IHS Energy
COAL & ENERGY
Price Report Volume 16, No. 91 May 12, 2014

Market Commentary by Jim Thompson

- **BNSF's delivery issues have been well noted, but at the recently completed Eastern Fuel Buyers Conference in Orlando the discussion was both CSX and Norfolk Southern have showed signs of strain in the East.**
- **One source believes that if CSX rail pricing stays above $60/ton there could be a shift of 10 million to 12 million tons from the met market into the thermal market.**
- **Utility fuel buyers still haven't seen a substantial decline in the number of coal supply offers they are receiving or in the tonnage they are being offered. Several buyers said they are still seeing normal to better-than-normal response to RFPs.**
- **Natgas storage levels are still 43.0% below year-ago levels and 48.2% below the 5-year average, according to the EIA. There were 26 more weeks in the injection season when the EIA released its latest update, May 8.**

"By the time I get to Phoenix she'll be rising. She'll find the note I left hanging on her door. She'll laugh when she reads the part that says I'm leaving, 'cause I've left that girl, so many times before."
Jimmy Webb

Being asked 10 or 12 times for my key takeaways from last week's Eastern Fuel Buyers Conference, I am given to assume that folks are interested in the key takeaways from the Eastern Fuel Buyers Conference -- either that or people wanted to be

See Market Commentary, page 2

Wyoming governor, WVCA speak out on EPA regulations

Wyoming Gov. Matt Mead sent a letter to EPA Administrator Gina McCarthy on Friday asking that the agency withdraw its proposal to require carbon capture technology on all new coal-fired power plants.

It was the last day of public comments on the proposed rule, which the EPA says would go into effect as early as next year.

In his letter Mead said the standard is a threat not only to the Wyoming coal industry – which employs 7,000 with a payroll of about $560 million – but it's a threat to the economy of the entire state.

"Numerous air regulations have been proposed and promulgated to eliminate use of the United States' leading source of low-cost, reliable energy — coal," Mead said in his letter. "This proposal is yet one more example. The proposed regulation will adversely impact Wyoming's economy as the leading coal supplier to the United States. It lacks sound reasoning, technological justification and will not provide regulatory certainty."

In the letter Mead said the agency has overplayed its hand on how viable carbon-capture technology really is. Wyoming has been at the forefront of a series of lawsuits against the agency's rules, none of which have to pass muster with votes from congress.

Wyoming coal production has slipped from more than 430 million tons in 2011 to 385 million tons last year, according to a recent state report. Those numbers are expected to improve this year and in 2015, but could again be impacted by EPA's next round of regulations.

The West Virginia Coal Association invited state lawmakers, heads of agencies and others involved in the coal industry to a meeting Friday and WVCA President Bill Raney said it's important the people understand the potential hazards if the proposed rule becomes actual regulation.

"During the polar vortex….(the electric companies) came very, very close to a grid failure," Raney said. "There's three plants we have here in West Virginia that (the EPA) is going to close next year that were operating during that vortex at 89 percent capacity.

"They're not going to be here in 2015. So I don't know what (the EPA) is going to do. They have not addressed that. The EPA says they don't have to be concerned with that."

Coal sales improve for Vectren

Vectren Corporation reported first quarter net income of $51.2 million compared to net income of $49.8 million during the first quarter of 2013.

Utility Group earnings were $61.3 million, or $0.74 per share, in the first quarter of 2014, compared to $55.1 million, or $0.67 per share, in 2013. Nonutility Group losses were ($9.7) million in the first quarter of 2014, compared to a loss of ($5.4) million in 2013. Excluding the results of ProLiance, the first quarter loss in 2013 was ($0.8) million.

"We experienced much improved results from our coal mining operation compared to last year given that the second Oaktown mine is now fully operational and the cost improvement initiatives implemented at the Prosperity mine are working," said Carl Chapman, Vectren's chairman, president and CEO.

Continued on page 4

Market Commentary

Continued from page 1

polite but couldn't think of anything else to say to me.

