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Petroleum Week

Week #37: 12-16 September 2011

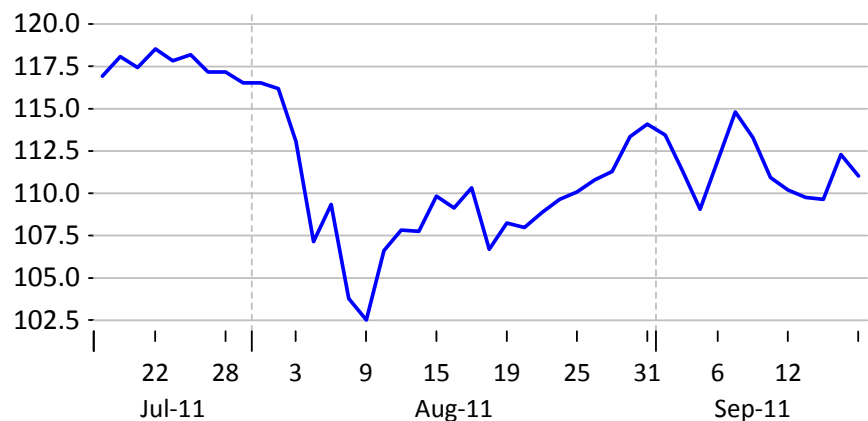
Short-term review

Oil rally stumbles on doubts over economy

Short-term forecast for Brent (second-position): \$110-\$114/barrel

A brief rally in European petroleum markets stumbled in the week ending Friday 16 September, as markets remain doubtful about the strength of the next economic upturn. The benchmark ICE Brent second position (now moving to December, expiring 15 November) finished the week at \$111.02/barrel, after closing at \$112.30/barrel on Thursday. The week-on-week performance was less impressive, with the average closing value for the second-position contract across the five sessions slipping back to \$110.58/barrel, compared with \$112/barrel for the previous week. These closing values validated our forecast last week for prices to move between \$108-\$115/barrel with increased volatility. As trading volumes for the December contract gained momentum, intraday price movements became more obvious. We had forecast price swings of \$5/barrel, which was borne out by Thursday's high-low trading range of \$4.56/barrel. But in the current phase of economic recovery, oil prices remain brittle and price rises will be difficult to sustain until there is a batch of unqualified good news. While that is certainly not going to happen in the week ahead – which will be dominated once again by the unfolding drama in the eurozone and the apparent inability of European banks to control their traders – we still expect prices to edge higher, but to bed down around \$110-\$114/barrel.

Brent 2nd position settlement, ICE Futures, \$/barrel



Source: VM Group

The week in detail

Gasoil

Prices in the European gasoil market ebbed and flowed last week as selling pressure hit crude oil on Friday. The October ICE gasoil contract, which now moves to the front of the queue, hit a midweek low of \$922/tonne but rebounded to \$952.50/tonne on Thursday before closing off the week at \$950.50/tonne. Even though the contract posted a notional rise for the week, the average closing price for the five sessions for the front month contract was \$937.80/tonne compared with \$949.30/tonne in the previous week.

In the physical market, gasoil discounts were steadily whittled away across the five sessions. On Monday, when Vitol and Shell sold five barges to Gulf, Gunvor, North Sea Group and Morgan Stanley, discounts to the October gasoil contract were pitched at \$3/tonne but by Friday, when Shell and North Sea Group sold two barges to Vitol and Fina, discounts had fallen to \$1.50/tonne as the price of Brent began to sag. At this point, the October-November backwardation, which had been \$2/tonne on Tuesday after the expiry of the September contract, widened to finish the week at \$4.50/tonne. Traders have been hoping to see demand from the German heating oil sector, which traditionally begins to replenish stocks at this time of year, but the Germans have yet to blink, preferring to buy on an ad hoc basis.

Gasoline

Another busy week in the European gasoline market saw 65,000 tonnes of benchmark Eurobob change hands, with a sizeable chunk of that transacted on Friday when 14 barges were sold. The increased buying (coming mainly from Trafigura, Gunvor, Cargill and Morgan Stanley) boosted prices from a Monday level of just over \$1,00/tonne fob ARA to as high as \$1,040/tonne by Friday morning before dropping back to \$1,024/tonne in the afternoon as crude oil prices softened.

In the premium unleaded sector prices were pushed higher, with about 20,000 tonnes of fuel changing hands across the five sessions. Trafigura, which was on both sides of deals during the week, finished Friday as a seller when it sold a barge to Total at \$1,041/tonne.

