

THE SCHORK REPORT

A VIEW OF THE ENERGY & SHIPPING MARKETS



Thursday, August 10, 2006

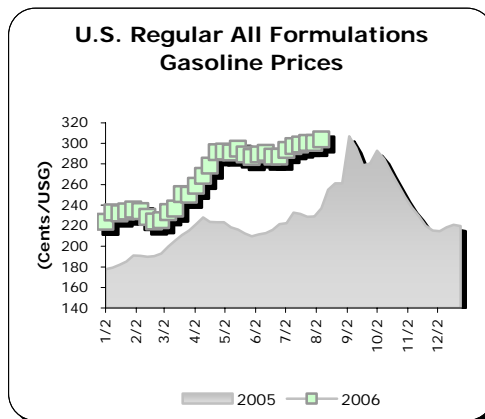
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BLOOMBERG TV THIS MORNING... Mr. Schork will be interviewed on "Bloomberg on the Markets" by Matt Nesto in the 9:40 AM EST time slot.

EIA Summary Stats w/e July 28, 2006

	Inventory	Surplus/ (Deficit)	%Δ
Current	2,775		
Last Year	2,420	355	12.8%
5-Yr Avg	2,338	437	15.7%



National Weather Service 6-10 Day Forecast

New England	Normal
Middle Atlantic	Normal
South Atlantic	Above Normal
E.N. Central	Above Normal
W.N. Central	Above Normal
E.S. Central	Above Normal
W.S. Central	Above Normal
Mountain	Below Normal
Pacific	Normal

CRUDE AWAKENINGS

TRADING BIAS

CL: NEUTRAL 😊 a/o Jun 29...S-73.43 R-77.95
NG: NEUTRAL 😊 a/o Jun 15...S-6.480 R-8.050
HU: NEUTRAL 😊 a/o Aug 01...S-206.39 R-237.00
HO: NEUTRAL 😊 a/o Jul 30...S-174.44 R-218.28

Nota Bene: Yesterday the DOE reported a much larger than expected draw in gasoline and the second highest weekly average in demand, 9.70 MMBbl/d, ever tallied. Yet, the contract has decoupled from the complex, down 2.7% this week. What gives?

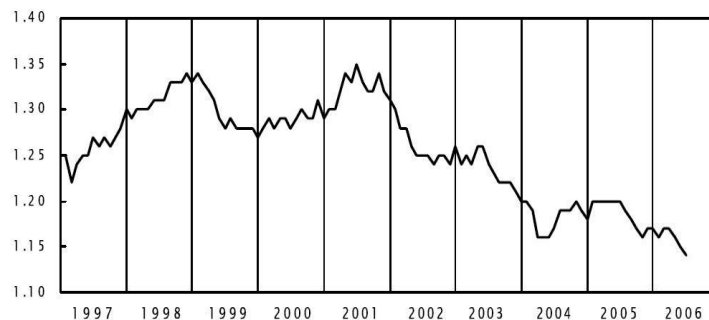
One theory we are entertaining is the "Goldman Roll", i.e. the portion of the GSCI that is attributable to the NYMEX Unleaded Gasoline contract (HU), and which must be rolled forward each month. Goldman has already announced that beginning with the Oct'06 contract they will transition out of the HU, into the Reformulated Blendstock (RB). Thus at some point, rather than roll, Goldman must liquidate extant length in the HU. What better time to do it then on the Prudhoe Bay news?

It's just a theory... but it's a good one.

ENERGY PRICES ARE MIXED... as the liquids trended lower for a second straight session, while nat-gas rocketed higher on speculation the EIA will report yet another draw this morning, plus the possibility that another "cockroach" has been spotted in the nat-gas pit (see our *nat-gas* section for further detail).

