



## ***ENERGY RISK MANAGEMENT***

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### **ENERGY MARKET REPORT FOR JULY 8, 2008**

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A senior Iranian official warned that Iran will strike Israel and the US navy in the Persian Gulf if it is attacked over its nuclear program. Ali Shirzi, an aide to Iran's Supreme Leader made his comments amid reports of possible US and Israeli plans to strike Iran's nuclear facilities. He said Iran and its forces were at the peak of their capability, power and readiness. Iran's President Mahmoud Ahmadinejad said Iran will maintain its nuclear program. He said Iran has the right to develop a nuclear program. He said Iran will not accept illegal demands.

Separately, Iran's ambassador to the UK, Rassoul Movahedian said world powers are

#### Market Watch

JP Morgan said crude oil futures may reach \$150/barrel later this month. It said it expects the price of WTI to remain above \$130 for the rest of the summer and \$115 throughout this year. Meanwhile, Lehman Brothers increased its oil price forecast to an average \$127/barrel for 2008 from its previous estimate of \$105/barrel.

The chief economist at AMP Capital Investors said oil prices may fall to \$100 within six months.

T. Boone Pickens said oil prices will not fall below \$100/barrel again. He said the US should invest more in natural gas to cut dependence on foreign oil. He said he has launched an ad campaign for a national energy plan aimed at educating Americans about the economic drag caused by foreign oil spending. He said the rally in oil prices was not driven by speculation. He said the price of oil was increasing because world demand was exceeding supplies. He also stated that the use of natural gas power vehicles can reduce oil imports by 38% while wind can generate 200,000 Mw of power by 2010 and account for 22% of the electricity supply.

Senator Charles Schumer said the Federal Reserve should regulate an over-the-counter clearinghouse for credit default swaps. He said such a clearinghouse should be chartered as a New York bank, which would shift regulatory oversight from the CFTC to the Fed.

Federal Reserve chairman Ben Bernanke said US financial markets need to be made more resilient and stable possibly by giving the central bank broader authority to collect information and exercise authority over the country's financial firms. Meanwhile, Federal Reserve Bank of Richmond President Jeffrey Lacker said even though the US economy still faces risks, the chances of a severe downturn appear to have receded. He added that as those risks recede, policymakers should consider taking back some of the recent cuts in official interest rates.

The China Association of Automobile Manufacturers said China's sales of locally made passenger vehicles in the January to June period increased by 17.07% on the year to 3.6 million units. The growth in sales slowed from the 22.26% increase in the first half of last year. In June, sales of passenger vehicles in China increased by 15.23% on the year to 588,300 units. It was up 4.19% on the month.

**June Calendar Averages**

CL – 141.45

HO – 398.22

RB – 349.59

wasting their time by insisting that Iran must suspend its uranium enrichment to end the standoff on their nuclear program.

US and British naval forces ended their military exercises in the Gulf on Tuesday and dismissed that they were related to tensions with Iran. The exercises took place against a backdrop of high tensions between Iran and the West over Iran's nuclear program. The US Fifth Fleet said the military exercise was part of ongoing training aimed at protecting the region's oil infrastructure from any attack.

According to DEBKAfile, secret talks between the US and Iranian delegations that were started last month yielded as hoc understandings on controversial issues. One is an agreement not to allow the price of oil to rocket past \$150/barrel. It said its Gulf and Iranian sources disclosed that the bilateral negotiations were deliberately masked by rhetoric indicating that a US or Israeli attack on Iran's nuclear installations was imminent. However its understandings are ad hoc and could well break down in the volatile climate generated by hardline elements of Iran's Revolutionary Guards. DEBKAfile reported that the US was willing to refrain from military action against Iran before the end of the Bush presidency in January 2009 cut could not promise Israel would not act unilaterally. Iran undertook to open the way for the US military to continue to fight al Qaeda and the Sunni insurgents in Iraq to allow President Bush to claim his Iraq campaign had ended successfully before leaving the White House. They also discussed the Bush administration's ambition to help fellow Republican Senator John McCain to get elected to the White House. It said that while some of the understandings were still work in progress, the oil price ceiling was agreed upon.

Russia said it would use military means if the US deployed a missile defense shield close to Russia's borders.

