

July 19th, 2010

MF Global Daily Report

COMMODITIES | ENERGIES

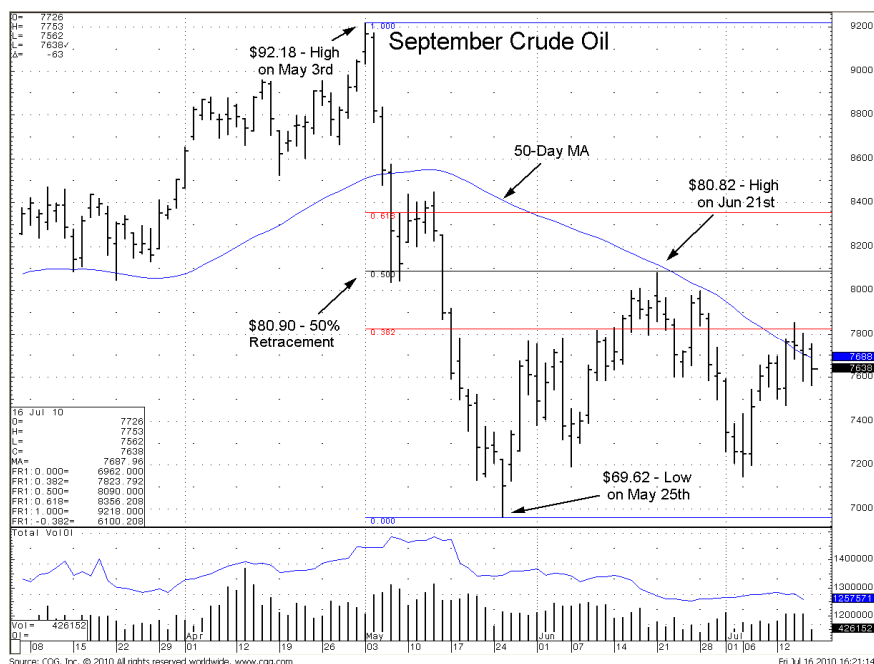
# Energy Weekly

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**\*I will be out of the office on Monday, July 19th.**

## Price Outlook

Energy markets are expected to trade in a fairly mixed direction this week. Crude oil will roll into Sep futures today and will find support at last week's \$74.70 low. Resistance will come from last week's high at \$78.55. Most factors lean toward the negative side this week, with a weaker stock market, falling oil demand, and technical factors leading the charge. Any chances of support will come from the European banking stress tests and potentially from a contrarian point of view. We favor changing our neutral bias to negative this week, and looking for oil prices to trade heavy.



The oil market has been closely tied to the stock market in recent weeks, due to the recognized usefulness of stocks as a leading indicator of economic activity. The stock market careened lower on Friday after disappointing revenues were reported by Bank of America, Citigroup, and GE, even though all three beat on EPS. The slight weakness in those stocks was made worse by a 10.1 point decline in the University of Michigan sentiment index, as well as the suggestion by Barney Frank that he would revive the White House's \$90B tax on banks because he "didn't want to let Goldman Sachs and JP Morgan off the hook entirely." Bank stocks took another hit late Friday when Bank of America said that the Durbin amendment in FinReg would cause it to take a \$10B charge. Despite favorable earnings from Alcoa and Intel earlier in the week, the feeling of economic weakness continues to exist. The Fed cut its outlook for growth and raised its forecast for unemployment in Wednesday's FOMC minutes. There are two things that the market may be noticing about the Fed. It's falling short of its mandate of price stability and full employment, and it's not undertaking any new actions to fix problem #1. Money that the Fed has attempted to pump into the

economy has wound up as excess reserves, so it's not expected that the Fed could resume its asset purchase to fix current problems. The upcoming expiration of the Bush tax cuts at the end of this year appear also to be causing corporations to pull earnings forward so that they can be taxed at a lower rate. Such a development would be seen as ensuring a double dip next year, which is being priced now.

Oil market fundamentals are also unfavorable for oil prices, as demand fell a sharp 781 kb/d in Wednesday's report. In order for the four-week average not to fall this week, demand would have to increase by 698 kb/d...something that seems unlikely given the fall in sentiment reported on Friday. The high levels of refinery utilization and low levels of demand will likely cause product inventories to gain in Wednesday's report, and thus add pressure on energy prices. Inventories of crude oil, gasoline, and distillates are now a combined 64.81 MB above their five-year average. Pressure on risk markets may also come from rumors that John Paulson is liquidating gold and holdings of other stocks. He is said to have large holdings in Bank of America and Citigroup along with the GLD ETF, and it's possible that the stock market's selloff was exacerbated because it smelled blood in the water. If that's the case, we don't know how low gold or equities could go, as these liquidations are never made public until they are completed.