Chart of the Day

Monthly Inventories/Sales Ratios of Merchant Wholesalers, Except Manufacturers' Sales Branches and Offices: 1997 to 2006
 (Estimates adjusted for seasonal and trading-day differences, but not for price changes)



Source: U.S. Census Bureau

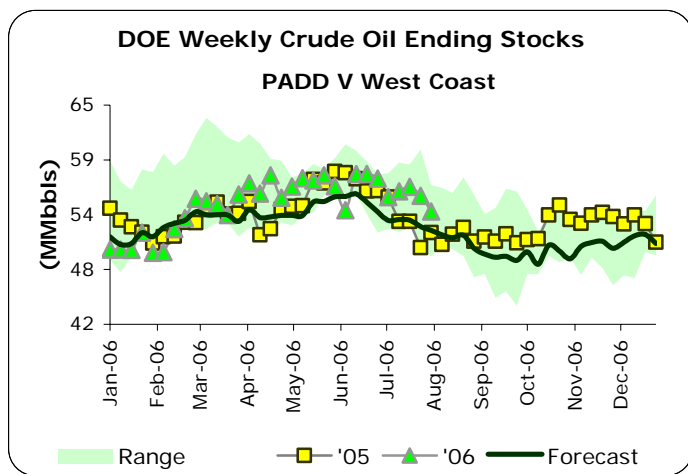
Wholesale Inventories

Yesterday the Commerce Dept announced that inventories at U.S. wholesalers were \$378.9 billion in June, up 0.8% month-on-month, while sales jumped 1.4%. Wholesaler's inventory-to-sales ratio dropped to 1.14 months, the lowest level ever, as a result. In other words, inventories remain constrained. This in turn suggests further strong demand on the part of wholesalers to keep up with the strong sales pace. Meanwhile, end-of-June inventories of nondurable goods jumped 1.1% despite a 0.1% decline in the value of petroleum stocks. On the month, petroleum sales jumped 6.1%, while the value of wholesale petroleum inventories fell to \$10.9 billion. Consequently, the supply on hand at the nation's petroleum bulk stations, terminals and merchant wholesalers fell to a perilously low 8.7 days.

DOE Recap

According to the latest numbers from the government, net crude oil and finished products stocks decreased as of last Friday, for a third straight week and for the sixth time in the last seven weeks. Stocks of the major fuel categories fell 4.3 Mbbls or 0.5% for the week ended August 04th. A much larger than expected draw in gasoline and an unexpected draw in combined distillate fuel inventories compounded a 1.1 MMbbl draw in crude oil stocks.

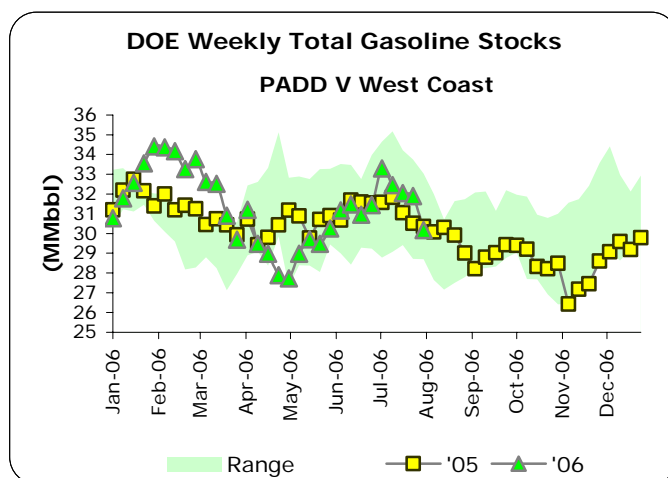
Of course, in light of the shut-in to Prudhoe Bay, all eyes are on the disposition of inventories on the West Coast (PADD V), which consume virtually all of Alaska's crude oil production. According to the EIA, PADD V downstream capacity processes about 2.7 MMbbl/d of crude oil, of which output from Alaska's North Slope (ANS) supplies 30%. Thus, under a worst-case-scenario, upwards of 15% of PADD V's crude oil supplies will be off the market through to the end of the year... and possibly beyond. That translates into approximately 60 MMbbls of oil that refiners from Anacortes to El Segundo will have to now bid for elsewhere. Given the tightness in global spare capacity, the chances that incremental production will be able to fill this void seem remote. Rather, these lost barrels will have to be made up from a mélange of sources; beginning with existing stocks.



