

MUSINGS FROM THE OIL PATCH

November 13, 2007

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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

Oil Prices, The Dollar, Consumers and OPEC

The U.S. dollar remains the primary currency for world trade and the global economy's reserve currency

The daily financial news is dominated by discussions about the weakness of the United States dollar versus other major currencies such as the Euro, the Japanese yen and the Canadian dollar. In all three cases, the U.S. dollar has been sinking in value against these currencies for some time, resulting from global trade and investment patterns and the view by financial markets of the relative strength and future direction of the U.S. economy. The U.S. dollar has been, and remains the primary currency for world trade and the global economy's reserve currency.

Exhibit 1. U.S. Dollar Value Continues to Slide



Source: Wall Street Journal

The weakening U.S. dollar is impacting the price of crude oil

The continuing weakening of the U.S. dollar, and the media's attention to the situation, is beginning to gain the attention of the average U.S. consumer. As a result, the consumer is trying to understand how this country's deteriorating financial health, coupled with the prospect of an impending economic recession, could impact the future value of the dollar. The long-term trend in the weakness of the U.S. dollar is reflected in the chart of the trade weighted dollar index contained in Exhibit 1. What it shows is that since 1973, with the exception of periods of dollar strength in the 1980s and then again late 1990s and early 2000s, the trend of the dollar's value has been steadily downward.

A major concern for U.S. consumers as a result of the weakening U.S. dollar is the impact this trend is having on the price of crude oil and its derivatives – gasoline and heating oil. A recent article in *The Houston Chronicle* highlighted this concern among Houstonians based on comments they made to a reporter. These statements were contained in a story about the impact on consumers' pocketbooks from the recent jump in gasoline pump prices, especially given their likely further rise.

The headline was: 'It's all about the dollar'

A *Houston Chronicle* reporter interviewed customers filling up their vehicles at a Fuel Depot service station in the Heights. The headline for the section of the article containing the quotes was: 'It's all about the dollar.' In the section, the reporter quoted comments from three customers. All were bemoaning the high cost of gasoline on their budgets. One, however, Frances Parales, a 71-year-old retiree, putting \$10 worth of gasoline into her truck, actually proved more astute than the reporter based on her quote. She said, "I don't think it's fair because I think there's a lot of gas and a lot of oil. It's all about the dollar."

It seemed from the article that the reporter was more interested in focusing only on the supply and demand impact on oil prices and not the dollar's impact. One interesting consideration about the article was the view of the jump in current gasoline prices and the impact on consumption. The Texas statewide average price for a gallon of regular gasoline was \$2.95 on last Friday. This compares with the Texas statewide record price of \$3.09 a gallon reached last May. Experts are suggesting that we will surpass that record shortly, and especially if crude oil prices shoot pass \$100 per barrel as many commodity traders and analysts expect.

Energy industry experts say that \$3 per gallon gasoline prices are not impacting consumption

Nationally, according to the AAA Automobile Club, the average price for gasoline last Friday was \$3.08 per gallon, after having jumped 31 cents in the past month. A year ago, the national gasoline average price per gallon was \$2.22. Interestingly, the national record gasoline price of \$3.23 per gallon was reached last May, but the historic inflation-adjusted price was \$3.29 in March 1981. The comments from gasoline and energy industry experts contained in the article were that \$3 per gallon gasoline prices were not impacting consumption patterns because consumers have adjusted to them. (We're not sure if we buy that analysis.)

There has been a recent report that OPEC oil ministers will likely discuss creating a basket of currencies for oil pricing at its next summit due to start December 11

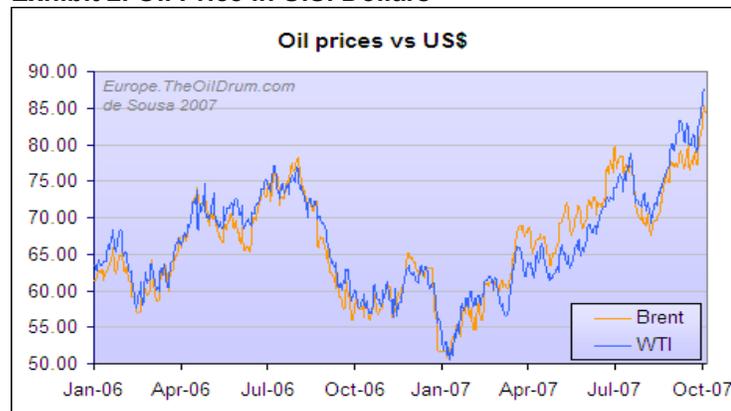
American and Chinese consumers have seen petroleum prices in their countries climb substantially more than experienced by consumers in many other countries around the world

If it is all about the dollar, should we be concerned? It appears, although it is not totally clear, that OPEC members are growing more concerned about the impact of the U.S. dollar's weakness on global oil markets. There has been a recent report that OPEC oil ministers will likely discuss creating a basket of currencies for oil pricing at its next summit due to start December 11. The motivation behind this discussion is the steady decline in the value of the dollar, at least according to Venezuela's Energy Minister Rafael Ramirez. The reason for pricing oil based on a basket of currencies is that it would help eliminate some of the distortions currently thought to be impacting the global petroleum market. Immediately after the Venezuelan energy minister spoke, other OPEC member officials discounted the need to adjust pricing.

Of course, the major beneficiaries of a change in oil pricing in favor of a basket of currencies and away from a U.S. dollar price would be the United States and China, the two largest oil consumers. To understand the disparity in pricing of crude oil between U.S. dollars and other currencies, we found a series of charts prepared by Luis de Sousa from The Oil Drum: Europe that helps explain the phenomenon. What these charts show is that the American and Chinese consumers have seen petroleum prices in their countries climb substantially more than experienced by consumers in many other countries around the world. This is largely because the Chinese currency is tied to the U.S. dollar, and as it has declined in value, the producers want to inflate the price more to offset the lost value.

