

ENERGY MONTHLY REPORT- DEC 2010

WINTER THRUST

A Comprehensive report on Crude Oil and Natural Gas



OVERVIEW:

Energy prices traded on a bullish note last month on thrilling winter in the US. Rise in heating oil demand from US and Euro-zone supported oil prices. Crude oil prices rose maximum as compared to natural gas based on strong economic and fundamental factors. The stockpiles of total crude oil inventory declined the most in November along with petroleum products. Global economic growth supported oil prices to rise. Similarly, natural gas storage level declined in the last month, which resulted into rise in gas prices also witnessed in the last month. Ongoing bullish trend in energy market is likely to continue in December as winter season demand may emerge in US. However, short span correction can be seen due to profit booking.

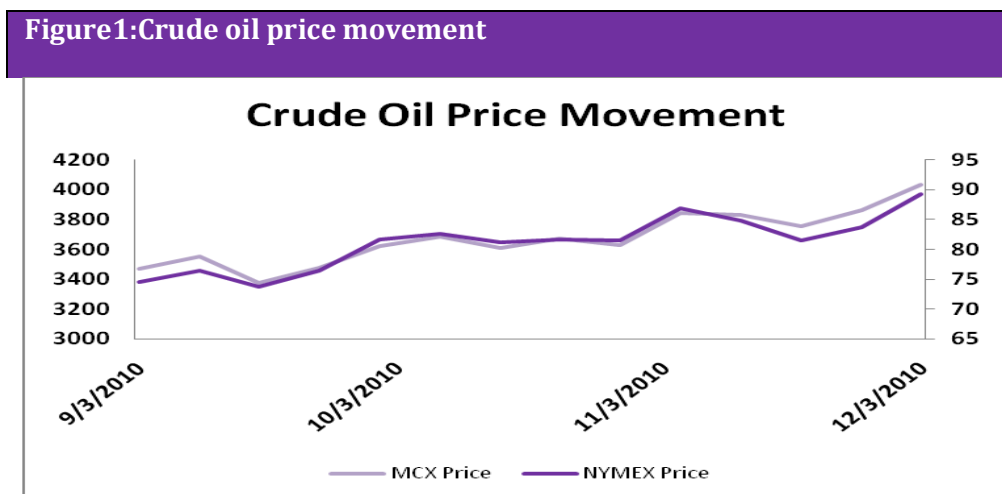
CRUDE OIL

The crude oil prices on NYMEX rallied to 2-years high on robust demand for heating oil (winter season demand) in US. The rise in demand was seen with continuous drop in the inventory levels week-on-week basis. Recovery in global economy last month also supported the price to rise. On the global commodity derivative market, MCX crude oil prices rose more than NYMEX in November.

Table 1: Crude oil price change (*Data collected till Nov 30, 2010)

Commodity	Nov	Oct	Sep
NYMEX Crude Oil	3%	2%	11%
MCX Crude Oil	8%	1%	4%

Source: Bloomberg & KCTL Research

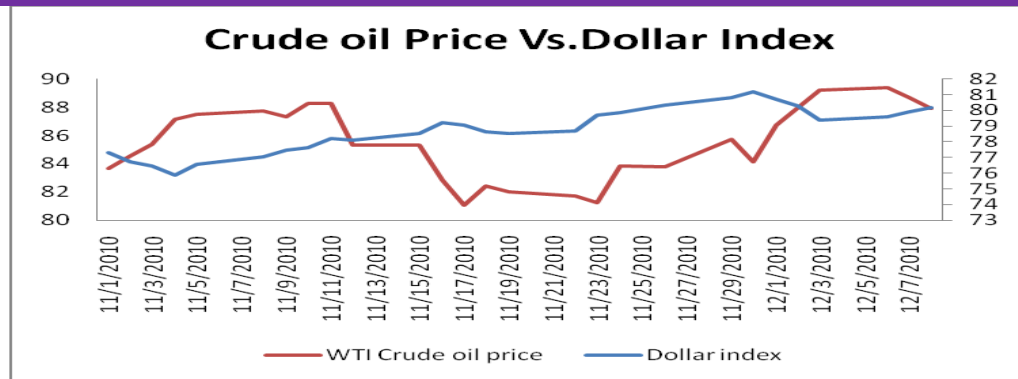


Source: Bloomberg & KCTL Research

Crude oil futures prices traded on a positive note till mid-November supported by intrinsic fundamental and economic factors. Pick in manufacturing activity in major oil consumers like US and China along with rising industrial production was the major driving force for the crude oil price movement. Trade balance of China increased whereas slight increase in US trade deficit was witnessed. Weakness in dollar index on the news of Federal Government's decision to buy govt, bonds worth of \$600 billion supported the energy prices. Tightening monetary policy concern in China led the oil prices to plunge 6% from the monthly high.

