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NGL Prices: Industry Experts Weigh In

Brian O'Connell July 30, 2012

New data out from Devon Energy Corp.'s management sees natural gas liquids prices bottoming out through the fourth quarter, as prices remain depressed in 2012.

Devon's Chief Financial Officer, Jeff Agosta, tells *Oil and Gas Investor* 2013 is more "uncertain". But investors want to know -- does uncertainty mean opportunity for natural gas stocks?

Analysts have maintained that natural gas has been one of the few drivers of the anemic U.S. economic recovery, as lower natural gas prices have prodded major industries, like trucking, away from pricier crude oil and toward natural gas, especially shale gas.

That trend should continue, OGI's panel of experts says in a review of the natural gas liquids (NGL) industry in the second half of 2012, and into 2013. ("NGLs" are components of natural gas--propane, butane, pentane, hexane and heptanes--that are liquid at surface in field facilities or in gas-processing plants.)

"Currently, natural gas prices are so low that many fleet-based companies will continue to convert their fleets to LNG (liquefied natural gas) and CNG (compressed natural gas) use -- either through existing truck conversions or new truck purchases," says Fuels Quest's vice president of marketing, David Zahn.

That's a hybrid strategy that works for more and more companies, he adds -- including one of the biggest companies in the U.S.

"For instance, the largest waste company in the U.S., Waste Management Inc., is doing both and has already developed fueling facilities at roughly 27 locations," says Zahn. "As demand for natural gas liquids continues to increase, we expect government agencies to adopt and enforce laws (many are on the books today) to gain additional fuel tax revenues from natural gas. These are costs that many fleet-based companies have yet to see and may change the economics of conversion."

That doesn't necessarily mean that investors should leap on to the natural gas bandwagon, no matter how low NGL prices go -- but it doesn't hurt to measure the landscape for opportunity.

"Experienced investors know to look for opportunities where the selling is overdone, and the asset is misunderstood," says James DiGeorgia, editor/publisher of *The Gold and Energy Advisor*. "Natural gas is such an opportunity," he says.

DiGeorgia points out that natural gas prices were up to $13 in 2008, and had fallen to $1.90 in April, 2012. He says that nose-dive has pushed natural gas stock prices down, in turn, with "many" down more than 50%.

He lays out an investment scenario for natural gas going forward, with lower NGL prices a key plank in that scenario.

"When buying an oversold, undervalued asset, you need to look for catalysts for higher prices," he advises.

Here are DiGeorgia's catalysts for natural gas stocks for the remainder of 2012:

- Natural gas has always been considered a bridge energy alternative for oil. It makes a lot of sense today.
- Crude oil is much more difficult, and expensive to find and develop. Natural gas is now abundant.
- Most energy companies are now focusing on oil and natural gas liquids now that natural gas prices are so low.

DiGeorgia says that fracing and time-sensitive leases from Uncle Sam play into the NGL equation for investors.

"Hydraulic fracturing and horizontal drilling technologies have allowed energy producers to find and develop an abundant source of natural gas," he says. "Natural gas production has also increased over the last few years partly because leases from the government require production. If you don't use it, you lose it.

"Also, dry natural gas is a byproduct of NGLs and oil exploration and production," DiGeorgia adds. "NGLs and oil exploration and production have increased, leading to higher natural gas production and inventories. Now, natural gas liquids are able to fetch about 50% of the price of crude oil."

Another factor for NGL pricing is momentum. DiGeorgia says the natural gas industry is working to build facilities that can convert its natural gas to liquefied natural gas so it can be imported globally. "Natural gas prices are much higher in other places in the world like Asian countries," he says. "After last year's earthquake and nuclear plant accidents, Japan would like to replace 30% of its nuclear energy with natural gas, and would be a likely customer for our liquefied natural gas."

Bruce Bullock, director of the Maguire Energy Institute at the SMU Cox School of Business, tells OGI that NGL prices, going forward, are the victim of lower demand -- and that trend will roll on through 2014, at least.

"NGL prices have been trending downward this year, significantly," he says. "Just as the shale drilling created a significant surplus of natural gas, drilling of so called "wet gas" shale plays rich in NGLs--as a response to dropping natural gas prices--has created a similar surplus in NGLs, causing the price to drop," Bullock says. "We can expect several years of depressed prices until demand catches up."

Bullock adds that NGLs have some huge potential positives--they can be used as both a feedstock and a fuel and have made the U.S. quite competitive in terms of locating new chemical and petrochemical manufacturing facilities, for example. But that advantage won't pan out for a few years.

"Until these are all on-line and increasing demands, we can expect prices to remain depressed," Bullock advises. "While some analysts are predicting a quicker rebound, natural gas prices have remained stubbornly low due to continued supply of the market. I would anticipate NGLs following a similar pattern."

That leaves the NGL market searching for a bottom, and natural gas investors searching for a "buy-in" point. Neither is likely until the end of 2012, if then, and only if the experts have it right. And the data seems to be on their side.

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1616 S. Voss, Suite 1000, Houston, Texas 77057-2627
Tel: +1.713.260.6400; Fax: +1.713.840.8585