



ENERGY RISK MANAGEMENT

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ENERGY MARKET REPORT FOR MAY 31, 2006

US Secretary of State Condoleezza Rice said the US would join European Union countries Britain, France and Germany for talks with Iran if the country suspended its uranium enrichment and reprocessing activities. She said the US agreed on the essential elements of the package and hoped Iran's government would consider the proposal. She also promised Iran greater economic cooperation if it abandoned its nuclear weapons plans. A senior State Department official said Russia and China also supported the package but final details still had to be worked out. US Secretary of State is expected to travel to Vienna to meet with the permanent members of the Security Council as well as Germany to

Market Watch

Iran's Oil Minister Kazem Vaziri Hamaneh said current prices had not affected world economic growth. He added that he remained concerned that crude inventories were building over the next few months. He also dismissed any talk that Iran may consider blocking the Strait of Hormuz.

The unusually hot weather forecast for China this summer may put extra strain on its power grid, helping extend a recent increase in domestic demand for oil. The National Development and Reform Commission forecast in March a shortfall of under 10 gigawatts this summer, less than half last year's level. However the government was urging caution as the Chinese economy continued to grow at or above 10%.

BP's chief executive John Browne said he expects the world oil market to normalize in coming years and the relationship between supply and demand to improve.

ExxonMobil Corp's chief executive Rex Tillerson warned that moves by Venezuela and other countries to tighten state control over energy resources could be damaging and threaten future investment in the region. Most worrisome for US oil companies is Venezuelan President Hugo Chavez's campaign to increase state control over the oil industry and increase government revenue to adjust what he said were unfavorable deals with foreign companies.

According to forecasters at Colorado State University, the probability of at least one major hurricane making landfall in the US Gulf Coast is higher than normal this season, but slightly less than previously forecast. It said the probability of at least one Category 3 or higher storm striking from the Florida Panhandle westward to Brownsville, Texas has been lowered to 38% from 47% in its last forecast. However it remains above the 30% average seen in the past century. Overall, it forecast 17 named storms, nine hurricanes and five hurricanes of Category 3 or higher for this season. It stated that in the region from Cameron County to Harris County, Texas, with about 3 million bpd of refining capacity, the Colorado State forecast saw an 85.4% probability of a named storm making landfall. In the region from Jefferson County, Texas to Calcasieu, Louisiana, home to about 1.8 million bpd of refining capacity, there is a 36.6% chance of a strike by a named storm. In the region from Iberia, Louisiana to Holmes, Florida, which has about 1.8 million bpd of refining capacity, the odds of a tropical storm making landfall are 99%.

The Chicago Board of Trade added ethanol futures to the list of products traded simultaneously in electronic and open auction trading systems on Wednesday. The CBOT ethanol futures would trade from 9:30 am to 1:00pm, the same as the pit traded contract.

discuss the package of incentives and threats to get Iran to abandon its nuclear plans. US President George W. Bush said the US was taking a leadership position to resolve the dispute diplomatically with its new offer to possibly join European talks with Iran. A senior administration official said the Bush administration believed it had a consensus among allies to pursue UN sanctions against Iran if an offer for talks failed. The New York Times reported that the Bush administration on Tuesday agreed to language ruling out the immediate threat of military force as it sought to enlist Russia's support for a UN Security Council resolution on Iran. Meanwhile, an Iranian lawmaker, who does not speak for the government, said the direct talks with Iran over its nuclear program should be conducted without preconditions.

Iraq's Prime Minister Nouri al-Maliki traveled to Basra after vowing to end infighting among Shi'ite factions threatening oil exports from the city. He declared a month long state of emergency in the southern city of Basra, amid increasing violence. Tensions have been rising as rival factions from the Shi'ite Muslim majority struggle for a share of power. Iraq's Prime Minister vowed to crack down on gangs threatening security in Basra. He said he would use force against gangs holding oil exports and other trade to ransom. A Shia faction has also threatened to sabotage oil exports through Basra to exert leverage over the Iraqi government. Iraq's Prime Minister said the oil gangs belong to militias run by the two main Shi'ite parties in the government, which is why no Iraqi military or security force is capable of contending with them. The Shi'ite militias have developed a trade in oil pirated from Iraqi oilfields and its transport up to Iraq's borders with Syria, Jordan, Kuwait, Saudi Arabia and Iran. About 20% to 30% of Iraq's entire production is smuggled. To corner the market, Shi'ite militias have agreed to act as the main channel for smuggled arms to reach Sunni and Baathist insurgents and al Qaeda's contingents in Iraq. Iraq's Prime Minister is attempting to stop the oil smuggling because the more weapons they carry to these end users, the more oil smugglers are willing to push across the borders.