Leaders from the Group of Eight industrialized nations expressed their concern about rising oil and food prices, saying they hurt the poor, stoke inflation and threaten global economic growth. However the proposed counter steps do not appear to offer any quick fix for the problems. The group stopped short of recommending any approaches such as tighter regulations on speculators trading oil or concerted action to reverse the dollar's downtrend that some analysts blame for helping drive crude prices higher. The G8 members said that while they remain positive about the long term resilience of their economies and future global economic growth, the world's economy is facing uncertainty and downside risks persist. They said they were worried about soaring oil prices and pledged to create a forum that would discuss ways to avoid future spikes. At the behest of Britain's Prime Minister Gordon Brown, leaders agreed to convene a world energy forum, which will be held in Japan this September to discuss energy efficiency and new technologies. A second summit of oil producers and consumers will be held in December in London. They also pledged to promote clean energy and carbon trading schemes to curb greenhouse gas emissions and recognized the importance of sustainable biofuel production.

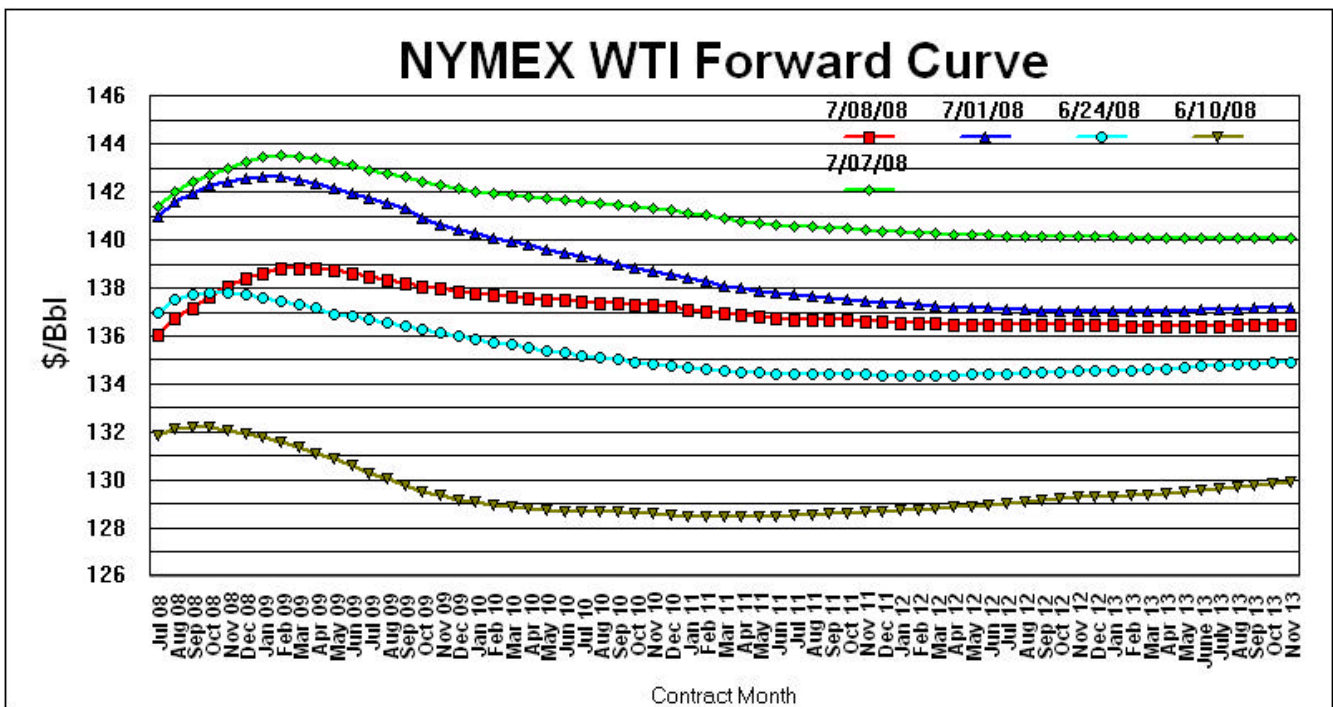
The EU presidency announced that European Union finance ministers reached a political agreement on Tuesday to publish weekly oil stocks.