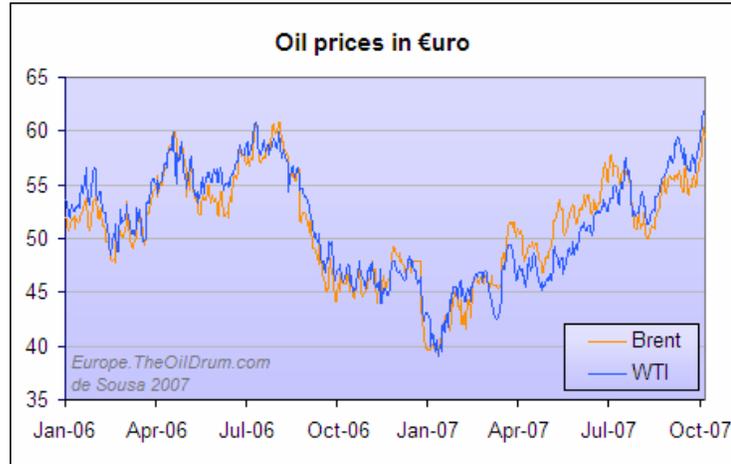
Pictured in the following exhibits are charts showing the price of WTI oil and Brent oil priced in the local currency for the U.S. dollar, the Euro, the Canadian dollar, the Japanese yen, the British pound, the Russian ruble, the Chinese renminbi, the Australian dollar and in terms of the value of gold. Most of the oil prices are slightly higher given the latest run up in crude oil prices, but in terms of the Australian dollar, Canadian dollar and gold, they are lower. The point is to examine the pattern of oil prices in the local currencies over the period since the start of 2006.

