

June 1st, 2010

MF Global Daily Report

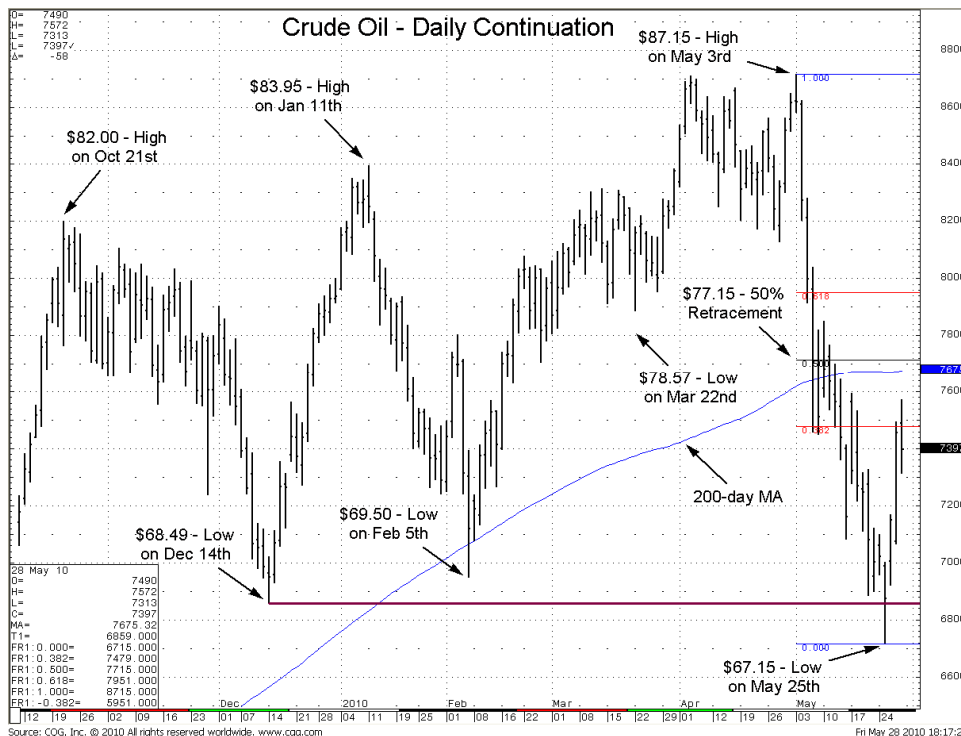
COMMODITIES | ENERGIES

Energy Weekly

MF Global
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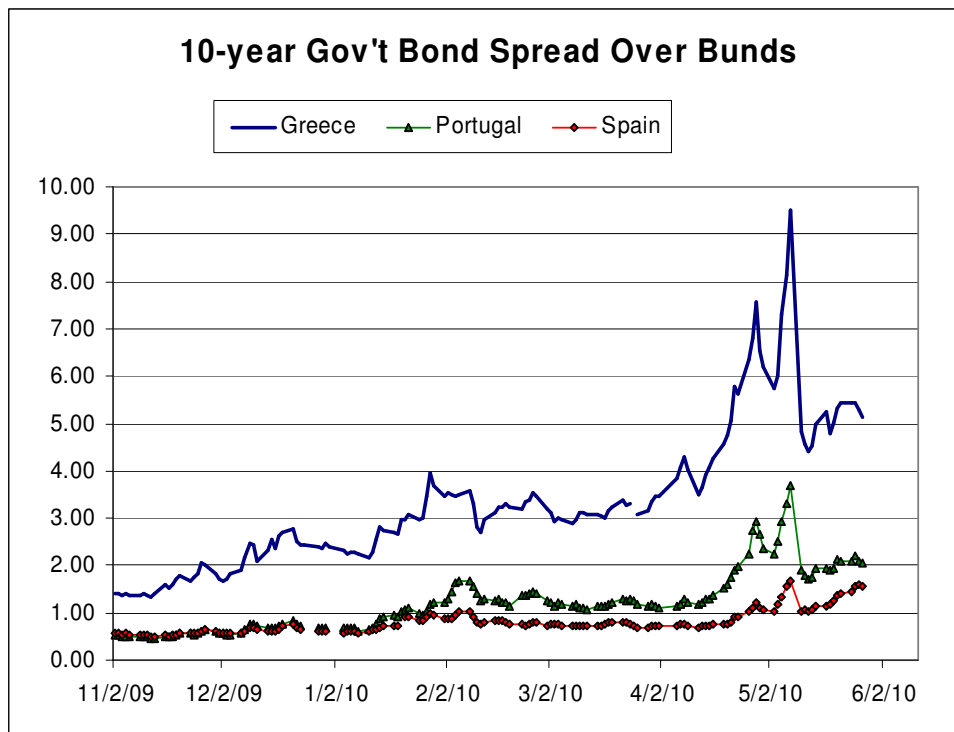
Price Outlook