We all knew the weather was great.

Beyond that the most important takeaway -- people are still mightily concerned about transportation.

EFBC draws some Western delegates, of course, but its primary focus is on coal issues east of the Mississippi River. That being the case, Powder River Basin delivery concerns weren't at the forefront the way they were during the recently completed National Coal Transportation Association spring meeting.

But BNSF's challenges were a subject of conversation. There were more complaints than I've heard in a while that CSX and Norfolk Southern have had some hiccups. And one source mentioned that Union Pacific and Canadian National haven't navigated totally still waters.

When people are talking about railroad delivery shortfalls one can surmise that inventory problems remain. At more than one large utility the threat of running out of PRB coal persists. So power plants are still being taken out of dispatch at times in order to conserve inventory.

That's a big deal. It is certainly bullish for coal burn at bituminous coal plants.

Gimme some trains

This helps to explain why service from CSX and NS is under the microscope. A buyer with one Eastern utility said his coal burn will be up 40% compared to where it was in 2012 and 2013. And the current projection is that the increased demand will continue through 2015.

Suddenly every unit train is precious. There are power plants in the East with less than 10 days of inventory.

Seth Schwartz, president of Energy Ventures Analysis, noted during his presentation to the EFBC that stockpiles were at 49.6 days of burn by the end of March, the lowest level since August 2008. He also pointed out that his company's inventory measure is based on historical plant usage, while many utilities measure days of available burn by their expectations of future usage.

Assume that a "look back" inventory assessment would target current Eastern inventories at 50 days of supply. A 40% increase in anticipated burn puts real inventory at perhaps 30 days of supply.

The market is behaving as if we are in a 30 days scenario. That's true at least for everything except prices outside the PRB. Prices are more reflective of a 50-day "normal" inventory environment.

What we're seeing

Why is that? Let's consider a few of those EFBC takeaways --

- Low international prices are curtailing U.S. exports and creating fresh opportunities for imports. "If CSX rail stays above $60.00, I think 10-12 million tons shift from met to thermal," one highly respected export source said. That doesn't include thermal exports that could be turned back to the domestic market. And it doesn't include possible import growth of, say, 1.5 million to 2 million tons. The total "swing" that results from the imbalance between supply/demand in the U.S. versus supply/demand around the globe might be in the neighborhood of 20 million tons. "World coal markets" are the primary impediment to U.S. coal price increases, according to Seth.
- The metallurgical coal market is awful. That explains the comment above from the export source. Low met prices are "going to drive every pound of high-vol coal that can be taken out of the export market back to your boilers," Seth told utility buyers among the EFBC delegation. "There really is too much coal in the market. Somebody needs to close coal mines."
- Utility fuel buyers still haven't seen a substantial decline in the number of coal supply offers they are receiving or in the tonnage they are being offered. Several buyers said they are still seeing normal to better-than-normal response to RFPs. A comment by Seth addressed that point. "Why won't people close money-losing coal mines? The market is terrible." The reason, in EVA's view, is the high cost associated with maintaining an idle mine.
- People are still waiting to see whether we have a mild, normal or hot summer. Opinions are mixed, but some sources think a mild summer would be sufficiently significant to prevent supply/demand to swing to the coal producers' favor.
- Natural gas prices haven't responded to the gas storage deficit as robustly as many folks had anticipated. While $4.50ish Henry Hub numbers through to winter aren't negative for coal burn, they aren't conducive to substantial increases in coal prices. And the forward curve is at $4.70ish prices for the winter month -- still not supportive of price increases, especially from Central Appalachia. In fact, natgas prices, at many locations, aren't supportive of heavier CAPP coal burn.

New or increased second half production from mines in the Illinois Basin (Alliance Coal, Foresight Energy and White Oak Resources) and from mines in Northern Appalachia (Alliance, CONSOL Energy and Murray Energy) has created some confidence that coal supply will be adequate even if the summer isn't mild.

