THE SCHORK REPORT
A VIEW OF THE ENERGY & SHIPPING MARKETS

Tuesday, February 08, 2011
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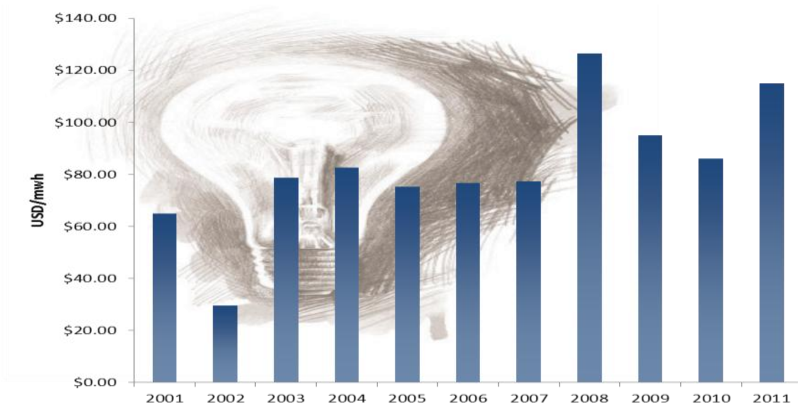
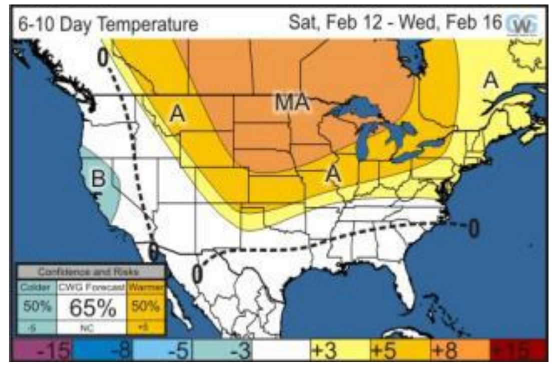


January Highest Daily On Peak PJM West Spot Price

Weather forecast courtesy of
Commodity Weather Group



CRUDE AWAKENINGS

TRADING BIAS DAILY

- 😐 **WTI: NEUTRAL a/o Feb 07 ...S- 85.85 R- 89.11**
- 😐 **BRN: NEUTRAL a/o Feb 07 ...S- 98.22 R- 100.28**
- ☹ **NG: BEARISH a/o Jan 21 ...S- 4.004 R- 4.204**
- 😐 **RB: NEUTRAL a/o Feb 07 ...S- 240.34 R- 249.76**
- 😐 **HO: NEUTRAL a/o Feb 07 ...S- 267.15 R- 274.07**

TRADING BIAS WEEKLY

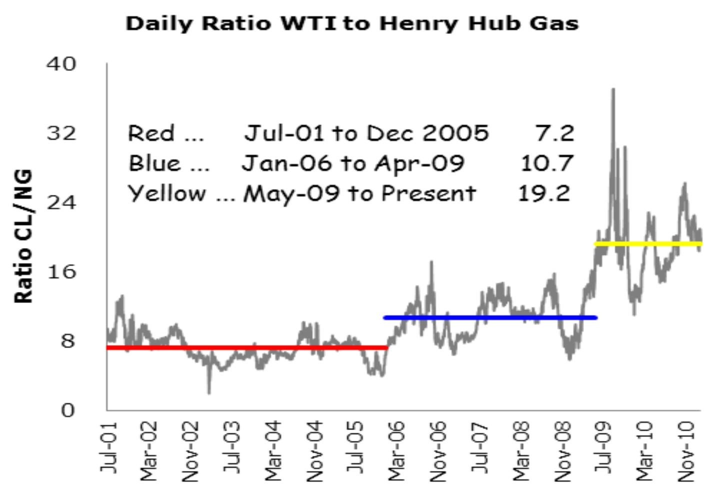
- ☺ **WTI: BULLISH a/o Nov 08 ...S- 86.18 R- 91.88**
- ☺ **BRN: BULLISH a/o Sep 12 ...S- 97.06 R- 102.6**
- 😐 **NG: NEUTRAL a/o Nov 08 ...S- 4.078 R- 4.542**
- ☺ **RB: BULLISH a/o Dec 06 ...S- 237.24 R- 249.82**
- ☺ **HO: BULLISH a/o Jan 10 ...S- 262.92 R- 280.42**

