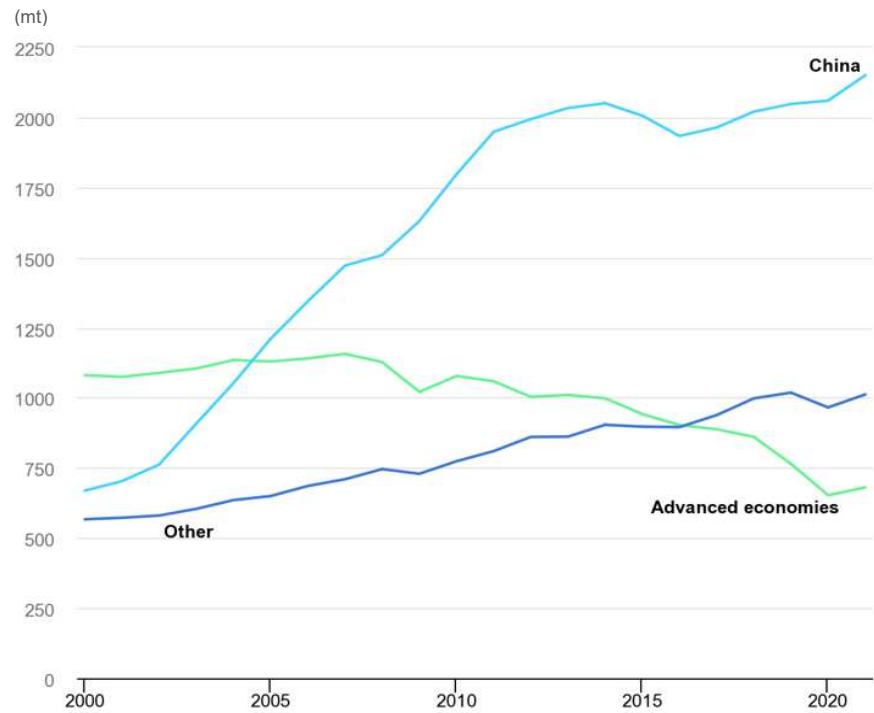


**Fig 1 – Coal price at significant premium to mid-cycle level**



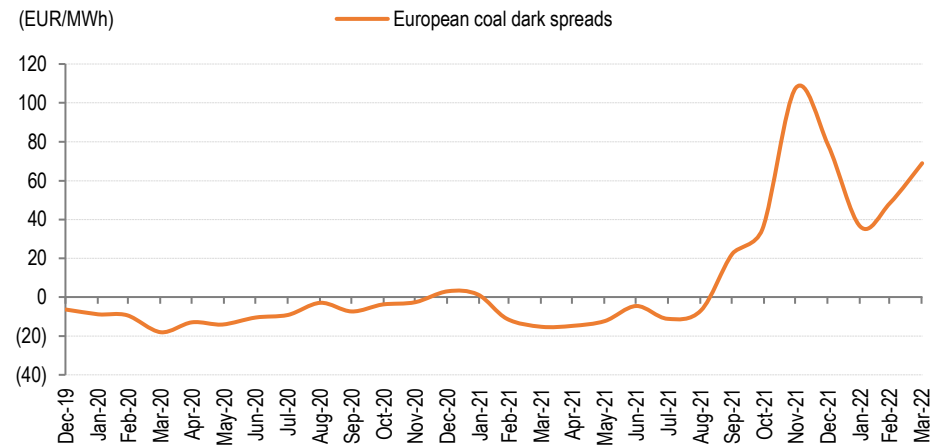
Source: Bloomberg, BOBCAPS Research

**Fig 2 – Coal consumption by region**



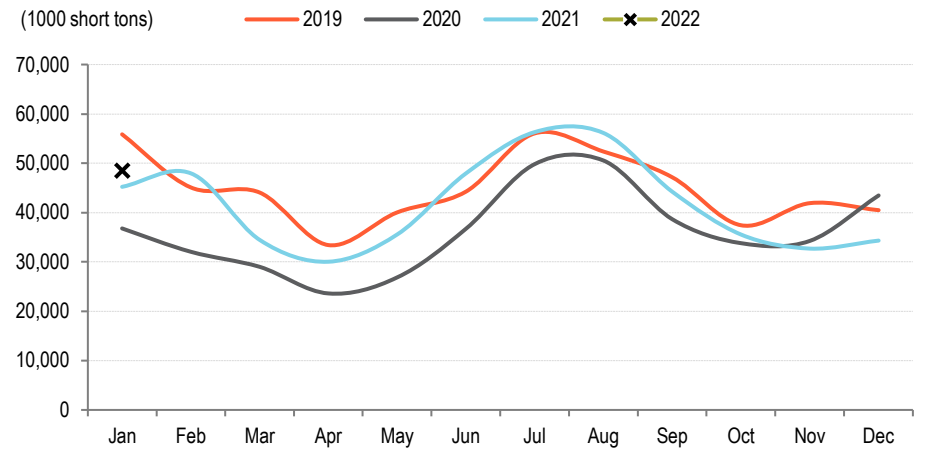
Source: IEA, BOBCAPS Research