All of those factors are valid to some extent, at least, though the last one might be overly optimistic. It appears that most of the extra coal expected to be produced in the second half of the year has already been contracted.

Extra weekend work might create 2-5 million tons of additional, uncovered production, but probably not more than that. The low end of the 2-5 million-ton range might be more likely than the high end.

The 20 million-ton international swing is guesswork, but based on a lot of conservations, the number seems to be pretty good.

Of course we could have a mild summer. And we could have a hot one. When you're hot you're hot, and when you're not you're not.

It appears more and likely that natgas prices are going to behave differently than one would expect based on the storage outlook. Obviously the market is optimistic about natgas production. So far the optimism seems sufficient to make people sanguine about the prospect of entering winter short storage and surviving without supply-related shocks.

Why didn't you warn me?

There is still time, though, for an "Oh (bleep)!" turn in sentiment that creates the contango market necessary to force

See Market Commentary, page 3

Market Commentary

Continued from page 2

more natgas into storage. Remember, a price spread is necessary to incentivize traders to push natgas into storage.

It's too late for natgas storage to be refilled to a level close to where it was when we entered last winter. But it isn't too late for the market to make a strong effort to significantly improve the refill picture.

Natgas storage levels are still 43.0% below year-ago levels and 48.2% below the 5-year average, according to the EIA. There were 26 more weeks in the injection season when the EIA released its latest update, May 8.

In order to reach EIA's forecasted end of October working natural gas inventory level of 3,405 Bcf, an average injection of 90 Bcf per week will need to occur through the end of October. EIA's forecast for the end of October inventory levels is below the 5-year (2009-13) minimum value of 3,792 Bcf.

To reach the 5-year minimum, average weekly injections through the end of October would need to be 105 Bcf. Injections for the week ended May 2 were 74 Bcf. From the week ended April 4 to the week ended May 2, net storage injections totaled 233 Bcf.

There isn't anything there to suggest that injections through the end of the storage season will average anywhere close to 90 Bcf/week, much less 105 Bcf/week, particularly when July and August demand is factored.

Who wears short shorts?

We'll be short natgas headed into the winter, which means we'll almost certainly be short gas headed into next spring, which means we'll probably still be looking for refill. That explains why utilities are anticipating heavy coal burn through next year.

In the meantime, U.S. coal production was down 1.2% year-on-year for the 52 weeks ended May 3. Wyoming production was down 0.3% though PRB power has been seamlessly in the money throughout that stretch. National railcar loadings were down 1.7%, according to the EIA's estimate.

Electric utility coal stockpiles declined by more than 40 million tons from April 2013 through January of this year. The EIA expects electric utility inventories to be at 121.8 million tons by the end of this year, down from 148.0 million tons at the end of '13. But the EIA expects coal inventories to grow to 126.6 million tons by the end of next year.

Where will the inventory growth come from? It doesn't seem likely that natgas prices will moderate enough to push coal back out of regular dispatch. Nobody is confident that PRB deliveries will increase substantially until deep into 2015, if then. Bituminous power plants will be dispatched more heavily than anyone would have predicted a few months ago.

The railroads are under intense pressure. It takes roughly 18 months from order date to get delivery of a locomotive. BNSF is adding 500 to its fleet. Other railroads are adding power as well. CSX just leased the last 10 locomotives available in the U.S.

The EIA figures U.S. coal production will grow in 2014 4.4% to 1.028 million tons. But by May 3 it was down year-to-date by 0.4%. Production the week ended May 3 was up 2.15 from the comparable 2013 week, but that still doesn't create a lot of confidence that the current 0.4% deficit will be eliminated a 4.4% growth achieved.

Given transportation disarray in the PRB, one wonders how U.S. coal production can reach EIA expectations.

The EIA expects the electric power sector to consume 901.4 million tons of coal this year, up 4.8% from 858.4 million tons in 2014. It might be that utility stockpiles must be drawn down further than projected in order to accommodate that extra demand. That could be the case this year as well as next year.

