MUSINGS FROM THE OIL PATCH
June 24, 2008

Allen Brooks
Managing Director

Note: *Musings from the Oil Patch reflects an eclectic collection of stories and analyses dealing with issues and developments within the energy industry that I feel have potentially significant implications for executives operating oilfield service companies. The newsletter currently anticipates a semi-monthly publishing schedule, but periodically the event and news flow may dictate a more frequent schedule. As always, I welcome your comments and observations.* Allen Brooks

Energy Reflections on Surprising and Mind-Altering Events

For the ten plus years we have been a regular in the area, the media and public are more concerned with getting and using cheap energy and attacking the suppliers of its energy

In reading last Saturday's *The Providence Journal* and the previous Thursday's issue of the *Westerly Sun* newspapers, we have become aware of how much the issue of high and rising oil and gas prices and the issues behind them are finally permeating the thinking of citizens living in the nation's smallest state. The Westerly paper carried a small article, but positioned in the center of the back page of one of its sections (we're not sure whether the placement was intentional or merely for convenience), announcing an upcoming meeting of the Westerly Peak Oil study group at the downtown library scheduled for a Friday evening in late July. Unfortunately, we will not be around to attend – if for no other reason than to see how many and what types of people show up. One does not associate this region of the country with an enlightened attitude about energy supplies. Generally, for the ten plus years we have been a regular in the area, the media and public are more concerned with getting and using cheap energy, attacking the suppliers of its energy, but heaven help anyone proposing local solutions that might intrude on the area's attractiveness because they too will be vilified. That does not mean we are in favor of tearing up the area for new energy facilities, but there are many locations in the region that would support minimally intrusive facilities yet help to assure more affordable energy supplies for the region. One of these projects is the Cape Wind proposal for a wind farm in Nantucket Sound that has drawn much intense political opposition and lobbying in the area and increased national media exposure in recent times.

Maybe more interesting was *The Providence Journal's* editorial on Saturday entitled: The energy enemy is us. The title is a play on the statement from the character Pogo in the award-winning carton series drawn by the late Walt Kelly. In the cartoon, Pogo announces that "we have met the enemy and it is us" signaling that people are often the biggest obstacle to accomplishing things, especially politically. Here are some of the key points and quotes from the editorial that reflect an enlightened view of the energy and global warming situation and some of the necessary steps needed to begin to solve it.

"Everybody wants someone to blame when gasoline goes above $4 a gallon"

The editorial began with the popular view of who is at fault for, or clearly benefitting from, high oil prices. "Everybody wants someone to blame when gasoline goes above $4 a gallon." With that opening line, the editorial goes on to focus on the oil companies as the "most obvious villain" and that they have become a convenient target of politicians, including Democratic presidential hopeful Barack Obama. That is why the newspaper finds it regrettable that politicians are intent on levying a windfall profits tax on the oil companies. The editorial quotes Sen. Obama's comments on his rationale for taxing the oil companies and using the money to help families pay for their energy and other bills. But the editorial writers point out that there is a slight problem with this approach: "It would either depress oil production or drive up the cost of oil products, or probably both."

"A windfall-profits tax will produce less energy and not more"

The editorial quotes former Louisiana Senator John Breaux who has pointed out, "A windfall profits tax may make you feel good as a punitive measure against the energy companies….A windfall-profits tax will produce less energy and not more." The editorial further makes the point that it costs money to find, develop, refine and market petroleum products. But importantly, the editorial recognizes that "Government makes far more off a gallon of gasoline than the oil companies do, and oil-company profit margins are lower than those of many industries." (Hallelujah! Finally someone realizes that the oil industry's profitability is not dramatically improved by high oil prices.)

A recent Gallup poll found that support for more drilling in U.S. coastal and wilderness areas has increased to 57% from 41%

The editorial finally enumerated various "serious steps" to take to address the energy problem rather than "simply scapegoat someone." Their first idea was to drill for more oil. They pointed out that America is highly dependent upon foreign oil and the money we are sending our oil suppliers is going to "kleptocratic dictatorships" and is being used against us. They pointed out that a recent Gallup poll found that support for more drilling in U.S. coastal and wilderness areas has increased to 57% from 41% in the past year. The writers recognize that there are environmental tradeoffs, but they pointed out that China is drilling for oil off the coast of Cuba, some 60 miles from Florida.

The second step is to build new refineries so we can refine more oil, again recognizing the environmental trade-off. They said we must also force greater fuel conservation through education, taxes and new fuel standards for vehicles. Next they suggest we need to step up our efforts to develop alternative fuels – including wind, geothermal and solar power, all of which are environmentally friendly. But they also recognize that there are trade-offs. Within

Within the span of the readership of *The Providence Journal* are three major energy projects that will require environmental trade-offs

the span of the readership of *The Providence Journal* are three major energy projects that will require environmental trade-offs from the local citizens. The editorial writers take on these objectors with the following comments: "…there are also trade-offs (windmills sharing the horizon with yachts for three months a year!), leading to such outrages as wealthy Cape Cod summer-home owners like the Kennedys using their political muscle to block wind turbines in Nantucket Sound. And politicians have pandered to NIMBYs in blocking a plan to transport liquefied natural gas (the cleanest fossil fuel) in Narragansett and Mount Hope bays."

The pendulum of anti-energy sentiment in the region may be shifting in the opposite direction

The final step that should be taken according to the editorial is to use taxpayer money in a crash program to develop new energy-saving inventions such as cars that can run on meaningfully less fossil fuel or use none at all. They also argue that the nation needs a revolution in battery technology. But the final line of the editorial makes the most telling point. "America's economic prospects and national security argue that the adjustments above are long overdue." Before seeing the notice of the Westerly Peak Oil group meeting, we would have taken *The Providence Journal's* editorial as the equivalent of "spitting in the wind," but now we think the light bulb may be going on in the heads of many more Rhode Islanders than before and that the pendulum of anti-energy sentiment in the region may be shifting in the opposite direction.

April Driving Shows Impact of High Gas Prices

The U.S. Department of Transportation last week released its latest monthly data for miles driven by American citizens during the month of April. You may remember that the data for March showed the largest month to month drop in vehicle miles driven ever experienced - 11 billion miles. The April data reflected the continuing trend of sequential monthly mileage declines, in this case a 4 billion mile drop. This declining trend is happening as American's experience record gasoline pump prices; and gasoline prices that have literally exploded in the past few months as the spot price of a barrel of crude oil has jumped from slightly below $100 per barrel at the start of the year to almost $140 last week.