Euro declined against the dollar on Ireland debt concern. However, it recovered later as IMF and Europe Government declared bailout to Ireland. China increased its reserve repo rate to 50bps. Overall, rally in equity market and weakening dollar provided support to the crude oil market. As per CFTC data releases, long positions of hedgers increased, however a huge fall is seen in speculators positions.

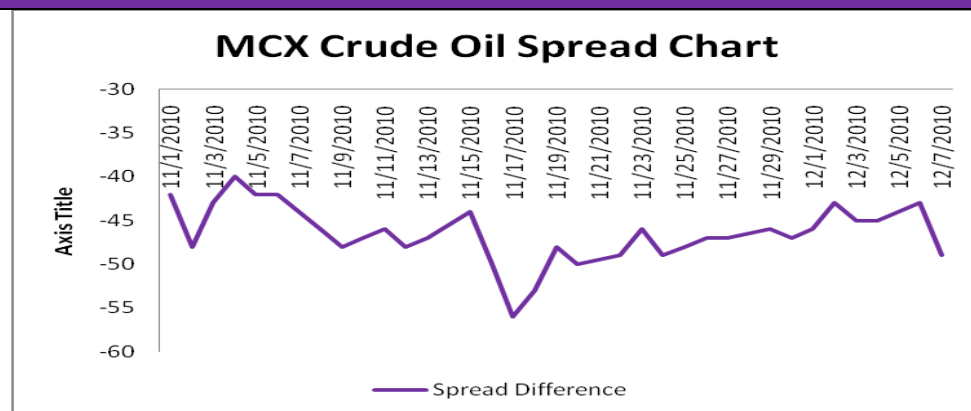
Figure 2: WTI crude oil Price vs. Dollar index



Source: Bloomberg & KCTL Research

Calendar Spread: The average spread between two contracts was `46 last month. Rise in spread was also witnessed in mid of the month as demand for December contract was more than November futures. Current spread between December and January contract is in a rising trend, as investors are investing more in January contract. **Thus current trend suggests spread may rise as demand for December futures is lower than January futures.**

Figure3: Spread chart



Source: Bloomberg & KCTL Research

Huge increase in volume and open interest was witnessed with upward trading oil prices in last month. Volume increased more than 350%, whereas open interest climbed by 250%. Currently the same trend is continuing in the market. We are expecting the trend to remain bullish.

FUNDAMENTAL FACTORS:

In the month of November, total crude oil inventory declined by more than 1% from October. Similarly, fall of Gasoline and Distillates inventory 3% and 6% respectively. A continuous trend of falling stocks is seen in distillates since August. Currently, total crude oil inventory is at 359691 million barrels, which is lower than last six month's average. Declining inventory level has been supporting the crude oil prices to trade higher since November. Winter season demand for heating oil has been increasing resulting into decline in inventory level. Thus, ongoing winter season may lead to further fall in inventory level, which might render support to the prices.

In November 2010, Saudi Oil Minister Ali-al-Naimi said, even though crude oil inventory is slightly oversupplied; oil prices are likely to remain in a very comfortable zone. However, price above \$80 a barrel is encouraging the Organization of Petroleum Exporting Countries to exceed its own quotas. The International Energy Agency estimated that the group achieved 54 percent of its promised supply cuts in September. Consuming countries are happy with prices between \$70 and \$90 a barrel, al-Naimi said. Thus, oil prices were trading in a range of \$81 to \$87 in November. OPEC has revised World oil demand growth forecast for 2011 at 1.2 mb/day upward revision of 0.12 MB/Day. In 2010 world demand was estimated to 85.78 mb /d. Thus, we can expect a positive trend for crude oil in short-term.

Tropical storm Tomas appeared as Hurricane in first week of November and had positive impact on oil price movement. It was the last named storm of this year Hurricane season.

