



ENERGY UPDATE

2021 Q1 Review

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MARKET DETAILS¹

January Avg Pool Price

\$72.89/MWh

January Demand

10,266 MW (Avg)

February Avg Pool Price

\$151.98/MWh

February Demand

10,620 MW (Avg)

March Avg Pool Price

\$66.92/MWh

March Demand

9,784 MW (Avg)

Q1 Avg Pool Price

\$95.45/MWh

Note: \$10/MWh = \$0.01/kWh

FORWARD PRICES²

(as of April 21, 2021)

2021 - \$69.66/MWh

2022 - \$62.96/MWh

2023 - \$53.40/MWh

2024 - \$50.67/MWh

2025 - \$51.19/MWh

2026 - \$51.92/MWh

5 Year Avg:

\$56.48/MWh

Monthly Avg Actual Electricity Pool Price + Forwards
Jan 2014 to Dec 2026



Monthly Avg Actual Natural Gas Price + Forwards
Jan 2014 - Dec 2026



COMMENTARY

2021 Q1 General Overview

As we look back on 2020, pool prices for the year were relatively stable, with a full year average price of \$46.72/MWh (\$0.0467/kWh). January 2020 was the lone outlier month as the average pool price reached \$120.67/MWh while the remaining months of the year averaged in the \$40/MWh range. The economic impacts from COVID-19, the oil-price crash, moderate summer temperatures and a relatively warm start to this past winter were all factors leading to lower pool prices through much of 2020.

Both higher average pool prices and periods of significant volatility returned with a vengeance in the first quarter of 2021. The average pool price for the Q1 reached \$95.45/MWh. This is the second highest level for Q1 pool prices since deregulation commenced in 2001, second only to the first three months of deregulation in Q1 2001.

The Q1 2021 quarterly average was particularly impacted by an average pool price of \$151.98/MWh in February 2021, which itself was the third highest monthly average pool price ever, since deregulation began, and the highest level reached since July 2007. The key drivers contributing to the high pool prices were a period of very cold weather in the first two weeks of the month, leading to higher electricity demands, and a significant

reduction in wind generation during that same period, which put upward pressure on prices. These factors of higher demand and lower supply also provided the market conditions for more opportunistic pricing behavior by generators, which also contributed to increased pool prices.

Pool prices were lower in January 2021 and March 2021, at \$72.89/MWh and \$66.92/MWh respectively, but still contained periods of higher prices driven generally by the same factors mentioned above.

On-peak pool prices (defined for this report as 7:00 am to 11:00 pm weekdays) averaged \$136.72/MWh for Q1, while off-peak prices averaged \$55.45/MWh. Higher prices during weekday hours are expected, but we have also seen higher prices in Q1 during the late evening and weekend hours which is unusual for the Alberta marketplace.

Although the Alberta economy is showing signs of life with both oil and natural gas prices rising, along with modest signs of an overall economic recovery, as we continue to navigate through the COVID-19 pandemic, we are not currently seeing any significant changes in electricity demands.

Pool prices for April 2021 have continued the upward trend seen in Q1, with pool

prices for the month settling at \$87.99/MWh. An outage at a large natural gas generating unit appears to be a primary factor contributing to this price level. Pool prices are historically lower in April to mid-June, with typical price volatility occurring in later June to middle August arising from hot weather and the resulting increase in electricity demand as consumers turn on their air conditioners and ceiling fans.

Electricity Markets


Background

The Alberta electricity market continues to operate under its long-standing “energy-only price” design, which has been in place in its current form since January 2001.

As discussed in our last market update, January 1, 2021 represented the beginning of a new era in the wholesale electricity market. Some electricity generation units (coal and hydro) that were previously being managed by a quasi-government agency under long-term power purchase arrangements (PPAs), were returned to the full offer/dispatch control of their private sector owners.



