



## ***ENERGY RISK MANAGEMENT***

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## **ENERGY MARKET REPORT FOR AUGUST 26, 2008**

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Hurricane Gustav is seen threatening energy interests in the Gulf of Mexico within days. Hurricane models have reached a consensus about its general path but it remains unclear exactly which part of the Gulf the storm will traverse and how intense it will become as it nears oil and gas platforms. The National Oceanic and Atmospheric Administration's Geophysical Fluid Dynamics Laboratory said Hurricane Gustav, currently a category 1 hurricane, may enter the Gulf of Mexico on Sunday as a

### Market Watch

Royal Dutch Shell Plc said personnel evacuations from the Gulf of Mexico could start as early as Wednesday as Hurricane Gustav moves northwest through the Caribbean Sea. Shell said it was making logistical arrangements to evacuate staff who are not essential to production or drilling operations, given the expectation that it may enter the Gulf of Mexico this weekend.

The US dollar climbed back towards a six month high against the euro amid continuing fears about the European economy. The dollar strengthened as German business confidence fell to its lowest level in three years in August according to the Ifo Institute. GDP data also showed that the German economy fell in the second quarter of 2008. The US currency has benefited as the economic outlook has darkened in both mainland Europe and the UK. Warren Buffet said last week that he had no bets against the dollar, underscoring the currency's strength.

US consumer confidence recovered more than expected in August as worries over inflation eased. The Conference Board said its index measuring consumers' confidence increased to 56.9 in August from July's 51.9. It also said its gauge of inflation expectations fell to 6.7% from July's revised 7.5%. Meanwhile, sales of newly built US single-family homes in July were lower than expected but increased from a June pace that was the slowest in nearly 17 years while the glut of homes on the market also eased. The S&P/Case-Shiller composite index of home prices in 20 metropolitan areas fell by 0.5% on the month and by 15.9% on the year.

The fall in US oil demand may be even greater than previously forecast, raising the prospect that third quarter demand could fall below the second quarter level for the first time in 20 years. Demand has declined due to the weak economy and surging prices. Signs of weaker than expected demand cast doubt on the EIA's projection that US demand in the third quarter will average 20.46 million bpd, an increase of 520,000 bpd from the second quarter.

Mexico raised diesel prices as the country's President Felipe Calderon seeks to lessen the cost of subsidizing imported fuel. According to the Amegas gas station association, diesel prices increased to 6.48 pesos or 63 US cents/liter, an increase of 0.10 pesos/liter.