Exhibit 2. Oil Price in U.S. Dollars



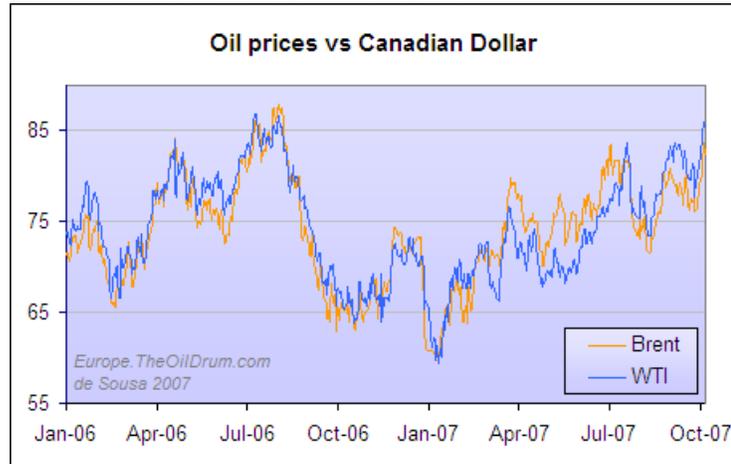
Source: de Sousa, The Oil Drum: Europe

Exhibit 3. Oil Price in Euros



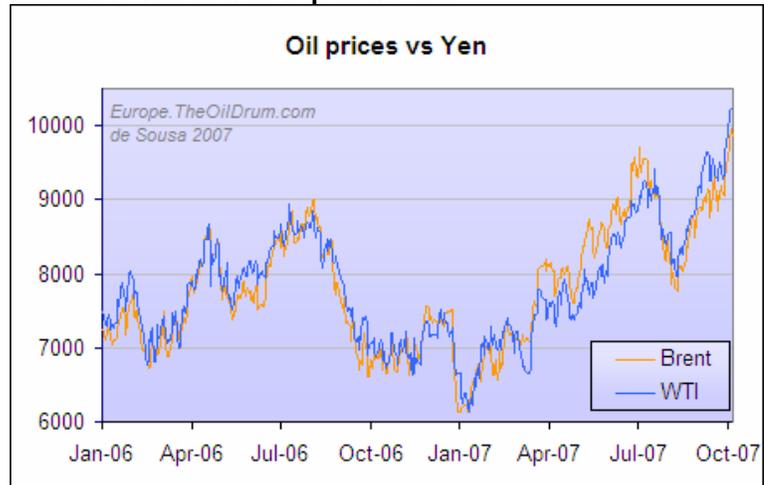
Source: de Sousa, The Oil Drum: Europe

Exhibit 4. Oil Price in Canadian Dollars



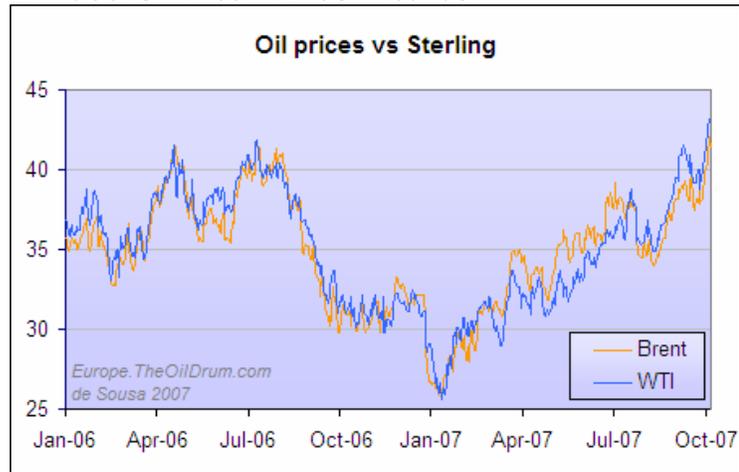
Source: de Sousa, The Oil Drum: Europe

Exhibit 5. Oil Price in Japanese Yen



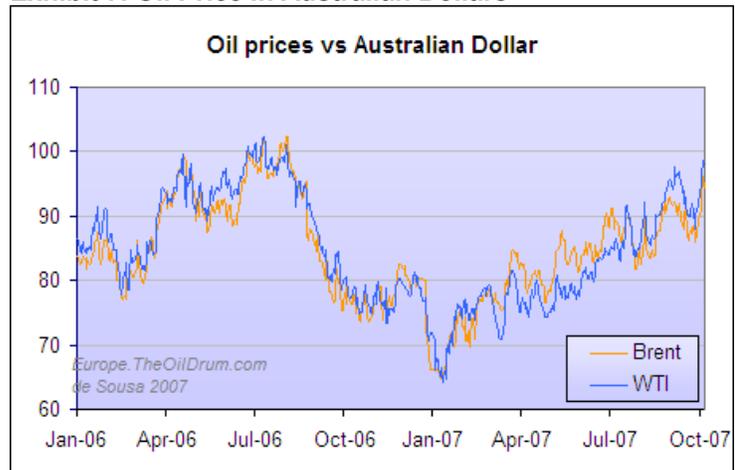
Source: de Sousa, The Oil Drum: Europe

Exhibit 6. Oil Price in British Pounds



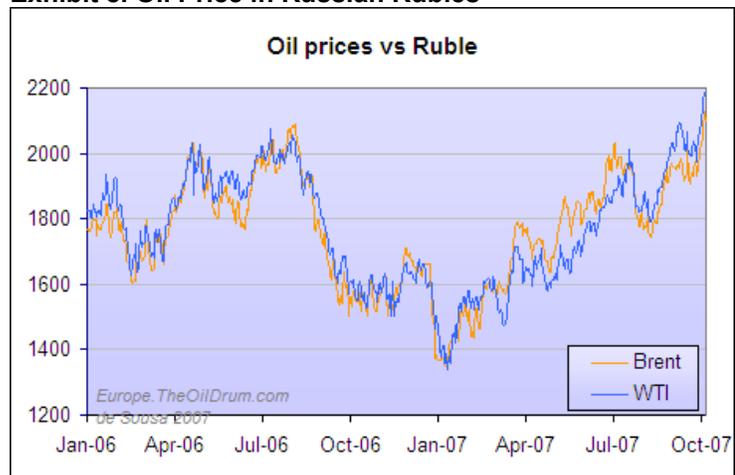
Source: de Sousa, The Oil Drum: Europe

Exhibit 7. Oil Price in Australian Dollars



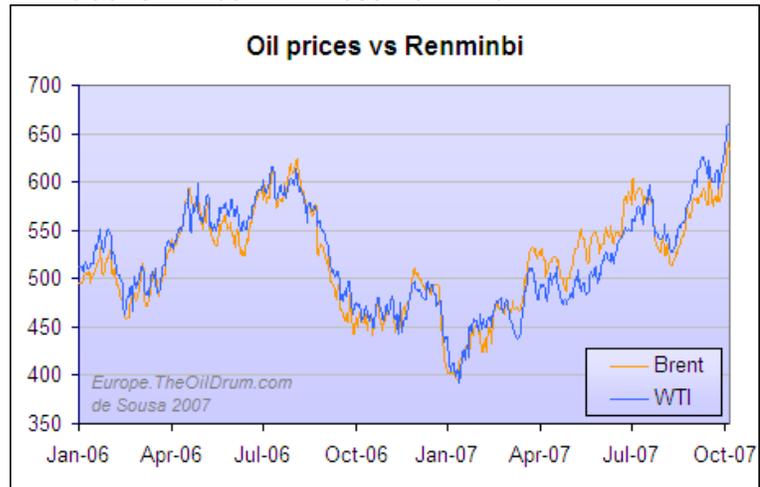
Source: de Sousa, The Oil Drum: Europe

Exhibit 8. Oil Price in Russian Rubles



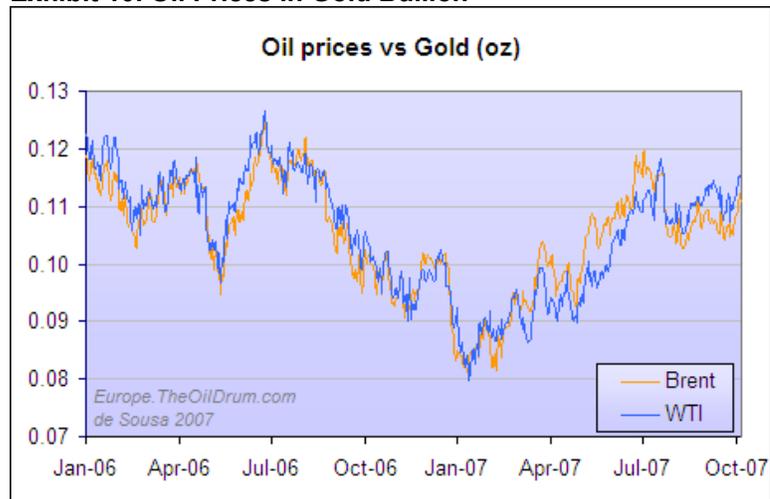
Source: de Sousa, The Oil Drum: Europe

Exhibit 9. Oil Price in Chinese Renminbi



Source: de Sousa, The Oil Drum: Europe

Exhibit 10. Oil Prices in Gold Bullion



Source: de Sousa, The Oil Drum: Europe

Many Middle East members of OPEC conduct a substantial amount of their global trade with European countries

As OPEC producers see the dollars they are paid for their oil output depreciate while the price of goods they buy from other countries inflate in dollar terms, they want to protect themselves. Many Middle East members of OPEC conduct a substantial amount of their global trade with European countries, so they are being paid in U.S. dollars and purchasing goods and services in Euros. As the Euro has increased in value relative to the U.S. dollar, reaching \$1.47 for each Euro last week, the pressure on oil producers to protect the value of the petroleum they sell is growing.

For example, as the chart in Exhibit 11 shows, the price of the 10-Year U.S. Treasury Note denominated in Euros has declined about 7% since the start of 2007. Over the year, the blue line on the chart shows the view a European buyer has of American debt. With the growing likelihood of a further interest rate cut by the Federal

Exhibit 11. Value of U.S. Debt in Euros

Source: StockCharts.com, Mauldin Letter

Reserve in December, the U.S. dollar will stay weak and possibly depreciate further. That prospect is a factor behind the strong momentum last week that drove crude oil prices toward that magic \$100 per barrel mark.

