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Energy Risk  
Management Services

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**HIGHLY CONFIDENTIAL**

February 25, 2009

**Good Morning**

**Overview**

- Hydrocarbon prices were once again mixed overnight. **Crude oil up \$0.50 to \$40.46 per barrel; natural gas down \$0.005 to \$4.231 per mmBtu.**

**News/Views**

- We are sure it is just our cynical imagination at work. However, given the equity market's recent negative reaction to Administration officials' inability to talk the talk, let alone walk the walk, we sense it was left up to Fed Chairman Bernanke to try and set a new tone for things, which, at least for one day, had the intended result. His claim, as spun by the media, that the recession could terminate with extreme prejudice by the end of the year appears to be more optimistic than previous government expectations and now even falls into the realm of our optimistic assumptions, so of course we hope he is right.
- Perhaps the greater market impact came from his playing down the idea of nationalizing the banking system. In any event, crude oil followed suit, clearly negating for the moment our thought of yesterday morning that WTI could not depend on the equity market for any help with our constructive longer-term forecast. Also helping crude oil was word that yes, Virginia, OPEC is trying to restrain output, with tanker-tracking mavens such as Petrologistics reporting that compliance early in 2009 has been better than market expectations. Once again one day does not a market make, so we all will be quite interested to see whether all this has any "legs" or not.
- Obviously one element to the equation will be the weekly DOE stats, due out later this morning. Yesterday afternoon the API reported a smaller crude oil build than analysts' expectations, with a draw in gasoline instead of an anticipated gain. Distillate supplies rose more than the market was looking for, but as we move through the remainder of the first quarter gasoline and crude oil should set the market tone. While overnight prompt WTI managed to trade above \$40.00 per barrel once again, partially in response to the API stats, trading should remain somewhat restrained until the DOE numbers are released, given the frequent tendency for the numbers to diverge on a short-term basis. In this regard, our guesstimates would suggest a crude build of less than 1.0 million barrels, but a smaller gasoline draw than the API reported. However, we would also look for a more constructive distillate number.
- Otherwise, we wish to emphasize a couple points we made in our most recent monthly natural gas report since many of you may not have had time to read it yet given all that is going on the markets. Our bottom line is that although we have retained our longer-term forecast for a "rebalancing" of the gas market by the end of the year and thus expect prices to improve, the ability thus far of the NYMEX to hold at around \$4.00 per mmBtu on a settlement basis has given us even more confidence in our outlook, right or wrong. We would therefore recommend that those who trade the commodities take a shot at the long side, but keep tight stops for the time being and wait for tomorrow's storage stats. We would normally suggest buying natural and selling crude oil against it as a hedge, but since we also believe that crude oil will gradually work its way higher we would just as soon take the risk for the bigger bang for the buck.

Although we were compelled to revise down our industrial sector gas demand expectations to some degree given recent abysmal manufacturing activity, we also cut our dry gas production outlook, such that by the fourth quarter U.S. output falls below last year. This sounds quite absurd, given all the shale gas development, but the literal collapse in rig activity should lead to a major impact on aggregate production rates over the next several months. Our analysis suggests that if all this falls into place, prompt NYMEX natural could hit \$7.00 per mmBtu or so in September.

William H. Brown, III

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