Gasoline inventories held in independent storage in the ARA complex were further chipped away by 21,000 tonnes to 514,000 tonnes, the lowest level since last December, as stocks were pushed towards Germany where work on the

MiRo refinery cracker in Karlsruhe is expected to finish in the coming week. Strong demand continues from Libya as local oil company Agoco tendered for 90,000 tonnes of gasoline for early October delivery, while Kenya emerged again as a steady buyer. In the US, the Energy Information Administration revealed during its weekly audit that gasoline inventories rose by 1.7m barrels compared with analysts' forecasts of a stockbuild of just 700,000 barrels. The bloated inventories reflect a poor US summer driving season and continued concern over the state of the economy.

Jet fuel

Jet fuel trading evaporated by Friday having seen a busy three-session phase in the early part of the week. Six barges changed hands on Monday at a \$66-\$67/tonne fob ARA premium over October gasoil prices with Morgan Stanley and Vitol buying the lot. Morgan then went on to sell a cargo to BP at a \$70/tonne premium and remained a prominent buyer for the rest of the week. BP dominated selling on Tuesday, offloading four of the five barges sold as differentials dipped to \$65/tonne. With the European summer flying season drawing to a close, jet fuel premiums continue to lose ground, as KLM disposed of two barges at a week-low premium of \$64/tonne fob. But even at these levels, the market is well supplied. While the price of crude oil may have jumped 25% in the past year, jet fuel premiums are now more than 50% higher than last September, when jet fuel cargoes changed hands at premiums of just \$40 cif NWE. Jet fuel inventories held in ARA lost a further 51,000 tonnes to 522,000 tonnes despite the arrival of a cargo from Korea.

Diesel

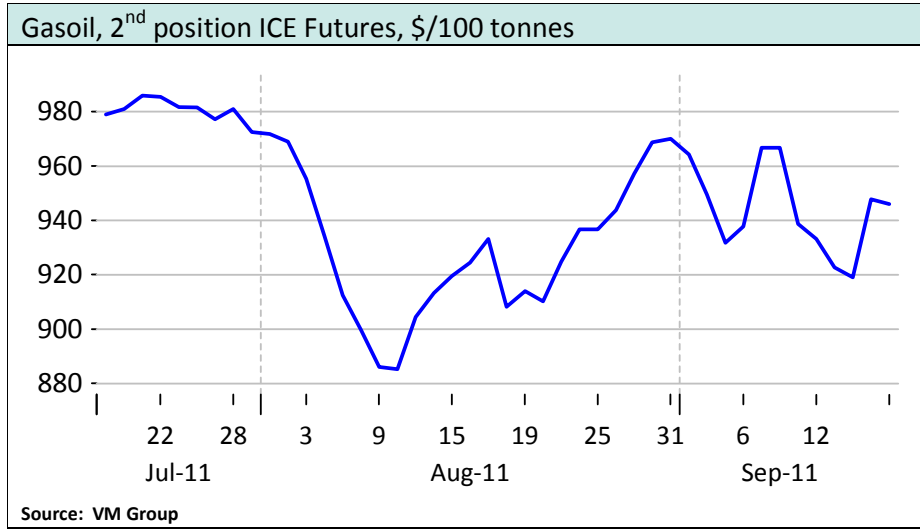
Trading in the diesel market built up a head of steam last week with 26 barges changing hands, half of which were sold on Thursday when BP bought 11 of the 13 barges traded. Premiums peaked at \$23-\$24/tonne fob ARA over ICE October gasoil futures on Wednesday and slipped back by \$2/tonne the following day. Prices in the European diesel sector are expected to flatten in the next month as a fleet of US cargoes is expected to arrive, with up to 500,000 tonnes of product which cannot find a ready buyer in the US.