Despite the high price in U.S. dollars, the American economy is the one most able financially to absorb the impact of the higher price

As crude oil prices soar in the United States, they have barely risen above prior peak levels when priced in local currencies around the world. This oil pricing disparity has helped drive global oil demand. Despite the high price in U.S. dollars, the American economy is the one most able, financially, to absorb the impact of the higher price. Many analysts believe that U.S. oil demand is not being impacted by high crude oil prices (something we remain skeptical of).

If China were to allow its currency to rise, it could likely cut the country's energy bill by upwards of 20%

China has been hurt by the rise in crude oil prices as it has tied its currency (Renminbi) to the U.S. dollar. That has resulted in the currency being weaker than it would be if based solely on the country's financial health. The weaker currency has been a strategy of the Chinese government to enable it to gain a global cost-competitive advantage in manufacturing. On the other hand, the weaker currency has hurt the country's economy because it has inflated the cost of imports, primarily energy and raw materials. If China were to allow its currency to rise, it could likely cut the country's energy bill by upwards of 20%, along with reducing its raw material costs. Would a reduced oil price translate into increased Chinese oil consumption? If so, it would further complicate the Chinese government's efforts to control inflation, even though material input costs would be lower.

At this point, we don't expect OPEC members to alter their oil pricing scheme. There are substantial geopolitical factors that have to be factored into any such move, and we doubt the leaders of OPEC, in particular Saudi Arabia, want to disturb their current political relationships. Every time an OPEC official such as the Venezuelan energy minister tosses out the idea of changing the OPEC pricing

scheme, there will be volatility in the oil and currency markets, but at the end of the day, we think it will be mostly smoke with no fire.

The Roads Less Traveled – HOV Lanes Are Largely Unused

We recently wrote about plans for a planned major highway system in the Boston area that would encompass toll lanes, high occupancy lanes (HOV) and regular highway lanes to help ease road congestion, and implicitly lower carbon emissions. After that article, we found out that there are already some HOV lanes that were designed and constructed as a part of the Big Dig program in Boston that relocated Interstate 93's traffic lanes under the city. The problem with these HOV lanes is that they are barely being used and, according to a *Boston Globe* article, many key Boston politicians don't even know about the lanes.

Traffic engineers now believe that HOV lanes do little to ease traffic congestion

The HOV lanes were conceived nearly two decades ago in order to enable the Big Dig plans to meet state and federal clean-air rules as these lanes would encourage shared commutes. At that time, highway engineers were convinced that Americans would embrace carpooling if given sufficient incentives such as special-access lanes, and that carpooling would translate into fewer cars being driven with less air pollution. Unfortunately, by the time the Boston HOV lanes opened, traffic engineers now believe that HOV lanes do little to ease traffic congestion.

Under Massachusetts law, state highway officials are required to file regular reports on how many drivers are using carpool lanes on other sections of I-93, but not those within the Big Dig. The Federal Highway Administration does not require states to keep track of HOV lane use unless local officials are considering opening them up to solo drivers.

Since there are few statistics, a *Boston Globe* reporter monitored one hour of peak commuting time traffic on the roads. In the northbound lane, he counted 181 cars and buses, or about three cars a minute. In the southbound lane during the same time period, there were 122 cars and buses, or about two vehicles per minute. This usage was substantially below the 1,600 cars an hour the lanes were designed to accommodate.

The general lanes on I-93 within the Big Dig zone carry 10 to 20 times as many vehicles an hour, on average than the HOV lanes

The *Boston Globe* then asked Massachusetts Turnpike officials to gather statistics based on road sensors. Those statistics showed that the lanes carried an average of 59 to 167 vehicles per hour during the month of September. The general lanes on I-93 within the Big Dig zone carry 10 to 20 times as many vehicles an hour, on average than the HOV lanes. The disturbing point about the use of these HOV lanes is that the miles of roadway were constructed at a total cost of roughly \$250 million, or about \$80 million per mile.

In Boston, the primary beneficiaries of the I-93 HOV lanes have been bus passengers and taxicab and limousine drivers. Part of the

The effectiveness of HOV lanes increasingly is being questioned by transportation specialists

reason for their use is because the buses bringing passengers can more easily come into and out of the South Station terminal. The taxicab and limousines are primarily accessing the Ted Williams Tunnel, adjacent to the Big Dig, heading toward Logan Airport.

The decision to build these HOV lanes was not made exclusively by local officials. Like most communities, Boston decided to build them to comply with state and federal air quality standards. They are the most popular among several ways to meet those requirements because they can be, in some cases, cheaper to build than public transit, and, with enough carpooling, can improve air quality. However, the effectiveness of HOV lanes increasingly is being questioned by transportation specialists. According to Pravin Varaiya, an engineering and computer science professor at the University of California, Berkeley, who has spent four years study the effectiveness of HOV lanes, "HOV, as congestion mitigation or encouraging carpooling, has just proved not to do that except in a few places. The empty lane syndrome is common." At \$80 million a mile, that is an expensive empty lane.

In the brave, new energy world dominated by Peak Oil and Climate Change considerations, will states and cities decide to spend the extra money to build true mass transit facilities rather than perceived alternatives such as HOV lanes?

More Support for Cape Wind, But Not From Planners

The survey results showed strong bipartisan support for the Nantucket Sound offshore wind project