Exhibit 1 shows the monthly data for vehicle miles driven for both 2007 and 2008. As noted in the chart, each month this year has produced a lower number of miles driven than at the same time in the prior year. Cumulatively, miles driven have declined by 2.1%. This is the largest correction in miles driven since 1979 when the gasoline market was hit by a physical shortage of oil due to the Iranian oil industry's shut down following the overthrow of that country's government by the religious leaders.

Since the beginning of the year there also has been a dramatic rise in the average price of a gallon of gasoline climbing from $3.047 cents per gallon in January to $3.441 in April, a rise of 13%. The data in the table in Exhibit 1 shows that the pace of year-over-year

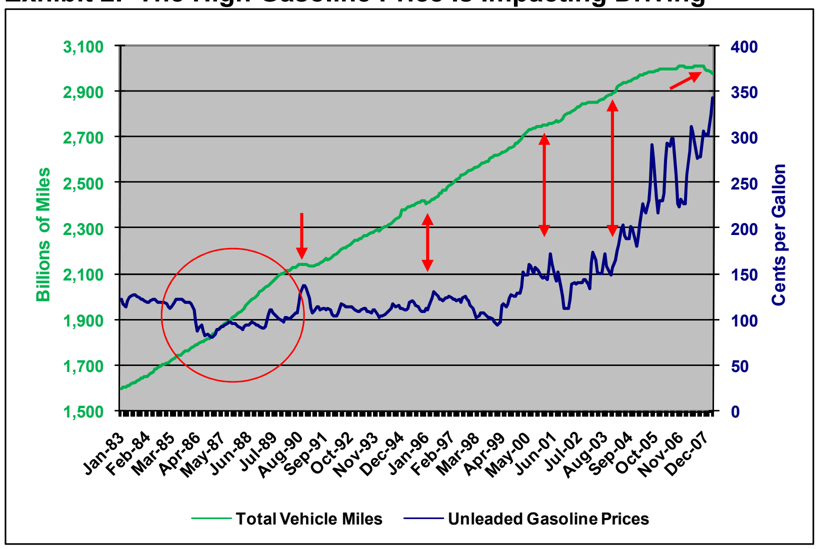
Exhibit 1. 2008 Monthly Driving Data Shows Y-o-Y Decline

	Miles Driven		Pct.	Gasoline Price		Pct.
Month	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
January	226.9	230.7	-1.6%	304.7	227.4	34.0%
February	215.8	216.9	-0.5%	303.3	228.5	32.7%
March	246.2	257.3	-4.3%	325.8	259.2	25.7%
April	245.9	250.3	-1.8%	344.1	286.0	20.3%
4-Month Total	934.8	955.2	-2.1%			
4-Month Avg.				319.5	250.3	27.6%

Source: Federal Highway Authority, PPHB

monthly increases have slowed, but the comparison of the average for the first four-months this year is 27% higher than a year ago.

Exhibit 2. The High Gasoline Price Is Impacting Driving



Source: Federal Highway Authority, PPHB

When gasoline prices breached the $3 a gallon barrier, the pace in miles driven not only slowed, it actually began to decline

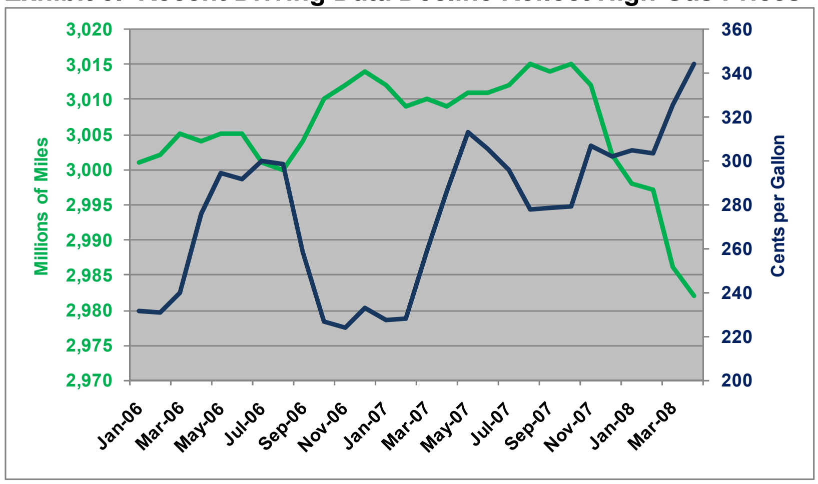
In our last issue of Musings we displayed a chart tracking the 12-month moving average of vehicle miles driven against the average monthly price for a gallon of regular gasoline nationwide. Our conclusion was that until gasoline pump prices rose above $2.20 a gallon, the pace of miles driven continued unabatedly upward subject to variables such as weather, seasonal factors and the health of the general economy. However, when gasoline prices breached the $3 a gallon barrier, the pace in miles driven not only slowed, it actually began to decline. As U.S. Department of Transportation Secretary Mary Peters said, "Previously, people might change their pattern for a short period of time, but it almost always bounced back very quickly. We're not seeing that now."

We have updated our long-term chart tracking monthly average gasoline prices and vehicle miles driven to reflect the latest April data. More importantly, we have prepared a chart showing the impact on vehicle miles driven versus gasoline prices over a much shorter and more recent time period – January 2006 through April 2008. While monthly data may often be volatile, the trend in miles

When gasoline pump prices went above, and stayed above, $3 per gallon, the number of miles driven started to decline

driven compared to the level of the price of a gallon of gasoline becomes much more obvious. As gasoline prices rose above the $2.20 per gallon level, one can see the slowing, and periodically an actual drop in miles driven. But when gasoline pump prices went above, and stayed above, $3 per gallon, the number of miles driven started to decline and has been in a steady and apparently accelerating decline trend in recent months.

Exhibit 3. Recent Driving Data Decline Reflect High Gas Prices



Source: Federal Highway Authority, PPHB

There has been a 20 billion decline in vehicle miles driven so far in 2008

When the April miles driven data was released, Mary Peters pointed out the negative impact this trend is having on the government's ability to fund highway maintenance and construction work from highway trust funds that are dependent upon gasoline taxes. April marked the sixth month in a row of a decline in miles driven. That means less tax revenue flowing into the highway trust fund. According to the Secretary's press release, there has been a 20 billion decline in vehicle miles driven so far in 2008. If you calculate the entire six-month period of declining miles driven since November 2007, American's have driven 30 billion fewer miles, or slightly over a 1% decline in annual miles driven. While this may not appear to be a major change in the long-term miles driven trend, when we look at the recent shape of the long-term chart of miles driven with average gasoline pump price above $3 per gallon, it suggests the possibility of the start of a more ominous gasoline demand trend.