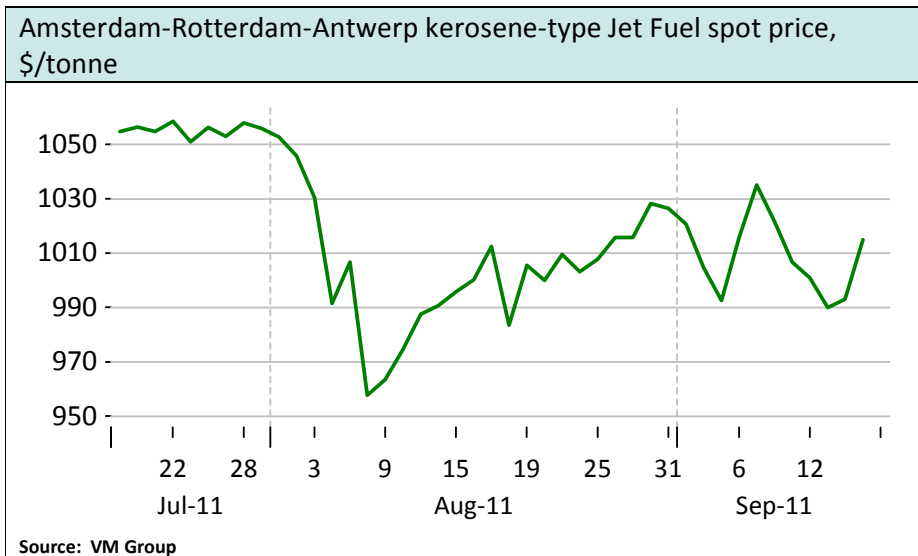
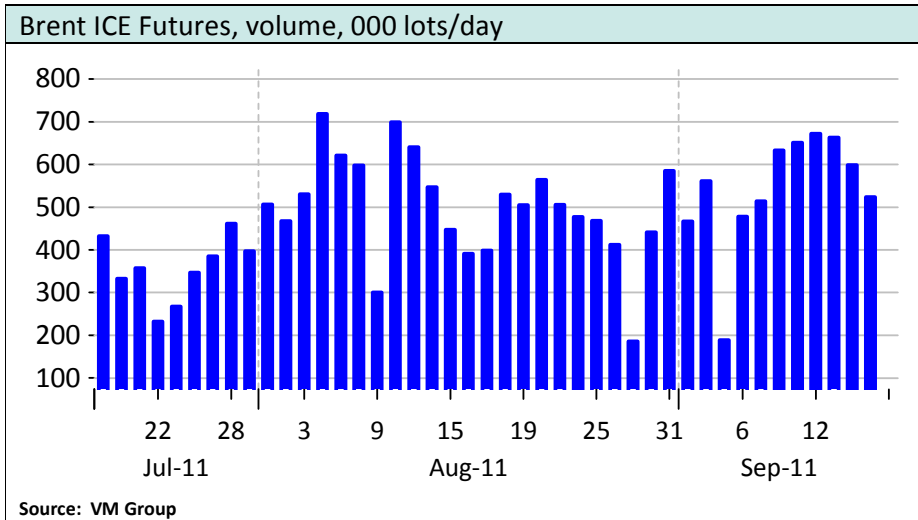
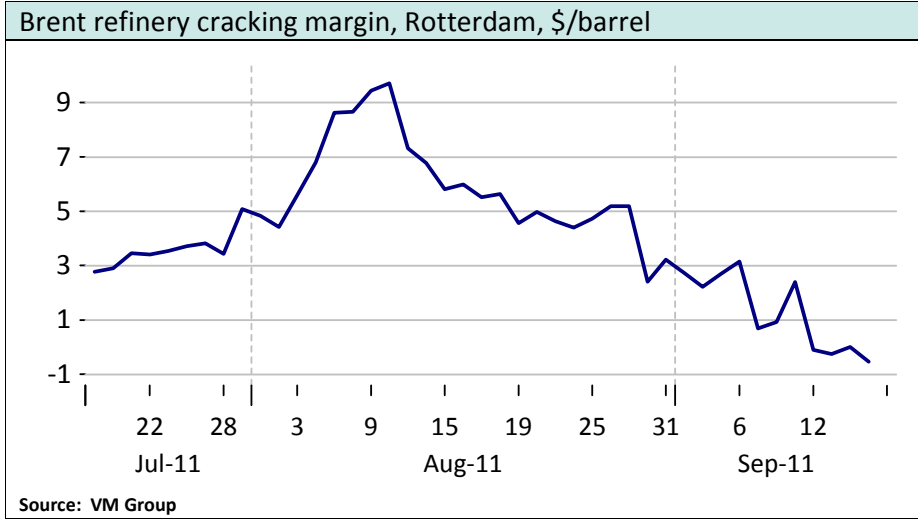
Elsewhere, in the fuel oil market, prices hit a high on Thursday as low sulphur barges traded at \$659/tonne fob ARA but then slipped back to \$648/tonne the following day to finish the five trading sessions slightly higher. High sulphur barges fared better adding \$10/tonne to close off the week at \$636/tonne.

