



HIGHLY CONFIDENTIAL

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WEEKLY INVENTORY REVIEW

The DOE released the latest Weekly Petroleum Status Report for the week ending August 29, and we wish to provide our thoughts on the numbers within the context of our forecast U.S. refinery balances. Relative to consensus expectations, the crude oil and distillate draw were constructive, while the decline in gasoline inventories was not as large as the market was expecting.

With regard to crude oil, inventories declined by 1.9 million barrels. Stocks now stand at 303.9 million barrels and lie some 18.2 million barrels below last year. Supplies in PAD II were unchanged on the week, but rose at Cushing by 800,000 barrels. Stocks in PAD III fell by 1.8 million barrels. Adding up all other districts yields a net inventory decline of 200,000 barrels.

Refinery crude oil runs rose by 147 MB/D on the week to average almost 15.3 MMB/D, and were almost unchanged in PAD III revealing that there was little pre-Gustav run reduction. Gross crude oil imports declined by 149 MB/D and averaged around 9.8 MMB/D, perhaps suggesting some pre-Gustav slow steaming. Taking the DOE estimate of domestic production, crude oil stocks "should have" declined by about 2.3 million barrels.

Turning to refined products, total primary gasoline inventories fell by 1.0 million barrels, which included a 900,000 barrel gain in finished mogas supplies more than offset by a 2.0 million barrel drop in blendstocks. Inventories total 194.4 million barrels and retain a 600,000 barrel deficit to last year at this time.

Refinery production of finished gasoline rose by 295 MB/D from the prior period to average around 9.4 MMB/D. Gross imports of total mogas dropped by 485 MB/D and averaged 883 MB/D.

Implied gasoline demand rose by 13 MB/D from the previous week to average some 9.4 MMB/D. Over the last four weeks implied gasoline demand is off by 1.6% from last year, while year to date has declined by 2.0% versus the comparable period in 2007.

Finally, the DOE reported that distillate fuel oil inventories fell by 400,000 barrels. The decline included a 700,000 barrel fall in ultra low-sulphur diesel stocks, a 500,000 barrel increase in other diesel supplies, and a 300,000 barrel decline in heating oil inventories. Total distillate supplies stand at 131.7 million barrels and lie 2.5 million barrels below last year.

Refinery production of distillate rose by 123 MB/D on the week to average around 4.5 MMB/D. Gross distillate imports fell by 30 MB/D and averaged only 93 MB/D.

Implied distillate demand rose by 160 MB/D from the previous period to average more than 4.3 MMB/D. For the past four weeks implied distillate demand is up by 2.7% over last year, while year to date is down by 2.8% versus the comparable period in 2007.

As we issue this report, despite the constructive crude oil and distillate data NYMEX crude oil is declining in response to a recovery in the dollar versus the euro, suggesting that the inverse link remains more influential than short-term fundamentals. While next week's numbers suggests a larger stock draw is possible, we retain our Base Case that for the remainder of the third quarter supplies will not fall materially below 300.0 million barrels.

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