



## **ENERGY RISK MANAGEMENT**

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### **ENERGY MARKET REPORT FOR JULY 29, 2008**

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OPEC's President Chakib Khelil said current oil prices are "abnormal" and added that OPEC members should not cut supply if they continue to fall. He said oil prices could continue to fall by another \$50/barrel to \$70-\$80/barrel in the long term, if the US dollar continued to strengthen and geopolitical tensions eased. He also stated that the recent price move did not reflect supply issues.

Royal Dutch Shell declared force majeure on Tuesday on its Nigerian Bonny Light crude exports for July to September following an attack by militants on an oil trunk pipeline in the Niger Delta on Monday. It confirmed that parts of its Nembe Creek trunk line were damaged in the attack. It however

#### Market Watch

The Conference Board said its overall monthly measure of consumers' mood increased to 51.9 in July, from an upwardly revised 51 in June. It was the first rise since December. It said its gauge of inflation expectations fell to 7.6% after reaching a record high of 7.7% in May and June.

SemCrude Pipeline has been stripped of management control of a \$120 million pipeline construction project from Colorado to Cushing, Oklahoma. A Delaware bankruptcy judge ordered that the pipeline, connecting terminals in Platteville, Colorado with Cushing will be managed by PE-Pipeline Services, although SemCrude is to remain on the job. Meanwhile according to court filings, SemGroup LP is seeking court approval to obtain \$250 million in debtor in possession financing from Bank of America as it proceeds with its bankruptcy case. The US Bankruptcy Court for the district of Delaware is scheduled to rule on the financing project on July 31.

A Commodity Futures Trading Commission official said that billions of dollars in speculative investment are having an impact on futures markets. However CFTC commissioner Bart Chilton is calling for an independent study to determine just how much. Despite his concern over possibility volatility from speculators on futures markets, he said any remedy should not push large index funds out of the futures markets.

China's cabinet, the State Council, approved the set-up and composition of a new entity that would help put together the country's energy strategy development, planning and policies. The National Energy Administration will include an electricity, coal, oil, natural gas, alternate energy and renewables, energy conservation and technological equipment, development and planning, policies and regulations and international cooperation department. The National Energy Administration can raise proposals and suggestions on adjusting prices of energy categories such as oil products while the National Development and Reform Commission continues to have the final say on price revision proposals.

China and Russia will hold their second round of talks on energy cooperation in Moscow later this year. China wants to focus energy cooperation on crude oil trade, construction of oil and gas pipelines, prospecting and exploitation and refining and chemical industries.

**July Calendar Averages**

CL – 134.29

HO – 381.19

RB – 330.29

said it was still continuing to check its facilities for further damage. Exports of Bonny Light were originally scheduled to average 175,806 bpd in July, 222,581 bpd in August and 235,000 bpd in September.

Venezuela's Oil Minister Rafael Ramirez said the country plans to maintain its stance not to increase its oil production at the upcoming OPEC meeting in September. He noted that the latest developments in oil prices indicate that market speculation is at fault.

Iran's President Mahmoud Ahmadinejad said that the world's major powers were in decline and added that developing countries could play a greater role in resolving world conflicts. He also stated that Iran would continue talks with world powers aimed at resolving the crisis over its nuclear program provided the talks proceed on equal footing. He however said illegal conditions should not be imposed on the talks and added that Iran will not give up on their rights. Iran was given a two week deadline, which expires Saturday, to give a final answer to world powers that have offered a package of incentives to try to persuade Iran to halt sensitive nuclear work. Meanwhile US Secretary of State Condoleezza Rice warned Iran not to delay a decision on the incentive package.

Turkish warplanes bombed a Kurdish rebel hideout in northern Iraq on Tuesday, destroying the base and killing an unspecified number of militants. The raid targeted a large cave in the Qandil mountains used by the Kurdistan Workers' Party as a base.

According to MasterCard Advisors, US gasoline demand increased by 0.7% or 62,000 bpd on the week to 9.625 million bpd. In the latest four weeks, demand was down 4.1% on the year. Year to date demand for gasoline is still 2.23% below last year's level due to high prices. It also reported that US retail average price of gasoline fell by 2% or 8 cents/gallon to \$4.02/gallon on the week.