Iran said it planned to build two 1,000 Mw nuclear reactors and would solicit bids within the next two months. The Deputy head of Iran's Atomic Energy Organization, Mohammad Saeedi, said the tender would be open to domestic and international firms. Iran's first 1,000 Mw nuclear power plant, being built with Russian help in the southern port of Bushehr, is expected to come on stream in late 2007.

OPEC's Ministerial Monitoring Committee recommended the group maintain its oil production unchanged at its meeting on Thursday. While most OPEC members favor keeping their quotas unchanged, Venezuela has called for a cut in production, arguing that world oil supplies are above requirements. Venezuela's President Hugo Chavez said current oil prices above \$70/barrel were fair and added that the market was oversupplied. He said prices should not be allowed to fall below \$50/barrel. Venezuela's Oil Minister Rafael Ramirez said market fundamentals suggest OPEC needs to cut production. He said if OPEC decided against a reduction in supplies then it may be necessary to cut production later in the year. Meanwhile, Libya's oil official Shokri Ghanem said he would not be surprised to see oil prices reach \$80/barrel.

Refinery News

Valero Energy Corp said there was no significant impact to production at its 250,000 bpd Port Arthur, Texas refinery following a problem with a fluid catalytic cracking unit on Tuesday.

According to a report filed with the Texas Commission on Environmental Quality, the operation of a diesel hydrotreater at Alon USA's 70,000 bpd Big Spring, Texas refinery was interrupted on Tuesday.

The Texas Commission on Environmental Quality said a pump malfunction at Valero Energy Corp's 250,000 bpd Port Arthur, Texas refinery early Tuesday morning caused a brief upset and emissions at its fluid catalytic cracking unit.

Italy's ERG said it would restart operations at its Isab Nord refinery in Sicily on June 4 following a fire in April. It said production would be at 80% of capacity or 120,000 bpd. It is expected to resume full capacity in a month's time. The restart coincided with the gradual resumption of output at the 310,000 bpd Saras refinery in Sarroch, Sardinia following scheduled maintenance. Shipping agents said oil and gas discharge and loading operations at ERG's Augusta terminal were slowly returning to normal.

China's West Pacific Petroleum Corp restarted a 600,000 ton/year reformer unit following a six month closure as a domestic fuel price increase lifted margins of gasoline. However this is not expected to lead to a large increase in the company's gasoline exports due to China's tight control over fuel exports to meet peak domestic demand in the summer.

A spokesman for the South Oil Co said one of Iraq's offshore oil export terminals, Khor al-Amaya, needed 4 months of repairs following an explosion last week. He said investigations were still continuing to find the cause of the fire that started on Friday and lasted several hours. The head of the State Oil Marketing Organization, Falah Alamri said crude product to be loaded from Khor al-Amaya would be transferred to the Basra terminal. On the contrary, shipping and port agents stated that crude exports from the Khor al-Amaya terminal should resume in the next couple of days.

Iraq's State Oil Marketing Organization said Iraq has issued a buy tender for between 60,000 and 75,000 tons of gasoil over the period of three months. SOMO also announced two tenders for gasoline. One tender is for between 40,000 and 60,000 tons and would be allotted to the first two to three bidders while a second tender for between 200,000 and 300,000 tons would be allotted equally between the first three to five bidders. It also announced tenders for between 90,000 and 150,000 tons of LPG.

Ecuador's Energy Minister Ivan Rodriguez said that despite an agreement signed between Ecuador and Venezuela to refine up to 100,000 bpd of Ecuadorean crude in Venezuelan refineries, Venezuela is expected refine only 65,000 bpd. Ecuador's Energy Minister said it would refine its crude in Curacao and in PDVSA's refinery in the US starting in July.

According to Japan's Ministry of Economy, Trade and Industry, oil product sales in Japan increased 0.3% in April to 18.73 million kiloliters or 3.93 million bpd. It reported that gasoline sales increased 0.2% to 4.97 million kl or 1.04 million bpd in April. Gasoline inventories fell by 0.19% to 2.09 million kl or 13.15 million barrels in the week ending May 27. It reported that Japan's 30 refineries ran at an average of 69.8% of their 4.77 million bpd capacity last week, down 0.1% on the week. Commercial crude stocks increased by 2% or 2.7 million barrels to 115.1 million barrels. Crude oil imports totaled 20.91 million kl or 4.38 million bpd in April, up 14.3% on the year.

