



HORNSBY & COMPANY, INC.

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Energy Risk
Management Services

HIGHLY CONFIDENTIAL

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WEEKLY STORAGE REVIEW

The DOE released the latest weekly natural gas working storage data, reporting an 85 bcf increase from the previous week, which had no revisions. Working storage totaled 1,614 bcf as of Friday, May 16. The details are provided below:

| Region | Current Week Stocks (bcf) | Prior Week Stocks (bcf) | Net Change (bcf) | Year Ago Stocks (bcf) |
|----------------|--|--|---------------------------------|--------------------------------------|
| East | 797 | 743 | 54 | 886 |
| West | 222 | 210 | 12 | 297 |
| Producing | 595 | 576 | 19 | 733 |
| Total Lower 48 | 1,614 | 1,529 | 85 | 1,916 |

The latest weekly storage build suggests, as discussed last week, that our end-May working storage target of around 1.77 tcf may end up on the lower end of the scale, since it implies only an average 75-80 bcf build for each of the two weeks left in the month. The data once again appear to reflect continued gains in domestic dry gas production, partially offset by lower LNG imports. The numbers would also continue to imply relatively anemic manufacturing activity, but not materially out of line from our Base Case assumption for industrial natural gas demand. Overall, however, in contrast to the more bearish outlooks for the natural gas balance for the remainder of the year, we do not anticipate beginning the 2008-2009 heating season at record levels of working storage.

In terms of price, our June target (basis July NYMEX) now lies about \$.90-\$1.00 per mmBtu below the current level as we issue this note. Clearly, the surge in crude oil prices has continued to pull natural up somewhat in sympathy, and on a prompt basis natural is trading at about 53% of crude oil value. Recently, gas prices were trading back toward our target for June, but the rise in prompt WTI from \$125.00 per barrel to \$135.00 per barrel has led to further short covering in natural. Obviously no one knows for certain at this juncture when the crude oil market will top out, with \$150.00 per barrel now becoming the most popular "bogie" for both analysts and the media. Although there is still time for sentiment to shift we would suggest that if our June target is off the mark it will likely come in somewhat too low and not too high. Although this sounds like an obvious statement from current perspectives, given the likely severe volatility that we believe lies ahead we believe prudence dictates not to materially revise up our target at this time. Clearly, however, if WTI in fact reaches \$150.00 per

barrel over the next few weeks, our model suggests \$12.50 per mmBtu for the prompt natural contract, implying in turn some lag relative to crude oil's upward surge.

William H. Brown, III

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