As of last Friday commercial crude oil inventories in PADD V fell 1.67 MMbbls or 3% to 53.8 MMbbls. As such, the year-on-year overage was more than halved, but remains 2.20 MMbbls or 4.3% above last year at this time. Keep in mind, the seasonal decline in crude oil stocks began last month. Prior to the Prudhoe Bay news, TSR was forecasting a 6.67 MMbbl draw in PADD V inventories between mid June and September. This would have left

inventories at around 49.0 MMbbls. We now expect to see an additional 6.0 MMbbls drawn between now and then. This will push mid September stocks down near the five-year low, 43.9 MMbbls. What's more, commercial stocks in PADD III (GoM) now enjoy a 17.9 MMbbl or 11% surplus to the five-year average. Thus, in the weeks ahead we can expect to see this overage transferred west through the Canal, thus lending a boost to the panamax market.

Certainly, the West Coast is going to need it. Last week gasoline inventories there plunged 1.71 MMbbls or 5.3%, the second largest drop of the year. As such, a 2.11 MMbbl surplus to the five-year average at the beginning of last month has since morphed into a 503 Mbbl deficit.



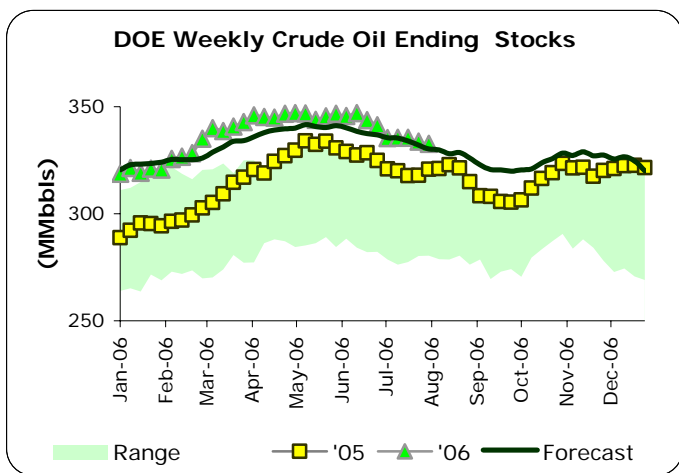
Furthermore, we can also expect to see a drawdown from the Strategic Petroleum Reserve (SPR). The DOE has assured the market that barrels will be made available upon request to offset any loss of supply from the disruption of ANS production. The SPR currently has 687.8 MMbbls in stock, broken down between 273.6 MMbbls of sweet and 414.3 MMbbls of sour crudes. That equates to approximately 59 days worth of import cover. Keep in mind; it will likely take up to two weeks to ship commercial and/or SPR barrels from the GoM to the West Coast. Hence, similar to the situation following Katrina, we will likely see a suspension of the Jones Act.

Finally, substitute ANS barrels will likely be sourced from current production out of Latin America. Namely, Mexico which normally ships 7/8^{ths} of its export barrels to the United States already, will likely see U.S. refiners outbidding PEMEX's European clients for that remaining 1/8th. Through the first five months of this year Mexico was the second largest source of U.S. foreign oil. What's

more, U.S. West Coast downstream capacity can certainly accommodate the heavier (less than 25 degrees API) Mexican export streams. We will also likely see U.S. capacity outbid European and Asian refiners for the remaining 50% of Ecuadorian and Colombian export crude that does not already come into the states.

Bottom line, the shortfall in ANS production, which could last for “months” and be as high as 400 MMbbl/d or 8%, i.e. 1 out-of-every 12 barrels of typical U.S. production, will be offset by a combination drawdown and market transfers. That can not help but imply a bid into the market.

Meanwhile, as far as the other sectors are concerned, total crude oil stocks last week fell 1.11 MMbbls or 0.3%. The report was within the Street’s guesstimate, as well as historical parameters for this point in the season. As such, the current disposition to the five-year average moved out to 30.4 MMbbls or 10%. Overall, draws are tracking nicely with our pre-season forecast. The U.S. oil market is in peak production and we can expect weekly crude oil draws now through the end of the third quarter as refiners work to sate waning seasonal gasoline demand and build winter burnstocks. Be that as it may, we expected to see crude oil inventories in excess of 300 MMbbls, or 10% above the five-year average. That was of course prior to the shut-in of half of ANS production.



