Global energy markets are in the early stages of a once-in-a-generation supply spike as hydraulic fracturing in the United States releases increasing volumes of oil and gas. Producer and consumer countries, energy companies and trading houses alike are trying to calculate what the fracking revolution means for the price of oil and gas in the years ahead. But fracking is only one among many uncertainties facing the global energy industry.

The political fall-out from the 2011 Arab Spring still resonates across Middle East and North African oil and gas producing countries. Sanctions-bound Iran could see output rise or fall sharply, depending on its nuclear negotiations with the West. Trade flows are changing rapidly, sending China to the top of the league of world oil importers. The banks that dominated the energy trading landscape over the past 20 years are facing increased regulatory pressure, opening the door for already powerful trading houses to take a larger market share.

The Reuters Global Commodities Summit looked to answer all the above questions, generating exclusive, news stories for Thomson Reuters clients. Read on for highlights from the week.
China may have overtaken the United States as the world’s biggest oil importer, but America is now the land of opportunity for traders looking to profit off energy markets, thanks to changes brought by the shale gas revolution.

After a generation in which traders salivated over emerging markets, executives at the Reuters Global Commodities Summit this week spoke about the good old fashioned U.S.A. - soon to overtake Russia as the world’s biggest oil producer - the way they once used to gush about BRICS.

“The shale oil revolution has been faster than people generally anticipated. The production increases for oil and gas have been quicker than even the most optimistic forecasts,” said Torbjorn Tornqvist, CEO of Swiss trading house Gunvor, which earned its name as one of the main traders of oil from Russia.

“Five years ago the U.S. was net importing more than 2 million barrels a day of refined oil products, and maybe even up to 3 million bpd at the peak of the resource boom. Now it is a net exporter of around 1.2 million bpd. That’s a huge swing in such a short period of time.”

Freepoint chief executive David Messer said his biggest focus was North America as the production of oil and gas was increasing faster than the infrastructure can accommodate.
“That creates all sorts of logistics opportunities where we are involved,” he said.

The changes in the United States are not only big, they are complicated, music to the ears of traders who thrive on market volatility and price differentials.

“The shale gas boom and plentiful supply of gas have created a series of very interesting and complex knock-on effects,” said Daniel Jaeggi, co-founder of Mercuria. “If the U.S. burns more gas, what happens to the coal, and coal needs to find a way out of the U.S.?”

Tornqvist of Gunvor noted the opportunities to make money as “ hugely efficient” U.S. refineries rev up production and become big exporters. Among the opportunities: the spreads between different types of crude needed for refining.

“There are obviously tremendous arbitrage opportunities given the logistical bottlenecks between domestic crude oils and imported crude oils,’’ he said.

All that excitement is a contrast with China, where, despite huge volumes, there is little money to be made for freewheeling traders, thanks to a centralized system in which imports are largely controlled by state entities.

“This is going to be a big volume but very, very small margin business,” Ian Taylor, chief executive of the world’s top trading house Vitol VITOLV.U, told the summit.

**GIANTS**

The global commodity boom of the past decade has turned little-known trading houses into multinational giants with assets across many continents and made their executives staggeringly rich.

Glencore Xstrata (GLEN.L) went public and is valued by the market at over $70 billion. Vitol remains private, owned by some 300 employees. With an annual turnover of $300 billion, it buys and sells more energy each year than ExxonMobil produces.

But to continue to make big profits, the trade houses need markets that are not only big but interesting.

China overtook the United States as the biggest net crude oil importer in September, but its rise offers few opportunities.

As its energy needs soared, Beijing sought to ensure stable supplies through national oil companies Unipec (0386.HK) and PetroChina (0857.HK), which account for nearly 90 percent of shipments. They purchase a lot of oil directly from producers like the Middle East or Venezuela. China is also expanding its own fleet of tankers, which could account for a fifth of the global fleet.

“Fundamentally, the number of barrels that are tradeable these days is shrinking,” said Alex Beard, head of oil trading at Glencore.

Prospects might improve over time as Beijing is considering opening up trading licenses to private Chinese firms, said the chief executive of trader Mercuria, Marco Dunand.

But even if some market liberalization takes place, private traders will have to rein in their cutthroat instincts when the state is such a huge player.

“I think to do something on the larger scale in China you have to work with the (state Chinese) companies, not against them,” Gunvor’s Tornqvist said.

**SLEEPING GIANT**

The U.S. market, by contrast, is not only big but interesting, and changing fast.

Cheap gas meant U.S. industry switched away from coal, making the country a large coal exporter. Soon it is expected to export gas itself in the form of liquefied natural gas (LNG). And although Washington still bans exports of crude oil, the United States has become a big seller of refined products.

Those traders who unlike Vitol, Glencore or Mercuria haven’t yet built large U.S. operations, are keen to catch up.

Assets they might look to buy include parts of JP Morgan (JPM.N) commodities trading business, which the bank put up for sale this summer for $3.3 billion, including oil storage tanks in Canada and a global network of metal warehouses.