TRADING BIAS MONTHLY

- ☺ **WTI: BULLISH a/o Oct 2010 ...S- 72.84 R- 95.65**
- ☺ **BRN: BULLISH a/o Oct 2010 ...S- 82.63 R- 96.24**
- ☹ **NG: BEARISH a/o Oct 2010 ...S- 2.041 R- 4.549**
- ☺ **RB: BULLISH a/o Oct 2010 ...S- 212.68 R- 256.76**
- ☺ **HO: BULLISH a/o Oct 2010 ...S- 216.79 R- 248.12**

ENERGY PRICES WERE WEAK YESTERDAY…. some sense of normalcy is returning to Egypt and that means the Suez Canal is (supposedly) safe and OPEC will not (supposedly) increase output to preempt supply disruptions. Thus liquids markets on both sides of the market were lower for the most part. Meanwhile natural gas sold off hard despite forecasts of a cold winter and warm summer.

Figuring the new normal
(See omnium-gatherum below)



Omnium-Gatherum

Through the first half of the 2000s the relationship between crude oil (spot WTI) and natural gas (spot Henry Hub) averaged ≈7.2 ±.05. That is to say, the price of crude oil in $/bbl averaged more than 7× that of natural gas in $/MMBtu. For those of you who recall, despite 9/11, wars in Afghanistan and Iraq, a major strike in Venezuela and the 2005 hurricane season, crude oil prices were relatively stable during that timeframe. Spot WTI averaged $37.09 a barrel from July 2001 to December 2005, whereas natural gas averaged $5.54 per MMBtu or ≈$32.13 BOE. Furthermore, the correlation between oil and gas was solid; intuitively, 72% of the change in gas could be explained by the movement in oil.

(Continued p.5)

Electricity and Natural Gas Prices

Shocking news for the bears

In yesterday's report we stated that during last week's trading "the bulls failed to hit [natty front month's 50 day moving average of 4.373] on Friday which could lead to a technical sell-off this week." Yet we were still surprised to see the severity of yesterday's ~5.00% drop to 4.104.

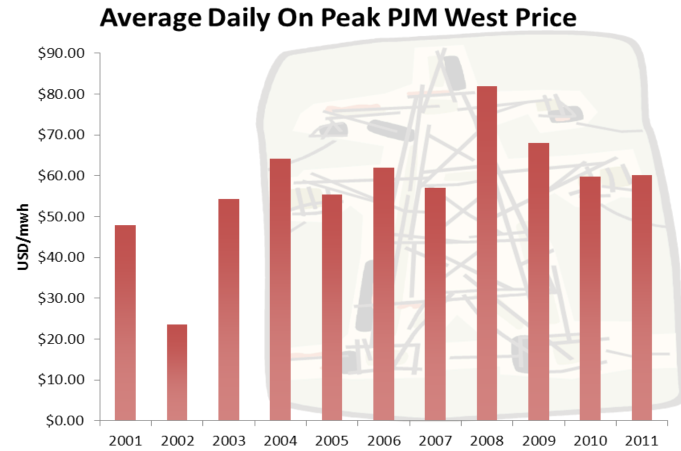
Support came in around the 100 day MA of 4.093 and prices could not get lower than 4.101. We are trading around technical levels, but is there a fundamental reason for the weakness? Yesterday Commodity Weather Group came out with its intermediate seasonal outlook update, in advance of the more extensive outlook report at the end of the month.