Potentially more ominous for fuel consumption trends is the observation that in 2007, car sales were less than half of new vehicle sales, but this May they accounted for 57% of vehicle sales

Secretary Peters pointed out that the change in driving is happening at the same time the U.S. is experiencing huge increases in mass transit usage. She also pointed out that in May midsize Sport Utility Vehicle (SUV) sales dropped 38% from a year ago. Potentially more ominous for fuel consumption trends is the observation that in 2007, car sales were less than half of new vehicle sales, but this May they accounted for 57% of vehicle sales. We have already highlighted this trend with statements from auto dealers around the country recounting the lack of buyer interest in SUVs, and in particular large SUVs.

Acknowledging this shift in buying sentiment among U.S. auto consumers, General Motors (GM-NYSE) announced it was extending the life cycle of its GMT900 lineup of full size trucks (Chevrolet Silverado) and SUVs (Cadillac Escalade, for example). The auto maker is shifting its design resources to more fuel-efficient and hybrid vehicles that are in greater demand. While the GMT900 lineup was not due to be updated before 2012, by shifting engineering and design resources away from it, GM is signaling it does not plan for these vehicles to be the central focus of its future new vehicle offerings. Reports continue to circulate that GM is looking at shutting down production of one of its Hummer brand vehicles while it considers what to do long term with this brand.

GM has also created new dealer incentives to help move bloated inventories of gas guzzler vehicles

GM has also created new dealer incentives to help move bloated inventories of gas guzzler vehicles. GM has had a $2,000 per vehicle incentive program in place to which it is adding up to $4,000 for select models for current GM vehicle owners. The $4,000 per unit 'loyalty incentives' are being offered for the Chevy Tahoe and Suburban SUV and Silverado pickup trucks. GM is also offering an additional $3,000 per vehicle incentive for current owners who purchase hybrid models of its Chevy Tahoe and GMC Yukon models – something it has never done before. This part of the GM incentive program may be in response to Ford Motor Company's (F-NYSE) introduction of an 'employee pricing' incentive for its lineup of full size F-Series trucks. Ford has also announced a slashing of its vehicle production by 25% for the 3rd quarter and between 8% and 14% for the 4th quarter along with a delay in a new version of its F-150 pickup truck. Ford also reduced its estimate of industry sales for this year to 14.7-15.2 million (including medium and heavy-duty trucks) from its already reduced estimate of 15.0-15.4 million units.

With few options other than conservation, consumers know they need to make adjustments in their lifestyles

What appears increasingly evident is that high gasoline and diesel prices are reshaping American consumer vehicle driving and buying habits. Part of the shift underway is in response to the rapid rise in fuel prices that are impacting consumer budgets, but part is in response to the growing recognition that there is little the government can do to reduce high energy prices. With few options other than conservation, consumers know they need to make adjustments in their lifestyles. At the present time, the cutback in miles driven is putting America on a pace similar to 2005 when there were eight million fewer people than today. Conservation can be a powerful tool, and one often overlooked by energy forecasters.

Can High Fuel Costs Lead to Other Benefits?

No longer can the department's cruisers patrol the streets at night

In the Colorado Springs region of the country, high gasoline prices have inflicted financial pain on the El Paso County Sheriff's Department. No longer can the department's cruisers patrol the streets at night. In 2000, the sheriff's department budgeted about $160,000 a year for fuel. That bill had doubled by 2004 and has increased every year since. This year, even with driving reductions in place, the department expects to spend $700,000 on fuel. Were the cruisers to drive all night, the department's fuel bill would approach $1 million this year. This created a financial crisis that necessitated some action.

The deputies who are not responding to emergencies will be asked to wait in two-person teams in their cars, relying on their handheld radios whenever possible and turning on their cars only to recharge the radio batteries

An editorial in *The Gazette* discussing this problem suggested that Sheriff Terry Maketa had no option but to park the patrol cars. They opined that this financial situation was not grounds to ask for new taxes since the citizens have their fuel tanks to fill and with people getting pink slips rather than salary raises, higher taxes are not an option. The new policy for officers during the night shift, which became effective June 1, will be for them to sit in their cars outside fire stations and other central locations and wait until someone in their district phones 911. The deputies who are not responding to emergencies will be asked to wait in two-person teams in their cars, relying on their handheld radios whenever possible and turning on their cars only to recharge the radio batteries. The policy will be revisited after 30 days to see how it affects response times and other services for county taxpayers according to the sheriff. We do wonder how the policy will be adjusted during the winter months.

While applauding the sheriff's actions, the editorial suggested that rather than run big cars to charge tiny batteries, the officers should be supplied with multiple batteries, portable pre-powered chargers or multiple charged radios. Their conclusion was "[c]onsidering the price of gas, any investment in efficient charging equipment could pay off in a few short weeks, or even days."

Now that the deputies will be sitting idle, they should be able to complete paper work that Sheriff Maketa explained had been a "huge problem"

The editorial writers also pointed out that the parked patrol cars won't only save gasoline, but will solve another problem that has been facing the sheriff's department. According to the writers, in 2006 a law enforcement consultant noted that the county's deputies had difficulty completing written reports on time because of their heavy workloads. Now that the deputies will be sitting idle, they should be able to complete paper work that Sheriff Maketa explained had been a "huge problem."

The editorial made the point that: "Like it or not, we can't live business-as-usual when oil thugs decide to tighten the screws on us. Adjustments must be made." They went on to list many adjustments in our lifestyles that will and need to change. The editorial concluded by saying, "The energy crisis demands that individuals rely more upon themselves, and less upon third party oil dictators, public utilities, and roving law enforcement. In that sense, at least, the high cost of fuel may strengthen us all." We agree that our lifestyles are starting to change and how much and in what ways they change is largely unknown. The prospect is that we will be consuming less energy in the future than today, and probably liking it better.

Drivers Making Adjustments – Airlines Forcing Changes

A week ago, *The New York Times* (NYT) had two small articles

The reactions of consumers to high energy prices are proving, and will to continue to prove, a challenge for forecasters to capture in their models

juxtaposed that generated an amused reaction. Both articles considered how people are dealing with high and rising prices for fuel. In one case, it was the impact of climbing gasoline and diesel fuel prices on vehicle use. The other reflected on changes the airline industry was implementing to deal with the cost of sky-high jet fuel. The reactions of consumers to high energy prices are proving, and will continue to prove, a challenge for forecasters to capture in their models. How many of the changes being undertaken by drivers or forced on airline passengers will prove permanent or stimulate further adjustments?