“ To be a global player, which is our ambition, growth in North America is going to be a big part of our future. I would not exclude right now any growth... not only hiring people, but also buying into some positions,” said Marco Alvera, who oversees trading at the Italian oil major ENI.

Even top tier banks, which have been squeezed by regulations in recent years and forced to retreat into trading on behalf of commodity clients rather than trading their own books, are eyeing the United States as a place to expand.

“The sleeping giant is U.S. gas. If it picks up it could get busy again for banks,” Mike Bagguley, head of commodities at Barclays, told Reuters. “A global liquefied natural gas (LNG) market would be exciting for us. We could work for both sides of supply.”

Additional reporting by Julia Payne, Alexander Winning, Alex Lawler, Claire Milhench, Simon Falush, Dmitry Zhendannov, Peg Mackey and David Sheppard in London and Jonathan Leff in New York; Editing by Peter Graff
A decades-old rivalry between banks and trading houses in commodities markets is taking new forms, as banks adjust to tighter regulations and merchant traders mount increasingly sophisticated challenges.

Banks have long been the dominant players in hedging - when commodities producers and consumers buy derivatives to help offset potential sharp price swings.

But as banks recalibrate their exposure to commodities under tight regulator scrutiny, trading houses are looking to grab a share of this business.

Likewise, traders have always dominated physical supply. But banks have been adept at finding niches trades and sometimes even oust merchants by offering supply arrangements together with a wide range of financial services.

“As the market becomes more liquid, especially on natural gas and power, as it becomes more sophisticated in developing specific hedging expertise and volatility trading expertise, the first step is to regain control of our flows,” Marco Alvera, Senior Executive Vice-president at Italian oil major Eni (ENI.MI) told the Reuters Global Commodities Summit.

“This is a very profitable business because not only you save on fees and commissions, but also because you make some interesting money if you monetize this properly,” said Alvera, who began his career at one of the most active banks in commodities, Goldman Sachs, in the 1990s.

Trading desks of oil majors such as BP (BP.L) and Shell (RDSa.L) have tradition-
ally been active in hedging but with the likes of Eni joining the ranks, some top talents are on the move. Two high-profile traders left Morgan Stanley’s European desk earlier this year for a trading house.

Eni is the largest gas buyer from Russia, Libya, Norway and Algeria and hedges those activities through fuel oil and crude oil as gas is indexed to those fuels in long-term contracts.

“Typically we would go in the market and just hedge through a third party ... What we do now is that we execute in the market directly without offloading it to a bank,” Alvera said.

He said the second step would be to take this activity to Eni’s existing customers.

“I would not say we will go to third party customers and offer hedging solutions. But if we have a customer who is already buying a commodity from us, we may as well build the commodity contract in a way that will effectively offer him a hedge or a contract that is more similar to what he needs industrially.”

He said that would increasingly become a norm in Italy and southern Europe where gas and power markets were becoming more liquid: “Before some of these guys would just buy the commodity from us and then go to a bank to do their hedging”.

**MORE CHALLENGING TIMES**

Mike Bagguley, head of commodities at Barclays, which alongside Goldman Sachs, Morgan Stanley, JP Morgan and Deutsche Bank is among the most active banks in commodities, said the client flow business such as hedging was indeed slower in 2013.

Part of it was due to lower market volatility.

“People got used to high volatility. Now with lower volatility and in backwardated curve, times are more challenging for everyone in the industry,” he said.

Backwardation is when future prices are lower than prompt prices, discouraging consumers from hedging and also making storing operations unprofitable.

Banks have expanded oil and metals trading aggressively over the past decade but had to scale back in the last few years.

Most of the downsizing happened on the proprietary side, where banks traded with their own money, as regulators said those actions might have added to market froth. JP Morgan said it was looking to sell its physical commodities business.

However banks now offer trading services as part of a mix of capital solutions and merger advice.

Barclays showed such ambitions earlier this year with a deal to supply a Hawaiian refinery. It already has a similar deal with Stanlow, the second-largest British refinery.

As European refineries struggle under low margins and as the cost of capital is expected to increase with the global central bank rate tightening, such deals could be repeated.

“On financing, we have started to get a critical mass. People know that we are capable of executing these deals,” said Bagguley.

“It works well with the energy markets. It means that banks can help producer clients and also with jobs and the real economy”.

As the rivalry between banks and traditional merchants takes new shape, a set of new entrants are adding fuel to the already dramatic commodities landscape reshuffle.

U.S. merchant Freepoint Commodities, launched with backing by private equity fund Stone Point Capital, is also seeking out niche plays, often in the oil sector.

“We find that it’s not enough just to participate in some part of the supply chain either by simply being a buyer or seller of physical commodities or leasing assets and providing some sort of distribution function,” CEO David Messer said.

“But we actually now find for ourselves and for our fellow merchants that we have our best opportunities come when we can bring capital to a commodity production or to an upstream or midstream development project or distribution project,” he said.