The intermediate picture looks bullish in the short and long term. March 2011 is expected to be 21% colder than 2010, which would place heating degree days in 2011 13.44% above the 2005-09 average. Further out, summer is expected to trend hotter on the East Coast, though not quite as hot as last year. In the south, the hurricane season is expected to be busy and start early. So why the sell-off?

Consider that in October 2010 (the latest data available) natural gas as a source accounted for 24.96% of total electricity generation in the U.S. This is up from 23.64% in October 2009, 21.57% in 2007 and 13.73% in 1997. At the same time, total electricity generation has been trending higher, with 2009 standing 2.9% above the historical average. Needless to say, the electricity markets are a large and increasingly larger factor for natural gas prices.

Yet we are not seeing cold weather in winter and warm weather forecasts for summer being priced in to electricity prices consistently. Sure, on peak spot prices at the PJM West spiked to $115.00/mwh on January 21st, well above January 2010's highest price of $86.06/mwh as snowstorms battered the coast. In fact, as shown by the chart on p.1, it was the second highest value seen for January in the past decade, topped only by $126.50 in 2008 in the run up to the commodity bubble.

Yet this single day is skewing the rest of the month, if we exclude it and take average electricity prices at PJM West, the chart is much different, as shown below. The average electricity price in January 2011 came to $60.15, just 0.64% above January 2010's average. From a historical perspective, prices are no longer the second highest, but the fifth highest, below 2008, 2009 and even 2004.



In turn, electricity output in the Mid-Atlantic region in 2011 was strong for certain weeks, but the January average stood just 2.72% higher YoY and 5.12% above the 2005-09 timestep. The lack of sustained high prices and electricity output comes despite January's heating degree days in in the Mid-Atlantic standing 12.13% above 2010 and 19.59% above the 2005-09 timestep.

Contrarian traders may state that while natural gas is used somewhat to fuel electric heaters in the Mid-Atlantic, it is far more prevalent in the summer months when it is used to satisfy air conditioning demand. Yet the picture further out is no less troubling.

Keep in mind that electricity spot and forward prices do not have the same relationship as crude oil (or gold or cocoa) prices. The latter commodities can be bought today, transported, stored, insured and then sold off in the future. Thus for crude oil the price differential between spot and forwards incorporates not only future supply/demand but also the "cost of carry". In contrast, electricity must always be moving, generated and consumed at the same time. Electricity cannot be bought at today's prices and stored for sale at a later date. Thus there is no cost of carry, and forward prices are a more 'pure' measure of supply/demand.

Electricity futures for July 2011 are not the most liquid contracts on the market, but current On Peak PJM Interconnect futures prices come to $59.59/mwh, suggesting that the supply/demand ratio will not be much better in summer than it is today. Of course we will see inter-day spikes (as we saw in January) but traders do not seem concerned about generation shortages in advance.

The bottom line is that natural gas is locked in a bear market, and while we will fade spikes in either direction for technical trades, we are maintaining our bearish daily and monthly biases.

NATURAL GAS

NAT-GAS H Open 4.260 High 4.274 Low 4.101 Close 4.104 Chng -0.206

Natural gas prices crashed below our 4.216 inflection low and our 4.121 intra-day low to crater at 4.101, close to the 100 day MA of 4.093. Traders seem to be concerned about lack of demand, as the front month spread weakened for the third consecutive session to -0.33 as of writing. Surprisingly, weather forecasts were mild, and we are hearing reports that an Arkansan official is looking to raise the state's severance tax on natural gas (think shale drilling) from $54 mn to $250 mn. If the measure passes and other legislators follow suit we could see a recovery in natural gas prices, but that is a very big if.