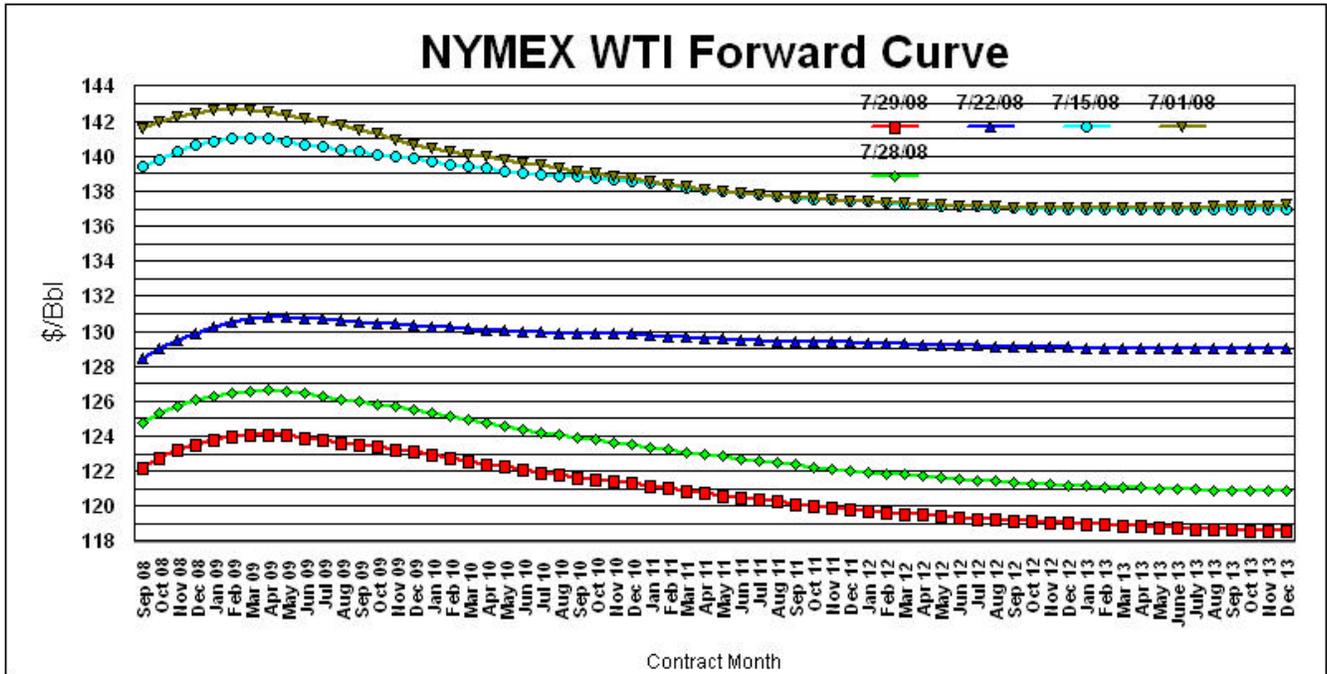
The EIA reported that US crude oil imports in May fell by 671,000 bpd or 6.5% on the year to 9.657 million bpd. It is down 264,000 bpd or 2.7% on the month. Canada was the top supplier, with 1.84 million bpd while Saudi Arabia was the second largest supplier at 1.579 million bpd. Crude oil imports from Mexico fell by 143,000 bpd or 11.4% on the month to 1.116 million bpd.

**Refinery News**

Chevron Corp said its 260,000 bpd refinery in El Segundo, California was not affected by the 5.8 magnitude earthquake that shook southern California on Tuesday afternoon. BP Plc also stated that there was no impact to its 265,000 bpd refinery in Carson California following the earthquake while Valero Energy Corp also said there was no damage to its 135,000 bpd refinery in Wilmington, California.

BP Plc said the second residue hydrotreater at its 475,000 bpd Texas City, Texas is due back on stream in coming days. It will increase its runs to 80% of capacity following the restart of the unit. It also plans to restart a gasoline reforming unit in the second half of the year, increasing its operations to 95% of capacity. It will resume full output at the refinery by early next year after it has been running under normal rates following an explosion in 2005 that killed 15 workers. Meanwhile, BP said it was ready to take its Whiting, Indiana refinery to the next phase of conversion to run heavy Canadian crude. It has received the air and water permits to convert the refinery to run the heavier Canadian crude. It will upgrade the refinery to run on 80% Canadian heavy crude oil. The expansion is scheduled to be completed in 2011 and will increase gasoline production by 1.7 million gallons/day.

Separately, BP reported that its net income increased 28% to \$9.47 billion in the second quarter from \$7.38 billion a year earlier. BP Plc's chief executive, Tony Hayward, said he saw demand destruction of 5-10% for gasoline in developed OECD economies due to high prices. He also said BP would



defend its disputed investment in Russian joint venture, TNK-BP. BP's chief executive also stated that Russia's decision to offer tax breaks on oil production should increase output, although it could take a couple of years.