Energy markets are expected to maintain last week's rebound in this shortened week's trade. Crude oil should rally toward the \$77.15 level, while gasoline and heating oil both progress toward \$2.10/gal. Energies should receive support from a resumption of the "risk-on" trade, which began last week following four weeks of rapid liquidation. Energies will also be supported by massive fund liquidation in the past two weeks, indications of higher oil demand, potentially bullish rhetoric from OPEC, upgrades to hurricane forecasts, and from positive comments on global commodity demand made by Rio Tinto. Pressure could be applied to energies if the risk trade turns to "risk off" again, but we think that is unlikely. We favor buying CLN0 at \$71.50 and targeting \$77.00 while risking \$70.00.



The oil market sold off exactly \$20.00/bbl on the continuation chart from its May 3rd peak to its May 25th bottom. The 22.9% decline was significant because it came as the Dow Industrials sold off only 13.2% and took place amid an environment of generally improving fundamental data in energies. Granted, global stock markets fell in May on concern that weakness in the Eurozone economy would snowball into a contagion-based drop in global economies. However, the consensus by the end of the week seemed to be that the selloff was overdone. By Friday, risk markets struggled to maintain Thursday's rebound, and were pressured again mid-session by a downgrade of Spain's credit rating by Fitch, and again near the close on fear that Europe would run into problems again over the weekend. However, we take solace in the fact that neither energy markets nor high yield stocks avoided falling alongside

equities. Bond spreads between southern Europe and Germany still remain off their highs as well (chart below). We think that there is still further room for risk appetite to grow this week, which should benefit oil prices.



In the latter stages of May's price decline, commodity fundamentals began to improve. U.S. oil demand recovered by rising 818 kb/d over the past four weeks, which compares to an average change in the five-year average of 76 kb/d. Total oil demand is running 1.23 mb/d above year-ago levels, and only 597 kb/d below the five-year average. Demand for transportation fuel during the Memorial Day holiday should improve as well, with AAA forecasting a 5.4% y/y increase in travel. Earlier in the week, Rio Tinto said that demand for iron ore remained strong and said that global growth fundamentals remained the same as before the financial crisis. The reference to the effects on demand from the Eurozone debt crisis were echoed by several companies' earnings reports, which beat expectations and indicated that orders from European customers hadn't shown any signs of cancellations. Companies with positive remarks included Deere, Network Appliance, and Analog Devices.

Energy markets are also likely to keep a keen eye on supply, which we believe could be supportive this week. NOAA issued its 2010 Atlantic hurricane season forecast last week, with a prediction that there will be 14-23 named storms. The prediction is much higher than the next highest of 16-18 storms predicted by Accuweather. Colorado State University last week said that it will raise its forecast on Wednesday, which could bolster the oil market's upside. The basic cause of the upgrades is the shift from El Nino to La Nina that will prevent the wind shear that tends to inhibit storm formation. Supply concerns may also come from OPEC, which has commented recently on prices dipping below their preferred \$70-\$80/bbl price band. We found Libya's comment most interesting last week, as they said that OPEC was conducting informal talks on oil prices. Just three weeks earlier, Libya had said that it cannot act on the basis of one week or even one month's worth of price data. A Reuters poll on Friday showed a likely 130,000 b/d increase in OPEC production to the highest level since Dec '08. Our feeling is that rhetoric about compliance will be made, but action will be taken only on a sustained decline below \$70/bbl.