Technical View: Crude oil Nymex

Review

- ✚ Crude oil Nymex traded higher for the fourth consecutive months. Currently trading at \$ 90.46 after making a low of 83.63 levels
- ✚ Crude oil breached the resistance at 87.15 levels which were the highs of the previous swing (month of May 2010). It is witnessing trend line resistance at 90.50 levels on breach above would lead the prices to trade further higher
- ✚ Crude oil is witnessing "**TREND CHANNEL**" formation on the upper side allowing the prices to trade higher. The target of the upper band is seen at \$ 94.60 levels
- ✚ The principle of Fibonacci retracement states that prices are witnessing resistance at 89.80 levels which is 50% retracement of the range (32.40 – 147.27) levels. Only on breach and sustained trade above is likely to test next resistance at 103.35 levels which is 61.8% retracement of the above same range

- ✦ Crude oil made a **Symmetrical Triangle** breakout in the weekly chart on the higher side suggesting bullish trend is still intact. The momentum indicator **RSI 14** monthly is trading at 0.587 showing higher potential for the prices to trade on the upper side
- ✦ Another momentum indicator **Stochastic** indicating prices to move on the higher side though K% and D% are trading higher at 0.99 and 0.845 respectively, with no sign of over lapping or turning around each other
- ✦ As per the **moving average** analysis prices are trading well above the EMA's of 8, 21 and 34 also suggesting the bullish trend. **Volume indicator** analysis also suggesting the price to trade on the higher side as the volumes has been increased from 6.452 M to 6.759 M contracts on the previous month.
- ✦ Crucial support is seen at 87.15 levels. In case market breaches below 87.15 levels is likely to cut the gains and remain lower till 82.97 levels which again is the previous swing highs.
We recommend buying at the support levels.



Recommendation: Crude oil- February NYMEX: Buy in the range \$87.50-88.50 targeting 95 then 103 with stop loss below 83.50.

Recommendation: Crude oil January MCX: Buy in the range 3970-4000 targeting 4275-4300 with stop loss below 3800.

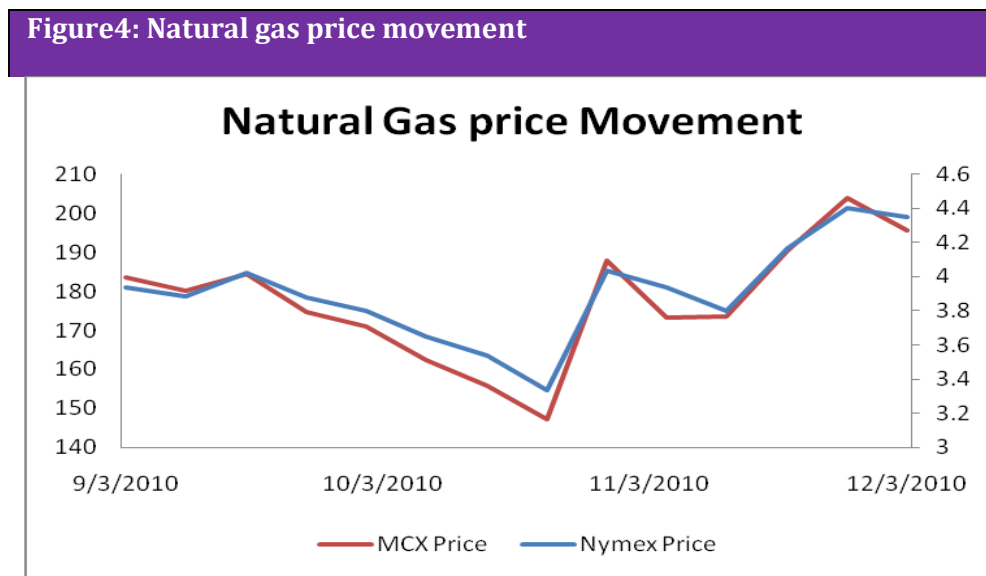
NATURAL GAS

A continuous rise in Natural gas prices was witnessed last month on account of rising winter demand in the US. Bullish trend continued since October and led prices to recover loss of last three months. Cold weather in US and Euro-zone is boosting natural gas demand, thus a fall of storage is also witnessed in the last month.

Table 2: Natural Gas price change (*Data collected till Nov 30, 2010)