Putting this event aside for the moment, the domestic supply-side disposition of the crude market is well positioned to accommodate extant seasonal demand through the Labor Day holiday in early September. After all, inventories are at their highest level for this point in the season since 1998 and their second highest level

since 1994. Year-to-date crude oil stocks are averaging 21.5 MMbbls or 7% above last year’s pace. However, that overage is about to evaporate.

As of last Friday refinery utilization rates increased for only the second time in the last month-and-a-half, up 8/10^{ths} of a point to 91.6% of capacity, thanks in part to the remediation of the Calcasieu ship channel closure. Accordingly, in light of the increased utilization, crude oil runs increased for the first time in three weeks, up 92 Mbbl/d to 15.6 MMbbl/d. Capacity is now plateauing and should remain near 15.5 MMbbl/d through the next month-and-a-half. As such, we expect utilization to drift slightly lower, but remain above 90% through the end of next month... assuming normal PADD V supplies and barring a GoM tropical storm event between now and then.

What conclusions can we draw from yesterday’s *weekly* snapshot of U.S. downstream capacity? Demand for products remains strong. For the fourth time this season, and for only the sixth time ever, gasoline demand came in above 9.6 MMbbl/d last week; and this is with real gasoline prices at the pump fast approaching record highs. Over the last three weeks the price of gasoline averaged \$3.015 per gallon, which is only about a dime below the peak set back in 1981 in the wake of Iran’s Islamic Revolution. Nevertheless, demand this season is averaging a record 9.54 MMbbl/d, up 0.7% year-on-year and 4.8% above the five-year average. In other words, we will likely see a new real all-time peak in retail gasoline before the season ends. Furthermore, demand for distillates averaged above 4.0 MMbbl/d for the first time ever in a July and has averaged 4.10 MMbbl/d, 1.2% high year-on-year since the start of the summer season. Nevertheless, season-to-date demand has been held in check by supply, both imports and production. As a result, inventories continue to build. Heating oil stocks in PADD I (East Coast) are 17% ahead of last year’s pace, and in PADD IB (which encompasses New York Harbor), inventories are 17% above year earlier levels. As a result of near-record output and robust imports, combined crude oil and petroleum products of 1.743 billion barrels remain near a sixteen year high. Now the only question is... will that be high enough?

NATURAL GAS

The whisper number for today's EIA lottery ranges from a 17 Bcf *injection* (PFC Energy) down to a 14 Bcf *withdrawal* (Wachovia, et al.) for an average estimate of unchanged per a Bloomberg survey. This is obviously a bullish fundamental metric, and is no doubt partially responsible for the rebound this week in gas.

However, we are left to ponder how much of this week's strength is attributable to the "cockroach theory". That is, you turn the light on in the kitchen and spot one. Although you just see one, you are confident a whole bunch of the nasty little creatures just scurried underneath the refrigerator before you turned the light on. Moral of the story... there is never just one.

So it was on the NYMEX last week. On July 31st the front-month contract rocketed 14% on the day, the odds of which were about 200/1 against. Two days later news broke that a major energy hedge fund, MotherRock, was going under because of "bad bets" in nat-gas. But was this fund the only one? It's doubtful. We would not be surprised to see one or two more "MotherRocks" float to the surface in the weeks ahead.