Although we believe that the risk trade will recover this week, the market didn't trade that way on Friday. Both stocks and the euro currency sold off in the last 15 minutes of the session toward new lows for the day. The selloff showed that a recovery in the risk trade is anything but a sure thing, but perhaps it was in anticipation of adverse weekend developments in the Eurozone. Our only consolation is that high yield didn't weaken and oil held somewhat firm during the late decline.

TRADE: Buy NGN0 at \$4.07, target \$4.50, risk \$3.97
Buy CLN0 at \$71.50, target \$77.00, risk \$70.00

Upcoming Energy Events

Wed - API Weekly Stats 4:30 pm EST

Wed - Colorado State Hurricane Forecast Update

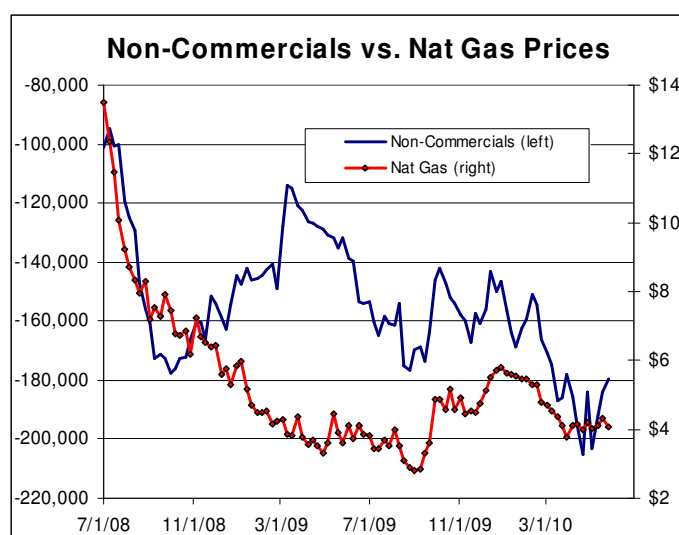
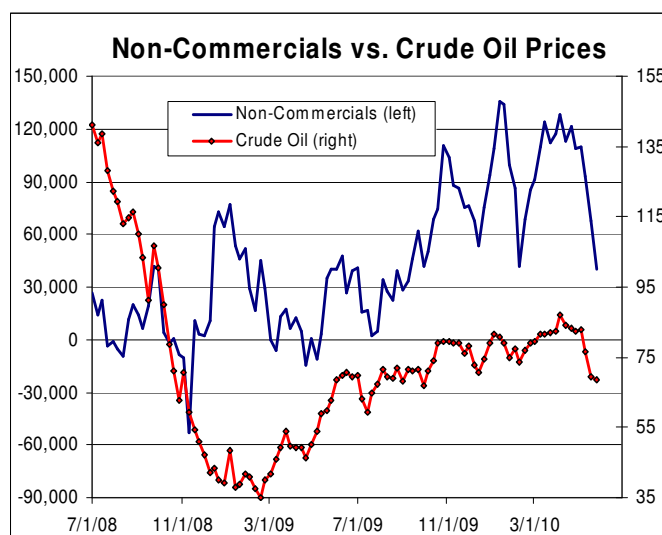
Thu - Oil Inventories 11:00 am EST

Thu - Natural Gas Inventories 10:30 pm EST

Oct 14th - Next Ordinary OPEC Meeting

Commitment of Traders May 18th-May 25th Net non-commercial (large funds) (Legacy Report)

	Net Position	Change	Price Change
Crude Oil	40,443	-26,918	-\$0.66
ICE WTI	28,125	+8,732	-\$0.66
Heating Oil	9,614	-8,261	-8.98c
Gasoline	29,408	-19,967	-11.23c
Natural Gas	-179,712	+4,483	-29.1c



Global Economic & Dollar News

The dollar moved slightly higher throughout the NY session on Friday, with support coming from weakness in the U.S. equity market. There wasn't equal follow-through in Europe or Asia on Thursday's sharp rally, and it appeared that traders began questioning the viability of the rally.