Commodity	Nov	Oct	Sep
NYMEX Natural Gas	4%	4%	1%
MCX Natural Gas	3%	8%	-4%

Source: Bloomberg & KCTL Research

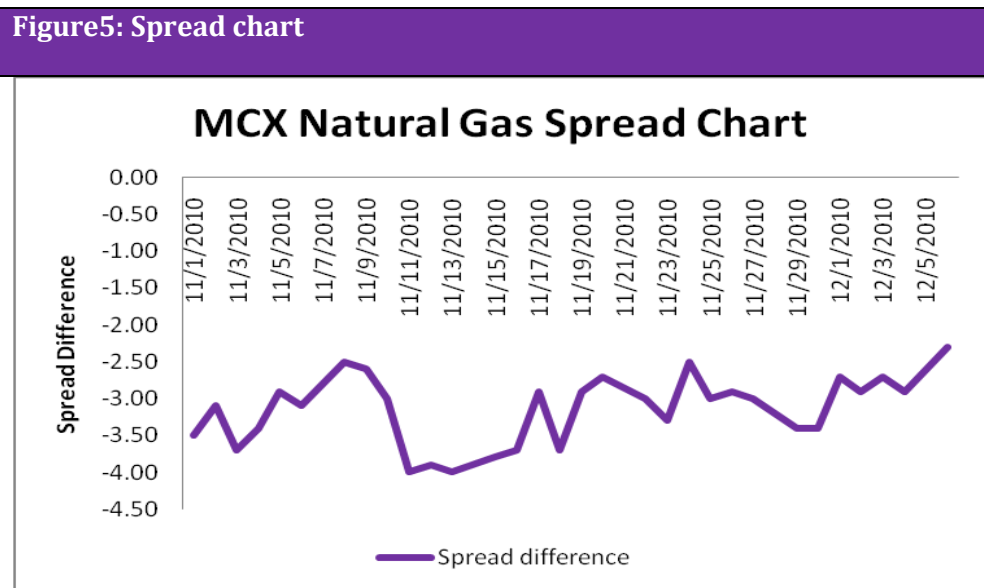


Source: Bloomberg & KCTL Research

Natural gas prices made a four month high in November. Henry hub natural gas spot prices climbed by 24% in November and closed at \$4.17. Increase in volume and open interest was witnessed last month. Total volume has been climbed to more than 300%, where as open interest increased by 150% in MCX. This shows, investors are expecting a positive trend in market, which may move gas prices to trade high in short term. As per CFTC data released, Hedgers have increased their long positions, whereas a slight fall of long positions was also seen in Speculators positions.

MCX December futures contracts demand was higher than November contracts which made spread to rise in November. However, spread started to decline after November

contracts expired. Average spread in November was at Rs. 3.23, which is expected to rise in short term as far month contract is expected to raise more.



Source: Bloomberg & KCTL

WINTER WITHDRAWAL OF INVENTORY

Natural gas demand picks up in cold weather basically due to rising heating oil demand. The US Energy Information Administration reported about a huge fall of storage in November last week. Natural gas storage has declined 23 bcf from prior week to 3814bcf. However, gas storage is still higher at last five year's average. Baker Hughes natural gas rig counts declined by 14 numbers, whereas 15 numbers of total oil and gas rigs increased in October. Cooler-than-normal weather in US and Euro-zone is supporting heating oil demand to rise. In US east region, more withdrawal of working natural gas happened last month. However, withdrawal of more than 40 bcf and 28bcf is seen from last year in this time is seen in East and West region.

Natural gas consumption started increasing since November on account of stronger cold weather in US. As per BENTEK Energy, US natural gas demand has increased in November on the back of rising heating oil demand for space heating. Demand from residential and commercial sectors increased more than 20% in November. US imports of LNG increased from Canada, to meet the demand of heating oil.

National Weather services stated that temperature will be lower than normal weather in the US, especially in Florida. Thus more demand for natural gas is expected in winter, which may pull up prices. So, fundamentally we can expect gas prices to continue the bullish trend in short run.

Technical analysis - Natural Gas January futures NYMEX

- ✚ Natural gas future prices were seen trading in the band of \$4.515-3.853 levels for the past two months. As of now market is trading higher at \$4.544 levels by breaching the previous month high of \$.515 levels. Closing above the same level would lead the prices to test \$4.737 levels for short term
- ✚ As per the candlestick principle previous two months candle resembles **“Double bottom”** pattern. However, if market closes above the resistance at \$4.515 levels then it is possible to test \$5.00 levels (Possible target of the pattern)
- ✚ According to Fibonacci principle market is witnessing a stiff resistance at \$4.737 levels (23.6%). A significant break above the same leads the prices to gain till \$5.284(38.2%) levels for short to medium term
- ✚ Indicator analysis stochastic oscillator is impending bullish view as the %K took higher crossover and currently hovering above the %D



Outlook: We expect natural gas future prices to remain higher. A convincing break above the \$4.737 levels would confirm further uptrend. The strong support is seen at \$4.160 levels.

Recommendation: Natural gas Feb Nymex: Buy at \$4.00-4.30 TP \$5.00 then \$5.30 SL \$3.75

Recommendation: Natural gas Dec MCX: Buy at 202-205 TP 220-225 SL below 195

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