The transaction costs involved in buying and selling vehicles and moving closer to work mean that consumers not only believe current energy cost trends will continue for a long time or worsen

The NYT reported on the results of a survey carried out by the NPD Group, a research firm, on the impact rising fuel prices have had on automobile drivers – forcing both long-term and short-term adjustments. The survey pointed out how drivers were making choices – some long-term lifestyle changes and others more-reversible changes. As one would expect from a survey of this type, the relatively short duration of the "pain and suffering" American consumers have experienced due to high gasoline prices leads to a very small percentage of drivers making significant lifestyle changes. Only 2% of respondents have moved closer to work, while 3% have sold their less fuel-efficient vehicles. Some 6% of those surveyed said they have purchased more fuel-efficient vehicles. The transaction costs involved in buying and selling vehicles and moving closer to work mean that consumers not only believe current energy cost trends will continue for a long time or worsen, but they are willing to pay the price now to try to offset higher future costs.

Exhibit 4. Consumers React to Higher Gas Prices

Driven to Change

"Considering the price of gasoline over the past year, which of the following have you actually done?"

Canceled vacation	12%
Carpooled	12
Used public transportation	8
Vacationed closer to home	8
Bought a more fuel-efficient vehicle	6
Telecommuted	6
Worked closer to home	5
Worked less	4
Sold a less fuel-efficient vehicle	3
Moved closer to work	2

Survey of 43,000 drivers in April.

Source: NPD Group

THE NEW YORK TIMES

Source: ***The New York Times***

When one looks at many of the other steps auto drivers have taken, they generally reflect postponement actions rather than lifestyle adjustments. Some 12% of respondents have either cancelled a vacation or begun to car pool, clearly reversible actions. Another 8% either vacationed closer to home or used public transportation, while 6% telecommute. Interestingly, there were 4% of respondents who said they had actually worked less. A novel idea!

The newest, and most ominous trends for altering the flying experience, is the checked-bag fee

Although consumers are making choices about how to offset the cost of rising commuting costs, they are having little choice in adjusting to the fees airlines are implementing to try to offset rising jet fuel costs. The newest, and most ominous trends for altering the flying experience, is the checked-bag fee. American Airlines (AMR-NYSE) announced several weeks ago it was going to implement a $15 per bag charge each way for the first bag checked by passengers except those paying premium fares or members of its exclusive travel club. This charge stopped the prior thrust of airlines to impose fees on the second checked bag, and it has started a stampede of other airlines to implement the first-bag charge. The good news is that this fee is only now going into effect and it doesn't impact passengers who bought their tickets earlier this year. But when it does start to impact all passengers, watch how customers react.

For experienced business travelers who are used to carrying on their roller bag and a brief case, they will now have to fight more passengers for the limited overhead luggage space on planes that will be even fuller than before due to the airline capacity cutbacks

The airlines expect more passengers will try to carry on more of their luggage than they did in the past. For experienced business travelers who are used to carrying on their roller bag and a brief case, they will now have to fight more passengers for the limited overhead luggage space on planes that will be even fuller than before due to the airline capacity cutbacks. So the businessman who now simmers when caught behind first-time flyers going through the airport security inspection stations, he will soon have to endure what will seem endless announcements about carryon luggage restrictions and instructions about where and how to stow baggage on the plane. A representative from American Airlines suggested that "we're going to enhance communications with the customer as they're sitting in the lounge." That's code for lots of irritating announcements. How valuable will airline club lounges become in that environment?

Talk about a customer relations nightmare about to be un-leased, the bag-check fee is a ticking time bomb

Besides the verbal abuse of all these announcements, the airline gate agents will become more like prison wardens inspecting the passengers lining up for boarding on order to make sure none of them are trying to sneak on extra bags. But the big question will be the business traveler making a tight connection only to find that all the available overhead space has been taken. How will he react to being told he will have to "gate check" his bag and for that honor, pay a modest fee? Or will airlines waive that late arrival bag-checking fee, which would surely create a public uproar. Talk about a customer relations nightmare about to be unleashed, the bag-check fee is a ticking time bomb.

The writer of the airline article captured the impact of these new

"Travel is a curse, but here we strive to lighten your purse…Charge'em for the lice, extra for the mice: Two percent for looking in the mirror twice!"

airline fees when he quoted from the song sung by the landlord, Thenardier, in the Broadway version of "Les Misérables." The song goes, "Travel is a curse, but here we strive to lighten your purse…Charge'em for the lice, extra for the mice: Two percent for looking in the mirror twice!" To help our fellow travelers and readers of the Musings, we found the following tables on the travel web site FareCompare.com, which they promise to keep updated. The fees show airline bookkeepers to be more creative than one would otherwise think. We wonder if the airlines will eventually discover that the hotel industry once tried to boost its profits with similar revenue-raising gimmicks such as charging for local telephone calls, daily newspapers that they gave away for free, etc. These charges were eventually jettisoned in favor of marginally higher room rates. We are embarking on an interesting period in our lives when many of us will experience flashbacks to the People Express era of the 1980s or the low-cost European airline experiences of the past few years. Just thinking about those experiences makes us want to shout: Raise the ticket fare by $10.

Exhibit 5. Data On New Airline Fees

	Reservation by Phone (per person)	1st Checked Bag Fees (each-way)	Baggage Fees (2nd bag) (each-way)	"Seat Selection / Priority / Leg Room"
American	$20	$15	$25	None
Continental	$15	Free	$25	None
Delta	$25	Free	$25	None
Northwest	$15	Free	$25	$5 - $35
United	$25	$15	$25	$14 - $109
US Airways	$15	$15	$25	$5 - $30
AirTran	$10	Free	$10	$6 - $20
Alaska	$15	Free	$25	None
Frontier	$15	Free	$25	None
JetBlue	$15	Free	$20	$10 - $20
Southwest	Free	Free	Free (3+ $25)	$10 - $30 [1]
Spirit	$20	$10	$20	None
Midwest	$10	Free	Free (3+ $100)	None
Hawaiian	$10-30	Free	$25.00	None
Go	Free	Free	Free	None
Express Jet	Free	Free	Free	None
Virgin America	$10	Free	$25	$15 - $50
Allegiant	$10 ea/way	$10-20 [5]	$10-20 [5]	

