



HORNSBY & COMPANY, INC.

www.hornsbysco.com

Energy Risk  
Management Services

## HIGHLY CONFIDENTIAL

March 31, 2009

### Good Morning

#### Overview

- Hydrocarbon prices firmed overnight. **Crude oil up \$1.12 to \$49.53 per barrel; natural gas up \$0.079 to \$3.818 per mmbtu.**

#### News/Views

- Yesterday morning we suggested the market was likely to test \$50.00 per barrel as prices declined, and it obviously did so with extreme prejudice and with little respect. Our "backing and filling" characterization of the market prior to further price recovery now appears a bit conservative, but given this market the jury is clearly out in terms of whether we will begin rebounding again over the short term or if \$45.00 per barrel is in the cards. The latter would clearly occur if the equity markets were to decline further back toward the March lows and if forthcoming economic data fell short of expectations. Adding to the weakness, although as discussed yesterday not a consistent influence thus far this year, would be any further strengthening of the dollar in response to the outcome of the G-20 confab. We have to admit in all this, however, that the Street's reaction to the auto industry problems was overdone, particularly with regard to any assumed influence on oil demand, if one believes the neopress as to part of the rationale for yesterday's price drop. It does not strike us that the economic influence, from employment to production, would be materially different under a "controlled" bankruptcy scenario than if management were left to their own restructuring timetable.
- As we issue this note, crude oil is rebounding for the time being above \$49.00 per barrel, aided by a recovery in Asian equity markets, higher S&P 500 futures, and a weaker dollar. Aside from financial factors, as also discussed yesterday and obviously more important than any of the above when considering the outlook for the next several months, is the "real" fundamental picture. With the financial variables working the other way on crude oil prices for the time being, there is nothing fundamental for the bulls to hang their hats on, unless the weekly stats, with the API data out later this afternoon and the DOE data tomorrow morning, are surprisingly bullish. In this regard, the latest Platts survey is looking for a 3.2 million barrel build in crude oil stocks, a 1.8 million barrel fall in gasoline supplies and a 1.4 million barrel drop in distillate inventories.
- In terms of our own guesstimates, we would be looking for a somewhat smaller build in crude oil supplies than consensus expectations, but nonetheless above 2.0 million barrels. The arithmetic is straight forward if, as we expect, imports tick down slightly and refinery crude oil runs tick up a bit. Although all variables are difficult to estimate on a week-to-week basis, imports remain the trickiest these days, given the overall uncertainty of weekly global crude flows, the timing of import booking and the drawdown in offshore storage that was built up over the last several months. Even with some effective expansions in Cushing storage, however, the numbers would still suggest stocks are near the effective shell capacity onshore the United States.
- For products, we would look for a bit smaller decline in gasoline supplies than the consensus expects at this time, unless implied demand rises significantly more than we believe from the following week. For distillates, however, we would look for a larger draw than the Platts survey suggests. Implied demand should be up a bit from the previous week as simply a reversion to the recent mean, while we believe that

refiners have consciously cut distillate yields in response to the end of the heating season in tandem with lower diesel sales. Distillate imports should also come in a bit lower than the previous week. Overall, however, we would not expect the weekly data to provide a fundamental catalyst for higher prices on a *sustainable* basis quite yet.

W.H. Brown, III

Information contained herein is believed to be reliable but its accuracy cannot be guaranteed. Past performance is not indicative of future results and the risk of loss is substantial in futures trading. Hornsby & Company, Inc. and W.H. Brown may, from time to time, have positions in the futures market relative to these recommendations.