- » **Japanese Core Nationwide CPI** was -1.5% m/m in Apr vs. -1.4% expected and vs. -1.2% previously.
- » **Japanese Household Spending** was -0.7% y/y vs. +2.4% expected and vs. +4.4% previously.

- » **Japanese Unemployment Rate** was 5.1% in Apr vs. 5.0% expected and vs. 5.0% previously.
- » **Japanese Retail Sales** were +4.9% in Apr vs. +3.7% expected and vs. +4.7% previously.
- » **UK's GfK Consumer Confidence** was -18 in May vs. -16 in Apr.
- » **Chicago PMI** was 59.7 vs. 62.0 expected and vs. 63.8 previously. New orders were 62.7 vs. 65.2 previously, while employment was 49.5 vs. 57.2 in April. Prices paid were 64.0 vs. 71.4 previously.
- » **Spain's Credit Rating** was downgraded to AA+ from AAA by Fitch. The rating agency cited expectations of slower economic growth resulting from fiscal austerity measures. The outlook was left at stable, and Fitch said that it doesn't expect any other changes over the next year.

Energy News Stories

- » **BP** said that it will be another 48 hours before a conclusive view will emerge of whether "top kill" has been successful.
- » **Royal Dutch Shell** paid \$4.7B in cash for privately held East Resources in order to gain exposure to shale gas in the Marcellus shale region. The deal will increase Shell's production of natural gas by 7.5%.
- » **OPEC Production** is expected to rise 130,000 b/d to the highest level since Dec '08, according to a Reuters survey.

ANALYSIS

EIA Oil Inventory Preview

The EIA oil data will be released on Thursday at 11:00 EDT due to the Memorial Day holiday. Natural Gas stocks will be released at their normal time on Thursday.

The EIA is expected to report a decline in oil stocks of 1.0 MB this week, which is less than the 2.6 MB decline seen in the five year average. Oil stocks typically begin falling in the w/e May 21st which was last week. Last week's inventories actually grew 2.5 MB, however, which we expect to begin to unwind. Refinery utilization has recovered toward its five-year average, which should help draw down inventories this week. Opposing the draw from utilization gains will be increases in imports, which could rise again this week. Oil Movements reported that OPEC seaborne shipments improved from -150 kb/d to -110 kb/d during the survey week, and improved another 280 kb/d for deliveries scheduled for next week.

