



Crude Outlook for Q2 - 2007

Ulhas Shenoy

Sr Research Analyst

April 9th, 2007

Nymex Crude oil futures have hit 6-month highs during the previous week on the back of concerns of disruption in supplies from the Middle East. The capture of British soldiers by Iran for trespassing its territorial waters saw an escalation of tensions in a region, which has been very volatile politically in the recent past. Iran has withstood enormous pressure from the West to abandon its nuclear program, however the Iranian President in a stand of astute defiance has maintained the Iranian program is for peaceful purposes.

The great deal of significance being attached to the geopolitical tensions in the Middle East can be understood with reference to the following table, which illustrates the **Top producers of crude oil in the year 2005:**

	Country	Total oil production (mbpd)
1	Saudi Arabia	11.1
2	Russia	9.5
3	United States	8.2
4	Iran	4.2
5	Mexico	3.8
6.	China	3.8
7.	Canada	3.1
8.	Norway	3.0
9.	United Arab Emirates	2.8
10.	Venezuela	2.8
11.	Kuwait	2.7
12.	Nigeria	2.6
13.	Algeria	2.1
14.	Brazil	2.0

(Source: Energy Information Administration, Dept of Energy USA.)

Following are some other factors, which are influencing the direction prices take:

- a) **Geopolitical tensions in the Middle East:** Despite the resolution of the standoff between Iran and Britain over the latter's sailors being taken hostage by Tehran, the Middle East continues to be a region of crucial importance. The Strait of Hormuz through which approximately 25 percent of the world's oil shipment takes place is located here. The blockage of the Strait by Iran, which controls the Strait in the event of further hostile action by the West could see a sharp spike in prices.
- b) **Approaching driving season in the US:** The United States' approaching driving season, which is likely to see a seasonal spurt in demand for gasoline. The Deputy Secretary of the US Energy Dept said in an interview last week the US oil inventories were sufficient to meet the demand during the driving season.
- c) **Falling OPEC production:** Production from OPEC during March is estimated to be lower by 200,000 barrels per day in March according to Geneva based Petrologistics. This has



reinforced concerns on the supply side. OPEC has cut production by 1.2 million barrels in November 2006 and another 500000 barrels from February 1 this year with a view to support prices. It remains to be seen how the group will react should there be a sharp rally in prices.

- d) **Strong US economic performance:** The release of the stronger than expected fourth quarter GDP from the US helped ease worries over a slump in demand due to the likelihood of an economic slowdown. Ben Bernanke in a testimony to the US Senate had reiterated rising energy costs continue to remain a source of concern. The International Energy Agency in a report released recently said it estimated global oil product demand to 86 million barrels per day in 2007, higher than 84.5 million barrels per day in 2006.
- e) **Sustained tensions in Nigeria:** The situation in Nigeria, one of the top producers in OPEC continues to be a cause of concern. Gunmen in two speedboats abducted a British oil worker last week. Militants have been seeking an ouster of foreigners from oil installations in the oil rich African country. The threat of further cuts looms large should there be a re emergence of the violence seen last year.

In addition to the factors listed above the market is keeping a very close watch on developments in Iran. The dispute between Iran and the West over Tehran's nuclear program has persisted for several months now; the Islamic Republic has withstood pressure from the West to suspend its nuclear program. The United Nations has imposed sanctions on Iran for continuing with uranium enrichment despite calls from the International community to suspend the pursuit of its nuclear program.