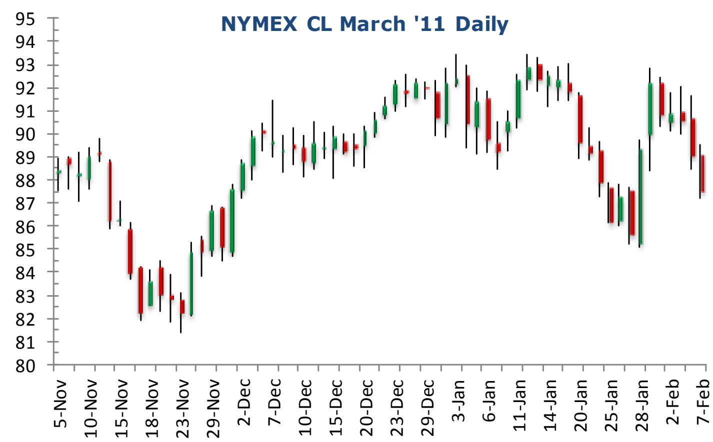
Daily Bias: BEARISH

As for today, strength above yesterday's 38.2% retrace of 4.167 opens the door to our 4.204 inflection high. Above here the bulls will potentially run towards our 4.303 intra-day. Then again, weakness below 12/27's 4.064 low print leads to our 4.004 inflection low. Below here we look for offers to hit support at our 3.905 intra-day.

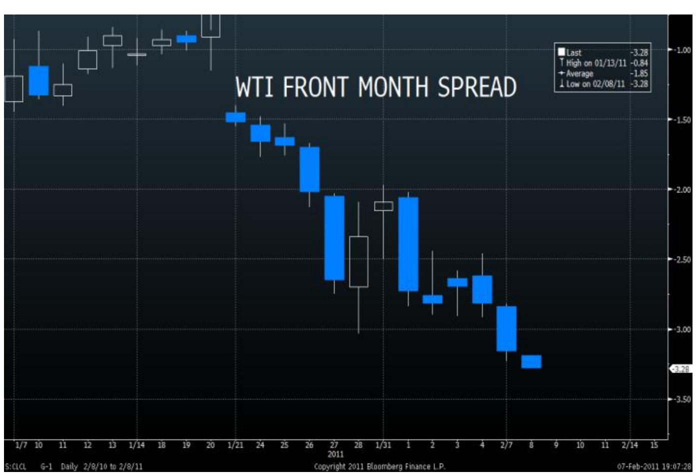
OIL

WTI H Open 89.06 High 89.54 Low 87.18 Close 87.48 Chng -1.55

WTI extended Friday's losses to drop 1.74% yesterday. Prices broke below our 87.40 inflection low before finding support at 87.18, close to the contract for March delivery's 100 day MA of 87.00. Traders were partly selling off any positions taken on the back of turmoil in Egypt, but there seems to be more than that. The front month spread fell sharply and now stands at -$3.28, its widest point since June 2009. Meanwhile the 321 crack rallied to 19.109, it seems very few are willing to hold WTI right now.



Daily Bias: NEUTRAL



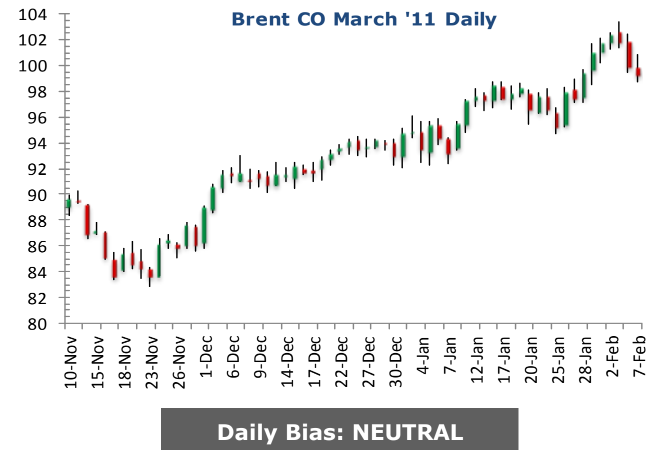
As far as today goes, weakness below March's 100 day MA of 86.99 alerts to our 85.85 inflection low. Below here we will look towards our 84.21 intra-day. On the other hand, gains above yesterday's 61.8% retrace of 88.64 clear a path to our 89.11 inflection high. Through here the bulls could run to (and in to resistance at) our 90.75 intra-day high.