The IEA executive director Nobuo Tanaka said biofuels in the US and Europe are playing an important role in the oil market. He said oil prices would be higher without biofuels. He said biofuels replaced about 1 million bpd equivalent of crude consumption since 2005. He urged governments to spend more on research and development of second generation biofuels.

Nigeria's President Umaru Yar'Adua called for an international effort to stop fuel smuggling in the country's Delta region. He said stolen crude aids corruption, violence and can provoke war.

In its latest Short-Term Energy Outlook, the EIA said US crude oil will average \$127.39/barrel this year, up 4.3% from its previous estimate. It sees crude oil averaging \$142.67/barrel in the third quarter of the year and increasing to \$145/barrel on average in the fourth quarter. It said gasoline prices over the summer will average \$3.99/gallon, up 4 cents from its previous estimate. It estimated gasoline prices will increase to \$4.21/gallon in the third quarter and \$4.23/gallon in the final quarter of 2008. Gasoline is expected to average \$3.84/gallon in 2008, up 6 cents from its previous estimate. The price of diesel is expected to average \$4.73/gallon in the third quarter, down 2 cents from its previous estimate while the retail price of diesel for all of 2008 is estimated at \$4.35/gallon, up 3 cents from its previous estimate. World oil demand is estimated to increase by 1.02 million bpd in the third quarter to 86.54 million bpd, up 0.23% from its previous estimate. Global oil demand is seen up 1% at 86.4 million bpd for the full year 2008, up 0.02% from its previous estimate. The EIA reported that China's oil demand is expected to increase by 6.3% or 480,000 bpd to 8.07 million bpd in the third quarter. Demand growth from China will account for about 37% of total world oil demand growth in the quarter. The EIA said commercial stockpiles held by OECD members increased by 36 million barrels in the second quarter, well below the average 83 million barrel build. OECD stocks were 2.57 million barrels or 26 million barrels below the five year average and equal to 53 days of forward demand. Total world production is estimated at 86.48 million bpd, down 0.7% from its previous estimate. Non-OPEC production is projected to increase by 240,000 bpd in 2008 and by 830,000 bpd in 2009 to 49.38 million bpd and 50.21 million bpd, respectively. The EIA reported that US oil demand in 2008 is expected to fall about 2% or 410,000 bpd to 20.29 million bpd. It is down from its previous estimate of 20.41 million bpd. For the current third quarter, the EIA revised demand down by 60,000 bpd to 20.64 million bpd. It cut its fourth quarter demand estimate by 120,000 bpd to 20.53 million bpd. US oil demand for 2009 was increased slightly to 20.33 million bpd. It reported that gasoline demand for 2008 is estimated at 9.2 million bpd, down 20,000 bpd from its previous estimate while its distillate demand estimate was cut by 30,000 bpd to 4.15 million bpd. In regards to OPEC, the EIA said OPEC increased its output by 20,000 bpd to 32.45 million bpd in June.

According to MasterCard Advisors LLC, US gasoline demand fell by 1.2% or 119,000 bpd on the week to 9.426 million bpd in the week ending July. Demand was down 3.9% on the year. The four week



moving average for gasoline demand fell 3% to 9.43 million bpd. It reported that the US average retail price of gasoline increased 0.5% or 2 cents/gallon to \$4.08/gallon.

### **Refinery News**

Colonial Pipeline said it was allocating cycles 36 and 37 on its Linden, New Jersey delivery line L2.

Motiva Enterprises LLC was restarting a 110,000 bpd hydrocracker at its 240,000 bpd refinery in Norco, Louisiana following a turnaround.

Declining exports of Mexico's heavy sour crude was seen having little or no effect on operations at the US oil refineries with long term contracts to buy it. Valero Energy Corp said it has no problem supplying crude to its refineries despite the decline in crude exports from Mexico. Valero's 325,000 bpd refinery in Port Arthur, Texas has a contract to buy 206,000 bpd of the heavy sour Maya crude from Mexico through 2011. Meanwhile, Shell said its 333,700 bpd refinery in Deer Park, Texas was still receiving heavy sour crude from its joint venture partner, Pemex.

