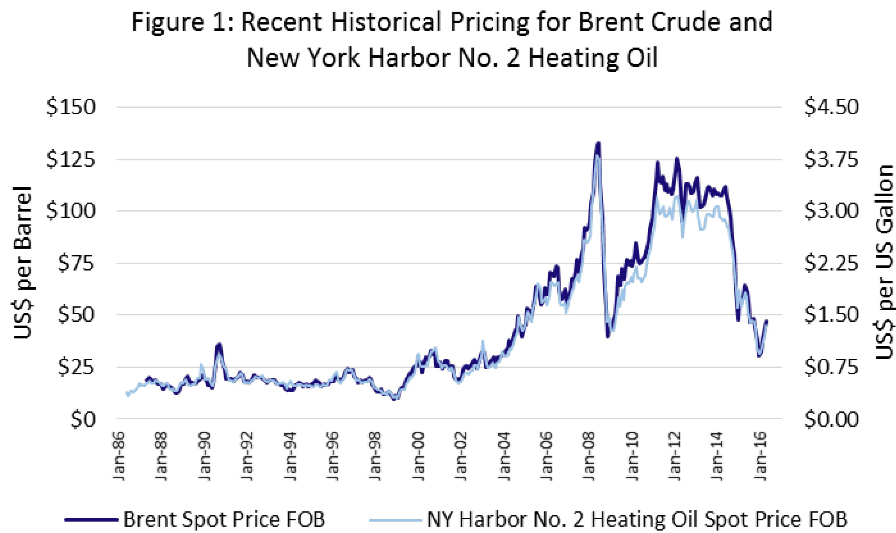
ELECTRICITY REGULATORY AUTHORITY
CAYMAN ISLANDS

Fuel Price Volatility Management

Oil is priced in a global marketplace and is sensitive to speculation, global supply and demand, geopolitics and global economic conditions. Although the price of oil is currently in a down cycle, it has increased steadily since 2002 and has experienced pronounced spikes in 1990 and 2008 (see Figure 1).



Pricing Source: U.S. Energy Information Administration

Caribbean Utilities Company, Ltd. (CUC) purchases large volumes of No. 2 Diesel for electricity generation on Grand Cayman. No. 2 Diesel is a refined oil fraction; therefore, its pricing is heavily reliant on globally-priced oil.

CUC's fuel costs are also a 100% pass-through to electricity consumers as a Fuel Cost component in monthly bills. Accordingly, the ERA and CUC agreed in March 2011 to guidelines for a Fuel Price Volatility Management (FPVM) Plan to mitigate and manage customer's exposure to fuel price volatility. CUC submits a FPVM Plan for ERA review and approval, annually.

The goal of the FPVM Plan is to protect CUC customers against severe fuel price increases, like the price spike experienced in 2008, by employing a fuel hedging strategy that is non-speculative and transparent.[1]

FPVM Plans typically call for purchasing twelve-month rolling fuel hedging contracts from multiple providers using NYMEX No. 2 Heating Oil as the underlying commodity, or proxy hedge.[2]

[1] The strategy utilizes non-speculative forward purchasing contracts to implement a degree of cost certainty for CUC's customers. The forward purchasing contracts insure a portion of the fuel volume purchased against severe price spikes.

[2] No. 2 Heating Oil is used as a proxy hedge for No. 2 Diesel as both fuels are virtually identical in the refining process. Figure 1 above shows that pricing for No. 2 Heating Oil has a strong correlation to Brent Crude pricing.

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