ICE Brent

Brent H Open 99.83 High 100.90 Low 98.77 Close 99.25 Chng -0.58

Brent sold off with the rest of the complex yesterday but its gains were muted – just 0.58% lower on the day as compared to WTI's 1.74% drop despite disappointing factory orders data out of Germany. The inter-market WTI/Brent spread also weakened to -$11.85 as of writing but seems to be finding support around the -$12.00 mark.

As far as today goes, strength above yesterday's 50.0% retrace of 99.84 opens the door to our 100.28 inflection point. If crossed we will look for bids to our 101.30 intra-day. On the other hand, a drop below yesterday's 98.77 low print alerts momentum to our 98.22 inflection low. Below here we will look for offers towards our 97.20 intra-day.

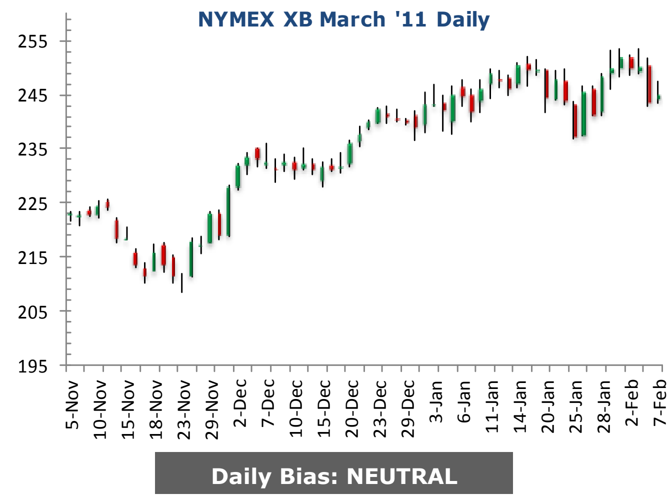


LIGHT ENDS

RBOB H Open 244.15 High 247.45 Low 243.53 Close 245.05 Chng +1.52

RBOB decoupled from the rest of the NYMEX liquids to rise 0.62% yesterday, though the bulls peaked at 247.45, well off our 248.20 inflection high. Keep in mind that the RBOB crack sold off sharply on Friday so this could be an arb correction. The front month spread for RBOB rose to -13.26 as of writing suggesting that, again, traders may have oversold Friday's disappointing jobs report.

As far as today goes, weakness below yesterday's 243.53 low print alerts to our 240.34 inflection low. Below here we look to our 235.63 intra-day. On the other hand, a rebound above yesterday's 247.45 high print opens the door to our 249.76 upper inflection point. Above here the bulls should bid towards our 254.47 intra-day high.