	Beverage/Snack Packet	Meal	Alcohol	Oversize Bag Fee (each-way)	Overweight Bag Fee (each-way)
American	Free/none	$3 - $6	$6	$150	$50 - $100
Continental	Free	Free [2]	$5	$100	$50
Delta	Free	$4 - $10	$5 - $6	$150	$80 - $150
Northwest	Free	$7 - $10		$100	$50
United	Free	$5 [3]	$5	$100	$100
US Airways	$2 bev/none	$5 - $7	$7	$100	$50 - $100
AirTran	Free	None	$6	$29 - $69	$29 - $69
Alaska	Free	$5	$5	$50 - $75	$50
Frontier	Free	$3	$5	$75	$75
JetBlue	Free	None	$5	$75	$50 - $100
Southwest	Free ($3 Energy)	None	$4	$50	$25 - $50
Spirit	Free ($4 R. Bull)	$5.0		$100 - $150	$100 - $150
Midwest	Free (Cookie)	$6 - $11	$5	$80	$50 - $65
Hawaiian	Free			$160 - $360	$50
Go	Free	None		$25	$25-50
Express Jet	Free	Free	$1 - $3		
Virgin America	Free	$6 - $8	$5 - $6	$50	$50 - $100
Allegiant	$2-$4	LAS-only $5	$5	may apply	may apply

	Travel w/ Pets (each-way)	Unaccompanied Minors (per flight)	Curbside Check-In	Non-Refundable Ticket Change Fee
American	$100 - $150	$100	Free	$150
Continental	$95	$75 - $100	Free	$150
Delta	$100 - 200	$100	$3	$100
Northwest	$80 - $359	$75 - $100	$2	$100
United	$100 - $200	$99	$2	$150
US Airways	$100	$100	$2	$150
AirTran	$65	$39	Free	$50
Alaska	$100	$75	$2	$50 - $75
Frontier	$100 - $200	$40	n/a	$100
JetBlue	$100	$75	$2	$100
Southwest	No Pets	Free	Free	Free
Spirit	$75	$75***	$2	$100
Midwest	$100	$50	Free	$100
Hawaiian	$35 - $175	$35 - $95		
Go	$25	$25	n/a	$20
Express Jet				
Virgin America	$100	$75		$75
Allegiant	$75	$75	n/a	$50 [4]

[1] Business Select Additional Fee for Priority Boarding
[2] Flights 2+ hours
[3] Snack Box
[4] Trip Flex Free
[5] $10 Pre-paid $20 Time of Check-in

Source: FareCompare.com

High Heating Oil Prices Stimulating Firewood Sales

They have heard of more people converting their heating systems from oil-fired to wood-burning

The Providence Journal reported that Maine firewood dealers are seeing more people switching to wood for heating. According to Annie Manley of J&M Logging of Augusta, Maine, people who usually order two or three cords of wood for the winter are now ordering five or six cords. They have heard of more people converting their heating systems from oil-fired to wood-burning. As a result, they are receiving a noticeable increase in phone calls inquiring about delivery options for wood, suggesting that the callers are planning on using wood stoves as their primary or back-up heating systems.

It is hard to conceive of wood and coal making big inroads in the residential heating market

We remember when our sister and brother-in-law installed a coal stove in their family room in their house in Connecticut to help offset rising heating oil bills and supply shortages that had developed in New England in the late 1980s. They struggled to find a supplier who could provide them bags of coal. Until that experience, the last time we remember seeing coal delivered to a home was in the 1950s when neighbors down the street from our childhood home had a coal-fired burner. The coal truck would stick a chute through a special window into the coal bin in the basement and then raise the back of the truck and pour all the coal down the chute. As nostalgic as these items seem, it is hard to conceive of wood and coal making big inroads in the residential heating market, especially given that these fuel sources are considerably less environmentally-friendly.

Check The Tire Treads On Canadian Government Officials

A major policy debate is underway in Canada about whether the federal government should establish a carbon-tax or a carbon cap-and-trade system to deal with CO_2 emissions

The Canadian government is wrestling with developing the most appropriate national energy policy while addressing the concerns of its citizens about the contribution of carbon emissions to global warming. A major policy debate is underway in Canada about whether the federal government should establish a carbon-tax or a carbon cap-and-trade system to deal with CO_2 emissions. While we watch from our perch south of the border, Canada's political party leaders are discussing and debating various ideas and possible legislation to deal with these complex and emotional issues. However, we were intrigued last week to see public announcements dealing with possible new nuclear power plants for various provinces. It seems that provincial political, regulatory and business leadership for green-energy policies is overrunning the policies of the federal government.

In Saskatchewan, the prairie province appears about to welcome nuclear energy as a possible long-term solution to its energy supply needs. Last week, Bruce Power, a privately owned nuclear power plant operator, unveiled plans to build two 1,000-megawatt reactors in the province. This announcement followed by a day another by the Ontario government that it intends to build two new reactors at the Darlington Nuclear Station located near Toronto. This announcement is part of the Ontario government's plan to expand and refurbish its existing fleet of nuclear power plants.

In the U.S. many of the planned plants have been announced in order to take advantage of federal government assistance

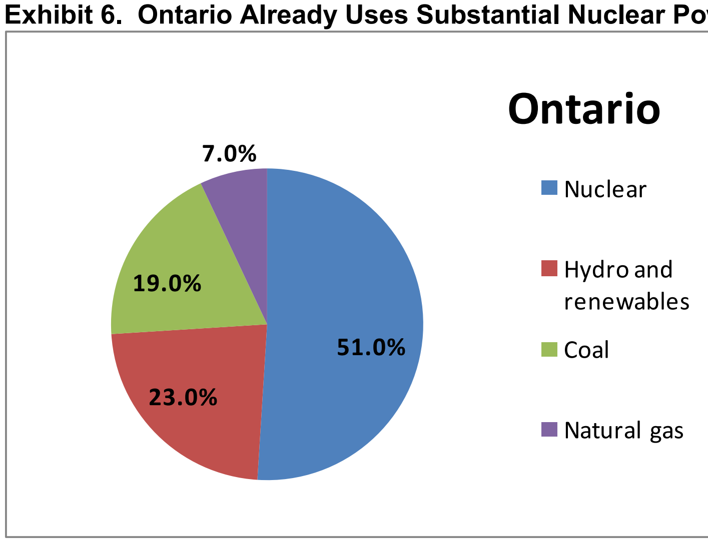
The nuclear power industry appears on the cusp of a global revival led by a wave of announced new nuclear power plants for the United States and Europe. It is true however, that in the U.S. many of the planned plants have been announced in order to take advantage of federal government assistance for designing and locating the plants along with obtaining insurance coverage. Globally, we are seeing a number of new nuclear power plants being planned or starting construction in countries as diverse as China, France, Germany and now Canada.