### August Calendar Averages

CL – 116.74

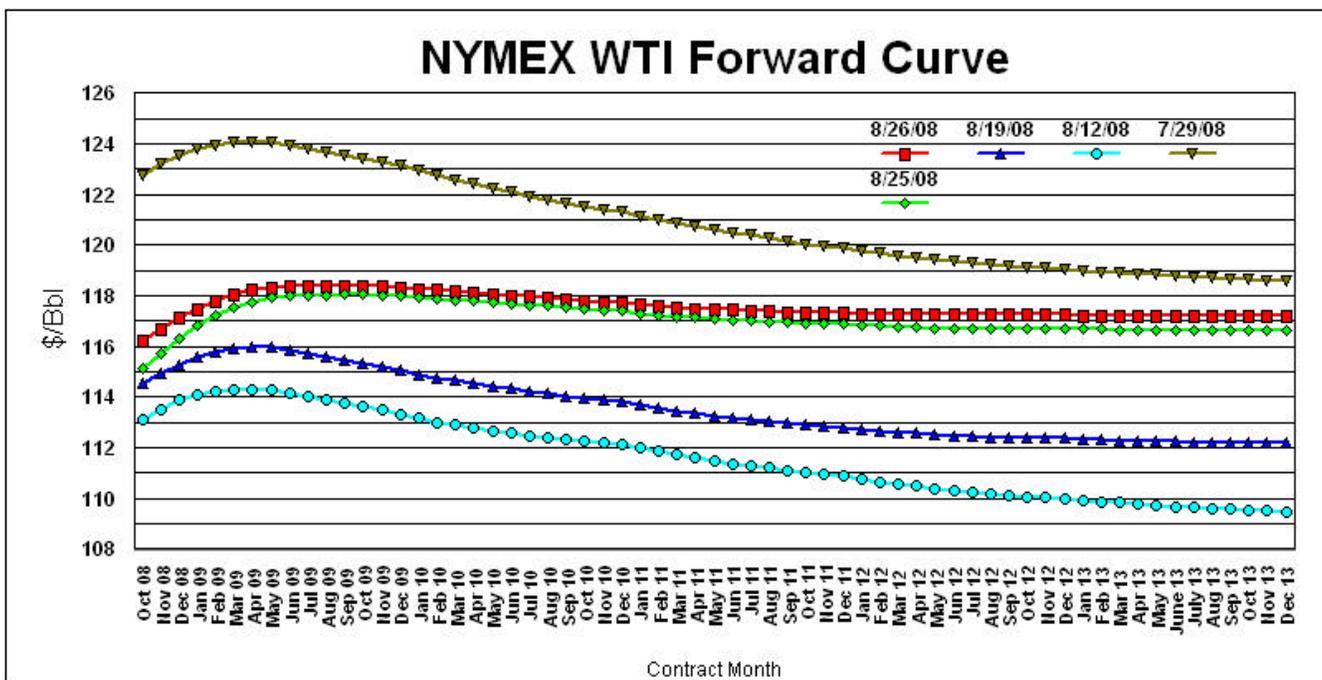
HO – 318.78

RB – 292.50

category 4 storm. It said Hurricane Gustav will bypass Cuba for the most part, allowing it to maintain its strength. By late Sunday or early Monday, Hurricane Gustav is forecast to enter the Gulf with winds of 135-140 mph. Hurricane models diverge widely in predicting where Hurricane Gustav would make landfall after it enters the Gulf. Two models showed an area of high pressure forcing Gustav westward toward Mexico's Yucatan Peninsula while three other models forecast that the storm would head toward the central Gulf, including the Texas, Louisiana and Mississippi coast.

Russia's President Dmitry Medvedev announced that he signed a decree under which Russia formally recognizes the rebel Georgian provinces of South Ossetia and Abkhazia as independent states. He instructed the foreign ministry to open talks with the provinces on establishing diplomatic relations with Russia. Separately, Russia's President said Russia would respond militarily to the deployment of US missiles close to its borders under a US missile shield plan. Meanwhile, Russia's Foreign Minister Sergei Lavrov said Russia is not facing international isolation for its decision to recognize two Georgian separatist regions as independent countries. In response Georgian National Security Council Secretary Alexander Lomaia said Russia's decision to recognize the rebel Georgian regions of South Ossetia and Abkhazia as independent has no legal force and will lead to harsh political consequences for Russia. Georgia's President Mikhail Saakashvili accused Russia of seeking to change Europe's borders by force. He accused Russia of seeking to break the Georgian state. Meanwhile, US President George W. Bush denounced Russian recognition of Georgia's rebel regions, warning it must reconsider its irresponsible decision. The UK rejected Russia's formal recognition of the rebel Georgian provinces, reaffirming its support for Georgia's territorial integrity. Germany's Chancellor Angela Merkel also voiced support for Georgia's territorial integrity.

A top Russian general questioned the extreme level of activity of North Atlantic Treaty Organization naval forces in the Black Sea saying it could not be needed for the delivery of aid to Georgia or for routine naval exercises. He insisted that Russia was complying with a French brokered peace plan while Georgia's military was rearming. Meanwhile, a US embassy spokesman said a US navy destroyer carrying humanitarian aid to Georgia was headed to the port city of Poti, where Russian forces are deployed. The USS McFaul and another US ship will dock in Poti on Wednesday.



The head of the IEA, Nobuo Tanaka said OPEC should leave its output unchanged when it meets next month on September 9 to bring oil prices down further. He said the current oil price of \$113-\$115 was still high and harmful to the world economy. In the near term, he expects the market tightness will ease as new production capacity comes onstream.

Iran's OPEC Governor, Mohammad Ali Khatibi said OPEC members favor a balanced crude oil market and could still decide on rolling over or cutting output at their upcoming meeting on September 9. He said the market is currently not balanced and is oversupplied.

Norway's Petroleum and Energy Minister, Terje Riis-Johansen said the oil price remains quite high despite falling sharply from peaks in July.

A senior Botas official said two tankers with a combined capacity of 1.7 million barrels are expected to finish loading at the Ceyhan port of the Baku-Tbilisi-Ceyhan oil pipeline on Tuesday. It is the first loading at Ceyhan following an explosion on the 1 million bpd pipeline in eastern Turkey earlier this month stopped flow on the pipeline.

Iraq suspended shipments of Kirkuk crude into the Turkish export terminal of Ceyhan for unknown reasons on Tuesday. The pipeline to Ceyhan was pumping about 20,000 barrels/hour or 480,000 bpd before shipments were halted. A VLCC was loading 2 million barrels of Kirkuk crude on Tuesday. There was enough oil in storage to complete the loading. Once that vessel loads, storage would stand at about 370,000 barrels. Another ship is due to start loading 1 million barrels early Wednesday for Italy's Eni.