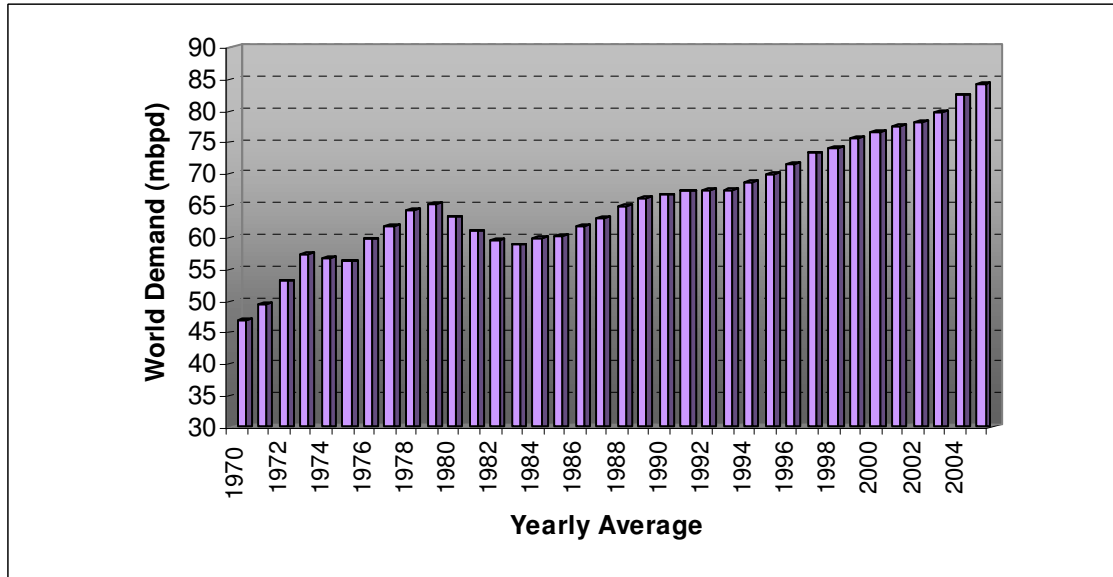
CFTC Commitment of Traders Report: The latest report released by the Commodity Futures Trading Commission on March 30th said net long positions in crude oil were down to 40179 in the week ending March 20 compared to 44366 during the previous week. Speculative long positions in Gasoline increased to 33671 compared to 28769 during the previous week. In the medium term it is more likely the market will look to gasoline to determine the direction of prices.

Backlog in supplies from Marseille: Though the strike at French port of Marseille ended on April 2nd, nearly 40 tankers are still waiting to get into the port. It is estimated the backlog would take nearly two weeks to clear which could see a strain on supplies in the near term.

Latest Dept of Energy inventories report: The latest report released by the DoE showed crude inventories increased by 4.3 million barrels however Gasoline stocks fell 3.4 million barrels to 210.5 million barrels. This is a cause of great concern as Gasoline stocks have fallen 16.725 million barrels in the past six weeks. Presently gasoline inventories are 11.1 million barrels below a year ago and 782800 barrels above the five-year average. The disruption in imports from Marseille coupled with a fall in production on account of shutdowns in refineries for maintenance has left gasoline vulnerable to sharp price spikes as demand picks up during the driving season.

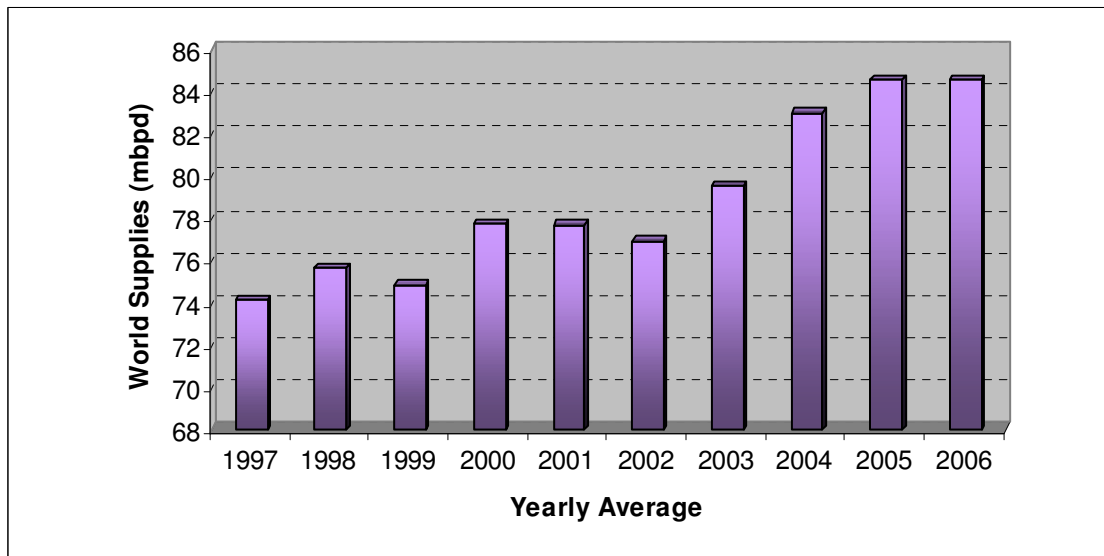
In addition to the geopolitical risks the market seems to be grappling with presently, there are other crucial factors, which are likely to be brought back into focus. Following are some factors, which could prove to be bullish over the medium and long term period:

Excess of demand over supply: Demand for crude has been consistently increasing over the past few years. This can be illustrated with the following graph:



(Source: Energy Information Administration, Department of Energy USA)

Notwithstanding efforts to increase supplies, the increase in supplies has not been able to keep up with the rate of increase in demand. As illustrated by the graph below, supplies have been relatively steady as compared to the surging demand.



(Source: Energy Information Administration, Department of Energy USA.)

Risk from weather related disruptions: Global warming is already inducing drastic changes in weather patterns worldwide. Any adverse weather related calamity is likely to impact installations worldwide. The world has already witnessed the brute strength of nature when a series of Hurricanes, most notably Katrina which saw crude futures to \$ 70.85 a barrel then the highest level crude traded at since the contract was introduced on the NYMEX in 1983. The threat of damage to installations from Hurricanes during the North Atlantic Hurricane Season, which lasts from June 1st to November 30th continues to persist. Weather forecasters at the Colorado



CommTrendz Research

State University team said they expect the 2007 hurricane season to be very active with 17 named storms, nine hurricanes and five major hurricanes.

Closure of refineries for maintenance: Refineries are closed at periodical intervals to undertake routine maintenance. Such shutdowns are likely to see a fall in supplies and hence lend support to prices. It also needs to be noted though the refinery utilization rate has increased in January 2007 as compared to the same period in the previous year, Crude output has in fact fallen in North America and Europe in January as compared to the previous month. This is illustrated with the help of the following tables:

	Refinery Crude Output (Million barrels per day)					
	Aug-06	Sep-06	Oct-06	Nov-06	Dec-06	Jan-07
North America	18.92	18.77	17.95	18.1	18.5	18.04
Europe	14.27	13.92	13.45	13.78	13.91	13.87
Pacific	7.22	7.08	6.59	7.1	7.32	7.35

(Source: International Energy Agency)

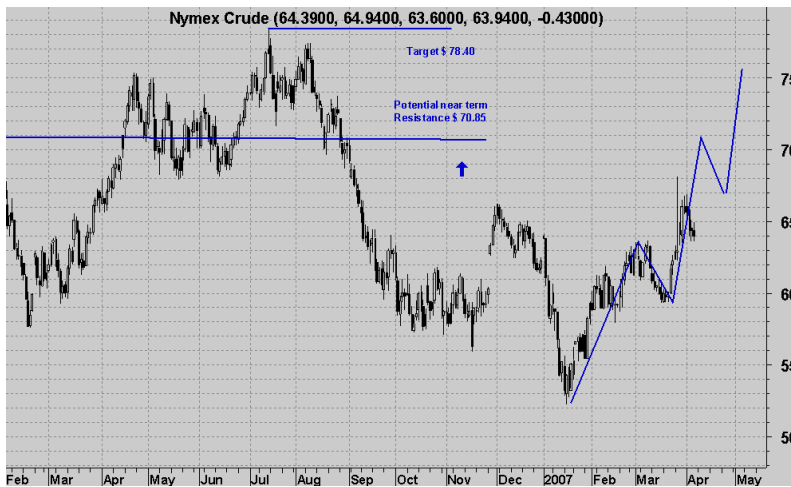
Refinery Utilization rate		
	Jan-06	Jan-07
North America	86.07	86.12
Europe	85.97	87.41
Pacific	87.64	87.49

(Source: International Energy Agency)