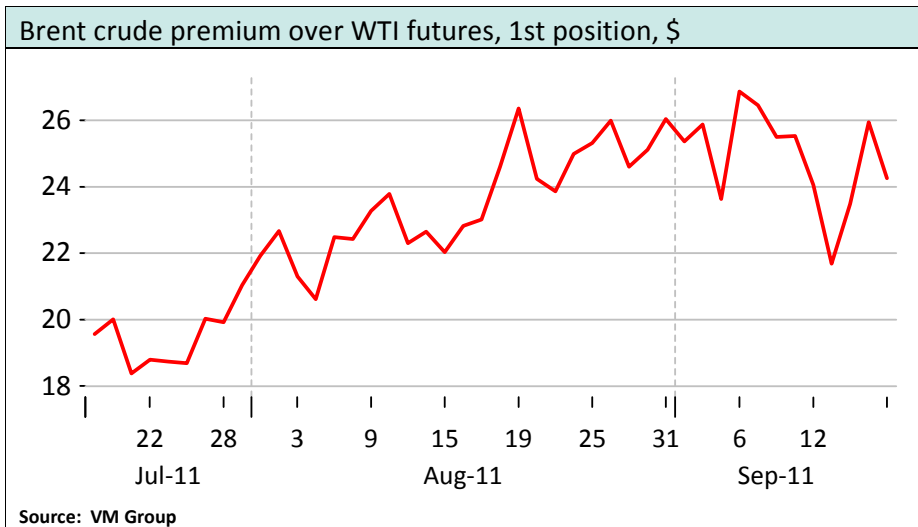
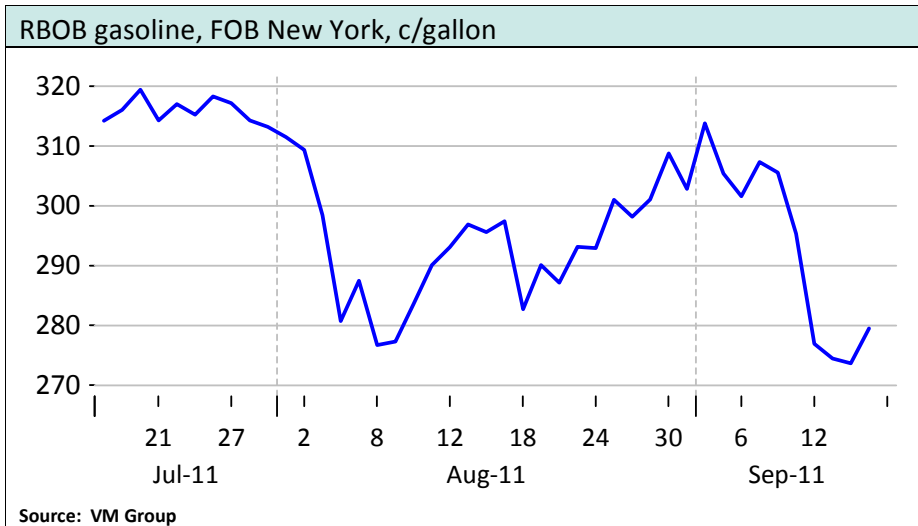
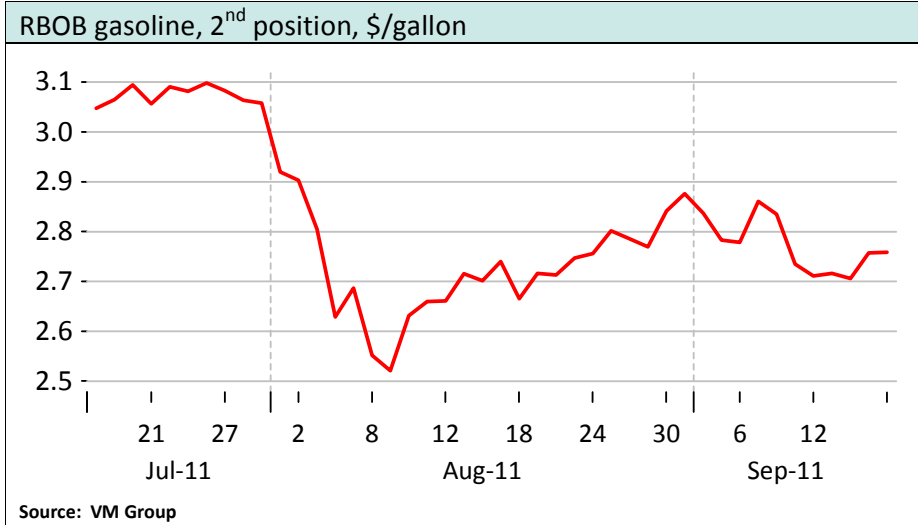
Outlook