I can see for miles

The message might be pay me now or pay me later. The question is whether the PRB's problems cause bituminous supply to be swamped by relentless demand even given the anticipated growth in imports and recession of exports.

For now that hasn't happened, though that is at least in part because utilities had a great deal of inventory to burn. That is no longer the case.

Assume that domestic thermal prices stall at or near current levels. Will met producers opt to continue to push coal into the thermal market or will they bite the bullet and idle more production?

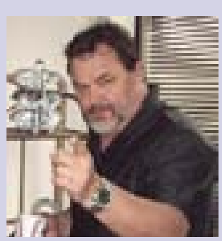
Will international prices remain low through 2015, allowing imports to continue to flow? Or will an increase in netbacks for Colombian coal moved outside the U.S. force a price increase here in order to maintain that supply source?

Will the met market recover enough of its mojo to regain the hearts and production of U.S. high-vol producers?

Ultimately, the question is whether adequate coal supply is sustainable through 2015.

Will Bob Seger prevail? "You always won every time you placed a bet..." Or does Jimmy Webb get the last word?

"By the time I make Oklahoma, she'll be sleeping. She'll turn softly and call my name out low. And she'll cry just to think I'd really leave her, though time and time I've tried to tell her so. She just didn't know I would really go."



Vectren ...

CONTINUED FROM PAGE 1

Vectren Fuels Coal Mining's results were a loss of $1.1 million during the quarter, compared to a loss of $6 million in the first quarter of 2013. Coal revenues were $81.5 million in the first quarter compared to revenues of $63.1 million in first quarter 2013, primarily due to additional volumes sold of 300,000 tons as well as an increased sales price per ton.

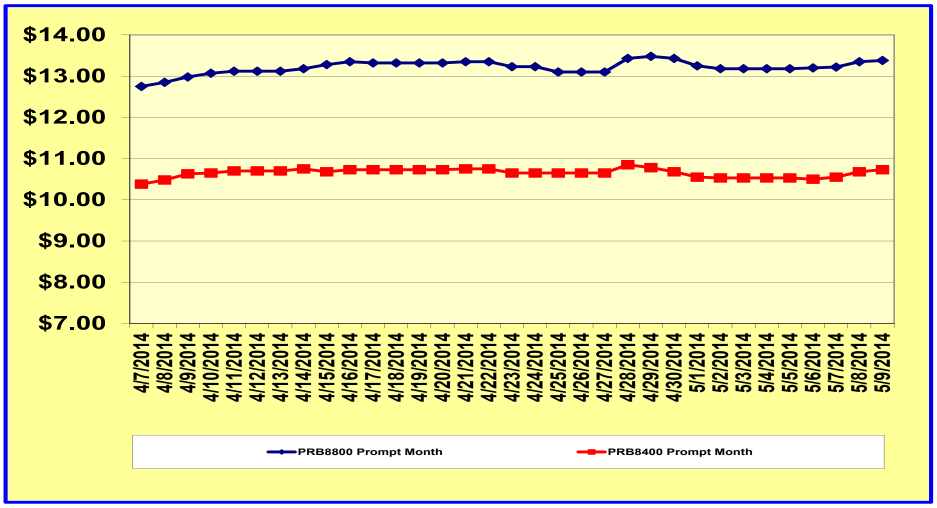
"While additional cost improvement measures are still being implemented at Prosperity mine, substantial progress was made in the second half of 2013 and continued into the first quarter of 2014," the company said. "The execution of the revised mining plan has resulted in significant improvement in the production costs at this mine."

Vectren Fuels' expected production is approximately 7.3 million tons in 2014, compared to 6.2 million tons in 2013. Sales in 2014 are estimated at 7.6 million tons, compared to 6.2 million tons in 2013.