Additional reporting by Julia Payne, Alexander Winning, Simon Falush, Lin Noueihed, Ron Bousso, Dmitry Zhddannikov, David Sheppard in London and Jonathan Leff in New York, editing by William Hardy
Unlucky once, U.S. trader Freepoint still open to deals

BY JONATHAN LEFF
NEW YORK, NOV 7, 2013

U.S. merchant Freepoint Commodities is still open to potential trading asset acquisitions after losing out on one deal this year, Chief Executive David Messer said, signaling he may yet take part in the industry reshuffle.

However, Messer told the Reuters Commodity Summit this week that he was unlikely to return to the metals warehousing business, beset by regulatory scrutiny and profit pressures, and will eschew the balance-sheet-heavy operations being shopped by banks in favor of more niche opportunities.

“I think that if we thought we could acquire an asset at the right value, we would be open and enthused to do that,” he said at the summit, held at the Reuters office in New York.

“It’s just a question of what assets out there fit our strategy. We’ve looked at some number of the platforms for sale, we’ve actually bid for one, but today we haven’t acquired any,” he said. He declined to say which one he had bid on.

The commodity trading landscape is in the midst of its biggest reshuffle in a generation, with U.S. and foreign banks and some corporates getting out of the business while new players line up to get a foot in the door.

At least two of those processes are still ongoing. JPMorgan Chase & Co (JPM.N) has only recently taken first-round bids for its physical trading operation -- the bulk of which is the former Sempra Commodities business that Messer once ran. And Morgan Stanley (MS.N) is expected to hold off concluding a deal until a Federal Reserve decision about its business.

Messer said he would “probably not” be buying a metals warehouse such as JPMorgan’s Henry Bath & Sons, a company that he ran for years. The owners of London Metal Exchange warehouses are embroiled in regulatory and legal battles amid allegations that they may have inflated prices.

Messer, who began his career as a trader at Drexel Burnham Lambert in the early 1980s, has in less than three years built Freepoint into a 230-strong global commodity merchant modeled on -- and largely staffed by former traders from -- Sempra Commodities, the trading house he ran for 12 years until 2009.

Unlike Sempra, which was a broad energy and metals trading operation with a heavy focus on natural gas, Freepoint is seeking out more niche plays, often in the oil sector, he said.

Nor will Freepoint -- which was launched with backing by private equity fund Stone Point Capital -- be seeking to pick up the kind of multi-year, long-dated power or gas trades that are bread and butter for many banks.

“It’s just that certain kinds of businesses don’t fit our strategy - if it’s a heavy balance sheet business, that’s not going to fit what we do,” he said.

Meanwhile competition for assets amid the U.S. shale boom remains intense among corporations, particularly those who enjoy tax advantages such as master limited partnerships (MLP).

On Wednesday, a little-known MLP named NGL Energy Partners LP (NGL.N) bought U.S. energy logistics and trading firm Gavilon LLC for $890 million. Hetco, Hess Corp’s (HES.N) joint-venture proprietary physical trading shop, was also put up for sale back in March. A deal is expected soon.

PUSHING CAPITAL

Messer set up Freepoint with dozens of his former colleagues two years after leaving the group in the hands of RBS, which had bought half of the firm from Sempra Energy (SRE.N) in 2008. RBS was forced to divest shortly thereafter and sold most of it to JPMorgan -- which has now put it up for sale again amid pressure to get out of the physical trading.

While Messer’s previous ventures have focused on trading and supply deals, this time around he is funding development projects, often together with a lender, as the commodity trading business shifts away from simple arbitrage toward deeper investment in assets and infrastructure.

“What we find now is that by not only providing a logistics function but also by bringing in capital, we are able to give our customers a more comprehensive solution,” he said.

“That has really developed faster than I would have thought... when I started Freepoint.”

Messer said the company had completed a half dozen structured finance deals this year, and said with a pipeline of new deals the pace should “continue if not grow”.

He is following a similar strategy with the metals concentrates trading arm that Freeport acquired from JPMorgan -- another former Sempra Commodities business - last year.

The firm has a “number of potential transactions in the pipeline”, Messer said, referring to structured debt financing deals that fund early-stage projects in return for offtake. Freepoint signed its first mine financing deal in January.

Editing by Andrew Hay
Trader Gunvor studying U.S. expansion, JPM’s business

BY DAVID SHEPPARD AND JULIA PAYNE
LONDON, NOV 6, 2013

Commodity merchant Gunvor, long known in the industry as one of the key traders of Russian oil, is studying growing opportunities in North America resulting from the shale oil boom and is looking at select trading assets including parts of JPMorgan Chase & Co.’s (JPM.N) business.

Speaking at the Reuters Global Commodities Summit on Tuesday, Gunvor chief executive and co-founder Torbjorn Tornqvist said the firm saw opportunities in North America and had been in contact with the Wall Street bank, which put its physical trading business up for sale this summer for around $3.3 billion.