The best hope for energies is that global risk markets stop falling this week as European stress test results are released. We would have thought that the results would provide some comfort to the market that European banks are not in as bad of shape as has been priced by markets. However, given the anti-risk tone that exists in markets currently, we wouldn't be surprised to see negatives from the stress tests hyped up. Problems could arise because the tests don't deal with sovereign holders of debt but rather commercial banks. The levels of the stress may be questioned, as well as the size of the haircuts taken by holders of the debt. There may also be worries that governments will put off dealing with bad debts until the economy is in better shape to handle them.

**TRADE:** None

### Upcoming Energy Events

Mon - CLQ0 Rollover

Tue - CLQ0 Last Trade

Tue - API Weekly Stats 4:30 pm EST

Wed - Oil Inventories 10:30 am EST

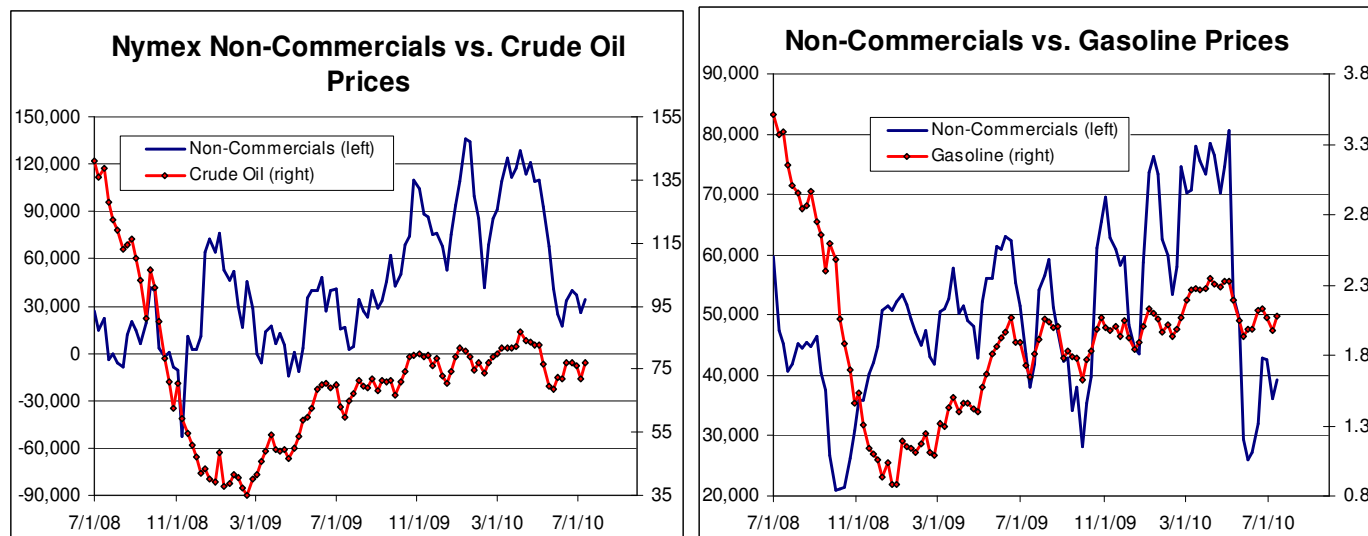
Thu - Natural Gas Inventories 10:30 pm EST

July 29th - RBQ0 & HOQ0 Rollover

Jul 30th - RBQ0 & HOQ0 Last Trade

Oct 14th - Next Ordinary OPEC Meeting

<b>Commitment of Traders Jun 29th-Jul 6th</b>			
<b>Net non-commercial (large funds) (Legacy Report)</b>			
	Net Position	Change	Price Change
Crude Oil	34,645	+8,430	+\$5.17
ICE WTI	23,631	+12,921	+\$5.17
Heating Oil	12,651	+4,203	+13.02c
Gasoline	39,342	+3,265	+11.08c
Natural Gas	-155,967	-9,686	-32.8c



### Global Economic & Dollar News

The dollar rose throughout the U.S. session as a steep selloff in U.S. stocks created a need for safe-haven. Gold failed to benefit and hovered above the day's lows throughout the session.