The Ontario plant announcements would mark the first new nuclear plants built in the province in several decades. The most recent plant to go on line there was powered up in 1992. Ontario Energy Minister Gerry Phillips wants the two new nuclear reactors to be built at the Darlington Nuclear Station and operated by privately-owned Ontario Power Generation. He wants the builder to break ground by 2012 and for the plants to be in operation by July 1, 2018, a decade from now. To facilitate the timeline, the awards for building the plants are to be announced by November 1, 2008.

Nuclear power already plays a significant role in Ontario in contrast to the prairie provinces of Saskatchewan, Alberta and Manitoba

Nuclear power already plays a significant role in Ontario in contrast to the prairie provinces of Saskatchewan, Alberta and Manitoba. Nuclear power currently accounts for 51% of the electric power produced in Ontario and while some of the additional output from the new plants will offset aging nuclear plants that will need to be decommissioned in the future, some of the power will meet future demand enabling the province to avoid building other hydrocarbon-powered plants down the road. How much of the province's existing nuclear power will be retired is uncertain since nuclear plants are having their lives extended through upgrades and refurbishments.

Exhibit 6. Ontario Already Uses Substantial Nuclear Power

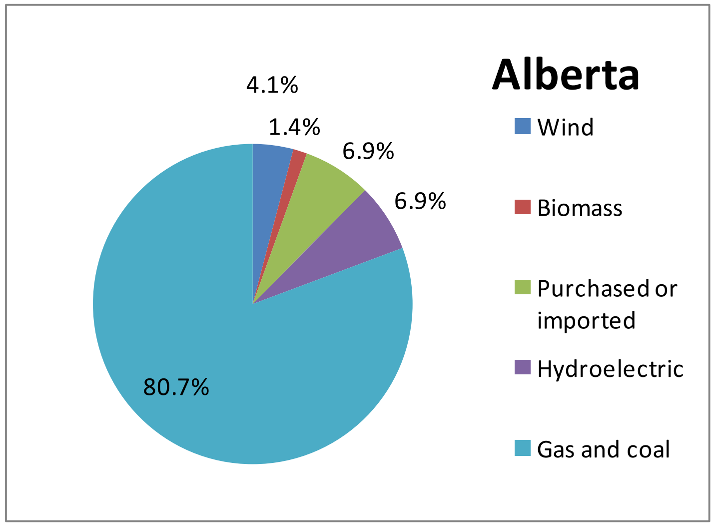


Source: Ontario Energy, PPHB

Saskatchewan and Alberta depend on natural gas and coal for a substantial amount of its power supply, while Manitoba is blessed with access to hydroelectric power, which supports almost all power supply in the province

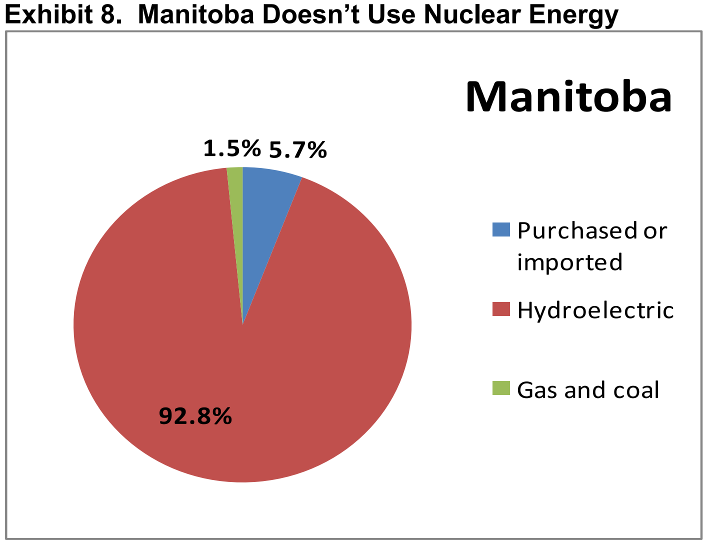
However, within the three prairie-provinces environmental issues are becoming more important. Nuclear power has not been a source of energy supply in any of them. Saskatchewan and Alberta depend on natural gas and coal for a substantial amount of its power supply, while Manitoba is blessed with access to hydroelectric power, which supports almost all power supply in the province. The issues driving the interest in nuclear power are quite different in Saskatchewan and Alberta. The latter province has had nuclear plants floated as an option for fueling the oil sands power requirements for bitumen extraction. On the other hand, Saskatchewan is interested in promoting nuclear power as a replacement for its coal power plants and to capitalize on the province's world leadership position in the mining of uranium, the fuel source for nuclear power.

Exhibit 7. Alberta Uses No Nuclear Power



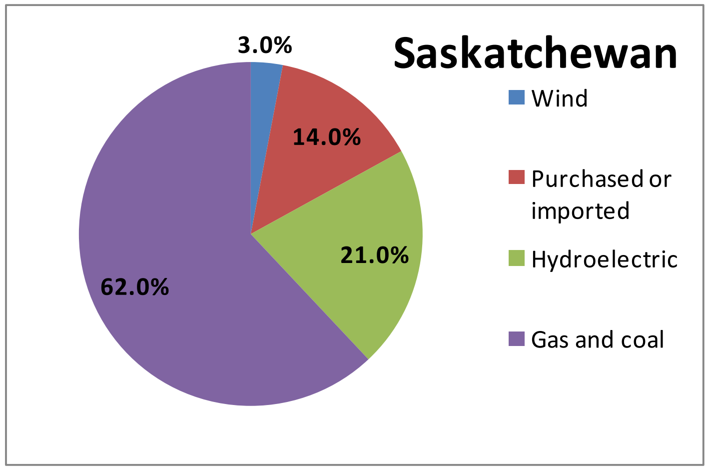
Source: ***Globe and Mail*****, Alberta Energy, PPHB**

Exhibit 8. Manitoba Doesn't Use Nuclear Energy



Source: ***Globe and Mail*****, Manitoba Hydro, PPHB**

Exhibit 9. Saskatchewan Wants Nuclear Power



Source: *Globe and Mail*, SaskPower, PPHB

The proposal for the two new nuclear power plants in Saskatchewan has been made by Bruce Power who said it plans to work with SaskPower, the province's electricity utility, to evaluate power demand for the province and to examine the issue of transmission requirements for the new plants. One of Bruce Power's shareholders is Cameco Corp. (CCJ-NYSE), the Saskatchewan-based, world leading uranium mining company.