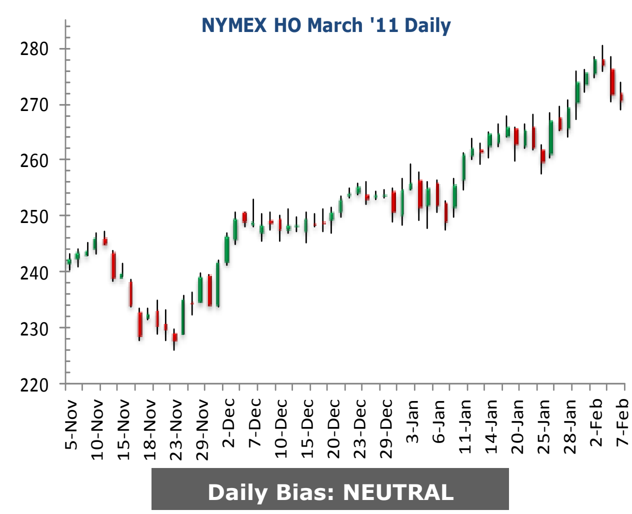


MIDDLE DISTILLATES

HEATING OIL H Open 271.89 High 273.89 Low 269.10 Close 270.61 Chng -1.06

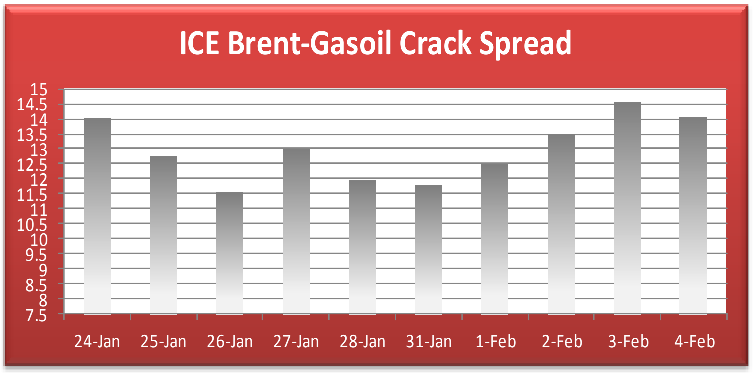
Strength in the ICE gasoil contract could not support NYMEX heating oil, which fell 0.39% yesterday. The bears hit resistance at 269.10, below Friday's 270.48 low print but safely above our 268.20 inflection low. Heating oil was also firm compared to WTI, and the crack widened to an intra-day high of 26.446.

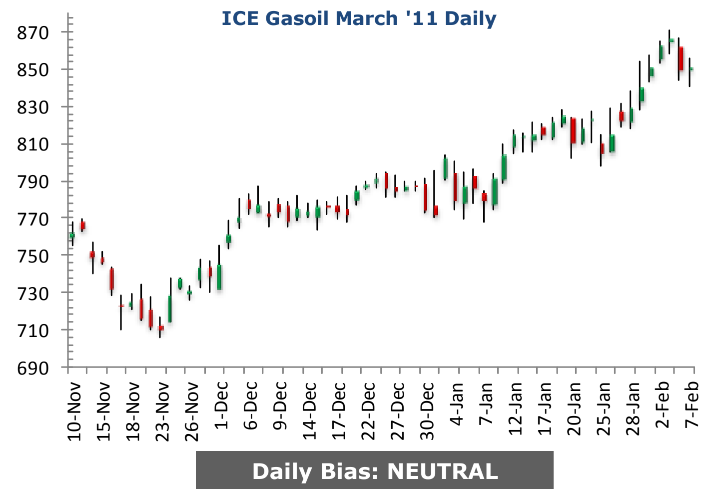
As far as today goes, strength above yesterday's 271.50 pivot high builds a bridge to our 274.07 upper inflection point. Once crossed, the bulls should run towards our 277.54 intra-day high. Then again, weakness below yesterday's 269.10 low print signals momentum to our 267.15 inflection low. Below here we will look for offers down to our 263.68 intra-day low.



ICE GASOIL

Gasoil for March rose 0.24% yesterday but more importantly the gasoil crack rose to fresh two year highs of 14.978. What's interesting is that the last time we saw similar values was 2009, when the crack fell between January and March, whereas this year it is rocketing higher.





As for today, offers through yesterday's 38.2% retrace of 846.88 alert to follow through momentum towards our 840.50 inflection. We will look for weakness below here towards our 829.75 intra-day. On the other hand, continued strength through yesterday's 856.00 high print clears a path towards our 861.50 upper inflection-point. Above here we will look for bids towards our 872.25 intra-day.