Valero Energy Corp announced plans for major work at six of its refineries during the second half of 2008. Its Port Arthur, Texas refinery will shut its 45,000 bpd hydrocracker for 38 days starting in July. Its Texas City, Texas refinery will shut its 85,000 bpd crude unit for 35 days starting in September and lasting into October. It will also shut a 50,000 bpd coker unit for 40 days, starting in September and lasting into October. Its Three Rivers, Texas refinery will shut its 30,000 bpd hydrocracker unit for 28 days starting in September while its Delaware City, Delaware refinery will shut its 180,000 bpd crude unit for 25 days beginning in October. Its Ardmore, Oklahoma refinery will shut a 12,000 bpd hydrocracker unit for 30 days starting in October. It will also shut a 30,000 bpd fluid catalytic cracking unit for 20 days that month. Valero's Wilmington, California refinery is also scheduled to shut its 55,000 bpd gasoline unit for 15 days starting in October.

Separately, Valero Corp reported a 67% decline in quarterly earnings on Tuesday as rising oil prices cut profits from gasoline production. Its net income in the second quarter fell to \$734 million from \$2.25 billion last year. Valero chief executive Bill Klesse said that gasoline margins will continue to be weak and industry wide refinery utilization rates will continue to fall through the end of next year. However he expects margins for distillates to be strong over that period. Valero also stated that it may not sell its Memphis and Ardmore, Oklahoma refinery amid lower refining margins. Valero expects its US Gulf Coast refineries to process about 1.5 million bpd of crude during the third quarter. It expects its mid-continent refineries to process about 430,000 bpd while its West Coast refineries process between 280,000 bpd and 290,000 bpd. It expects its Northeast refineries to process between 540,000 bpd and 550,000 bpd in the third quarter.

ConocoPhillips shut a fluid catalytic cracking unit at its 247,000 bpd Alliance refinery in Belle Chase, Louisiana for maintenance on Monday. It has been shut for three weeks of unplanned maintenance. Trade sources said that Conoco was buying about 250,000 barrels of gasoline on Monday in the Gulf, barrels which were destined for the New York Harbor market.

Citgo Petroleum Corp is shutting a fluid catalytic cracking unit at its Lemont, Illinois refinery this week for one to two weeks of maintenance work. It was seen as a major buyer in the Midwest's Chicago cash gasoline market late on Tuesday.

Nippon Oil Corp said it plans to refine 4.03 million kiloliters or 818,000 bpd in August, down 2% on the year amid slow domestic oil demand and high gasoline inventories. |

A Reuters survey showed that overall crude runs by South Korean refiners are expected to fall in August from this month due to maintenance at a crude distillation unit. SK Energy, GS Caltex, S-Oil Corp and Hyundai Oilbank are expected to run 2.17 million bpd of crude in August or 78% of capacity, down from 2.26 million bpd in July.

Indonesia's Pertamina will import 13.44 million barrels of oil products in August, the highest in nearly three years, due to a major refinery shutdown. It is up 5% from 12.82 million barrels estimated for July. Its August imports include 2.46 million barrels of fuel oil, 6.4 million barrels of diesel, 4.16 million barrels of gasoline and 420,000 barrels of jet fuel.

Sinopec Corp has completed a new crude terminal in northern China to receive very large crude carriers with a capacity of 300,000 tonnage or 2.2 million barrels and 800,000 cubic meters or 5 million barrels of storage tanks. A crude pipeline has also been laid to link the crude terminal to an oil transfer hub in the port city of Tianjin, where Sinopec operates a 110,000 bpd Tianjin refinery.

South Korea's GS Caltex plans to skip spot exports of gasoline in August due to a shutdown at its 130,000 bpd crude unit next month.

Transneft pledged not to postpone the launch of the East Siberia-Pacific Ocean pipeline again. In February, Transneft's President Nikolai Tokarev said the launch of the pipeline's first part would be delayed until late 2009. Initially, the launch was scheduled for late 2008.

### **Production News**

BP Plc said its Thunder Horse field in the US Gulf of Mexico was procuring over 40,000 bpd of oil and would reach full capacity of 250,000 bpd by the end of 2009. The long delayed field will produce a maximum of 200 million cubic feet/day of natural gas when it reaches peak production.

Norway's DNO International ASA said net entitlement production fell by 11% in the second quarter to 12,809 bpd from the first three months of 2008.