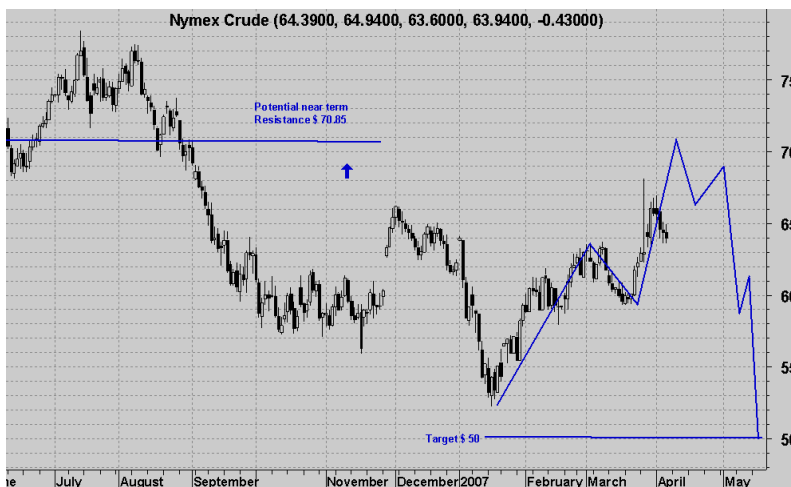


Technical Outlook:

Crude oil futures have seen a sharp rally after having tested \$ 52. After analyzing the present structures using Elliot Wave Analysis, a 5-wave impulse has been completed at \$ 78.40 followed by a corrective a-b-c pattern, which was completed at 52.40. Hence we could be in a new impulse wave at present, however a confirmation of the present wave being impulsive will be a break of the resistance at 70.85, which could see prices breaching the contract high at 78.40. This can be illustrated with the chart displayed below:



Alternate scenario: If the resistance at 70.85 caps rallies, an alternate view is prices could be in an A-B-C corrective pattern where Wave A is likely to be have a 3-3-5 structure.



The moving averages in the MACD are below the zero line in the indicator suggesting bearishness, only a crossover above the zero line in the indicator would signal a clear bullish trend again. The RSI in neutral conditions indicating prices are neither overbought nor oversold. Prices are above both the short term 8 period ema at 62.55 and the 34 period ema at 62.58. The convergence of the two moving averages indicating the possibility of a sharp move.



Comm-trendz Research

Price Outlook: Presently prices could face resistance in the \$ 70 - 71 region; a break of the resistance at \$ 70.85 will confirm the new impulsive wave. This could see prices testing the contract highs at \$ 78.40 and moving higher. Following are a couple of factors, which are likely to be supportive of prices:

- a) Geopolitical tensions in the Middle East
- b) Further production cuts from OPEC.
- c) Damage to installations from Hurricanes as the US approaches the North Atlantic Hurricane season.

As per the alternative scenario mentioned above, a failure to break the resistance at \$ 70.85 would indicate prices are in an A-B-C corrective pattern at present targeting \$ 50. Following are some factors, which could be responsible for prices moving lower.

- a) A fall in demand for crude oil due to tightening of monetary policies by Central Banks.
- b) The re emergence of bird flu which could drastically reduce travel across countries.
- c) The threat posed by the development of alternative fuels like biodiesel could see a drastic dent in demand.
- d) An increase in supplies from non-OECD countries could ease the vulnerability to price spikes in case of surges in demand.

Comm-trendz Risk Management Services Pvt. Ltd.

202, Crystal Tower,
Gundavali, Off Andheri-Kurla Road,
Andheri (E)
Mumbai, MH, INDIA 400 054.
Tel.: (91) 22 2682 6426
Fax: (91) 22 2683 1494
Email : info@comm-trendz.com
www.comm-trendz.com

Comm-trendz Risk Management Services Pvt Ltd is an independent research firm dedicated to the commodity futures and foreign exchange markets. For more information, contact us at +91 - 22 - 2682 3028 or info@comm-trendz.com

DISCLAIMER: Neither Comm-trendz nor any of its employees accepts any liability whatsoever, for any loss arising from the use of this report or contents thereof. Comm-trendz and its employees may from time to time have long or short positions in, and buy or sell the commodities mentioned herein. This research may not be independent from the proprietary trading and investment management interests of Comm-trendz, which may conflict with your interests. Comm-trendz and the author of this report reserve the right to change their views without giving prior notice. This report is meant for the exclusive use of its intended recipient(s). This report may not be redistributed or reproduced, in part or full, unless authorized in writing by Comm-trendz.