OMNIUM-GATHERUM

(Continued from p.1)

All the action back then was in the natural gas market. That was because the industry was assured by one consulting firm after another (from Wall Street to Houston to Calgary) of the coming maturation of North American gas supplies. Since shale drilling was thought to be uneconomical at the time, firms were encouraged to shift their focus to LNG. Therefore, for every 13 rigs employed in the U.S., 11 were gas. In Canada, for every 11 rigs on site, 8 were gas.

Yet, a funny thing happened on the way to the depletion of North American gas resources, i.e. economics got in the way. In other words, high prices were the cure for high prices. In the fourth quarter of 2005 (the quarter following the damage wrought by hurricanes Katrina and Rita), natural gas was trading at around $71.47 BOE against a crude oil market worth only $59.97.

Given these numbers, the shift towards gas, both LNG and– *newly re-discovered* – shale gas, was on. Thus, at its height in the first half of 2006, for every 15 rigs employed in Canada and the Lower 48 U.S., 13 were gas. Meanwhile, in between 2006 and 2007 LNG imports ballooned by one-third to 771 Bcf.

At that point something had to give… and that *something* was the historical relationship between crude oil and natural gas. Thus in between 2006 and the first half of 2009 (the start of the energy bubble to its implosion) the ratio between crude oil to gas jumped to ≈10.7 ±.08 as the irrationally exuberant rally in oil outpaced gas; spot WTI averaged $75.60 a barrel while gas came in at $7.14 per MMBtu ($41.42 BOE).

Since the second half of 2009 the oil markets have bounced back, but gas remains in a protracted bear market. The ratio between oil to gas has since averaged ≈19.2 ±.18 (oil at $77.20 a barrel and gas at $4.163 per MMBtu or $24.15 BOE). More importantly, the relationship between oil and gas has decoupled. For instance, since Baker Hughes rig counts bottomed in spring 2009, only 7% of the move in gas can be explained by oil's price path.

Bottom line, gas is cheap and oil is dear… and as long as shale drillers do not poison some municipality's drinking supply, it will remain that way for quite some time.

BIOFUELS

Monday, February 07th, 2011 - According to the DOE report for the week ended January 28th, discretionary gasoline blending (conventional + ethanol) increased for a third straight week. Output rose 0.8% to 4.68 MMbbl/d. Over the last four weeks discretionary blending averaged ≈4.57 MMbbl/d or 17% above the corresponding timestep from a year ago. Reformulated gasoline production with ethanol fell by 0.8% to 2.93 MMbbl/d. Consequently, discretionary blends' share of the entire gasoline pool jumped by 150 bps to 53.4% and averaged around 51.9% over the last four weeks.

Ethanol production fell by 1½% to 0.908 MMbbl/d. Over the last four weeks output averaged ≈0.907 MMbbl/d or 1% below the prior four-week timestep. Meanwhile, apparent demand for gasoline dropped by a relatively heavy 1% on poor weather-related road conditions, but nationwide stockpiles of ethanol fell by 0.8% from a five-month high to 18.9 MMbbls.

Meanwhile, ethanol values were generally stronger last week, but gross distillation margins are fading fast. Ethanol futures for March delivery in Chicago (CBOT) averaged around 2.37, a gain of 2% from the previous trading week and finished the week up 4.3% from the previous Friday. The rise however failed to keep pace with corn. As a result, the CBOT futures crush for March fell to negative $0.038 per bushel! Furthermore, the average weekly crush between prompt f.o.b. ethanol in Chicago and the bid for №2 yellow corn in Chicago plunged by three-eighths to $0.203 per bushel of corn.

As far as the Ag markets go, corn futures in Chicago moved once again to the psyche-critical $7 threshold. As far as this week goes, offers through 687.50 clear a path towards $7 and our 702.00 weekly inflection-point. We will look for strength above here towards our 740.00 weekly top. On the other hand, offers through 669.50 alert to further corrective weakness towards our 655.75 lower inflection-point. Below here we will look for offers towards our 622.25 weekly bottom.