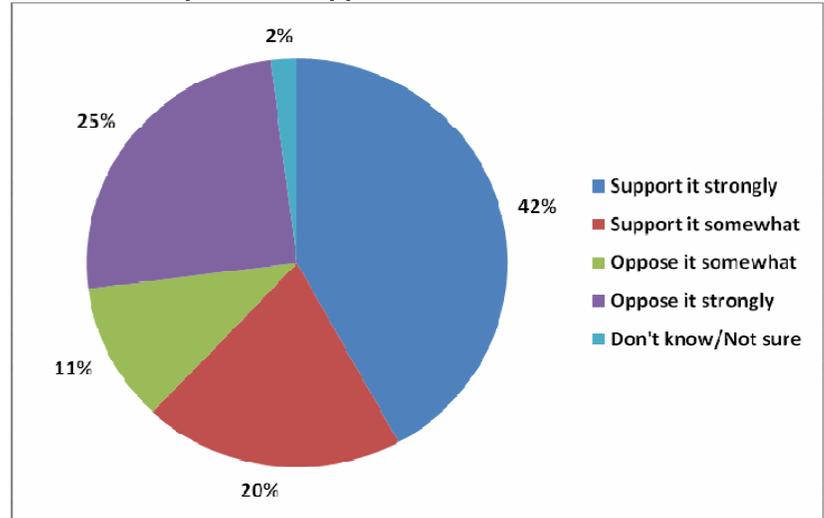
A new survey of residents of Cape Cod and the neighboring islands of Martha's Vineyard and Nantucket Island ("Cape Cod/Islands") shows that 61% of them support the Cape Wind wind-turbine project. The survey was commissioned by the Newton, Massachusetts-based Civil Society Institute (CSI) and was conducted by Opinion Research Corporation. The survey results showed strong bipartisan support for the Nantucket Sound offshore wind project with 54% of those saying they are Republicans in favor, 69% of Democrats and 50% of Independents, including 42% who support it strongly. Only about a third (36%) of residents is against Cape Wind, with only a quarter (25%) opposing it strongly. These results were consistent with the August 15, 2007, CSI survey about attitudes toward Cape Wind that found 58% of a smaller sample size in support of the project.

The results of the survey were released one week after the Cape Cod Commission regional planning agency voted 12-0 to reject Cape Wind's application as a Development of Regional Impact, a decision likely to be appealed. The survey's release also coincided with the annual meeting of a major regional environmental group, Clean Power Now, which actively supports the Cape Wind project.

Support reflects a strong belief that something needs to be done about global warming

The Cape Cod/Islands support for Cape Wind reflects a strong belief by the community that something needs to be done about global warming, which will involve reducing carbon emissions.

Exhibit 12. Cape Wind Support From Local Residents

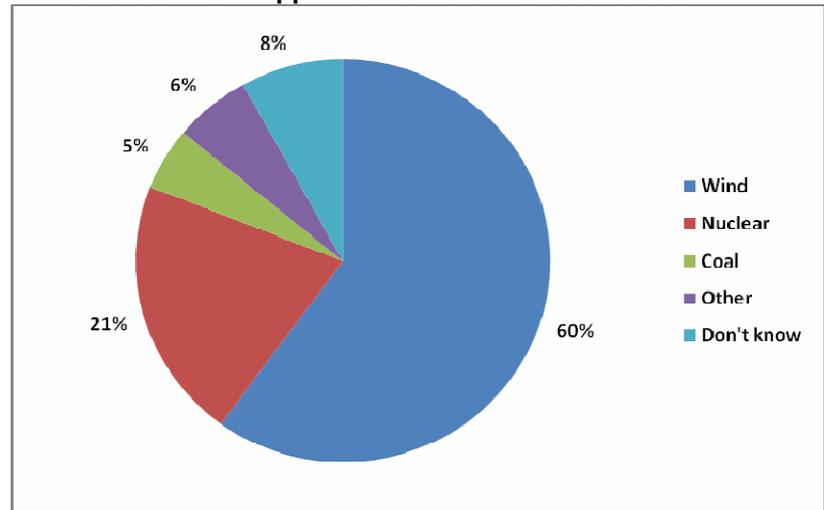


Source: CSI, PPHB

“The effects of global warming require that we take timely and decisive steps for renewable, safe and clean energy sources”

Respondents to the survey were asked their view about the following statement: “The effects of global warming require that we take timely and decisive steps for renewable, safe and clean energy sources. We need transitional technologies on our path to energy independence. There are tough choices to be made and tradeoffs. We cannot afford to postpone decisions since there are no perfect options.” Some 83% of the respondents, including 77% of Republicans, 88% of Democrats and 85% of Independents, agreed with the statement.

Exhibit 13. Locals Support Wind Over Other Alternatives



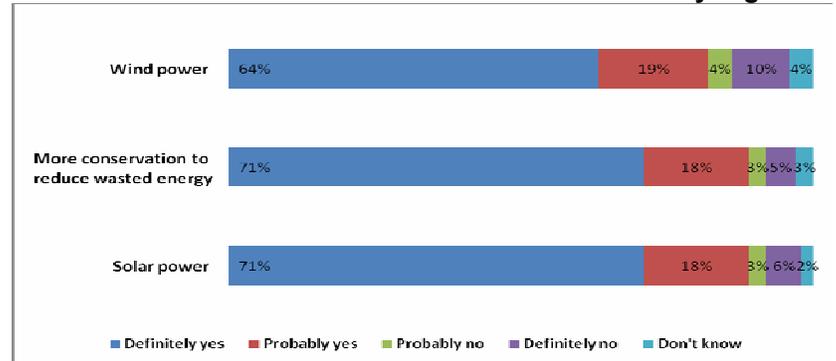
Source: CSI, PPHB

When it comes to generating electricity for the Cape Cod area, wind power is the preferred choice (60%), followed by nuclear (21%), other (6%) and last coal (5%). Cape Cod/Islands residents also

We find it interesting that conservation is the most favored solution

believe strongly that other solutions besides nuclear power should be considered. The survey asked about what should be done “before we resort to adding more nuclear power.” The favored alternatives include tougher energy conservation to reduce waste (89%); solar power (89%); and wind power (83%). Since local conditions are not highly favorable for extensive use of solar power, we find it interesting that conservation is the most favored solution. However, this alternative is increasingly being favored across the country and is forcing state utility commissions to try to figure out how to compensate electric utilities for getting people to consume less electricity. Traditional utility rate regulation is designed to reward the companies for growing its power output.

Exhibit 14. The Conservation Solution Ranks Extremely High



Source: CSI, PPHB

51% of respondents said “go ahead with Cape Wind now” using existing technology for the project

Another interesting result of the survey was that none of the attacks against Cape Wind from its detractors succeed in persuading half or more of Cape Cod/Islands residents to be more likely to oppose the project. About one in five (22%) respondents say that Cape Wind should be delayed until so-called “deepwater technology” is available to enable the project to be located further offshore. By contrast, 51% of respondents said “go ahead with Cape Wind now” using existing technology for the project. The issue of “deepwater technology” has little impact on the thinking of 22% of respondents who say that they “oppose any version of Cape Wind.”