At the heart of the debate over nuclear power plants is the growing recognition of the impact of carbon emissions on global warming

At the heart of the debate over nuclear power plants is the growing recognition of the impact of carbon emissions on global warming. A corollary issue is the rising cost of hydrocarbons. According to Shane Pospisil, president of the Ontario Energy Association, "We're certainly seeing resurgence in interest and activity in nuclear power around the world and in Canada. One of the key drivers here is obviously the direct benefits nuclear power will provide in a carbon-constrained world."

Saskatchewan Premier Brad Wall is a proponent of the nuclear power option since it fits with his plan to drive economic growth in the province by exploiting its natural resources including the uranium deposits. As Mr. Wall reportedly said earlier this year, "It's time for the country to have a new national vision on nuclear energy – and we want to aggressively pursue that."

This new interest in nuclear power reflects the growing economic and financial strength of the western provinces in combating greenhouse gases

This new interest in nuclear power reflects the growing economic and financial strength of the western provinces in combating greenhouse gases. The interesting trend in Canada is that the four western provinces – British Columbia, Alberta, Saskatchewan and Manitoba - are working together on common issues, including energy and emissions, and by-passing the federal government. At the same time, earlier this month there was a historic joint cabinet meeting of the governments of Ontario and Quebec, the country's two most populous provinces, dealing with how to combat global warming. For the Canadian federal government, these actions demonstrate the truth of American humorist Will Rodgers' comment, "Even if you're on the right track, you'll get run over if you just sit there." We suggest someone might want to check the tire tracks on the bodies of federal government leaders.

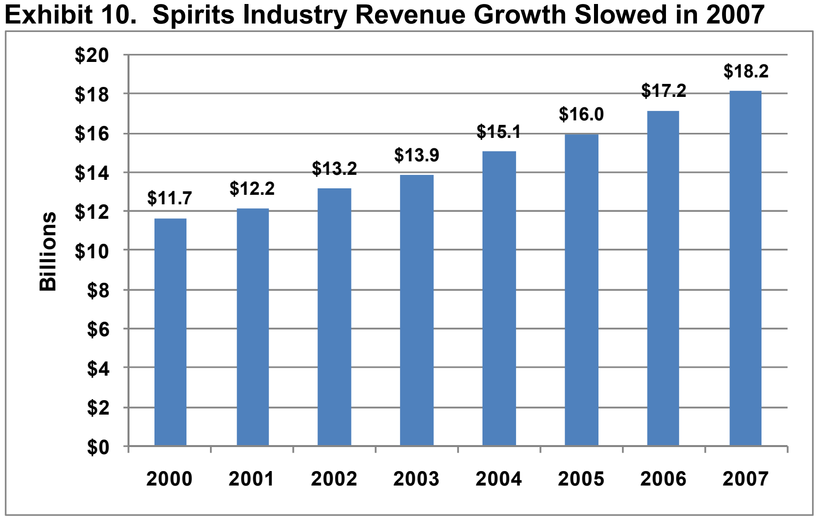
Drinking or Driving: The Impact of High Gasoline Prices

We were recently involved in a discussion about our articles dealing with the decline in miles driven by Americans as gasoline prices have increased. One of the participants opined that American drinking habits – beer and alcoholic drinks – may be keeping pace with the amount the drinkers are spending on gasoline. Not being familiar with the amount of money people spend on drinking, we were not able to concur or disagree with the offered opinion. That sent us to look at the data.

In terms of dollar volume, the industry's growth over the 2000-2007 time period was 6.5%, but it slowed to only 5.6% last year

We started our search about the spirits business with a goal of finding out exactly how large it is, its growth rate and the source of its growth. What we found, according to data from the Distilled Spirits Council of the United States ("DISCUS") is that since 2000, spirits volumes grew at a 2.9% average annual rate, although in 2007 the growth slowed to only 2.4%. (Annual growth rates are noted in Exhibit 11.) In terms of dollar volume, the industry's growth over the 2000-2007 time period was 6.5%, but it slowed to only 5.6% last year. We thought those trends were interesting since it appears the spirits industry's growth is following the trajectory of the gasoline business as the rate of consumption has slowed in recent years and in recent weeks the growth has actually turned negative.

Exhibit 10. Spirits Industry Revenue Growth Slowed in 2007



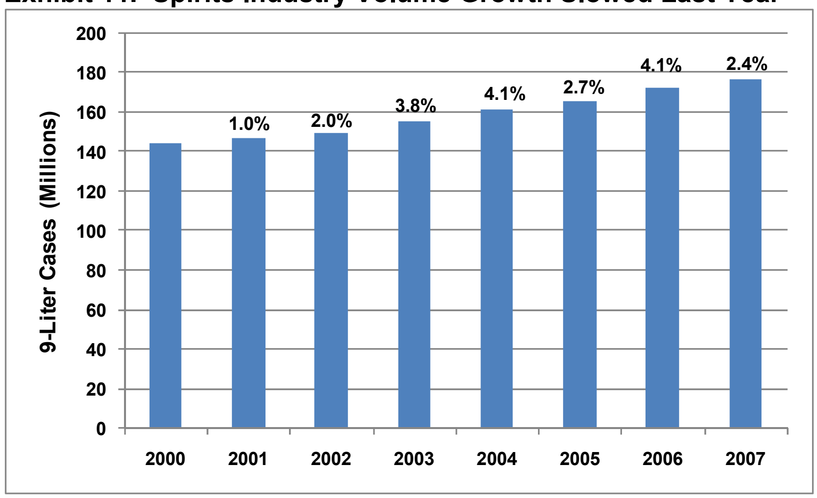
Source: DISCUS, PPHB

In 2007, the spirits industry generated $18.2 billion in revenues. Approximately 50% comes from beer, while wine represents almost 17% and alcohol accounts for 33%. The change in market share from 2006 was marginal with beer's share shrinking from 50.5% to 50.1% and the share was spread about evenly between wine and

In 2005, according to DISCUS, the retail price of a typical 750ml bottle of 80 proof spirits was $11.75 with 59%, or $6.92 of the price going to taxes and fees

alcohol. What we did find interesting was DISCUS making the point that its industry suffers from an excessive tax burden, much like the retail gasoline business. In 2005, according to DISCUS, the retail price of a typical 750ml bottle of 80 proof spirits was $11.75 with 59%, or $6.92 of the price going to taxes and fees. According to the Energy Information Administration (EIA) over the period 2000-2007, federal, state and local taxes accounted for 24% of the average price of a gallon of gasoline, which they calculate to have been $1.91 over the period. As the average gasoline price has risen, the percentage going for taxes has declined to about 17% last year, and likely lower yet this year.

