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Energy Risk
Management Services

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March 17, 2009

Good Morning

Overview

- Hydrocarbon prices firmed overnight. **Crude oil up \$0.45 to \$47.80 per barrel; natural gas up \$0.030 to \$3.880 per mmBtu.**

News/Views

- While once again not wishing to read too much into one day's trading activity and it may have been our imagination, yesterday's crude oil action suggested that our Base Case WTI outlook may have some merit after all. The day began with a typical neo/knee-jerk reaction to the outcome of OPEC meeting where the ministers agreed to retain the current ceiling and emphasize stricter compliance, however vague that strategy will end up being. As the day progressed, however, crude oil turned around. We had suggested yesterday morning that once the meeting ended, WTI's fate would fall back once again into the hands of weekly data, economic news and, of course the S&P 500. Lo and behold, thanks in large part to Ben Bernanke's 60 Minutes interview, equities rose, pulling crude oil back up. However, at the end of the day crude oil managed to hold onto most of its gains while the S&P 500 gave up its rally for various reasons, including American Express' statements about rising late payments in February. Granted, word emerged that Chevron had shut in some Nigerian output following pipeline sabotage, but the volumes were only 11.5 MB/D and the market has become rather immune to such news.
- Once again we do not wish to give the market too much credit in one day, but traders and funds may be coming to the realization that OPEC's actions were not only "appropriate" given the current financial situation, but "appropriate" within the context of the global demand and supply balance in terms of leveraging prices back up progressively over an extended period of time, therefore easing any economic impact. We, of course, are "talking our book" here in terms of how this all fits nicely into our Base Case outlook, but there is no question that the market has been more impressed with OPEC levels of compliance that we have seen in several years.
- The proof in all this is how the market may respond to weekly data that confirm such behavior via a progressive reduction in crude oil stocks, perhaps aided by implied demand data that appear less negative. We have emphasized that all this will take time, in part due to the presence of floating storage that needs to be worked off, but we believe the market may be willing to be patient, and not simply opt to drop back below \$40.00 per barrel because OPEC did not slash output further. Month to date, prompt WTI has averaged \$44.72 per barrel. Our Base Case as laid out back in January called for March to average \$47.80 per barrel, so we remain on our limb.
- Otherwise, the market may tread water until the latest API numbers are released late this afternoon, followed by the DOE data Wednesday morning. The latest Platts survey is looking for a 2.0 million barrel build in crude oil stocks, a 2.1 million barrel fall in gasoline supplies, and a 400,000 barrel build in distillate inventories. Our current cut at the numbers would suggest a smaller crude oil build than the market is looking for. Given the tricky nature of week-to-week volatility in crude oil imports, we nonetheless believe that the four-week rolling average we are witnessing now fairly reflects the impact of lower OPEC crude oil deliveries into the U.S., particularly from Saudi Arabia. The gross total is starting

to average a bit shy of 9.0 MMB/D, and assuming there is no material change in refinery crude oil runs and that the numbers are reconcilable, crude stocks “should” rise by less than 1.0 million barrels.

For products, however, unless implied gasoline demand recovers more than we estimate, we would look for stocks declining less than consensus expectations. Lower imports will help, but implied demand under 9.0 MMB/D and steady refinery output will largely offset. Finally, we expect a somewhat larger distillate build than the market is looking for, even if implied demand recovers from the previous week, reverting to the underlying mean. If we are close to the mark on all fronts, we would hazard to guess that the market may “lean” toward more constructive crude oil data.

W.H. Brown, III

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