It was interesting that tourism played a role in the thinking about the Cape Wind project. About a third of respondents (35%) said that concerns about the loss of tourism and other negative economic impacts made them less likely to support Cape Wind. On the other hand, 55% of respondents said that the tourism/economic impact issue made them more likely to support Cape Wind.

The history of the Cape Wind project is a sad commentary on the regulatory morass

As expected, the results of the survey were challenged by the opponents of Cape Wind, but that has been the normal course of action. The history of the Cape Wind project is a sad commentary on the regulatory morass surrounding many energy infrastructure projects. It is also a message about the challenges this country faces in trying to alter significantly our current energy consumption patterns.

With seven years of time invested in the licensing battle, it goes to show how hard it is to locate major environmentally-friendly energy producing facilities among the more populous areas of the country

The permitting process for Cape Wind began in November 2001 with the U.S. Army Corps of Engineers as the lead federal permitting agency. The 2005 Energy Policy Act transferred jurisdiction of federal regulatory oversight to the Minerals Management Service within the Department of the Interior. The MMS is due to release a Draft Environmental Impact Statement about the Cape Wind project in late November, followed by another round of public hearings. An MMS permitting decision on Cape Wind could come sometime in the second half of next year, with litigation virtually certain to follow any decision of the agency. With seven years of time invested in the licensing battle, it goes to show how hard it is to locate major environmentally-friendly energy producing facilities among the more populous areas of the country.

Canadian Activity Forecasts Call for Dismal 2008

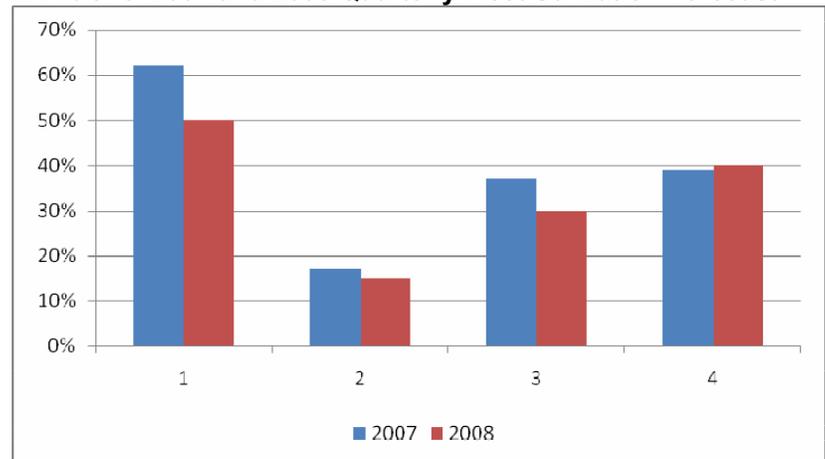
Natural gas revenues account for roughly 70% of Canada's conventional oil and gas receipts

Now that the Alberta royalty review is complete and the new royalty program announced, local oil and gas producers are adjusting their drilling plans for 2008. The continued weak natural gas price environment is expected to continue, which will depress oilfield activity since the Western Canadian Sedimentary Basin is primarily gas prone. Natural gas revenues account for roughly 70% of Canada's conventional oil and gas receipts meaning that the level and trend in gas prices is about the most significant driver for near-term activity. With the uncertainty surrounding the outcome of the royalty review, much of the planning time for this winter's drilling season has been lost, which will further depress next year's activity.

Both the Canadian Association of Oilwell Drilling Contractors (CAODC) and the Petroleum Services Association of Canada (PSAC) have issued revised forecasts for drilling and service activity in 2008. Both forecasts call for a bleak outlook for next year. Importantly, as pointed out by PSAC's president, Roger Soucy, the Canadian oilfield service industry has enjoyed an almost steady upward ten-year trend in activity. As a result, there is a whole generation of younger people working in the industry who have never experienced a significant slowdown. According to Mr. Soucy, "They're going to find out in the next few months just what it means."

CAODC expects an average drilling rig fleet utilization of 34% for 2008

The CAODC expects the current conditions of weak natural gas prices, high operational costs and a very strong Canadian dollar to continue in 2008, significantly impacting activity. The additional disruption from the Alberta royalty review will primarily impact the first quarter activity. Overall, the CAODC expects an average drilling rig fleet utilization of 34% for 2008. As they point out, this is a *sub-economic* [their emphasis] condition, meaning that contractors will be unprofitable.

Exhibit 15. 2007 and 2008 Quarterly Fleet Utilization Forecast

Source: CAODC, PPHB

Industry conditions will only support a 50% fleet utilization rate during the winter period, the traditionally strongest time of the year

Generally contractors need their rigs to achieve 50% utilization on average to cover the cost of operating the fleet for the year. An important ingredient to the CAODC forecast is the assumption that industry conditions will only support a 50% fleet utilization rate during the winter (first quarter) period, the traditionally strongest time of the year. The spring breakup-dominated second quarter will generate only 15% fleet utilization with the third quarter posting a 30% utilization increasing to 40% for the fourth quarter.

PSAC believes there is an even chance that we will not see the 2005 peak in wells drilled (24,000) ever again

The COADC rig forecast generates an estimated 13,735 wells to be drilled in 2008. This represents a 16% decline from the anticipated number of wells to be drilled this year. The CAODC forecast is consistent with the PSAC outlook. PSAC is forecasting 14,500 wells to be drilled, down 17% from its anticipated total for this year of 17,550, which is already down 18% from the trade association's original forecast for 2007. The negative implications of these forecasts were spelled out by the respective associations. PSAC believes there is an even chance that we will not see the 2005 peak in wells drilled (24,000) ever again due to commodity trends and the ongoing challenge of securing the necessary workers to handle that level of activity.