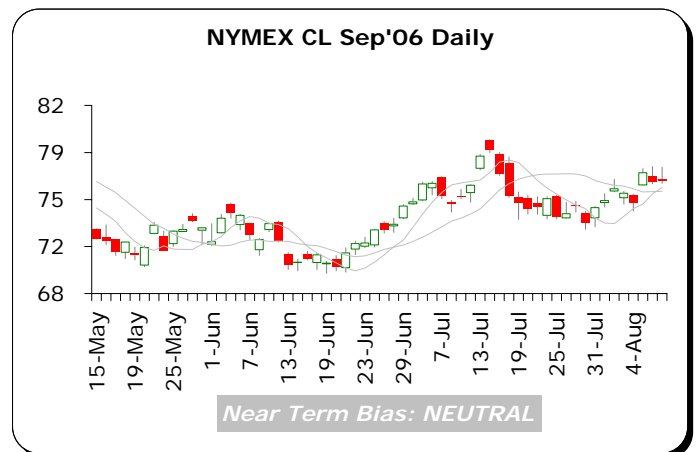
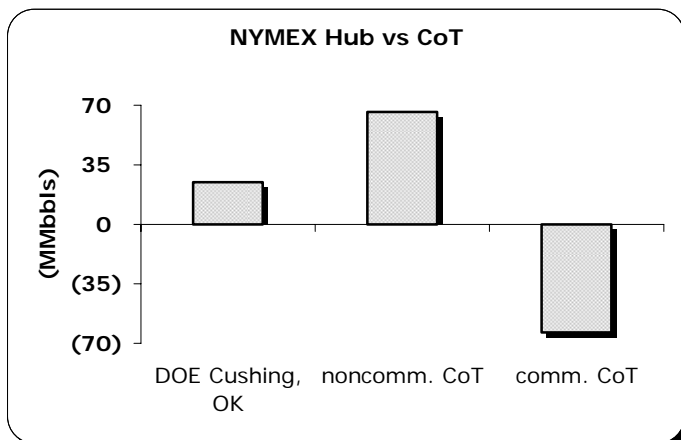
In fact, the New York Post might have spotted one already. In yesterday's edition the Post identified ABN Amro as MotherRock's clearing broker. In this capacity, ABN is supposedly now on the hook for MotherRock's leveraged position, \$100 million. There is even speculation this incident could queer ABN's \$386 million deal to sell its global futures business to UBS. According to the Post, ABN is now holding MotherRock's exposure, which according to the Post "... are mostly bets on the falling price of natural gas, [and] now have to be covered to close them out – most likely at a substantial loss because of the rise in gas prices".

That line must have had the Locals on the NYMEX salivating as they stepped into the pit yesterday.

Regarding today's session, post EIA bids above the 14-day pivot moving average, 7.663, alert to further bullish trade back towards the top of the weekly pivot area, 7.833 and yesterday's 7.940 high. Otherwise, failure to hold intra-day support, 7.495, cautions to further corrective trade towards Tuesday's 7.240 high, and closure of the gap.

OIL

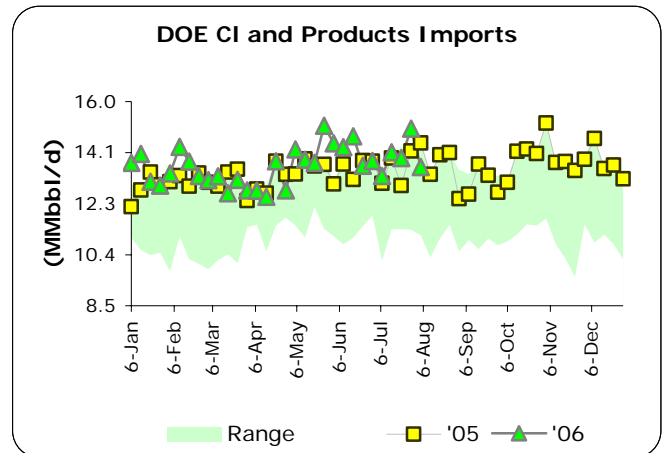
The DOE reported a second straight draw, and the fifth draw in the last seven weeks in crude oil stocks, down 1.11 MMbbls or 0.3%. Total commercial stocks now stand at 332.6 MMbbls, 30.4 MMbbls (10%) above the five-year range. Inventories in Cushing, OK, the delivery hub for the NYMEX WTI contract now stand at 24.8 MMbbls. In other words, per last Friday's CFTC report, the Large Specs own 2.7 times more "paper barrels" than actual physical barrels deliverable against the contract.



As far as today goes, the script is unchanged, i.e. failure to hold Monday's 76.05 low alerts to a move to close the gap at 75.40. A close today below here will stall bullish momentum and cautions to a push against the weekly trendline, 73.43. Alternatively, bids above Tuesday's 77.45 high alerts to further bullish trade towards the July 14th all-time front-month peak, 77.95. Penetration here will then allow bulls to take aim at the Sep'06 life-of-contract high, 79.45

