



Contact: Daphne Magnuson
(202) 824-7205

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AGA Survey Finds Natural Gas Utilities Intensified Use of Strategies to Manage Price Fluctuations in the Winter of 2005-2006, Following Hurricanes and High Commodity Prices

Washington, D.C. – In light of challenging market conditions, natural gas utilities stepped up their efforts to help minimize the impact of price fluctuations on their customers for the 2005-2006 winter, according to a new report by the American Gas Association (AGA). The report looks back at the conditions leading up to the 2005-2006 winter heating season, starting in the summer of 2005 when natural gas prices spiked in response to unusually hot weather that increased the demand for natural gas-fired electricity generation. This price spike was further exacerbated in the fall when multiple hurricanes shut down domestic production sources for months – at times eliminating more than 20 percent of the nation’s daily domestic supply.

The report – *LDC Supply Portfolio Management During the 2005-2006 Winter Heating Season* – documents gas delivery operations last winter, and provides insights into how natural gas utilities purchased and managed their gas supplies, while facing unprecedented supply challenges. This year’s report reflects responses from 29 natural gas utilities in 24 states.

“In the wake of Hurricane Katrina, spot market prices soared and the government projected that winter heating season bills would increase by 50 percent -- or more. It was clear to many natural gas utilities that hedging a portion of their gas supply and storing natural gas underground would help to shield their customers from potentially unprecedented increases in natural gas prices,” AGA President David N. Parker said, at an energy forum sponsored by CQ.

Natural gas utilities incorporated a number of tools, including financial hedging, underground gas storage and other techniques in order to cushion families and businesses from rising natural gas prices, according to the survey.

However, “Many consumers did pay significantly more to heat their homes during the 2005-2006 winter heating season. That did happen,” said Parker. “What didn’t happen was January – literally.” The month of January was nearly 30 percent warmer than normal.

As in previous years, gas utilities that responded to AGA’s survey reported purchasing natural gas supplies for their customers use during “peak month” under a mix of long-term (12 months+), mid-term (1-12 months) and spot contracts

- Long-term agreements, defined as one year or longer, were used by 20 of 29 companies within their “peak-month” gas supply portfolio, however natural gas purchased under these agreements comprised less than 50 percent of purchased peak-month gas for most of the companies in the survey.
- Mid-term agreements were utilized by all 29 companies; 16 companies used monthly agreements.
- Daily agreements were used by 18 companies.

“It should be no surprise that very few companies construct a supply portfolio with all of their eggs in one basket,” commented Chris McGill, AGA managing director of policy analysis and the report’s author. “In many cases, longer-term contracts contribute to baseload obligations, while shorter-term contracts allow companies to respond to market changes,” he said.

As in previous years, underground storage of natural gas was front and center in utilities’ gas supply portfolios during the winter of 2005-2006. Nearly all of the utilities surveyed indicated they used natural gas storage to meet peak demand and about half of the companies (15 of 29) indicated they were constructing or examining the potential for adding underground storage.

“Reliability is paramount. On winter’s coldest day, utilities’ ability to pull gas from underground storage to keep people warm remains critically important,” McGill said.

Most (87 percent) of the utilities surveyed said they had used financial instruments to hedge at least a portion of the natural gas they purchased on behalf of customers. Four years ago, only 55 percent of the survey respondents used financial tools. In 2004-2005, 70 percent of survey respondents reported using financial tools. Utilities used options, swaps and futures and even fixed-price contracts to protect a greater portion of their natural gas supplies from price fluctuations, thus providing greater predictability in gas costs for consumers, according to the report. Other companies combined the use of storage and financial tools to do the same.

Natural gas is the most popular home-heating fuel in the United States, with 52 percent of the nation’s heated households. It is also dominant in the new-home market, heating 69 percent of newly built single-family homes in recent years, AGA said.

Copies of AGA’s *Local Distribution Companies’ Supply Portfolio Management During the 2005-2006 Winter Heating Season* are available free of charge to AGA members and others who subscribe to AGA’s Policy Analysis series at www.aga.org in “Stats and Studies.”

The American Gas Association, founded in 1918, represents 197 local energy utility companies that deliver natural gas to more than 56 million homes, businesses and industries throughout the United States. Natural gas meets almost one-fourth of the United States’ energy needs. For more information, please visit www.aga.org.