When it comes to handing out lessons on fiscal rectitude, US Treasury Secretary Tim Geithner is hardly the ideal after-dinner speaker, but last week he admonished European Union leaders for their inability to grasp the nettle and solve the eurozone crisis before it caused irreparable harm. The message may have been sound, but the messenger failed to inspire confidence. While the Europeans may long for a local equivalent of the US Federal Reserve, they have to live with the shaky structure they created little more than a decade ago. Having been promised a currency that would pave the way for economic growth, European leaders are now faced with a destabilised, and increasingly expensive, future. Despite what some critics of the eurozone claim, the currency is not a rickety 17-story building that safety inspectors can demolish and tell the architects to try again. It is more akin to a car crash victim on an operating table, where surgeons do not have the time nor the moral leeway to pull the plug and start over. Instead, they must keep the patient alive at all costs and if one form of treatment does not work, they must move onto a different strategy.

But as Geithner suggested last week, time really is running out. While Germany implicitly acknowledges that the eurozone is too important to fail, the half measures that have been taken to restore it to health have failed miserably. There will come a point quite soon when the fiscal (and surgical) advice can no longer be ignored. Until then, economic recovery will be anaemic and oil prices will remain subdued at their current levels.







BRENT TECHNICAL ANALYSIS

Close of Business: 16-Sep-11

BASIS : Nov 2011 With the CRB index already losing precious altitude due to the Dollar's resurgence, the fate of this core component stands to be of paramount importance to a wide swath of commodities. And things were looking increasingly suspicious as this week ended. Admittedly, the market survived some rattling of the 109's area but the resulting boost faded shy of the overall spot channel ceiling (117.2) and Nov taking front

runner status gives that key feature more room to breathe. Either Brent must summon a determined blast into the 117's to inject new resolve into the interim rally or else a head and shoulders structure is threatening to evolve from action in recent weeks. Duly watching the 109.8 to 108.5 spot/Nov defenses as a twist back across the entirety would signal a crest and the prospect of a new downswing into double digits.

DAILY TECHNICAL INDICATORS

SUPPORT = 109.8/108.5, 105, 99, 96.2 (CHAN), 94.
RESISTANCE = 115.5, 117.2 (CHAN), 120.

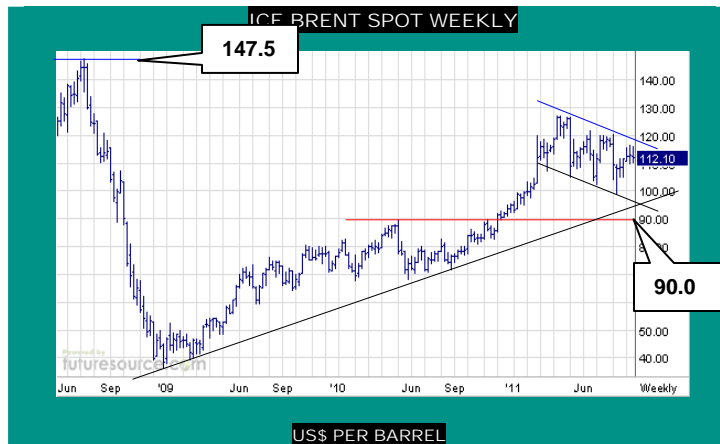
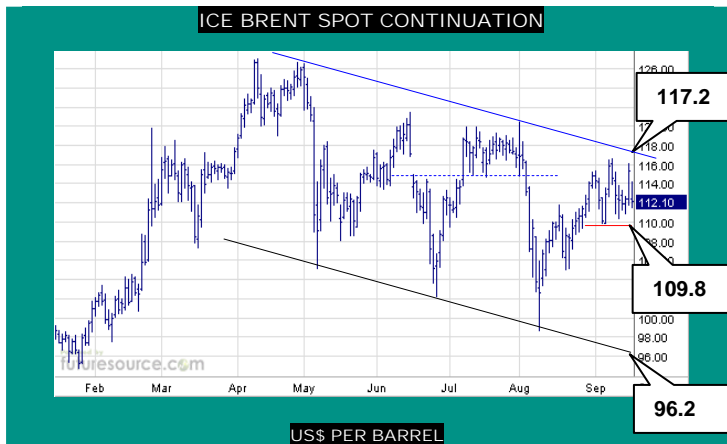
BOLLINGER BANDS

UPPER = 114.93
MID 20 DAY AV = 111.25
LOWER = 107.57

14 DAY RSI = 52 14 DAY ADX = 14

14 DAY STOCHASTICS
%K = 44
%D = 33

OPEN INTEREST = 870,656



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