TRANSPORTATION

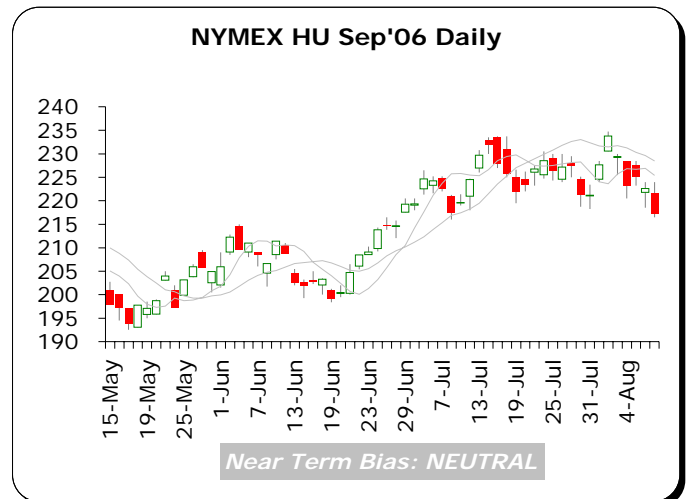
West African suezmax tonnage continues to find a bid at/near ws 150 as strong seasonal demand, coupled with a "war premium" has charterers paying up for vessels. Per the latest EIA numbers imports for crude oil, finished products and blendstocks continue to surge, thus lending further support to freight markets. Over the last four weeks crude oil and petroleum products imports averaged 14.2 MMbbl/d, 1.47 MMbbl/d (12%) above the five-year normal. Add to this mix the looming Atlantic Basin hurricane season, and the recipe is set for continued strength lasting into the fall. Four and five-month deferred IMAREX VLCC forward freight agreements are trading between ws 195 and 200.



LIGHT ENDS

So let's get this straight... BP is shutting in 8% of U.S. crude oil production, as a result WTI up \$1.59/bbl or 2.1% and summer heating oil is up 167 ticks or 0.9%. **On top of that, yesterday we see a larger than expected draw in gasoline stocks, topped by the second largest weekly demand figure ever... yet on the week, NYMEX mogas is 2.7% lower? Hmm... smells like the "Goldman Roll".**

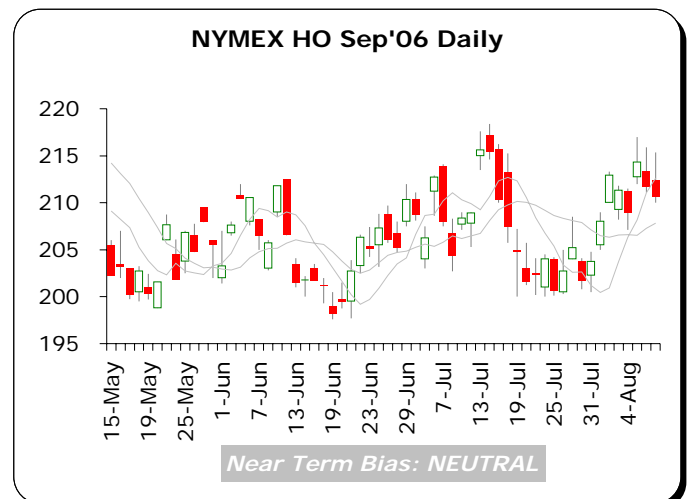
As far as today goes, offers below the June 28th/July 10th gap, 215.80, alert to a push towards the next ratchet of support inside the June 26th pivot area from 213.12 to 211.78, and intra-day support at 210.61. On the other hand, a rebound above intra-day resistance, 220.12, alerts to further corrective trades towards yesterday's 224.00 "double top" and the 14-week pivot moving average, 225.58.