**Fig 3 – High dark spreads supporting high coal prices**



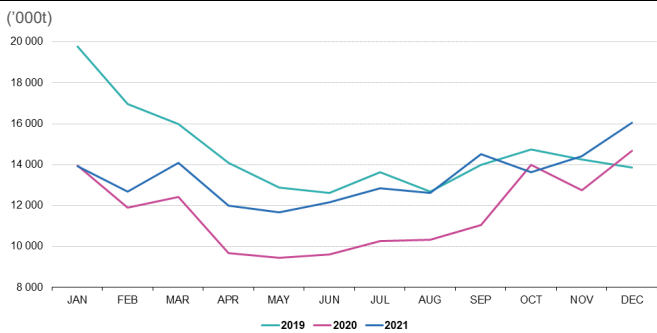
Source: Bloomberg, BOBCAPS Research

**Fig 4 – US coal consumption summer peak rose in 2021**



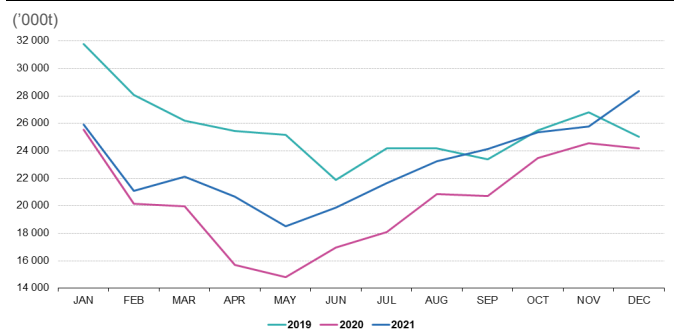
Source: U.S. Department of Energy, Bloomberg, BOBCAPS Research