India's oil product exports in April fell 7.1% on the year in April to 1.3 million tons on strong domestic demand. The sale of domestic oil products in India during April increased 5.9% on the year to 9.5 million tons.

India's government is expected to review retail fuel prices on Monday or Tuesday. The government has not raised the retail price of petrol and diesel since September despite increasing crude oil costs.

Saudi Aramco has set its June contract price for propane and butane at \$470/ton, unchanged on the month.

Kazakhstan's KazMunaiGas said it would pay \$1 billion to buy a 50% share in oil firm KazGerMunai from Germany's RWE Dea, Erdgas Erdol and the International Finance Corporation.

Production News

Venezuelan government officials said Venezuela would book an estimated 30 billion barrels of new heavy oil reserves by the end of the first quarter of next year. The new reserves would come from four blocks in the Carabobo are of the Orinoco river basin.

Thailand's Energy Ministry reported that Thai demand for oil products in April fell by 4.5% on the year to 649,830 bpd. Its data showed that rising world oil prices with no cushion of domestic fuel subsidies continued to cut sales of premium gasoline and diesel while demand for jet fuel continued to increase.

OPEC's news agency reported that OPEC's basket of crudes increased to \$65.41/barrel on Tuesday, up from Monday's level of \$65.12/barrel.

Market Commentary

The oil market gapped lower from 71.90 to 71.20 on the opening, in follow through selling seen in overnight trading after Tuesday's late sell off. The market traded lower early in the session in light of the news the Bush administration seeking to enlist Russian support for a UN Security Council resolution on Iran, agreed to language ruling out immediate threat of military force. The market sold off to a low of 70.05 later in the session following the announcement that the US was ready to join Britain, France and Germany in talks with Iran, if the country suspended its nuclear activities. The unexpected US diplomatic overture triggered the sell off in the market. The market, which held good support at its low, bounced off that level and rallied to a high of 71.50 ahead of the close. The market saw some short covering as the Islamic Republic News Agency dismissed the US overture as US propaganda. The crude market settled down 74 cents at 71.29. Volume in the crude market was good with over 245,000 lots booked on the day. The June gasoline contract settled down 88 points at 214.11 after it posted a recovery ahead of its expiration. The market gapped lower from 214.50 to 212.00 and sold off to a low of 207.25 amid the sell off in the oil market. The gasoline market however bounced off its low and extended its gains to over 4.5 cents as it posted a high of 219.50 ahead of its expiration. The July gasoline contract also posted a recovery in prices ahead of the close and settled down 2.32 cents at 209.57. Meanwhile, the heating oil market also gapped lower from 200.00 to 199.00 and extended its losses throughout most of the session as it sold off to a low of 193.50. The market however bounced off its low and retraced some of its losses ahead of the close. The June heating oil market settled down 4.34 cents at 196.05. The July heating oil contract settled down 2.96 cents at 199.53. Volumes in the product markets were good with 49,000 lots booked in the gasoline market and 64,000 lots booked in the heating oil market.

The oil market on Thursday will continue to remain headline driven as the market seeks further development

s during the meeting between the UN Security Council permanent members and Germany as they continue to discuss a resolution on Iran. The

Technical Analysis		
	Levels	Explanation
CL 71.29, down 74 cents	Resistance	72.75 to 72.95
	Support	71.50 to 71.90
		70.50, 70.05 69.90, 69.80
HO 199.53, down 2.96 cents	Resistance	204.70, 205.00 to 206.30
	Support	201.00 to 202.30
		198.00, 196.25 196.00, 192.50
HU 209.57, down 2.32 cents	Resistance	216.50
	Support	211.00 to 211.50
		203.25 202.00, 200.00

market will also seek further direction from the weekly petroleum stock reports, which are expected to a small build of about 500,000 barrels in crude stocks, a build of about 1.5 million barrels in each gasoline stocks and distillate stocks. If the market does see builds in product stocks, the UN Security Council members make some progress on their talks on Iran and OPEC leaves its output unchanged as expected, the market will continue to trade lower and breach its recent support at 70.00. The market is seen finding initial support at 70.50 followed by 70.05. More distant support is seen at its previous lows of 69.90 and 69.80 followed by 68.40. Meanwhile resistance is seen at 71.50 to 71.90 followed by 72.75 to 72.95.