Energy | Are High Prices Here To Stay?

Volatile, record-breaking gas, coal and power prices have diverging effects. We see prices remaining strong, with possible spikes, but likely moderating in 2022.

How this will shape 2022

Hydrocarbon producers will generate surplus cash. Financial policy decisions about capital expenditure, debt reduction, and shareholder returns are now important rating drivers.

Regulation and hedging can support ratings on utilities and power generation companies. Predictable regulation for networks, long-term contracted generation and hedging provide a cushion for many utilities since they can be a shield against spot price volatility.

Heavy industrial users of gas and power face tough decisions. Electricity prices and gas shortages have led to some shutdowns in 2021 for fertilizer producers and others. Securing supply for 2022 may mean committing to much higher prices, which would depress profit margins.

What we think and why

Oil prices will reduce somewhat in 2022. In our base case, we assume that Brent crude oil will average $65 a barrel from next year, and European gas, based on the Dutch benchmark Title Transfer Facility, will almost halve but remain higher than historical figures at $12 per million British thermal unit. We are mindful that supply constraints could push these prices higher.

Power prices will likely stabilize at a higher level. We have therefore rebased our price assumptions over 2022-2023 (see our related research). We also see increased volatility becoming the norm as the energy transition accelerates, owing to faster retirement of fossil fuel use and more unpredictable ramp-up of renewables capacity, alongside greater dependence on weather conditions.

Security of supply and affordability are again key energy issues. But global decarbonization isn’t going into reverse, as COP26 has signaled. While the current energy crisis may act as a wake-up call for markets and politicians, defining the role of gas in a decarbonized economy remains complex.

What could go wrong

Political intervention could deter investment. As already seen across Europe, governments may seek to manage the social impact of high prices through fiscal reforms or market adjustments. Such uncertainty about regulation and energy markets is usually negative for participants’ credit quality, but could also jeopardize investment decisions at a time when policies are aiming to accelerate the energy transition.

Power producers’ discipline could crack. A supply surge could up-end markets. A sharp increase in investments could reverse balance-sheet improvements made since 2020.

Price volatility brings spikes, troughs, and uncertainty. When unexpected price changes occur in commodity markets, energy producers can cope with them, but only if investments and shareholder distributions are still covered or can be adjusted when the cycle turns. For users, cost inflation may be the price of greater energy security.