“Yes we can confirm that we have contacted JPMorgan and we have been looking at some of their assets,” Tornqvist said. “It is an important part of our business to always look at assets. Out of the 10 we are looking at maybe one or two will go all the way.

“We are obviously in the area of looking to expand our arbitrage assets. And that goes for all commodities, not only oil, we are looking in other commodities as well.”

JPMorgan’s assets include oil storage tanks in Canada and its Henry Bath global network of metal warehouses. The bank sent out its prospectus to several potential
buyers last month as it decided to sell the unit due to tighter regulations and political scrutiny on banks active in commodities.

Several years ago, Switzerland-based Gunvor handled as much as 40 percent of Russia’s seaborne crude oil exports via a number of long-term deals with Russian energy majors such as Rosneft (ROSN.MM), Surgut (SNGS.MM) and TNK-BP.

It has moved to diversify, opening offices across the world and beginning to trade other commodities while ceding some parts of its Russian trading book to rivals Vitol and Glencore (GLEN.L) after premiums at tenders of firms such as Rosneft spiked steeply.

Tornqvist said that shipping Russian crude now makes up less than a third of the firm’s business, as it has moved into areas such as gasoline and diesel trading, refining, production and metals.

“We are a global diversified company whereby Russia plays an extremely important role,” Tornqvist said, adding the firm was already involved in projects looking at exporting liquid petroleum gas (LPG) from the United States, a by-product of the shale oil boom that is not subject to the same export restrictions as crude.

GO WEST

Tornqvist said the logistical bottlenecks that have sprung up in North America due to the shale oil revolution and growing output from Canada’s oil sands had generally created attractive trading opportunities. The United States’ emergence as a major exporter of refined products such as gasoline, diesel and natural gas liquids (NGLs) is another attractive area.

“Obviously we see a lot of opportunity there, there are certain things that we have done... We are involved in LPG as a by-product of natural gas, and taking that out from the United States. And we look forward to being involved in similar projects in the future,” Tornqvist said.

“There will also be blending opportuni-
ties between the heavy crude oils from Can-
ada and the lighter U.S. crude oils,” Torn-
qvist said. “There will be good opportunities in North America for many years to come.”

JPMorgan has a collection of long-term leases on more than a quarter of the oil tanks in Hardisty, Alberta, the main storage and transportation hub for output from Canada’s oil sands.

The bank holds over 6 million barrels of storage space in tanks leased from pipeline company Enbridge Inc (ENB.TO), according to market sources. Crude traders in Canada’s oil capital Calgary say they provide a powerful trading tool.

QUIET CHANGE

Gunvor has also diversified into commod-
ity extraction in recent years, buying a $400 million stake in a troubled Montana coal mine in 2011. In the past year, Gunvor has hired metals specialists and started trading.

Energy still represents the lion’s share of the business with refined products trading accounting around two thirds of the energy business.

“We have changed our strategy quietly in Russia. We have made a lot of investments in oil terminals. We are working a little bit less with volume but we try to have more quality in our trading, rather than chasing volumes,” said Tornqvist.

He said he expected the firm’s turnover in 2013 to remain near record levels seen in 2012 “with a slight bias to the upside”. He also said the firm was working on its up-
stream strategy in oil but it was likely to re-
main a rare, opportunistic activity with trading still very much dominating the business.

Gunvor owns two refineries in Europe having snapped them up a low prices in 2012 after independent refiner Petroplus went bankrupt.

“We had a good run on those refiner-
ies and even this year we have managed to keep them profitable,” he said, but added: “I have no illusions about the difficulties that the European refinery sector will have to go through.”

Over the next two years, U.S. plants as well as new refineries in China and the Middle East will take further market share away from Europe, prompting 5-10 plants in Europe to close down and reducing its refining capacity by a tenth or 1 million barrels per day, Tornqvist said.

“Governments would like to be seen doing something. But the reality is there is not much they can do. This is a process which is necessary and it is long overdue,” Tornqvist said.

Additional reporting by Lin Nouiehed, Ron Bousso, Claire Milhench, Simon Falush, Alex Lawler and Dmitry Zhdannikov in London; editing by Jason Neely

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Global Commodities Summit 2013

Top trader Vitol sees chance of steep oil price fall

By Dmitry Zhdannikov and Ron Bousso
London, Nov 4, 2013

Oil prices could drop by as much as $15 per barrel should countries such as Libya restore production and sanctions on Iran be eased, forcing some of the most expensive U.S. oil projects to stop pumping, the head of the world’s largest oil trader said.

Ian Taylor, chief executive of Swiss trading house Vitol VITOLV.UL, said he also expected a number of European refineries to close in the next few years under tremendous competitive pressure from rivals in the Middle East and Asia.

“We see a constant structural length in the dated Brent market and the West African sweet market and we are not quite sure how it clears yet,” Taylor told the Reuters Global Commodities Summit.

“If Libya does come back, God knows where that oil goes... And goodness knows what happens if Iran comes back.”

Perhaps the only way the market can actually clear properly is to begin to threaten the lower ranges, and therefore begin to threaten some of the higher cost developments and production.”