**Fig 5 – EU's hard coal consumption over 2019-21**



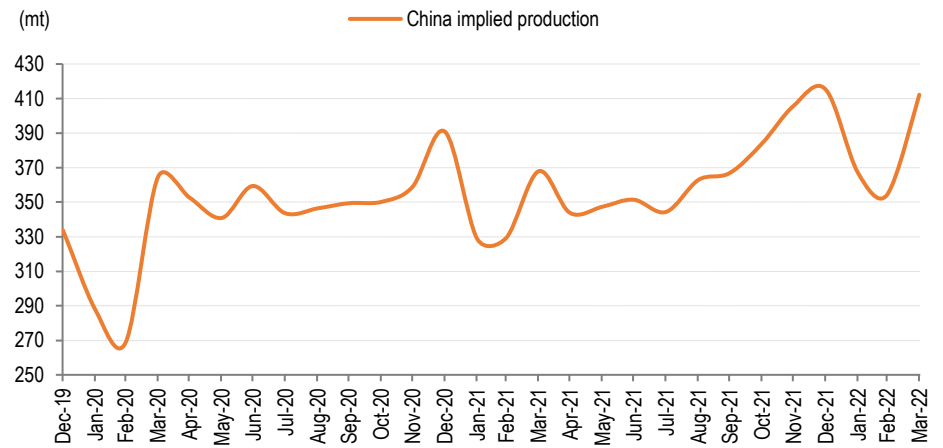
Source: Eurostat, BOBCAPS Research

**Fig 6 – EU's brown coal consumption over 2019-21**



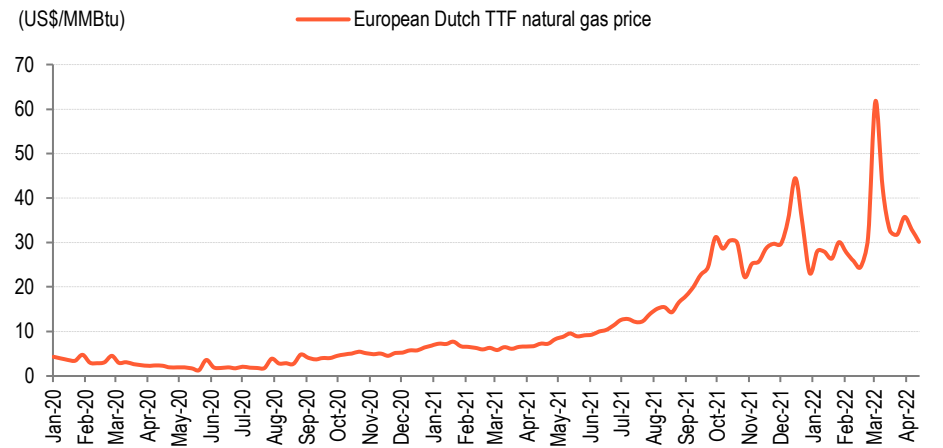
Source: Eurostat, BOBCAPS Research

**Fig 7 – China ramping up coal production**



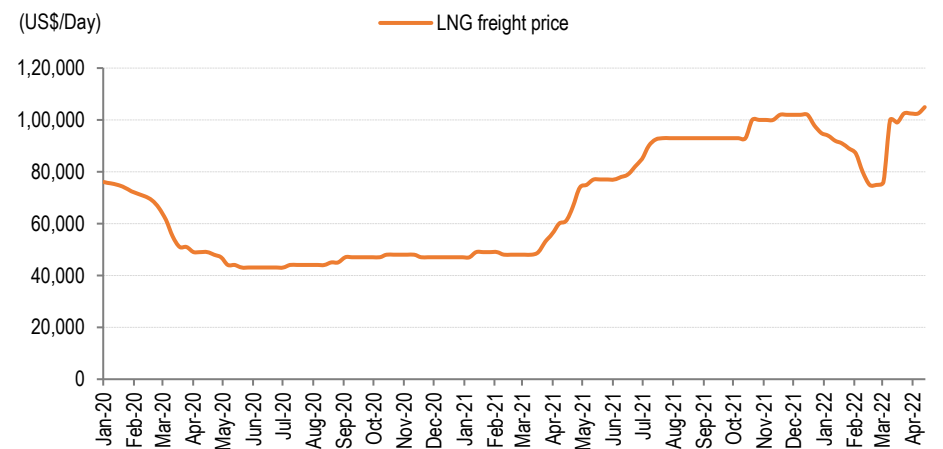
Source: Bloomberg, BOBCAPS Research

**Fig 8 – High natural gas prices driving coal demand**



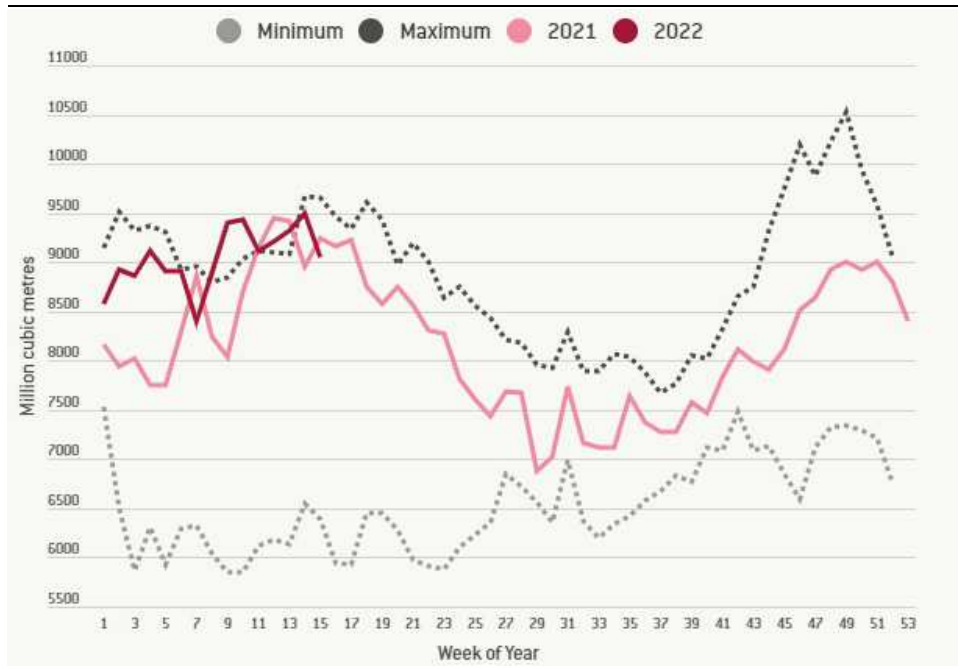