From the 22,298 wells drilled in 2006, by the end of 2008, the drop in activity will be 38%

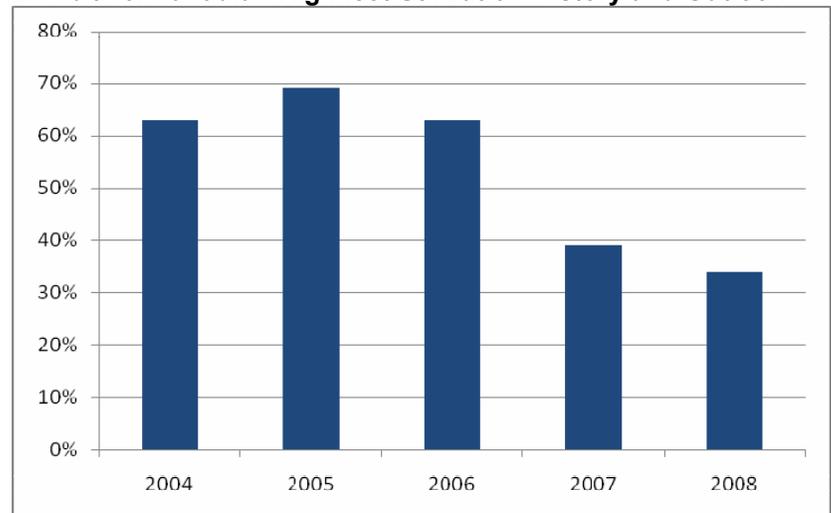
The negativity from CAODC was possibly greater. It pointed out that from the 22,298 wells drilled in 2006, by the end of 2008, the drop in activity will be 38%. After all the years of steadily increasing activity and expanding rig fleets and service industry capacity, the industry is looking at depressed activity and a poor financial outlook. To counter this situation, those oilfield service companies and drilling contractors that can do so will be looking to geographic markets outside of Canada for business opportunities. Already a number of newbuild rigs have been sent south to the United States and plans are for the industry to remove 30 rigs from the existing fleet that will also be sent south. The biggest problem is that Canadian drillers have tended to target the Rocky Mountain region of the U.S. because it is close to Canada making it easier to operate in.

How quickly will Canadian gas production fall forcing up natural gas prices?

Unfortunately, natural gas wellhead prices in the Rockies are well below \$1 per Mcf because of limited gas transportation facilities, which will not support a meaningful expansion in drilling activity.

For the Canadian oilfield service industry, there are two key questions. First is how financially sound are the companies in order to weather this period of inactivity? The second is how quickly will Canadian gas production fall forcing up natural gas prices and restarting drilling activity? We have already heard that there are several small oilfield service companies and drilling contractors who are in financial difficulty. Whether that condition spreads throughout the industry remains to be seen, but the danger is that low activity will be like a cancer that destroys the health of the industry before macro industry conditions strengthen the environment.

Exhibit 16. Canadian Rig Fleet Utilization History and Outlook



Source: CAODC, PPHB

For those newcomers to the industry, they may not be as prepared and will become victims as others have in the past

Both the CAODC and PSAC mentioned in their press releases announcing their revised 2008 activity forecasts that Canadian natural gas production has already begun to fall. Without a substantial amount of new well drilling, it is likely that gas production will continue to fall. Then it only becomes time before falling production encounters rising demand and gas prices begin climbing higher, stimulating future oilfield activity. For those of us who have been involved in the oil and gas business for a long time, we understand that these cycles have occurred in the past and that they are self-correcting. However, forecasting how long it will be before they do correct is extremely difficult, if not impossible. For those newcomers to the industry, they may not be as prepared and will become victims as others have in the past. We sense a lot of Canadian service company people would like to flip their calendar directly to 2009 and skip next year.

Oil Prices Drive Homeowners to Natural Gas Heating

As winter begins to arrive across the United States, the recent jump in crude oil prices has pushed up home heating oil prices that has pushed some homeowners to explore switching from oil-fired to natural gas-fired heating. As the homeowners are discovering, there are a number of considerations involved in making this decision, not the least of which is the cost of the conversion. A very important consideration, however, is whether a homeowner can access natural gas fuel supplies.

There has been a steady, albeit slow, shift toward natural gas-fired heating plants

There has been a steady, albeit slow, shift toward natural gas-fired heating plants. In 1999, about 9% of homes in the United States had oil-fired heating systems, while 53% had natural gas-fired systems and 29% were using electricity. Currently, that mix has shifted to 7% using fuel oil, 58% dependent on natural gas and 30% employing electricity. Oil-fired heating systems are found predominately in the Northeast region of the country, which does not have as much access to natural gas supplies.

A contributing factor in the homeowner's decision to change from heating oil to natural gas to heat the home is the age of the existing heating plant. Older homes tend to have less efficient and cranky heating oil plants that are candidates for a switch to natural gas. Electricity is seldom an option due to the high cost of electricity relative to either heating oil or natural gas. With crude oil prices in the \$90+ per barrel range, consumers with aging oil-fired heating plants are increasingly examining whether it makes sense to convert to natural gas-fired heating systems.

Costs for the conversion will vary depending upon the region of the country and the size of the home,

Assuming that there is natural gas in the area, the cost to switch from oil-fired to gas-fired heating systems can range anywhere from \$4,000-\$5,000 to upwards of \$8,000. The process may take as little as a couple of days to as much as a month if the local gas utility needs to lay a pipeline to get the gas to the house. Costs for the conversion will vary depending upon the region of the country and the size of the home, but the cost of the basic equipment should be in the range of \$4,000. Removing the oil tank, which needs to be done by the trained and licensed people, can cost upwards of \$2,000, additional.

The big advantage of switching from oil to natural gas for heating is that bills for this winter's heating season should increase less. According to the Energy Information Administration, those homeowners relying on heating oil will pay an average of \$319 more this winter than last year, while natural gas customers are projected to pay only \$78 more for heat between October and March.

A consideration in the switching decision is the fuel supplier situation and how competitive the market may be. In the New York region, a heavy heating oil market, there are about 150 heating oil suppliers according to John Maniscalco, a spokesman for the New York

Over the past decade about 35% of the 110,000 new customers came as a result of switches from heating oil to natural gas

Heating Oil Association. In contrast, there may be only one or two natural gas suppliers. Bob Gallo, the marketing director for New Jersey Natural Gas Company, a subsidiary of New Jersey Resources Corp. (NJR-NYSE), pointed out that over the past decade about 35% of the 110,000 new customers for the company came as a result of switches from heating oil to natural gas.