Royal Dutch Shell Plc is considering shipping oil sands crude from its Alberta project to be processed at its 165,000 bpd Martinez, California refinery and its 332,000 bpd Deer Park, Texas refinery. A Shell executive said the company could upgrade extra bitumen from a proposed expansion at its Athabasca Oil Sands Project into refinery ready crude in the US rather than proceed with a C\$27 billion expansion of its Alberta-based facility that would increase production by 100,000 bpd around the end of the decade.

Separately, Royal Dutch Shell Plc said it canceled plans to build a new heavy oil refinery near Sarnia, Ontario due to current market conditions and inflationary pressures. It was considering building a facility able to process crude from its Alberta oil sands operations, with a capacity of 150,000-200,000 bpd at its existing facility.

Pemex announced a tender for September maintenance work at a catalytic converter at the 320,000 bpd Tula refinery. The converter is located in the refinery's fluid catalytic cracking unit No. 1.

Petroplus Holdings AG plans to shut units at its 172,000 bpd Coryton refinery in the UK for maintenance next year, cutting gasoline supplies to London. Work on a fluid catalytic cracker and alkylation unit will start at the end of January.

Japan's TonenGeneral Sekiyu said it was preparing to restart its 170,000 bpd Wakayama refinery from Wednesday following an unplanned shutdown due to a lightning related power outage. It said operations of units including the two crude distillation units along with most secondary units would be restarted on Wednesday.

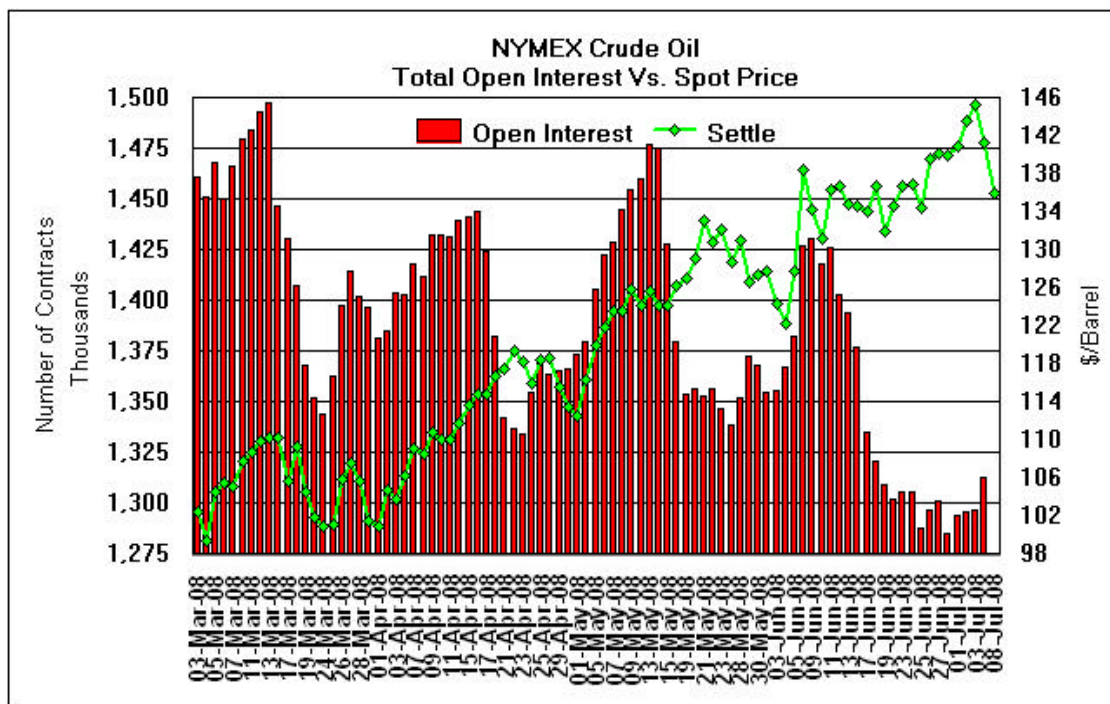
Japan's Cosmo Oil Co said it plans to restart a 130,000 bpd crude distillation unit at its Chiba refinery on Friday after a delay caused by underwater piping used to transport crude. The crude unit, which has been shut for planned maintenance since late April, was originally scheduled to restart on July 1.