Source: Bloomberg, BOBCAPS Research

**Fig 9 – Freight rate remains tight for LNG**



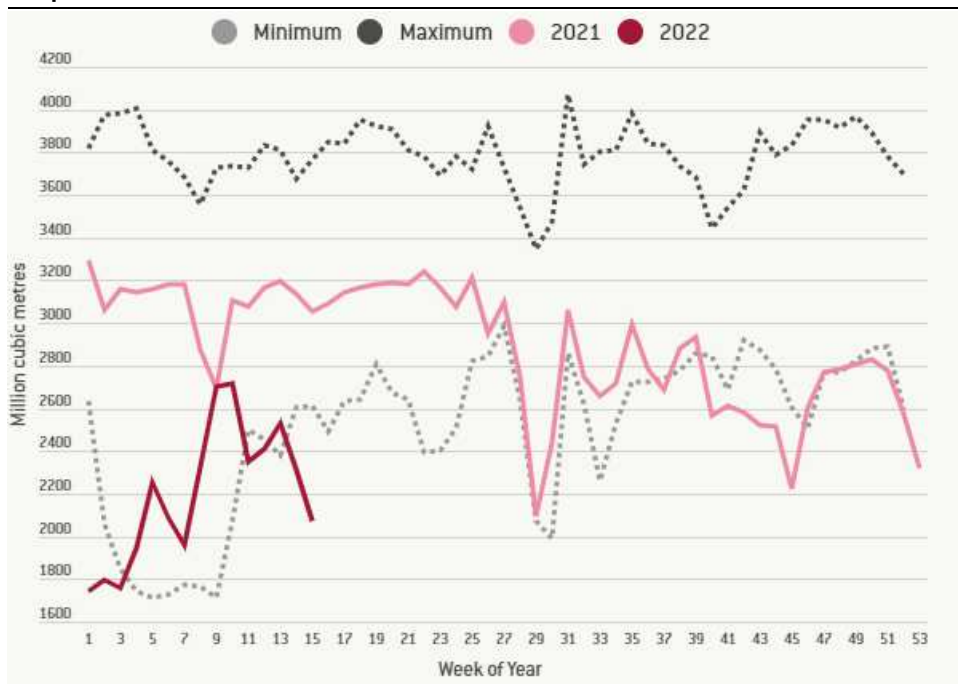
Source: Bloomberg, BOBCAPS Research

**Fig 10 – EU natural gas imports (total): Imports high even post-winter, supporting high LNG prices**



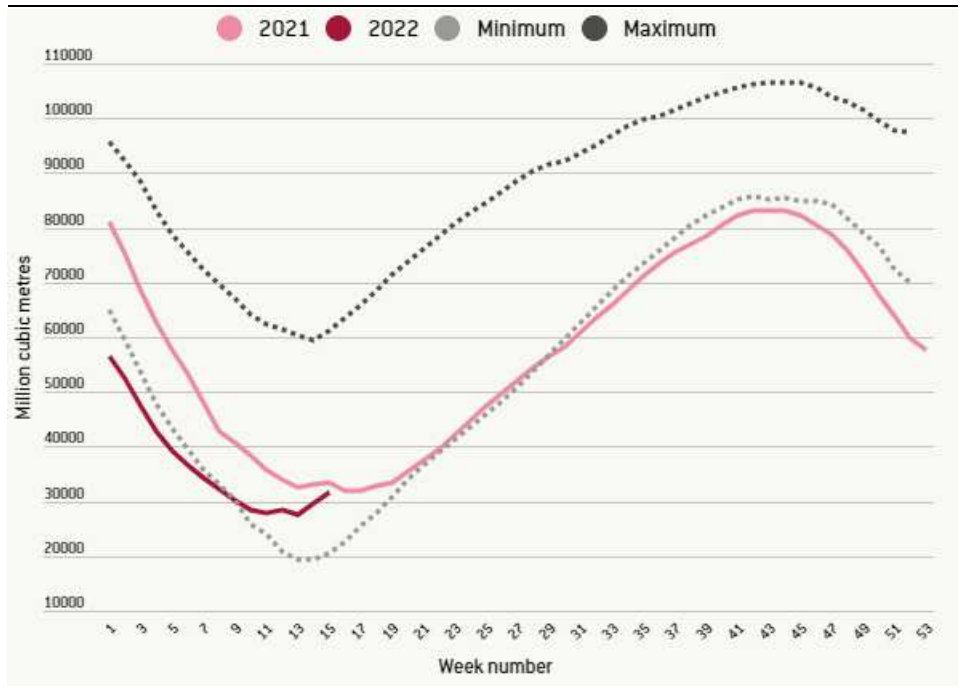
Source: ENTSO-G, BOBCAPS Research

**Fig 11 – EU natural gas imports from Russia: Lower Russian imports raising import demand from other sources**



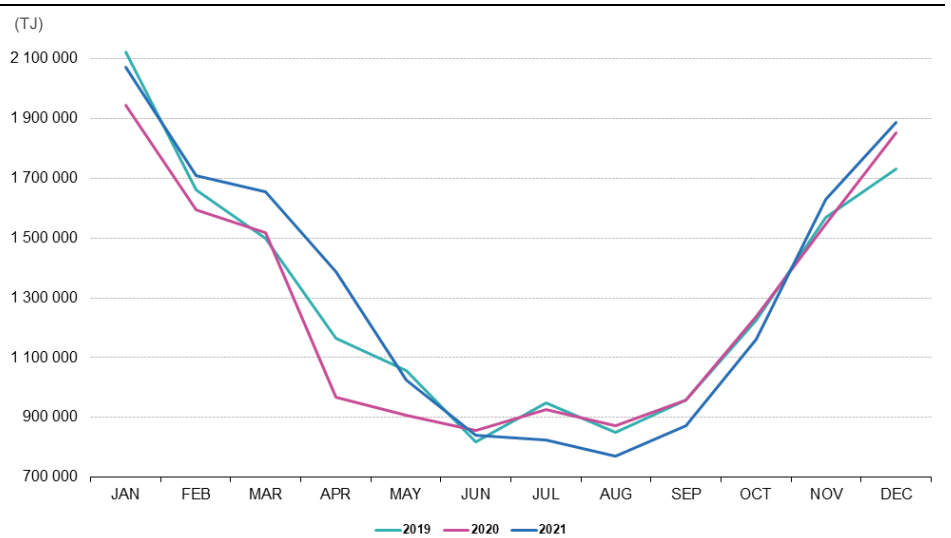
Source: ENTSO-G, BOBCAPS Research

**Fig 12 – EU gas storage: Low storage level will keep import demand high even through off-peak season of Apr-Sep**



Source: ENTSO-G, BOBCAPS Research

**Fig 13 – EU’s natural gas consumption over 2019-21: Lower natural gas consumption in Q4CY21 prompted rise in Europe’s coal usage**



Source: Eurostat, BOBCAPS Research

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