According to the EIA, US oil demand in June was 1.17 million bpd or 5.6% lower on the year at 19.553 million bpd. Demand was cut by 793,000 bpd or 3.9% from its earlier estimate of 20.346 million bpd. The revision for June put demand in the first half of the year at an average of 19.78 million bpd, down 936,000 bpd or 4.5% on the year. Gasoline demand was revised down 2.8% to 9.071 million bpd. It is down 4.4% on the year. The revised six month gasoline demand is down 2% or 180,000 bpd from a year ago at 9.071 million bpd. Demand for distillate was revised down 9.8% or 405,000 bpd to 3.728 million bpd in June. Distillate demand in the first six months of the year averaged 4.062 million bpd, down 4.7% or 199,333 bpd on the year. The EIA also reported that US exports of distillate fuel tripled in June from a year ago to 745,000 bpd.

MasterCard Advisors LLC's SpendingPulse report showed that US gasoline demand increased by 1.3% on the week but fell by 2.9% on the year to 9.579 million bpd in the week ending August 22. The four week average gasoline demand was down 4.5% on the year at 9.536 million bpd. It also reported that the US average retail price of gasoline fell by 7 cents to \$3.70/gallon on the week.

Norway's Prime Minister Jens Stoltenberg said Norway will remain a reliable supplier of energy. However he said the main political challenge will be to combine oil activity with protecting ecological resources.

### **Refinery News**

StatoilHydro ASA said its 200,000 bpd Mongstad refinery resumed operations on Monday. It said a fluid catalytic cracking unit was shut.

Traders said China's PetroChina will skip gasoline imports and may resume large exports in September due to high stockpiles. It has already booked 60,000 tons of gasoline for shipment next month, which are likely to head to Indonesia. Meanwhile, China's West Pacific Petrochemical Corp will ship 90,000 tons in September, little changed from August levels.

China's Ministry of Commerce said it has set the 2009 non-state import quota for refined oil products at 11.25 million tons, up from 10.65 million tons for 2008.

### **Production News**

Iraq's Oil Ministry reported that the country exported 1.9 million bpd in July, down from 1.94 million bpd in June. Crude shipments from Iraq's southern ports increased to 1.51 million bpd, up from 1.45 million bpd in June. Crude shipments from northern Iraq fell to 383,387 bpd from 483,000 bpd in June.

Norway's StatoilHydro said it wants to maintain production off Norway at 1.5 million barrels of oil equivalent/day for 10 years and increase output by 2012. Including international operations, StatoilHydro seeks to increase production to 2.2 million bpd of oil equivalent by 2012 from 1.9 million bpd of oil equivalent. It also stated that it is seeking more acquisitions after taking over the oil and gas operations of Norsk Hydro last year. StatoilHydro's chief executive Helge Lund said he expects oil prices to remain high as the industry struggles to meet increasing world demand for oil and gas.

Mexico's Energy Ministry reported that crude production from its Cantarell oil field fell for the tenth consecutive month in July to 974,000 bpd. The field is yielding half what it was yielding at its 2004 peak. The steady decline of about 15% annually in the field's output has pressured the divided Congress to change laws in the closed energy sector. The government hopes to push a bill through congress to allow more private participation in the state run oil business. While lawmakers debate the proposal, Pemex is trying to increase output at less productive fields, such as the Ku Maloob Zaap complex and the Chicontepec field.