Finally, bullish momentum spot (March) sugar futures in New York stalled 6 ticks ($62.2 per contract) from our 36.14 weekly inflection-point. As far as this week goes, offers through 33.12 alert to follow through weakness towards our 31.87 weekly inflection-point. We will look for weakness below here towards our 28.85 weekly bottom. Otherwise, a rebound through 34.78 clears a path towards our 36.14 upper inflection-point. Above here we will look for bids towards our 39.93 weekly top.

WEEKLY OUTLOOK (February 07th to 11th)

Henry Hub... weakness below the week ending 01/28's 4.252 low print alerts to our 4.078 inflection low. Below here we will look for offers to our 3.845 intra-week. On the other hand, a rebound above last week's 4.496 high print opens the door to our 4.542 inflection high. Once crossed, the bulls should run towards our 4.775 intra-week high. **WTI...** strength above last week's 90.62 pivot high should send the bulls towards our 91.88 inflection high. Above here they will likely hit resistance at our 94.73 intra-week high. On the other hand, a correction below last week's 88.40 low print leads to our 86.18 inflection low. Below here we look for offers to our 83.33 intra-week. **Brent...** strength above the week ending 01/31's 101.73 high print opens the door to our 102.60 inflection high. Above here the bulls will run to (and in to resistance at) our 105.37 intra-week high. On the other hand, a drop below the week ending 01/31's 98.50 low print alerts to our 97.06 inflection low. Below here the floor falls through to our 94.29 intra-week low. **RBOB...** strength above last week's 246.62 pivot point clears the path to our 249.82 inflection high. If the bulls break through here they could hit resistance around our 256.10 intra-week high. On the other hand, a correction below the week ending 01/21's 239.75 low print alerts to our 237.24 inflection low. Below here we look for offers to our 230.96 intra-week low. **Heating Oil...** strength above our 150.0% March extension of 277.79 opens the door to our 280.42 inflection high. Above here we look for bids to our 289.18 intra-week. Then again, a correction past last week's 266.90 low print alerts to our 262.92 inflection point. Below here the bears should claw to our 254.16 intra-week low.

SCORECARD

BUY NATURAL GAS

- Producers concerned about supplying at current price levels
- U.S. manufacturing improving, pushing up demand for electricity.
- Policy in Washington (if T. Boones gets his way) will steer demand growth disproportionally towards gas.

SELL NATURAL GAS

- Production rebound (per EIA-14 Survey).
- Spare capacity (nonconventional deferred production).
- Winter snowstorms milder than expectations.
- Residential natural gas use locked in to a downward trend since 2006.
- Shale plays have fundamentally altered the amount of domestic supply available – leading to large weekly injections.

BUY OIL

- Bulls have shown their ability to maintain prices above 80.00 in the short term.
- Strong distillate demand from freight and manufacturing sectors.
- U.S. recession officially over in June 2009.

SELL OIL

- Traders are looking for less volatile, safer assets such as bonds.
- Bulls have a tendency to disappear as prices approach the 90.00 psychological barrier.

CRUDE OIL	BULL	BEAR	NA	NAT-GAS	BULL	BEAR	NA
API		☒		EIA	☒		
DOE		☒		Weather	☒		
PAD 1 & 2		☒		Fuel Switching	☒		
Imports			☒	Rig Count	☒		
Production		☒		Imports - LNG		☒	
NYMEX Cracks		☒		Imports - Canada		☒	
OPEC		☒		Exports - Mexico			☒
ARB into USAC		☒		Nuclear Capacity		☒	
ARB into USGC		☒		Hydro Capacity		☒	
Transportation			☒	Transportation		☒	
Momentum			☒	Momentum			☒
Economy			☒	Economy			☒
Interest Rates	☒			Interest Rates	☒		
Outages	☒			Outages		☒	
Season	☒			Season	☒		
Market Sentiment			☒	Market Sentiment		☒	
COT			☒	COT			☒
Total	**3**	**8**	**6**		**6**	**7**	**4**

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