MIDDLE DISTILLATES

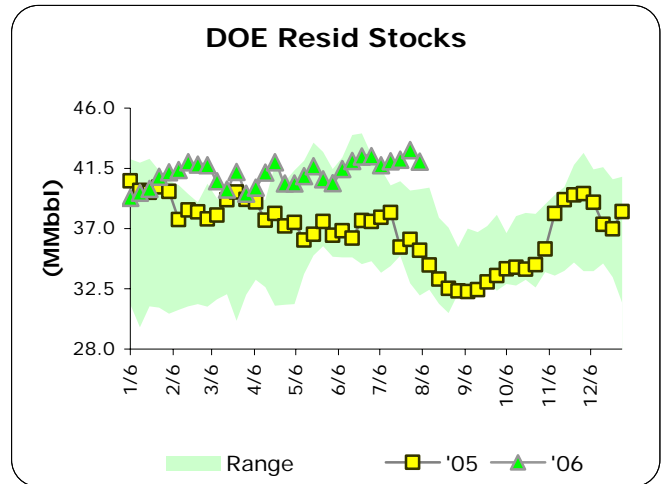
Yesterday the DOE reported the first draw in three months in distillate fuels. Combined stocks fell 0.1% to 132.4 MMbbls. Heating oil stocks in the New England and Mid-Atlantic market areas fell to 35.8 MMbbls or 36% above the five-year average. Meanwhile, terminals continue to make way for ULSD. As a result, diesel fell for a fourth straight week, with forward cover narrowing to 23.4 days.

Regarding today's session, sellers below yesterday's 210.00 low, signals further bearish trade towards the August 02nd pivot range from 207.69 to 207.00. Failure here should find support at 204.96. Otherwise, a rebound above the 14-day pivot moving average, 213.56, alerts to further corrective trade back towards Monday's 217.00 high print. Penetration here allows for a path towards the July 14th high, 218.40.



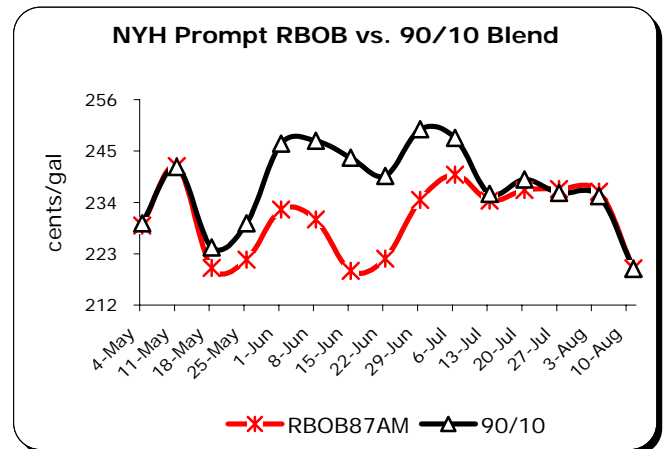
RESIDUAL FUEL OIL

Fuel oil in New York Harbor has been trading dear to gas since mid winter. Despite recent "record" cooling demand, gas at the gate in New York is back to trading at a discount to 0.7% FOB in the Harbor. As such, fuel oil consumption continues to soften. Since the Memorial Day holiday, average demand has plunged 13%. Consequent of the falling demand, storage remains well above average. As of last Friday storage decreased for only the second time in the last nine weeks, down 870 MMbbls to 42.0 MMbbls. That still represents a 6.62 MMbbl (19%) overage to last year, and 7.06 MMbbl or 20% surplus to the five-year average. As such, estimated forward cover is around eight days ahead of last year's pace.



BIOFUELS

NYMEX RBOB continues to follow the RFG contract lower. The contract has closed lower five straight days, capped by yesterday's 733 tick plunge. As such, since the beginning of the month the contract has lost 8.9% of its dollar value or \$8,975 per lot. Regarding today's session, offers below yesterday's 219.50 low, alerts to further weakness towards the next ratchet of support down between 215.00 and 214.00. Meanwhile, New York harbor ethanol was last assessed at 270.00. As a result, a 90/10 blend, federal tax credit inclusive, fell to 219.78, i.e. at economics such as this blending ethanol in scale makes sense.



OUTLOOK (August 07th to 11th)

NAT-GAS... Last week traders in the NYMEX Henry Hub pit lived up to the adage – with a little help from the funds – that what goes up, must come down. As far as this week is concerned offers below last week's 7.120 low print should find a path into the "box", i.e. the 50/62% retracements between 7.088 and 6.744. Sellers below here can then gun for the weekly pivot area from June 23rd between 6.570 and 6.480. Alternatively, bids above last Thursday's 7.540 high print alerts to further corrective trade and an attempt to close the gap at Wednesday's low, 7.760. A close here sets the table for further strength towards the Katrina/Ivan extensions from 8.050 to 8.251.