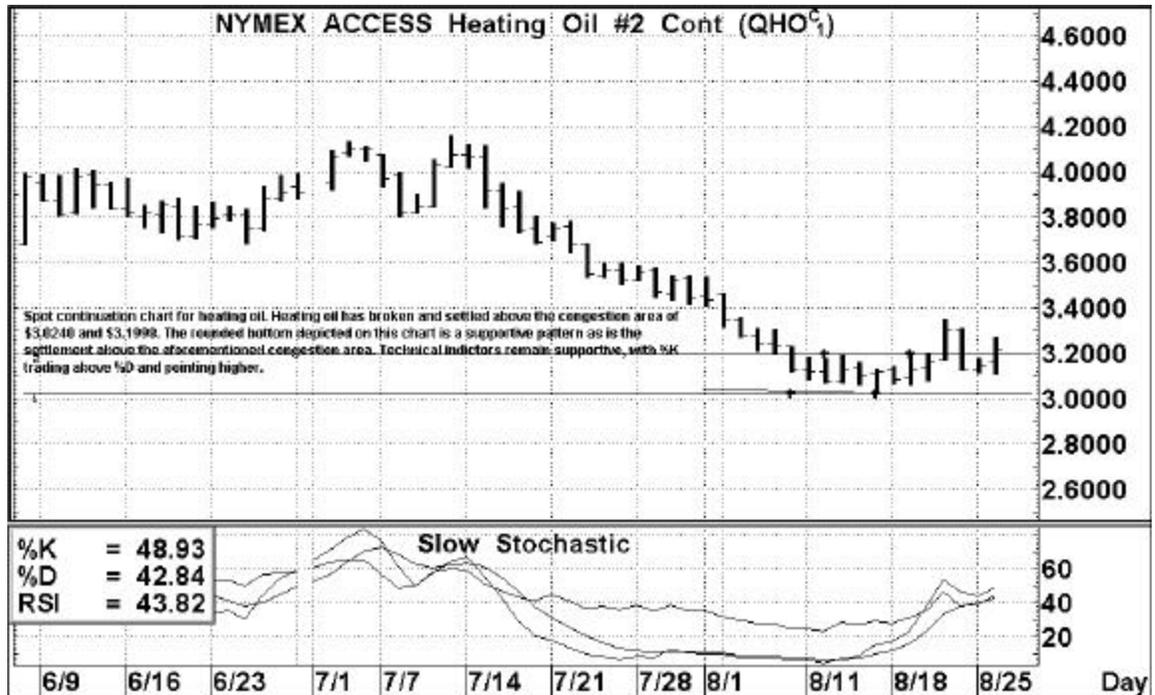
Libya's National Oil Co set its September official selling price for its Essider crude grade at a discount of 85 cents to Dated Brent.

OPEC's news agency reported that OPEC's basket of crudes fell by \$4.02/barrel to \$110.61/barrel on Monday.

### **Market Commentary**

The upgrading of Tropical Storm Gustav to a hurricane helped propel prices higher today. According to certain weather reports, Hurricane Gustav is on course to traipse over the Gulf of Mexico, stretching from Alabama to Texas. Should Gustav follow this path, it will pass right over several oil platforms located in the Gulf of Mexico. Despite the fact that the dollar was at a six-month high versus the euro, October crude oil gained almost \$3.00 at one point during the trading session. Had the dollar not been so strong today, this market may have been able to hold its strength, closing near the highs of the day. DOE/API numbers are due out tomorrow, with preliminary expectations indicating nothing alarming. Crude oil stocks are expected to increase by 1 million barrels, distillate stocks to decrease by 0.1 million barrels and gasoline stocks to down 3.0 million barrels. According to MasterCard's SpendingPulse, gasoline demand decreased by 4.5% based on a four-week average. The October08 crude oil contract seems to have found a range of congestion between \$117.40 and \$111.50. Technical indicators have moved higher in neutral territory, indicating the potential for this market to work higher. The projected upside objective based on this range is \$123.30. The October08/September 08 crude oil spread continued to trade within the range of -.61 and -.47 throughout most of the session, however it did settle outside of it at -.43. We would continue to look for this spread to gain strength with a possible test at the flat level. Based on this we would like to buy the October and sell the November contract. With refiners reducing their summer grade of gasoline, we may see this product strengthen further. Our near term upside objective for the October 08 contract is \$3.2110, the 50% retracement number using the range of \$3.6310 and \$2.7909. Heating oil

experienced an outside trading session, achieving a lower low and a higher high, settling higher on the day. This is considered supportive for prices. All three technical indicators have moved higher, further adding to the



supportive sentiment towards this product. Heating oil as with the crude oil, has seemed to find an area of congestion between \$3.0240 and \$3.1998. Prices broke out of this pattern and settled above it. Based on this pattern of congestion, the projected upside target is \$3.3756. Open interest for crude oil is 1,195,913 749, October 08 302,397 down 6,784, November 08 111,963, up 3,376 and December 08 180,732 up 2,309. Total open interest for heating oil is 225,279 up 1,443, September 08, 22,427 down 1,977 and October 08 52,114 up 1,627. Total open interest for gasoline is, 222,330 down 1,096, September 08, 29,534 down 2,831 and October 08 75,257 up 1,441.

<b>Crude Support</b>	<b>Crude Resistance</b>
109.55, 108.00, 105.18, <b>85.40</b>	128.60, 132.05, 139.30, 144.00, 147.90,
<b>Heat support</b>	<b>Heat resistance</b>
3.0540, 3.0229, 294.50	3.4574, 3.3798, 3.6135, 3.8215, 4.0210,
<b>Gasoline support</b>	<b>Gasoline resistance</b>
2.7014, 2.6435, 2.5920	3.0300, 3.0732, 3.1050, 3.1460, 3.1840, 3.2620