Exhibit 11. Spirits Industry Volume Growth Slowed Last Year



Source: DISCUS, PPHB

In trying to answer the question of how much the average American spends for alcohol versus gasoline and motor oil, we turned to the U.S. Bureau of Labor Statistics' Consumer Expenditures Survey. This survey is conducted annually and consists of both a survey and the collection of diaries completed by families. The data plays a role in the department's calculation of the monthly Consumer Price Index. The survey measures expenditures on specific consumer items by consumer unit grouped by income levels, age categories, ethnic and race composition and educational levels attained. The survey measures a number of specific items within broad categories such as food, alcoholic beverages, housing, apparel, transportation, healthcare, entertainment, personal care products and services, reading, education tobacco products, miscellaneous, cash contributions and personal insurance.

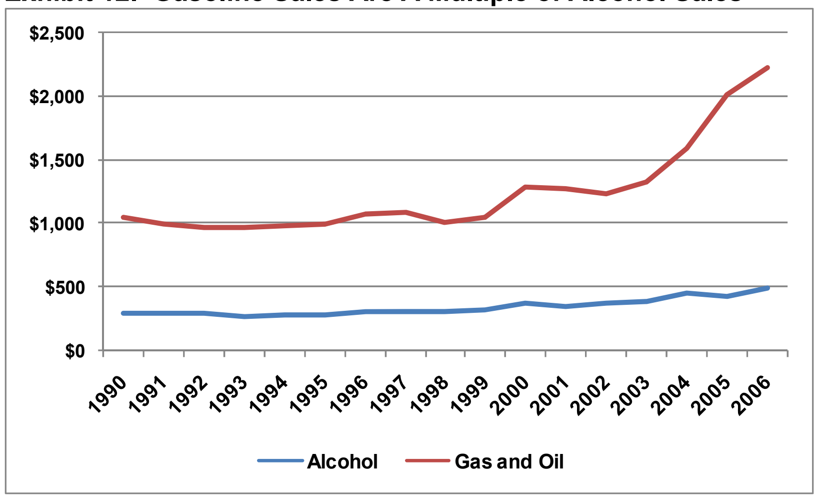
Americans spend considerably more on gasoline than on alcoholic beverages

Within the transportation category, there is a line item for gasoline and motor oil. We used that data to compare with the alcoholic beverages expenditure data. What we found was that Americans spend considerably more on gasoline than on alcoholic beverages. The chart of these two expenditures (Exhibit 12) over the time period 1990 through 2006 (the last year that detailed figures are available) show that both categories of expenditures were relatively stable

We were surprised at how stable the ratio was over time at 3.5X that subsequently jumped in 2006 to about 4.5X

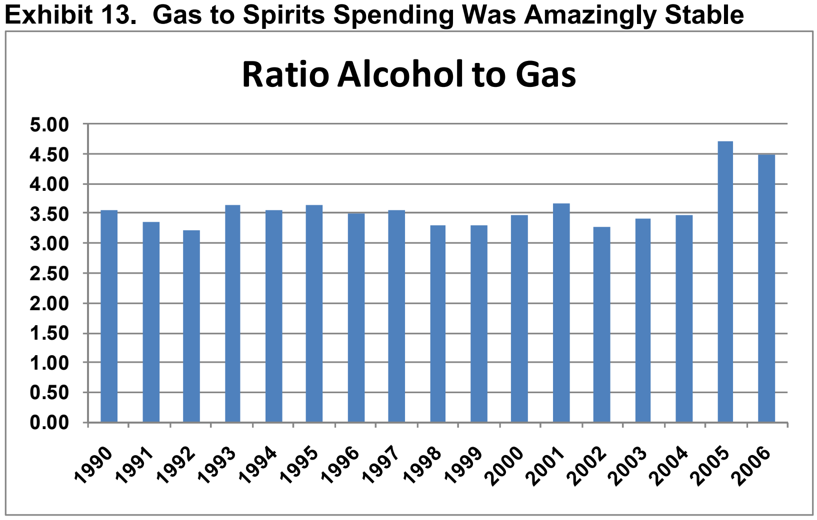
during the 1990s, and then began to rise after 2000. Gasoline expenditures since 2000 have risen much faster than for alcoholic beverages, consistent with the rise in crude oil prices. To reflect the rise in gasoline expenditures, we determined the ratio of gasoline to alcoholic beverage expenditures that shows a very stable ratio until 2005 and 2006. We expect that this ratio has increased further in 2007 and 2008. But we were surprised at how stable the ratio was over time at 3.5X that subsequently jumped in 2006 to about 4.5X. We can only imagine what this ratio is up to today given roughly $4 a gallon gasoline prices.

Exhibit 12. Gasoline Sales Are A Multiple of Alcohol Sales



Source: BLS, PPHB

Exhibit 13. Gas to Spirits Spending Was Amazingly Stable



Source: BLS, PPHB

What we now know is that Americans have consistently spent more to feed their vehicles' thirst than they have to quench their own thirst. While the conclusion is not surprising, what did strike us as surprising was how stable the ratio of gasoline expenditures to

If they can't drive their vehicles because of high fuel prices, it may leave drinking as the preferred recreational alternative

alcoholic beverage expenditures was for 14 years even as the oil industry experienced what at the time was considered "boom" and "bust" periods. Today, Americans would welcome a return to that old, 3.5X ratio. We doubt it will be achieved by Americans drinking a lot more, although if they can't drive their vehicles because of high fuel prices, it may leave drinking as the preferred recreational alternative.

Contact PPHB:
1900 St. James Place, Suite 125
Houston, Texas 77056
Main Tel: (713) 621-8100
Main Fax: (713) 621-8166
www.pphb.com

Parks Paton Hoepfl & Brown is an independent investment banking firm providing financial advisory services, including merger and acquisition and capital raising assistance, exclusively to clients in the energy service industry.