The United States is set to become the world’s biggest oil producer next year, overtaking Russia, and a spike in U.S. oil production has helped offset big supply outages from Libya, Iraq, Iran and Nigeria in recent months.

Taylor said that if most supply problems were solved, European benchmark Brent prices could come down to $90-$95 per barrel from the current $105 while U.S. WTI prices may decline to $80-$85 from the current $95.

“Then I think OPEC might begin to get worried,” said Taylor.

Europe Refining

Vitol made a foray into European refining last year and Taylor said the company could look at new opportunities in the future although he said the sector would have to shrink as it faces very low profitability on refining crude into products.

“It has been a disaster over the last two or three months as you all know... I believe that significant portions of the European refining business probably need to close over the next three or four years,” he said.

Taylor said he could see up to one million barrels per day or a roughly one tenth of current capacity in Europe closing down, especially outdated refineries in the Mediterranean.

“I think you’re going to see a constant battle between the big European majors, Europe, the politicians about this... I’m not sure what the result is going to be but the answer is we know the UK does not need seven or eight refineries.”

He added that Vitol could still buy plants.

“It depends what else it brings. If it brings a lot of flow with it you could always value your refinery in a negative sense if there are a lot of other things you get with the deal. But certainly I don’t think you are going to see us keen to pay multiples for refining businesses”.

Trading Margins

Vitol and most of its rivals such as Glencore (GLEN.L) or Gunvor have been chasing bigger trading volumes in recent years to compensate for shrinking profit-
ability amid lower market volatility.

Taylor said he expected the trading environment to remain difficult as traders have to compete with traditional rivals such as oil majors but also increasingly with national oil companies aggressively pursuing incremental trading profits.

“I do expect it to be incredibly tough. I do expect to see a continuation of trading companies buying selective assets to try to increase their optimization possibilities. Volumes among the trading houses will probably come off a little bit rather than increase because at the end of the day demand for oil isn’t going up that much.”

**GAS**

Taylor said that unless oil prices dropped sharply, there were realistic prospects for liquefied natural gas (LNG) to become a major fuel in the transport sector as big U.S. and Chinese manufacturers were already shifting towards using gas.

“The pollution question in China is huge so they will shift more towards gas for transportation and in power (generation), no matter how high the price is,” Taylor said.

The move will come largely at the cost of lower coal use, which is dirtier than gas but is still the world’s dominant electricity fuel.

“I personally worry that coal is going to be a problem as demand will come off much faster than we think,” Taylor said.

Natural gas is currently less profitable as a fuel for generating power but the U.S. boom in shale gas drilling has led to a collapse in gas prices there. The U.S. is expected to begin exporting LNG by 2015, which many users in Europe and Asia hope will help bring down prices there as well.

Taylor said Vitol was unlikely to invest into LNG assets on a big scale but added that smaller floating LNG terminals could be an option.

**U.S.**

Taylor said that in North America Vitol had made investments in pipeline and storage tank capacity in Texas’s Permian basin, but that the firm’s trading focus was likely to remain on seaborne shipments rather than competing directly with inland producers and refineries.

He said news that Philadelphia Energy Solutions’ 350,000-barrel-per-day refinery was bringing in up to one-fifth of the oil output from the Bakken shale fields in North Dakota may provide opportunities in finding homes for oil backed out of the United States.

“I think it is significant that people like the Philadelphia refinery are buying in significant amounts of crude by rail, and they were previously one of the biggest buyers of Nigerian crude,” Taylor said.

“Now they’re going to be buying 250,000 barrels per day of railed Bakken crude and very little Nigerian, and that’s the bit of the trade we need to work on.”

U.S. Gulf Coast refiners that benefit from the shale oil boom are supplying the U.S. East Coast and Canada, which will require less North Sea and West African crude, Taylor said.

“Where exactly that crude oil price moves is still a very big question which we haven’t really got to grips with in 2013... I am hoping it will be European refinery systems that get a little bit of a break because obviously they’ve been struggling pretty badly over the last two or three months,” he said.

But at the same time, the increased flow of diesel from the U.S. Gulf Coast to Europe “could potentially put a lot more pressure on margins in Europe and to a certain extent we are seeing that already”.

Asked whether Saudi Arabia would continue to sell large quantities of oil into the United States given the weak price relative to sales elsewhere, Taylor said he could see reasons for Saudi Arabia to keep doing this from a strategic perspective, but no rationale for other exporters.

“For Venezuela and Mexico, who in some ways have greater revenue concerns than Saudi, arguably they shouldn’t be putting any oil into the U.S. at all at current differentials. The way differentials are at the moment, nobody should be exporting to the U.S. at all.”

Reporting by Ron Bousso, Lin Noueihed, Claire Milhench, Simon Falush, Julia Payne, Henning Gloystein, David Sheppard; editing by Jason Neely

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Eni looking to expand U.S. energy trading

BY ALEXANDER WINNING AND LIN NOUEIHED
LONDON, NOV 7, 2013

Italian oil major Eni (ENI.MI) is looking to expand its trading operations in the United States and will study assets currently offered for sale by rivals, a senior executive said.