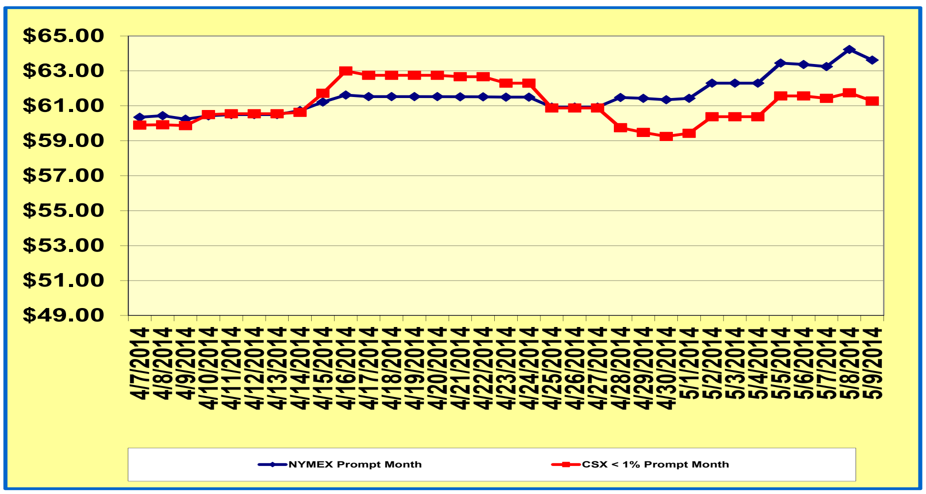
"The expected production increase in 2014 primarily relates to a full year of operation at the second mine at the company's Oaktown mining complex, which opened during the second quarter of 2013," the company said. "The increased sales in 2014 include 300,000 tons under contract carried over from 2013 that were not sold due to weather-related delivery issues. These tons were held in inventory at Dec. 31, 2013.

"As of Mar. 31, 2014, nearly all of the expected 2014 sales are committed and priced. Longer term, the company continues to believe that there will be reduced coal volumes available from Central Appalachia due to increased regulation and that the large number of scrubbers to be installed throughout the United States, including the Midwest, should continue to drive stronger demand for Illinois Basin coal."

Prompt Month for PRB 8800 and PRB 8400 Coals



Prompt Month for CSX < 1% & NYMEX Coals



Month Codes: Jan-F; Feb-G; Mar-H; Apr-J; May-K; Jun-M; Jul-N; Aug-Q; Sep-U; Oct-V; Nov-X; Dec-Z

OTC NYMEX Coal

(12,000 Btu/lb., 1% sulfur)

Term	Vol	Price	Bid	Offer
M14	5B	$0.00	$63.00	$64.00
N14	5B	$0.00	$67.25	$68.25
Q314	5B	$65.25	$64.90	$65.90
Q414	5B	$0.00	$65.30	$66.30
Q115	5B	$0.00	$65.70	$66.70
Q215	5B	$0.00	$65.95	$66.95
Q315	5B	$0.00	$66.15	$67.15
Q415	5B	$0.00	$66.40	$67.40
Q116	5B	$0.00	$67.25	$68.25
CY15	5B	$0.00	$66.05	$67.05
CY16	5B	$0.00	$68.55	$69.55

OTC PRB 8800

(at 0.8 lbs. SO2)

Term	Vol	Price	Bid	Offer
M14	1T	$13.40	$13.20	$13.60
N14	1T	$0.00	$13.30	$13.70
Q314	1T	$0.00	$13.45	$13.85
Q414	5k	$13.90	$13.70	$14.10
Q115	1T	$0.00	$13.85	$14.25
Q215	1T	$0.00	$14.10	$14.50
Q315	1T	$0.00	$14.30	$14.70
Q415	1T	$0.00	$14.55	$14.95
Q116	1T	$0.00	$14.80	$15.20
CY15	5k	$14.40	$14.20	$14.60
CY16	1T	$0.00	$15.20	$15.60