Indonesia's crude oil production is likely to fall to 857,900 bpd in July from 859,000 bpd in June.

Iran and Oman's Hengam field is scheduled to produce 16,000 barrels of light crude this year. The field is estimated to have 2000 billion cubic feet of natural gas and more than 700 million barrels of crude oil.

Iran has discovered a new oil field in the southern port city of Assaluyeh. The oil field has about 525 million barrels of in-place crude oil reserves with a 40 degree API gravity.

Mexico's Energy Ministry reported that it will be difficult for Mexico to reach 3 million bpd in oil production before 2020 due to the long time it takes projects to get off the ground.

Petroecuador reported export revenue of about \$3.74 billion between January and June, up 137% from \$1.58 billion reported last year. In terms of volume, Petroecuador exported 39.65 million barrels of crude between January and June, up 25% from 31.82 million barrels reported last year.

OPEC's news agency reported that OPEC's basket of crudes increased to \$123.19/barrel on Monday from Friday's \$122.63/barrel.

### **Market Commentary**

The oil market extended its recent losses and sold off to its lowest level in nearly three months amid the strength in the dollar. The market posted an outside trading day as it posted a high of \$125.85 in overnight trading. However the market breached its support at \$122.30 and sold off to a low of \$120.42, a level not seen since May 6<sup>th</sup> as the strength in the dollar reduced the appeal of commodities. The market also seemed to have shrugged off the news of Royal Dutch Shell declaring a force majeure on its Nigerian Bonny Light crude exports as it gave up its earlier gains. In light volume trading, the crude market later settled in sideways trading pattern before it traded back to \$123.45 in afternoon trading. It settled down \$2.54 at \$122.19. The market on Wednesday will be focused on the release of the weekly petroleum stock reports, which are expected to show draws in crude stocks of 1.4 million barrels, draws in gasoline stocks of 100,000 barrels and builds in distillate stocks of 1.7 million barrels. The crude market is seen finding support at \$119.18, \$117.71 followed by \$117.02, its 62% retracement off a low of \$97.93 to a high of \$147.90 while resistance is seen at \$123.45, \$124.10, \$125.85 and \$126.51. Open interest in the crude market fell by a total of 6,037 lots to 1,214,030, with open interest in the September contract falling by 10,727 lots to 296,497. Open interest in the October contract built by 774 to 113,283 while November and December saw builds of 1,020 to 70,060 and 2,252 to 170,615, respectively. Meanwhile, the product markets sold off sharply amid the reports of demand destruction. The RBOB market also posted an outside trading day as it posted a high of 308.95 in overnight trading. However the market extended its losses to 8.99 cents as it sold off to a low of 298.01. The market settled in a sideways trading pattern ahead of the close and settled down 6.23 cents at 300.77. The market on Wednesday will be driven by the inventory reports. The market is seen trading lower especially if the report does show an expected drop in gasoline demand. It is seen finding support at 298.01, 293.84 followed by 290.50. The heating oil market also settled sharply lower, down 8.98 cents at 347.22. The market, which is still trending lower, extended its losses to over 11.5 cents and retraced more than 50% of its move from a low of 280.69 and a high of 415.86 as it posted a low of 344.68. Similar to the rest of the complex, it retraced some of its losses ahead of the close. It traded back above the 350.00 level before a bout of selling on the close pushed it back towards its low. The market is also seen testing its low amid the expectation of builds in distillate stocks. It is seen finding support at 298.01, 293.84 and 290.50 while resistance is seen at

304.21,  
306.60,  
308.95  
and  
314.60.

		<b>Explanation</b>	
<b>CL</b>	<b>Resistance</b>	126.51, 128.70	Previous highs
	122.19, down \$2.54	123.45, 124.10, 125.85	Tuesday's high
	<b>Support</b>	120.42	Tuesday's low
		119.18, 117.71, 117.02, 114.22	Previous lows, 62%(97.93 and 147.90), Previous lows
<b>HO</b>	<b>Resistance</b>	359.78, 360.04, 368.34	Previous highs
	347.22, down 8.98 cents	350.39, 355.55, 358.22	Tuesday's high
	<b>Support</b>	344.68	Tuesday's low
		332.32, 328.01, 322.56	62% retracement(280.69 and 415.86), Previous lows
<b>RB</b>	<b>Resistance</b>	314.60, 324.47	Previous highs
	300.77, down 6.23 cents	304.21, 306.60, 308.95	Tuesday's high
	<b>Support</b>	298.01	Tuesday's low
		293.84, 290.50	62%(251.03 and 363.10), Previous lows