“As to the United States, I think we are subscale there,” Senior Executive Vice-president Marco Alvera, who oversees trading operations, told the Reuters Global Commodities Summit.

“Our Houston office is performing well, it’s mainly there to sell the equity oil and gas we produce. It has the potential to develop into more of a regional office to support our activities in South America,” he said.

Eni is one of the largest buyers of gas in Europe and with output of 1.7 million barrels per day is bigger than U.S. oil major ConocoPhillips (COP.N) although its output has traditionally been more focused on Africa and the Middle East.

Several trading assets have been offered for sale over the past year in the United States, including by Wall Street bank JPMorgan Chase & Co. (JPM.N), which is looking to exit the commodities business due to tighter regulations. Hess (HES.N) is also selling out of trading unit Hetco.

Alvera declined to comment on specific assets and acquisition targets.

“I think it’s our duty to at least look at those books,” he said. Trading house Gunvor told the Reuters Summit this week it is looking at JPMorgan’s business.

“I think to be a global player, which is our ambition, growth in North America is going to be a big part of our future, starting from a small base. I would not exclude right now any growth, which is not only hiring people, but also buying into some positions,” said Alvera.

WINNING BUSINESS BACK

Alvera, who began his career at Goldman Sachs (GS.N) in the 1990s, said that as part of its expansion strategy Eni’s trading division wanted to rival banks in some of their traditional commodities trading activities, such as hedging.

“As the market becomes more liquid, especially on natural gas and power, as it becomes more sophisticated in developing specific hedging expertise and volatility trading expertise, the first step is to regain control of our flows,” he said.

“This is a very profitable business because not only you save on fees and commissions, but also because you make some interesting money if you monetize this properly.”

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He said the second step would be to take this activity to Eni’s existing customers.

“I would not say we will go to third party customers and offer hedging solutions. But if we have a customer who is already buying a commodity from us, we may as well build the commodity contract in a way that will effectively offer him a hedge or a contract that is more similar to what he needs industrially.”

He said that would increasingly become a norm in Italy and southern Europe where gas and power markets were becoming more liquid: “Before some of these guys would just buy the commodity from us and then go to a bank to do their hedging”.

PRICE AND REFINING WEAKNESS

Alvera said he believed global oil prices could drop sharply if output from Iraq, Libya or Iran was to return to the already well-supplied market.

“We have seen that when Brent drops, it drops quite rapidly... I think 2014 is going to be a very interesting year because a lot of situations could result in more production. And this is production that’s very easy to bring on line from an industrial perspective.”

He also said he expected more refineries in Europe to close down: “I think the future is very bleak. There will be huge products flows coming from the Middle East, Asia and certain products from the U.S., as well.”

“Not only a lot of European refineries are subscale, they also have to cope with higher costs of electricity and natural gas to function. The good news is that capacity is coming off.”

Additional reporting by Peg Mackey, Alex Lawler, Dmitry Zhdannikov, Christopher Johnson, Simon Falush, Claire Milhench, Ron Bousso; writing by Dmitry Zhdannikov; editing by Jason Neely
The U.S. shale boom is causing a cascading series of changes in global energy markets that are altering the landscape for oil trading houses and opening up new ways for them to profit, a leading Swiss trader said.

“In the energy complex specifically, the shale gas boom and plentiful supply of gas have created a series of very interesting and complex knock-on effects,” Daniel Jaeggi, co-founder of Swiss trading house Mercuria, told the Reuters Global Commodities Summit.

The production of shale gas and oil using fracking technology has turned the United States from an energy importer to a major exporter of oil products and coal in recent years. Next year, the United States is set to overtake Russia as the world’s top oil producer, the International Energy Agency (IEA) said last month.

This shift has hit the global coal market as U.S. industries and power plants have switched to the abundant supplies of cheaper, less polluting gas.

“If the U.S. burns more gas, what happens to the coal, and coal needs to find a way out of the U.S.?” Jaeggi said.

“In reality the gas arbitrage is actually happening in the coal world, and LPG (liquefied petroleum gas) as well,” Mercuria Chief Executive and co-founder Marco Dunand told the summit in a joint interview.

Another example is gas arbitrage in the petrochemical world.

“At the end, it’s probably easier to move certain types of petrochemicals out of the U.S. than it is to move gas out of the U.S.,” Dunand said.

### REINVENTING YOURSELF

The resurgence of the U.S. oil and gas production has drawn a large number of producers and traders from all over the world.

“When you are interacting with the market, the efficiency is spotted by more than one player, and so the efficiency disappears and you have to find the next play,” Dunand said.

“It’s a constant model of trying to reinvent yourself.”

Shortly after the shale boom started, Mercuria invested in Bakken crude oil production and some storage capacity at the oil hub in Cushing, Oklahoma. It sold out of Bakken last year and has also reduced its position at Cushing, Dunand said.