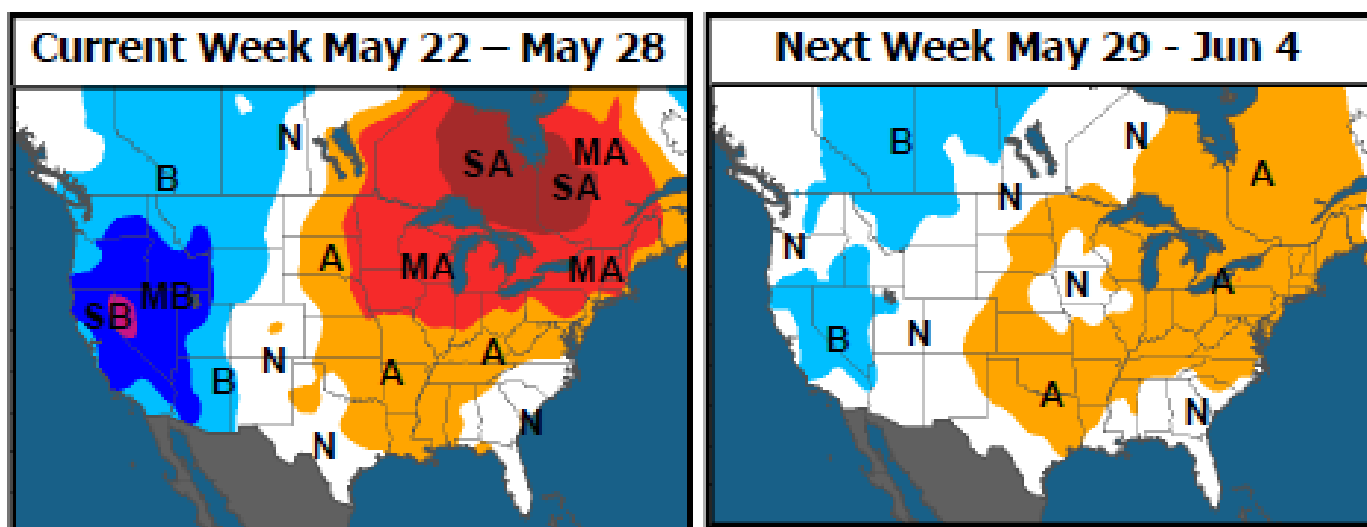
Product stocks should show gains this week, as demand for petrochemicals has outpaced that for transportation fuels. Gasoline stocks could gain 0.5 MB while distillates could increase 1.0 MB. Stocks of both gasoline and distillates typically increase beginning in mid-Apr, and the upward trend lasts until mid-Jul in gasoline and mid-Sep in distillates. This year isn't expected to be different. Countering our expectation for an increase in product stocks is the likelihood that refineries find reason to fully stock retail fuel stations in front of the U.S. Memorial Day holiday. AAA said that total travel would rise 5.4% y/y based on improved economic conditions, with auto travel up 5.4% and air travel up 2.4%. Another potential factor that could pressure inventories is the divergence with API statistics. The EIA's gasoline and distillate series are currently 3.5 MB and 4.4 MB above those of the API, meaning that either the API has to rise or the EIA has to fall. A decline of that magnitude in the EIA would be expected to offer a bullish impact on prices, while the potential for an increase in API's statistics will make those numbers equally important.

Natural gas stocks are expected to show a build of 87 bcf this week, which would represent a decline from last week's 104 bcf increase. Last week's build will likely remain as the highest build of the year, as the seasonal pattern shows declines in the rate of increase into the height of the summer cooling season. Our prediction is based on a cooling degree day forecast of 44.1, which is 13.3 degrees above the 30.8 ten-year normal. Temperature maps show generally above to much above-normal temperatures covering the eastern half of the country. Temps moderate slightly next week, with the eastern half of the country covered by either normal or above-normal temps. The early

CDD forecast is 49.0 compared to a ten-year normal of 38.1. The implication on inventories is for an increase of 94 bcf compared to a five-year normal of 96 bcf.

	EIA Inventories - w/e May 28th					API Inventories		
	Actual	Market Estimate	MFRG Estimate	Five-Year Average	Last Week	Converge with EIA	Actual	Previous
Crude Oil			-1.0 MB	-2.6 MB	+2.5 MB			+0.6 MB
Gasoline			+0.5 MB	-0.1 MB	-0.2 MB			-3.2 MB
Distillates			+1.0 MB	+1.1 MB	-0.3 MB			+1.5 MB
Utilization			+0.3%	+1.3%	87.8%			85.9%
Natural Gas			+91 bcf	+95 bcf	+104 bcf			

*The API convergence figures are the amounts that EIA data need to change in order to match the previous day's API figures



Weather Summary/Changes

On Thursday, NOAA issued its forecast for the 2010 Atlantic storm season, saying that it would produce 14-23 named storms, 8-14 hurricanes, and 3-7 major hurricanes. It said that this year could be one of the more active on record and added that conditions are favorable for La Nina to develop. NOAA's forecasts are on the upper end of the consensus of opinions.

On Wednesday, Colorado State University said that it will raise its hurricane forecast when it is updated on Jun 2nd. It said that the team sees a "hell of a year" and a "very active" season.

Current Hurricane Forecasts			
	Storms	Hurricanes	Major
NOAA	14-23	8-14	3-7
CSU	15	8	4
WSI	16	9	5
Accuweather	16-18	5	2-3

CWG	14	8	4
EarthSat	16	8	5
2007 Season	15	6	2
2008 Season	16	8	4
2009 Season	9	3	2
Average since 1950	9.6	5.9	2.3