CRUDE OIL... For the first time in three weeks WTI prices on the NYMEX found a bid. The contract for Sep'06 delivery finished last Friday at 74.76, up 1.52 per barrel; it was the first "up" week since the contract posted a life-of-contract high of 79.45 back on July 14th. As such, front-month WTI is presently tracking higher along a weekly trendline from March 24th. As far as this week goes... violation of the trend at 73.43, alerts to further weakness into the next ratchet of support in between the June 21st/26th pivot areas from 72.54 to 70.50. Further selling below the \$70 critical point of reference signals to a potential flush towards long-term support from 65.78 to 65.09. Alternatively, penetration of the July 18th pivot area top, 76.50, the "double top" from the last two weeks cautions to further bullish momentum towards the all-time spot peak, 77.95 and the 79.45 life-of-contract high.

SCORECARD

BUY NATURAL GAS

- ◆ Strong economy,
- ◆ Coal transport issues,
- ◆ Waning supply elasticity,
- ◆ Increased substitution,
- ◆ Growing demand inelasticity and
- ◆ Extant damage from Katrina/Rita.

BUY OIL

- ◆ **BP shut-in of ANS,**
- ◆ Strong global economic growth,
- ◆ Geo-political risks,
- ◆ Extant damage from Katrina/Rita,
- ◆ Conversion from MTBE to ethanol blending, plus adoption of RFS,
- ◆ Stricter diesel sulfur requirements and
- ◆ 2006 downstream capacity expect to grow half as fast as demand.

SELL NATURAL GAS

- ◆ Brisk Baker Hughes rig counts,
- ◆ Gas-weighted industrial demand destruction,
- ◆ Increased hydro capacity out West,
- ◆ Increased substitution,
- ◆ Increased LNG imports and
- ◆ Decreased NGL extraction.

SELL OIL

- ◆ Ample supplies and
- ◆ Pandemic OPEC cheating

CRUDE OIL	BULL	BEAR	NA	NAT-GAS	BULL	BEAR	NA
API		<input checked="" type="checkbox"/>		EIA		<input checked="" type="checkbox"/>	
DOE		<input checked="" type="checkbox"/>		Conuming East		<input checked="" type="checkbox"/>	
PAD 1 & 2		<input checked="" type="checkbox"/>		Weather		<input checked="" type="checkbox"/>	
Imports	<input checked="" type="checkbox"/>			Fuel Switching	<input checked="" type="checkbox"/>		
Production			<input checked="" type="checkbox"/>	Rig Count		<input checked="" type="checkbox"/>	
NYMEX Cracks		<input checked="" type="checkbox"/>		Imports - Canada		<input checked="" type="checkbox"/>	
OPEC			<input checked="" type="checkbox"/>	Exports - Mexico			<input checked="" type="checkbox"/>
ARB into USAC		<input checked="" type="checkbox"/>		Nuclear Capacity	<input checked="" type="checkbox"/>		
ARB into USGC		<input checked="" type="checkbox"/>		Hydro Capacity			<input checked="" type="checkbox"/>
Transportation	<input checked="" type="checkbox"/>			Transportation			<input checked="" type="checkbox"/>
Momentum		<input checked="" type="checkbox"/>		Momentum		<input checked="" type="checkbox"/>	
Economy	<input checked="" type="checkbox"/>			Economy	<input checked="" type="checkbox"/>		
Interest Rates	<input checked="" type="checkbox"/>			Interest Rates	<input checked="" type="checkbox"/>		
Outages	<input checked="" type="checkbox"/>			Outages			<input checked="" type="checkbox"/>
Season	<input checked="" type="checkbox"/>			Season	<input checked="" type="checkbox"/>		
Market Sentiment			<input checked="" type="checkbox"/>	Market Sentiment			<input checked="" type="checkbox"/>
COT		<input checked="" type="checkbox"/>		COT	<input checked="" type="checkbox"/>		
Total	6	8	3		4	8	5

A note about the Ibis: The Ibis folklore has it that other birds look to the Ibis for leadership. The Ibis uses its instinct to detect danger. It is the last sign of wildlife to take shelter before a hurricane hits, giving warning that danger is imminent. As the storm passes the Ibis is the first to reappear, a sign the clear skies are approaching.