“It’s about positioning yourself early in a dislocation, and when the market becomes more efficient to reduce your exposure,” he said.

Mercuria, which started as a small oil trader in 2004, has posted one of the steepest growth rates in the business over the past decade. Its turnover soared to $98 billion in 2012 from $75 billion in 2011 and $47 billion in 2010.

### OIL PRICE RANGE

Both Dunand and Jaeggi said the oil market had found its price equilibrium point, which was likely to persist.

“There is a broad consensus in the market that we’re in a $90 to $100 range, and I don’t see any compelling argument why in the foreseeable future we’d step out considerably from that range without some form of unforeseen turmoil,” Jaeggi said.

Dunand said that, despite downward pressure on prices from new sources of supply, he couldn’t see oil prices going much below $90 per barrel for a prolonged period of time.

“You still need to replace around 5 million barrels per day of production every year, and you would not be able to do that if the market were to be consistently below $90 a barrel for Brent,” he said.

Mercuria may continue to seek opportunities in oil production, but mostly to help its trading strategies rather than to become big in industrial activities.

“We’ve invested a little bit into Canada and West Africa in a couple of places. We’re doing it, but this is not a major focus for us.”

### REGULATIONS

Dunand said trading houses were engaging with regulators across the world to make sure traders understand the new rules in commodities markets.

“The biggest problem we can see in the regulatory world is that the rules in the U.S., Europe and Asia are not completely aligned,” he said.

Dunand said he believed there was a fair amount of transparency in oil markets, at least for the benchmarks.

“A lot of information is on record, but there’s not necessarily a great understanding of how those benchmarks work for people who are outside the industry,” he added.

“I think people are naturally suspicious of the commodities markets because they’ve seen prices increasing in the last 10 years, and some people may relate those price increases to market abuse.”

Additional reporting by Peg Mackey, Alex Lawler, Dmitry Zhdannikov, Lin Nouiehed, Christopher Johnson; editing by Richard Mably and Jane Baird
Olam sees global coffee prices bottoming out

BY EVELINE DANUBRATA AND NAVEEN THUKRAL
SINGAPORE, NOV 5, 2013

The global coffee market could find a floor around current levels as multi-year low prices prompt farmers to cut production, commodities trader and coffee supplier Olam International Ltd (OLAM.SI) said on Monday.

London robustas slid to their lowest since June 2010 on Friday, largely driven by prospects of a record crop in Vietnam, while December arabica futures on ICE Futures U.S. dropped to the lowest in more than four years last week.

“It does not make sense for farmers to fertilize at the same level or (carry out) weeding at the same level, so they will reduce the inputs,” Olam Chief Executive Officer Sunny Verghese said in an interview at the Reuters Global Commodities Summit.

“There might be a little bit more downside to coffee prices, but we see that we are reaching the bottom.”

The International Coffee Organization has raised its global coffee production estimate to 145.2 million 60-kg bags in the 2012/13 crop year, up 0.5 percent from its previous estimate, as output soared in Brazil and Colombia.

The new forecast for 2012/13, which ended September 30, is up 9.6 percent from 2011/12 and the highest on publicly available records that date back to the 1990/1991 crop year.

Robusta production jumped by 11.6 percent to an estimated 56.4 million bags in 2012/13, with arabica production rising by 8.4 percent to 88.8 million bags, the ICO said in a monthly report.

Olam, which produces and trades several agricultural products, is among the top global suppliers of coffee and cotton.

Bearish fundamentals in the cotton market are likely to put pressure on prices although stockpiling and imports by China, the world’s top buyer, could provide some support, Verghese said.

The spot month cotton contract on Friday hit a low of 76.54 cents a lb, its weakest since January.

“We believe it will trade in the range between 70 and 75 cents, so there is a downside to 70 cents. If the Chinese government policy continues the way it is, they will trade around 75-80 cents.”

China almost doubled the purchase of domestic cotton for state reserves in the latest week to 608,560 metric tons, boosting its buying after a sluggish start to this year’s stockpiling program, official data showed.

The International Cotton Advisory Committee on Friday raised its forecast for global inventories on an improving outlook for this season's crops and higher output in major producers.

SLOWER GROWTH PATH

Olam, a key player in global cocoa trade, is keen to expand its manufacturing and grinding business, Verghese said.

“We don’t want to be a major processor, but we will want to be a meaningful processor,” he said. “We will do a mix of organic and inorganic investments in the processing side.”

Olam shifted to a slower growth path in April, saying it will nearly halve its capital spending over the next three years and trim its businesses, after criticism from short-seller Muddy Waters last November sent the company’s stock and bond prices plunging.

Singapore state investor Temasek Holdings TEM.UL raised its stake in Olam from around 16 percent before the Muddy Waters allegations to 24 percent.

Verghese said Olam is on track to be free-cashflow positive in the year to June 2014, one year earlier than previously forecast. He added that the company’s debt-to-equity ratio is below two times and the company can maintain this level.