EXPENSE MANAGEMENT



As we also highlighted in our last report, these private sector owners will undertake rationale economic behavior, and take actions to ensure prices are able to generate and sustain reasonable economic returns while still being mindful of all market rules and fair competition guidelines.

We have absolutely seen evidence of this behavior so far in Q1 of 2021, and in April as well, via different pricing strategies of the generating units. This is a significant contributing cause to the higher prices that we have been experiencing in the Alberta power markets.

Current Price Environment

The high and volatile pool prices in Q1 as discussed above, have put additional upward pressure on forward prices for the balance of 2021 and for most of 2022.

Forward prices for the balance of 2021 are in the \$70/MWh range, up about \$5/MWh from our last report in late January. These forward prices translate to a fixed retail price for the balance of the year in the \$0.08/kWh range depending on the product and load profile. Forward prices for 2022 are in the \$63/MWh range, up about \$2/MWh from our last report. These forward prices translate to a fixed retail price for that year in the \$0.07/kWh range.

However, forward prices for 2023 to 2025 have remained relatively constant and

have in fact, slightly decreased. We also see reasonable pricing for 2026 as well. New generation supply is expected to come on-line in later 2022 and into 2023, from renewable projects and from some selected new/re-powered gas generation projects, which will increase the generation supply cushion in the market. Increased supply has a dampening effect on prices so this should provide some market protection from the higher volatile prices experienced thus far in 2021.

8760 Recommendation:

8760 continues to recommend exercising some caution if organizations are only contracting for 2021 and/or 2022. If the nature of your business and risk tolerance cannot tolerate volatility, we suggest contracting for a short-term fixed rate despite the current high levels of “insurance premium” to do so. For selected clients, or in specialized situations, an index/floating strategy or partial hedging strategy for these periods may be worth considering if the nature of your business and risk tolerance can tolerate some volatility as this may result in an overall lower cost for power.

Forward prices for 2023 to 2026 are in the lower \$0.05/kWh range. These forward prices imply a retail price in the upper \$0.05/kWh range, which we believe is good value for those time periods.

Contracting for a longer term from today, for example from 2021 to 2024/2025/2026, or from 2022 to 2024/2025/2026, would result in a lower average price as the lower forward costs in the later years would offset the higher forwards costs for 2021/22. Using this approach, we would expect a retail price in the lower \$0.06/kWh range depending on the exact term chosen. We suggest this is fair value and a prudent approach as a continued uptick in prices is expected.

Going forward we believe these price levels will be the new market reality.

Final Recommendations:

CAUTION for shorter-term contracts (2021/2022)

BUY for longer-term contracts (2023 to 2026, or for combined terms of 2021/2022 to 2024/2025/2026)





Natural Gas

Background

The Alberta natural gas market continues under the same market structure as in recent years. Natural gas prices have been gradually declining the last several years, due to an abundance of supply in both North America and Alberta. The supply surplus has been particularly accentuated in Alberta due to lack of pipeline capacity to move surplus gas out of the province to other markets.

Current Price Environment

Despite the general long-term declining trend, spot prices have been showing an upward trend over the last year, particularly this past fall/winter.

As background, simple average spot prices were \$2.11/GJ in 2020, up from \$1.66/GJ for 2019. Simple average spot prices were \$2.98/GJ for Q1 2021, with prices averaging \$3.77/GJ for February 2021 during the cold snap experienced in Alberta. The extreme cold weather in the U.S., including the catastrophe in Texas, did have a significant impact on North American gas markets and was also a secondary contributing factor to the higher prices in February. The \$3.77/GJ price is the highest monthly average gas price experienced in Alberta since September 2014. For this past winter

season, simple average spot prices were \$2.82/GJ for the period November 2020 to March 2021.