Taiwan's Bureau of Energy said its crude oil imports fell by 13.9% on the year to 27.18 million barrels in May. Taiwan's petroleum product imports increased by 45% on the year to 1.642 million kiloliters in May while its oil product exports increased by 13.3% on the year to 1.65 million kl. In May, Taiwan consumed 4.49 million kl, up 9.1% on the year.

Another 30,000 tons of diesel has been booked for Australia from Asia this month following an explosion at Apache's gas plant explosion on June 3. The shipment brings total Asian diesel shipments to Australia to 450,000 tons so far.

**Production News**

ConocoPhillips said its oil production in the second quarter fell by 60,000 bpd of oil equivalent from the first quarter. It said that while refinery margins improved in the second quarter compared with the first quarter, its profits were hurt by the



negative impact from secondary products. Refining margins increased by 43% from the first quarter to \$14.19/barrel.

Oil and Gas UK expects oil and gas output in 2008 to fall to about 2.6-2.7 million bpd of oil equivalent from 2.8 million boe in 2007.

The North Sea Ekofisk crude oil system is expected to load about 397,000 bpd in August, down from 408,000 bpd in July.

OPEC's news agency reported that OPEC's basket of crudes fell to \$138.44/barrel on Monday from a revised \$140.13/barrel level on Friday.

**Market Commentary**

The oil market ended the session in negative territory once again as the market remained pressured following Monday's sharp sell off. The market extended its losses to more than \$6.20 as it posted a low of \$135.14, the lowest level seen since late June. The oil market fell along with the world equity markets due to negative sentiment on the economy. Meanwhile, the strength in the dollar also provided little support to the oil market. The dollar's gains limited the appeal of commodities as a hedge against inflation. The oil market, which posted a high of 142.44 in overnight trading on Globex, sold off sharply early in the session and retraced more than 38% of its move from a low of 122.05 to a high of 145.85. The crude market later settled in a \$2 trading range during the remainder of the session and ended the session down \$5.33 at \$136.04. The August/September spread was relatively unchanged and settled at -.69. The spread is still seen targeting the -.95 level. The oil market on Wednesday will likely retrace some of its sharp losses as the weekly petroleum inventory reports are expected to show draws in crude stocks of 1.5 million barrels while gasoline stocks and distillate stocks are expected to see builds of 200,000 barrels and 1.8 million barrels, respectively. Support in the crude market is seen at 135.14 followed by 133.95 and 131.14. It is interesting to note the large increase in crude oil open interest of 16,301 lots following Monday's sell off. Open interest in the

August, September and October contracts built by 5,220 lots, 6,985 lots and 1,217 lots, respectively. Meanwhile, the RBOB market retraced almost 62% of its move from a low of 314.75 to a high of 360.21 as it sold off to a low of 336.30 early in the session. The market later retraced some of its losses and settled in a sideways trading pattern during the remainder of the session. It ended the session down 11.96 cents at 336.31. The market is seen finding support at 333.50 followed by 332.12, 329.97 and 314.75. The heating oil market also extended its losses to over 17 cents as it sold off to a low of 379.82 amid the losses in the crude market. It retraced almost 62% of its move from a low of 356.49 to a high of 413.50 before it retraced some of its losses and settled down 14.94 cents at 382.02. The heating oil market is seen finding support at 379.82, 378.27, 376.31 followed by 371.04 and 356.49.

		<b>Explanation</b>
<b>CL</b>	<b>Resistance</b>	144.53, 145.85, 146.48, 149.41, 150.00
	136.04, down \$5.33	137.15, 139.15, 140.00, 142.44
<b>Support</b>		135.14
		133.95, 131.14
<b>HO</b>	<b>Resistance</b>	407.65, 411.00, 413.50
	382.02, down 14.94 cents	385.85, 391.60, 395.00, 399.90
<b>Support</b>		379.82
		378.27, 376.31, 371.04, 356.49
<b>RB</b>	<b>Resistance</b>	355.75, 357.96, 359.27, 360.21
	336.31, down 11.96 cents	338.65, 345.00, 351.00
<b>Support</b>		333.50
		332.12, 329.97, 314.75