A small team of traders at Goldman Sachs made $100 million betting on natural gas — and it could be thanks to a 'bomb cyclone' driving prices to record level.
Natural-gas prices set records in early January when below-average temperatures accompanied by snowstorms dubbed the "bomb cyclone" led to soaring demand for the commodity, according to Natural Gas Intelligence.

Goldman's first-half performance was a reversal from 2017, when natural-gas bets in the second quarter went so poorly that the commodities-trading department turned in its worst annual performance in the bank's history as a public company.

This year's gains helped push Goldman Sachs back into the top spot for commodities trading on Wall Street in the first half, according to the industry consultant Coalition.

Goldman Sachs has bounced back from last year's commodities rout.

The investment bank racked up $100 million in the first half trading natural gas, according to people with knowledge of the matter. The money was made by Shane Lee, a Calgary-based trader who previously worked at the hedge fund Amaranth Advisors, and his team, the people said.

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Commodities trading, once one of the bank's most vaunted businesses, saw revenue plummet 75% to less than $300 million last year, Bloomberg has reported. That was down more than 90% from a high of $3.4 billion in 2009.

This year's gains helped push Goldman back into the top spot on Wall Street in the first half, according to the industry consultant Coalition. The bank shared the title with JPMorgan and Morgan Stanley after dropping out of the top tier last year.

Goldman has a rich history in commodities trading that began when it purchased the J. Aron trading house in the early 1980s. A generation of Goldman leaders got their start there, including the firm's chairman, Lloyd Blankfein, and securities division cohead Marty Chavez.

A Goldman spokesman declined to comment, and the firm wouldn't explain the details of how Lee made the money. Lee didn't respond to a request for comment.

Moving gas through the nation's pipelines

Natural-gas traders watch prices in local markets like the Northeast or the West and look to benefit from pricing abnormalities or the complexity of moving gas through US pipelines. They use futures and forwards, swaps, and even take physical delivery of the commodity to capture price differences, say, between a delivery point and the Henry Hub in Louisiana, the industry benchmark.

Changes in weather during winter and early spring typically spur activity in the natural-gas market as producers and consumers adjust stockpiles. To prepare for the activity,
traders can stock up on physical inventories or tilt their portfolios using financial instruments. While there was no suggestion among people familiar with the trade that the bank was flouting rules against trading for its own account, critics contend that inventory management like this is a form of speculation.

Lee, based in the east tower of a Calgary building known as Bankers Hall, runs Goldman's natural gas basis trading desk, one of the people said. The team helps clients move gas from one region to another and in some cases even buys inventory and offers it to clients in search of supply.

Much of the money was made trading in the Northeast natural-gas markets, the people said. The region, which extends from Maine through Kentucky and Virginia, has 10 major trading hubs with names like Algonquin Citygates in the Boston area and Transco Zone 6 in New York, according to the Federal Energy Regulatory Commission. Those hubs are served by pipelines with the same or similar names.

One of the ways the bank made money was by, in industry parlance, trading the basis, or the spread between two reference points, the people said.

Beyond this, Business Insider wasn't able to determine other specifics or precise timing of the trade.

**Betting on great-than-expected demand**

Industry experts pointed out several ways in which the trade could have worked. One possibility is that traders could have used forwards to lock in the difference between a specific price in the Northeast and the Henry Hub price, said Jeremiah Shelor, the markets editor for Natural Gas Intelligence, who added that he didn't know the specifics of Goldman's trade. Goldman may have also taken a position in the physical markets betting on the spot price to increase or decrease, he said, or have arranged bilateral deals with commodities users or producers.

"The key idea is that there is some spread that you think is too wide or too narrow and you put on a trade that will benefit if your view is correct," said Campbell Harvey, a professor of finance at Duke University who has written an influential paper on commodities markets.

Gas prices set records in early January amid snowstorms dubbed the "bomb cyclone," according to NGI. Below-average temperatures led to soaring demand for gas to heat homes. The highest individual spot trade ever recorded took place January 4 at a price of $175 per 1 million British thermal units in the New York City market served by Transco Zone 6 New York, according to NGI.

That same day, the basis or difference to the Henry Hub price was almost $136, according to NGI. Prices remained elevated in January. On March 2, amid milder weather, the Transco 6 Zone New York high was just $2.73.
"If I'm in the Northeast, there are different pipelines that service my area," said Elaine Levin, the president of Powerhouse, a Washington-based firm that helps companies hedge their commodities risk, explaining how traders think about the basis. "What happens is when it gets very cold, and you go through a period of sustained demand, you can't move the gas into the area fast enough. And so those local prices reflect local supply and demand."

At the time, Shelor added, "multiple pipelines in the region had notices out to shippers warning of constraints."

The trade 'could have gone the other way'

Lee, who reports to Ed Emerson, one of Goldman's global coheads of commodities trading, has been trading natural gas for years. He joined Goldman in 2010 and made managing director five years later. Prior to Goldman, he traded natural gas at Amaranth, the $8 billion hedge fund that collapsed in 2006. Lee had joined earlier that year, working there for five months, and wasn't accused of any wrongdoing.

While the first half went well, it easily could have ended up differently if the weather or supply and demand imbalances didn't cooperate, according to Harvey, the finance professor. An unexpected delay in the construction of a pipeline last year wiped out Goldman's natural-gas revenue, The Wall Street Journal reported.

"Natural gas is very volatile," he said, adding that this trade "could have gone the other way."

Get the latest Goldman Sachs stock price here.