One article we recently read discussing a homeowner's switch in heating systems figured the cost at \$4,400. The house being converted was a three-bedroom ranch-style home located in Little Egg Harbor, New Jersey. The decision to switch was influenced by the fact that the existing boiler needed to be replaced anyway. The natural gas utility was offering a discount promotion that further helped reduce conversion cost. The \$4,400 price tag to switch to natural gas included permitting, new equipment, installation and removal of the oil tank. The entire process took two days. Last winter the homeowner spent \$2,000 to heat his home. He is hoping this winter his heating bill will be less and the savings will help defray part of the cost of the switch.

Al Gore's Worst Nightmare: Europe Turns to Coal

As crude oil prices have climbed to record highs, coal prices have fallen to a historic low relative price. A ton of coal is currently so cheap at about \$47, that European utilities are willing to pay \$50 per ton to ship it across the Atlantic Ocean according to Galbraith's Ltd., a 263-year old London shipbroker. In 1998, the comparable energy content from oil and coal cost about the same, but today WTI crude oil is about five times more expensive.

Coal is by far the cheapest fuel available and that competitive position has stimulated coal consumption

U.S. coal prices are equal to \$1.98 for each million British thermal units of energy, compared with \$12.51 for fuel oil and \$6.91 for natural gas. Coal is by far the cheapest fuel available and that competitive position has stimulated coal consumption. The three largest U.S. coal companies, Peabody Energy Corp. (BTU-NYSE), Consol Energy Inc. (CNX-NYSE) and Arch Coal Inc. (ACI-NYSE) have forecast they will have the largest increase in their exports in 20 years. Coal use worldwide has grown 27% since 2002, three times faster than crude oil use according to BP's (BP-NYSE) statistics. The price for U.S. East Coast coal has risen 71%, while that of crude oil has tripled over the five-year period.

U.S. coal exports to Europe for the first nine months of this year have climbed by 15%

According to the Energy Information Administration, U.S. coal exports to Europe for the first nine months of this year have climbed by 15% to 11.4 million tons. Gianfilippo Mancini, the head of fuel purchasing for Enel SpA (EN-NYSE), Italy's largest power company, which is spending \$5.8 billion to convert oil-powered electric generating plants in the country to run on coal, said, "There is a huge advantage with coal, and this will continue indefinitely."

Global plans call for the construction of 1,000 coal-fired power plants over the next five years with China and India dominating the market.

China, the world's biggest coal producer, became a net importer for the first time this year

China has been opening new coal-fired power plants at the rate of one every five days. China, the world's biggest coal producer, became a net importer for the first time this year, taking coal supplies from Indonesia, Australia and South Africa and reducing the volume of coal available for Europe. With the prospects that the global coal juggernaut is not slowing anytime soon, Al Gore must be very disappointed.

France's Eco-Posturing Confronts Political Reality

The French citizenry, while embracing the goal of protecting the environment, appearing unwilling to pay the cost of all the proposed programs

Recently, France held a two-day national conference with the intent to put the country on the leading edge of global action to protect the environment. There was an extended period of consultation with the public during the weeks leading up to the conference. The net outcome of the conference was a mixed bag with the French citizenry, while embracing the goal of protecting the environment, appearing unwilling to pay the cost of all the proposed programs.

During the consultations, the French citizens were asked a series of questions such as whether they were prepared to accept lower speed limits on motorways and ordinary roads to reduce carbon emissions. They were asked if they were willing to pay more for their food by allowing "bio" or organic farming to take over one fifth of all the fields in the next 13 years? They were also questioned about their willingness to pay up to \$28,000 to better insulate their homes? The consultation effort was conducted using an internet questionnaire and by staging 17 public meetings. At the end of the consultation period, all parties were invited to the two-day conference in Paris.

The plan to impose a "carbon tax" on industry was postponed for "further study"

The outcome of the conference was a pledge to sharply reduce France's carbon "footprint" from road and air transportation and from home heating. There was a promise to increase organic farming to six percent of total land area in five years and to 20% by 2020. However, under pressure from various special interest groups, the conference rejected proposed plans to impose a sharp reduction in France's use of pesticides in its agricultural industry. Plans had called for cutting their use by 50% within 10 years, but instead the conference agreed to a largely meaningless statement promising to cut pesticide use by 50%, but it did not specify a date, other than to state when "alternatives" were available. The plan to impose a "carbon tax" on industry was postponed for "further study." Also, plans to reduce speed limits on highways were rejected.

The conference promised a shift in moving goods from road transportation in favor of railways and canals

One of the major policy initiatives that came from the conference was a government commitment to freeze investment in new airports and motorways and shift spending towards rail and canal transport. The conference agreed to a new tax on trucks operating on non-motorways and promised a shift in moving goods from road transportation in favor of railways and canals, including the construction of 3,000 miles of high-speed railways over the next 23 years. However, about the same time the conference was

establishing this policy, the French state railway, the SNCF, announced a winding down of part of its freight operations. The SNCF is planning to shut down access to 262 railway goods yards in western and southern France to single trucks. In other words, the railway system will only accept entire trainloads of goods such as cereals or oil or new cars or steel bars or coal, instead of single railcar loads of goods. SNCF has determined that railways are better suited to carrying bulk goods to single destinations and not dealing with multiple small loads moving from and to multiple locations. This decision instead will force those single truck loads to move by road that will increase the amount of traffic on roads and further add to the country's carbon "footprint."

French President Nicolas Sarkozy declared a French "green" revolution that will cut the nation's energy consumption and carbon emissions

French President Nicolas Sarkozy, speaking at the conference, declared a French "green" revolution that will cut the nation's energy consumption and carbon emissions, but achieving these goals may prove significantly more difficult than believed. Saying it and doing it are two different things. As they say on the streets, if you talk the talk, can you walk the walk? In the energy and environmental arenas, walking the walk still needs to be demonstrated.

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