CSX-BSK < 1%

Term	Vol	Price	Bid	Offer
M14	1T	$0.00	$60.75	$61.75
N14	1T	$0.00	$62.50	$63.50
Q314	5k	$63.75	$62.85	$63.85
Q314	5k	$63.60	$0.00	$0.00
Q414	1T	$0.00	$64.00	$65.00
Q115	1T	$0.00	$64.50	$65.50
Q215	1T	$0.00	$64.85	$65.85
Q315	1T	$0.00	$65.15	$66.15
Q415	1T	$0.00	$65.50	$66.50
Q116	1T	$0.00	$66.30	$67.30
CY15	1T	$0.00	$65.00	$66.00
CY16	1T	$0.00	$67.50	$68.50

Bid and offer prices provided by ICAP Energy

Hill Daily Index ©

Quality	Hill Price	Hill Index	Last Trades
NYMEX Current Quarter, Plus One	$65.25	272.44	05/09/14
NYMEX Current Quarter, Plus Two	$65.00	271.40	05/07/14
NYMEX Next Calendar Year	$64.75	270.35	04/25/14
PRB 8,800 Current Quarter, Plus One	$13.85	310.54	04/30/14
PRB 8,800 Current Quarter, Plus Two	$13.90	311.66	05/09/14
PRB 8,800 Next Calendar Year	$14.40	322.87	05/09/14
PRB 8,400 Current Quarter, Plus One	$10.20	294.80	03/12/14
PRB 8,400 Current Quarter, Plus Two	$0.00	0.00	07/15/13
PRB 8,400 Next Calendar Year	$0.00	0.00	07/15/13
CSX <1% sulfur Current Quarter, Plus One	$63.68	244.92	05/09/14
CSX <1% sulfur Current Quarter, Plus Two	$64.25	247.12	05/07/14
CSX <1% sulfur Next Calendar Year	$65.75	252.88	05/08/14
CSX compliance Current Quarter, Plus One	$0.00	0.00	03/09/11
CSX compliance Next Calendar Year	$0.00	0.00	10/15/07
NS <1% sulfur Current Quarter, Plus One	$63.50	244.23	12/05/13
NS <1% sulfur Next Calendar Year	$63.50	244.23	12/05/13
NS compliance Current Quarter, Plus One	$0.00	0.00	12/09/10
NS compliance Next Calendar Year	$0.00	0.00	12/19/11

All prices are based exclusively on latest actual trades, and are indexed against market as of 12/28/99, w hen NYMEX-spec coal had been traded most recently at $23.95/ton, 8,800 Btu/lb. Pow der River Basin coal at $4.46/ton and 8,400 Btu/lb. PRB coal at $3.46/ ton. The eastern rail index is measured against an arbitrary price of $26.00/ton. "Hill Index" reflects w eighted average of prices recorded on most recent trading day. On days w hen no trades occur, published index remains at previous level. "Mid-market" reflects mid-point of current bid/ask values.

OTC Broker Index

May 9, 2014

	NYMEX look-alike	CSX 12,500 -1% sulfur	PRB 8,400	PRB 8,800
Prompt Month	63.62 -0.61	61.28 -0.47	10.73 0.05	13.38 0.03
Prompt Quarter	65.11 -0.55	63.41 -0.83	10.75 0.00	13.58 0.15

NYMEX Futures

Term	Last	Open High	Open Low	Most Recent Settle	Prev. Day Total Vol
Natural Gas (Henry Hub)					
M14	4.484	4.535	4.463	4.531	16841
N14	4.491	4.541	4.472	4.54	5383
Crude Oil					
M14	100.81	100.88	99.93	99.99	55476
N14	100.11	100.19	99.26	99.31	20857

Price Markers

NAPP **13,000 Btu/lb., 3.4 lbs SO2/MMBtu, $62.50/ton (RAIL)**
ILB **11,800 Btu/lb., 4.8 lbs. SO2/MMBtu, $47.25/ton**

For subscription information, contact
EMEA
Tel: +44 1344 328155
Email CoalEMEA@ihs.com
APAC
Email: CoalAPAC@ihs.com
Americas
Tel: +1 303 736 3457
Email:CoalAmericas@ihs.com