- » **Japanese Nationwide Department Store Sales** were -6.0% y/y in June.
- » **Chinese President Wen Jiabo** said that Europe is still a key market for forex reserve investment.
- » **IMF's Strauss-Kahn** said that the stress tests will show all major European banks are sufficiently solid.
- » **ECB's Honohan** said that the stress tests will go some way in removing concerns about some risks.
- » **Eurozone Trade Balance** was -€3.4B in May vs. +€1.5B expected.
- » **The NY Fed** reported that no swaps with foreign central banks took place again last week.
- » **U.S. CPI** was -0.1% vs. unchanged expected and +1.1% y/y vs. +2.0% previously. Core CPI was +0.2% vs. +0.1% expected and was +0.9% y/y vs. +0.9% previously. Owners Equivalent Rent rose 0.1% and was the second consecutive gain.
- » **Preliminary University of Michigan Sentiment** was 75.5 vs. 84.0 expected and vs. 85.6 previously.
- » **Delta Air Lines** reportedly saw 65,000 applicants for 1,000 jobs it was offering.
- » **Rep Barney Frank** was reported on Friday to have conducted an interview to be aired over the weekend that he would push for the White House's proposed \$90B tax on banks, saying that he could not let Goldman Sachs and JP Morgan off the hook entirely.
- » **Bank of America** said that the new regulatory burden would cause it to take significant losses on revenue and charges to earnings. It said that the Durbin amendment would cause it to lose \$1.8B-\$2.3B in debit card revenue and take a \$10B charge. The Durbin amendment limits fees that banks can charge customers for debit transactions. Card companies have said that they would attempt to make up for the revenue by charging higher fees elsewhere.

### Energy News Stories

- » **China's Crude Oil Throughput** set a new record high in Jun of 11,800 mt per day.
- » **Angola's Sep Exports** will fall to 1.48 mb/d from 1.76 mb/d in Aug.
- » **The NHC** is tracking a tropical low pressure area in the Caribbean with a 10% chance of forming in the next 48 hours.
- » **BP's Macondo Well Cap** is yielding pressures of 6,700 psi. Anything below 6,000 psi is said to be an indication of a leak. BP hopes pressures will rise toward 8,000 psi.

## ANALYSIS

### EIA Oil Inventory Preview

The EIA is expected to report another round of inventory data this week that adds pressure on the energy market. Once again, oil demand figures will be the key driver of oil prices and have been very weak in the past six weeks. Demand is 1.24 mb/d below the peak made six weeks ago, and is falling at a time when it is typically flat. Demand could certainly increase this week due to the volatility in its series. However, it will take an increase of 698 kb/d just to keep the four-week average unchanged. That would be a reading of 19,475 kb/d compared to last week's 18,777 kb/d. Crude oil stocks are expected to fall near the 0.2 MB that is seen in the five-year average. Stocks should be boosted by higher imports but pressured by elevated levels of refinery utilization. Stocks are 400,000 bbls below the API numbers, so the divergence that existed last week is no longer there. Product stocks should benefit from high levels of utilization and weak demand. We anticipate builds of 1.0 MB and 2.0 MB in gasoline and distillates respectively.

Natural Gas inventories are expected to show builds that are below five-year averages for some time due to the ongoing presence of above-normal temps in the eastern half of the country. The warmer temps result in a CDD forecast of 73.2 which is 13.6 CDDs above the ten year normal. We predict a build of 56 bcf which compares to the five-year average of 65 bcf this week. Next week's temperatures look to be more of the same, with a CDD forecast of 98.5, or 22.3 CDDs above the ten year norm. That could result in a build of only 41 bcf, which would compare to +48 bcf in the five-year average.

EIA Inventories - w/e July 16th						API Inventories		
	Actual	Market Estimate	MFGR Estimate	Five-Year Average	Last Week	Converge with EIA	Actual	Previous
Crude Oil			-0.2 MB	-0.2 MB	-5.1 MB			+1.7 MB
Gasoline			+1.0 MB	+0.4 MB	+1.6 MB			+1.7 MB
Distillates			+2.0 MB	+1.4 MB	+2.9 MB			+3.2 MB
Utilization			90.3%	+0.3%	90.5%			87.1%
Natural Gas			+56 bcf	+65 bcf	+78 bcf			

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