Fundamental factors do suggest an increasing trend in gas prices, particularly over the next one to two years, and particularly for this coming 2021-2022 winter season. Factors behind the increase in gas prices include continued lower levels of drilling activity for both oil and gas, decreased levels of gas in storage, the growth of natural gas-fired generation (replacing coal and nuclear), continued strong commercial and industrial demand and the growth of liquified natural gas (LNG) exports primarily in the U.S. (and Canada to a small degree later in the decade). These factors have always been present, but they have started to make a more pronounced impact in the last six to twelve months. The current strength of the Canadian dollar relative to the U.S. dollar is offsetting these factors to a degree and is marginally reducing the cost to buy gas in Alberta/Canada.

Forward prices are in the high \$2/GJ to low \$3/GJ range from now to March 2022. Forward prices do drop for subsequent years and are in the \$2.30 to \$2.40/GJ range for these years, out to 2026. This translates into fixed retail prices in the \$2.60-\$2.70/GJ range for most terms, for the 2021/2022 to the 2024/2025/2026 timeframes.

Carbon Tax

The Federal Carbon Tax increased to \$2.10/GJ effective April 1, 2021 (based on an underlying price of \$40/tonne of carbon dioxide or "CO₂"). It will increase to \$2.63/GJ effective April 1, 2022 (based on \$50/tonne of CO₂), with further annual incremental increases in the CO₂ price of \$15/tonne until it reaches \$170/tonne by 2030. If/when the federal carbon tax reaches \$170/tonne, and assuming no Alberta replacement plan overrides it, the federal carbon tax on natural gas would be approximately a shocking \$9/GJ.

On March 25, 2021, the Supreme Court of Canada issued its ruling on the challenge by several provinces, including Alberta, on whether the Federal government has the constitutional jurisdiction to impose carbon taxes. In a 6 to 3 ruling, the Court did find that fighting climate change is a matter of national interest, it requires a coordinated approach for the country and the Federal government does indeed have the right to take the lead and impose a minimum carbon pricing standard for the provinces.





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Like most discussions on this topic, even the Supreme Court itself was fairly divided in its ruling. The provinces that lost the challenge will at least get some vindication from the minority opinions of the dissenting judges.

The Supreme Court ruling now puts the ball in Alberta's court, for the UCP government (or any other governing party) to try and come up with its own "made in Alberta" plan. The federal government would have to be convinced that any such plan meets the minimum federal standards.

Of course, an Alberta provincial election in fall 2022, and the ever-present possibility of a federal election due to the current minority government, may or may not result in future changes. The federal Conservative opposition party has recently announced a proposal for its form of carbon taxation, which is less punitive than the current federal regime, but many will question its effectiveness as a result.

One thing is highly certain, a price on carbon in one form or another will be here to stay no matter which party obtains power provincially or federally.

8760's Recommendation: Fix or Float

8760 remains of the opinion that current spot and forward prices still represent good value for both public and private sector clients. Our recommendations with respect to product selection strategy includes:

- Index natural gas – floating the market and accepting the average monthly index price is a viable strategy for many customers given the relatively low volatility in natural gas markets. The index price will almost always represent the lowest cost option in relation to fixed price contracts, particularly over a longer timeframe. This could be of particular focus for private sector customers looking to maximize savings so long as clients are willing to risk some short-lived volatility on occasion. We suggest this strategy does come with increased short-term risk of higher costs for winter 2021/2022.
- Fixed price contracts – this strategy offers the greatest cost certainty which may be required/preferred for some customers. Fixing your price also offers incremental protection for expected higher gas prices in winter 2021/2022. As per above, retail prices for fixed price plans are generally in the mid-upper \$2/GJ range, for both shorter and longer terms, which we suggest is favorable pricing. For selected private sector customers and all/most public sector customers, we recommend fixing 50% or 75% of your natural gas requirements for as long as your risk tolerance or corporate governance permits. For public entities, fixed price contracts are available at reasonable prices for term lengths out to 2028, which may be attractive in some circumstances.

Final Recommendation: BUY

¹Pool prices and demand levels attained from AESO system reports.

²Forward prices provided by CHASE Enterprises Ltd. Forward price for 2021 is calculated for April 1 to December 31.