“We regularly are in contact with our investors, they are very pleased with the recalibrated stand and they are waiting to see how we execute,” he said.

“But they have to be patient and we have to guide them to be patient because none of the measures that we are taking are short fixes, they will take time to execute.”

Editing by Muralikumar Anantharaman
Private oil companies, unable to get others to fork out enough money to buy them, are increasingly going to public markets to tap investors who are eager to get a piece of the U.S. onshore boom - especially if the firms target just one shale basin.

Tod Benton, the head of U.S. energy banking at Canada’s BMO Capital Markets, said initial public offerings are giving companies higher valuations at a time when buyers and sellers of oil and gas properties are having a tough time reaching agreements on price.

“The (IPO) pipeline is very full. The public markets are very active and giving people multiples on exits that they can’t get in the acquisition & disposition space,” said Benton, who spoke on Monday during the Reuters Global Commodities Summit.

Hydraulic fracturing, the process also known as fracking, and other technological advances have revolutionized the U.S. energy industry over the past five years and caused a massive jump in domestic oil and natural gas production. Ohio, Texas, North Dakota and several other states have seen a surge in energy production, causing an unprecedented rise in investment and employment in the sector.

Benton said firms backed by private equity funds were among those most keen to hold IPOs.

“We’re seeing guys going the public route rather than the sell-side route. Right now we see mergers & acquisitions kind of plateauing,” Benton said.

While there have been 18 energy and power IPOs so far this year compared with 21 last year, the value of those offerings is up more than 50 percent, according to Thomson Reuters data.

Benton said the IPO of Antero Resources Corp (AR.N), which valued the Warburg Pincus-backed oil and gas company at more than $11 billion, was among the deals showing the door is open for other firms. The company’s shares rose around 25 percent in their market debut and have held on to the gain, valuing the company at around $14 billion.

Other highly anticipated IPOs include Apollo Global Management’s (APO.N) EP Energy, which filed to go public in September, just 15 months after the company was bought by the private equity firm, and Rice Energy.

Benton said about half of the asset deals in the energy sector weren’t being completed.

“We’ve seen a lot of disparity between seller expectations and what buyers are willing to pay - partly because of low gas prices,” Benton said. “We’ve seen maybe a 50 percent completion rate” across the industry, he said.

**THE POWER OF ‘PURE-PLAYS’**

Investors are increasingly interested in buying companies that focus on one of a dozen or more U.S. regions that produce oil and gas from shale or other rock - the logic being they can add a company focusing on the Permian, Bakken or Marcellus to their portfolio if they want to diversify.

“Guys that are getting the best interest from the buy-side are the guys that are very focused; single, pure-plays that are easy to understand,” he said.

“Buy-side is looking at high-return plays where guys have running room, lots of inventory - up to 10 years in lots of cases. And they like a balance sheet that’s clean enough to develop the acreage they want to develop” without seeking joint venture partners or ‘crazy financing,’ Benton said.
Shares of Kodiak Oil & Gas (KOG.N), which primarily operates in North Dakota’s Bakken shale field, have surged nearly 250 percent since a 2006 IPO, tracking the field’s dramatic development.

CEO Lynn Peterson said in a September interview with Reuters that Kodiak’s exclusive focus on the Bakken appeals directly to investors looking for strategic investments in U.S. shale plays.

Diamondback Energy Inc (FANG.O), which is making a big push in the Permian, has seen its stock price rise some 200 percent to around $52 since its shares debuted a year ago.

GROWTH AFTER STUMBLE BY U.S. PEERS

Benton spoke at the Reuters office in Houston. BMO has been in Texas for more than 50 years and has gained market share in the United States since the 2008 credit crisis.

That is because Canadian banks generally steered away from risky assets and had higher capital ratios than U.S. banks sidelined by the crisis.

“We sidestepped the credit crisis because capital ratios were very high and because we have a focus on the energy industry we stayed in the game and actually chose to use it as a market share-gaining opportunity.”

Benton said BMO has hired numerous bankers from larger firms over the past five years that had backed away from the energy space.

“We’ve made incredible market share gains,” Benton said. “In the league tables we are one of the top five or six high-yield bookrunners at the moment, we are one of the leading equity capital markets underwriters in North America, our M&A business has really taken of, and we’ve always been a good loan shop.”

Additional reporting by Eileen O’Grady, Anna Driver and Ernest Scheyder; Editing by Terry Wade and Phil Berlowitz

Summit Speakers

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  CEO and President
  Vitol

- Matthew Rose
  CEO
  BNSF Railroad

- Alex Beard
  Head of oil
  Glencore

- Nev Power
  CEO
  Fortescue

- David Messer
  CEO
  Freepoint Commodities

- Stefaan Sercu
  CEO of North American Marketing
  GDF Suez

- Marco Dunand
  President and CEO
  Mercuria

- Ted Harper
  Fund Manager & Senior Research Analyst
  Frost

- Sunny Verghese
  CEO and Managing Director
  Olam

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