

# Hands on the Wheel

*strategy*

*Presented by Val Trinkley, General Manager  
EnergyUSA*



## Energy Trends Today

- Starting Thoughts
- Technicals
- Long Term Planning
- Pricing Trends
- Pricing / Buying
- Buying Pools
- Action Plan
- Summary

## Starting Thoughts

What Are You More Afraid Of?

Fixing Your Energy Price & Then Prices Fall... **BIG FEAR THIS YEAR**  
**OR**

Not Fixing Your Price & Then Prices Rise

Your Answer Determines What Kind of Buyer You Are –  
Conservative or Aggressive

Remember – Be True to Your Philosophy

## Starting Thoughts

“The art of business is managing risk”

Determine and Keep in Mind . . .

Are you Conservative or Aggressive?

How Much Time to Devote to Managing Energy Risk?

How Much is Energy to Your Company’s Bottom Line?

Can Your Company Pass Along Energy Price Increases?

How Much Risk Does Your Company Want to Take?

Can I Accomplish My Budget With This Hedge?

Do Not Lose Sight of Your Goals.

“ Business is nothing if not a speculative risk”

## Starting Thoughts

2005 Was Crisis Management . . .

2007 Was Risk Management . . .

2008 demonstrates what Volatility is... Do you think its going away?

Building a Strategy = Managing Energy

**Now is the time to act/plan for: Winter-Short Term - Done Yet?**

**1-2 Years-Mid-Term**

**3-6 years-Long Term**

Create an Energy Conservation / Resource Plan

We are the Stewards of our Companies' Energy - Explore Viable  
Alternative Energy Options

## Starting Thoughts – Goals

Know/Remain True to Your Goals/Objectives

Sample Goals . . .

Hedge Bottom of Market

Beat NYMEX Settlement

**Set/Meet/Beat Budget**

Avoid Super Price Spikes

**Beat Utility Prices**

Beat Last Year's Spend

Keep Spending Flat

Buy Lower Than Competitor

**The two most common goals – sometimes competing goals**

## Starting Thoughts - Implementation

### Physical

- Contract - NAESB, GISB, etc.

### Financial

- Contract - ISDA - Legal, Credit

### Accounting

- FASB 133 – Is it an “effective” hedge?

## Starting Thoughts – Who to Turn to

### Energy to Bottom Line – Politics & Importance

#### Internal

- Engineering/Operations, Purchasing, Management
- Corporate – Energy Manager, Purchasing, CFO, CEO

#### External

- Considerations
  - Costs
  - How Much Time Do You Spend on Energy?
  - What Support Do You Need?
  - What Can They Say?
  - How Many People Do You Want Involved?

## Starting Thoughts – The Players

- Energy Managers
- Marketers
- Banks
- LDCs
- Producers
- Hedge Funds

## Starting Thoughts - How Did We Get Here?

### Feb '08 – Early-July '08

- Long, steady-cold winter
- Hard draws on Storage led to 1,234 BCF in April
- Will storage get full by end of October? Need it!
- LNG & Canadian supply DOWN
- Domestic Production UP... enough?
- Oil, gasoline, diesel & all commodities WAY UP.
- Weak equities – commodities attracting money
- World-wide natural gas demand up
- Weak economy – Will US demand go down?
- Ethanol demand
- Fear of a hot summer – lots of gas demand
- Fear of Gulf hurricanes – Gulf gas production

The fear of the above SUPPLY, DEMAND & FINANCIAL issues took natural gas NYMEX from \$7.80/MMBtu to \$13+/MMBtu

### Early July – Early Sept.

- Weather for July & August Mild
- Stronger Dollar – Weaker Commodity Prices
- Strong local production – overcome lack of LNG
- Hurricane Gustav – not dramatic damage.
- Storage should get to 3,500+ by 10/31... lacking add'l Gulf hurricane surprises.

The above factors drove prices to retrace 100% of its upward move, and move from \$13+ to the low \$7

## Technicals Definition

**Numerically Driven Market Behavior on Charts & Graphs**

**Significant Day-to-Day Influence on Price Movement.**

**Many Funds use “Technicals” to Drive Buying and Selling.**

**The Market *Eventually* Returns to Prices Dictated by Fundamentals.**

**Could be LOTS of Movement or “Noise” Until Then.**

## Technical Front Month Strip



# Hands on the Wheel

strategy

## Technical

### Summer "Corrections"

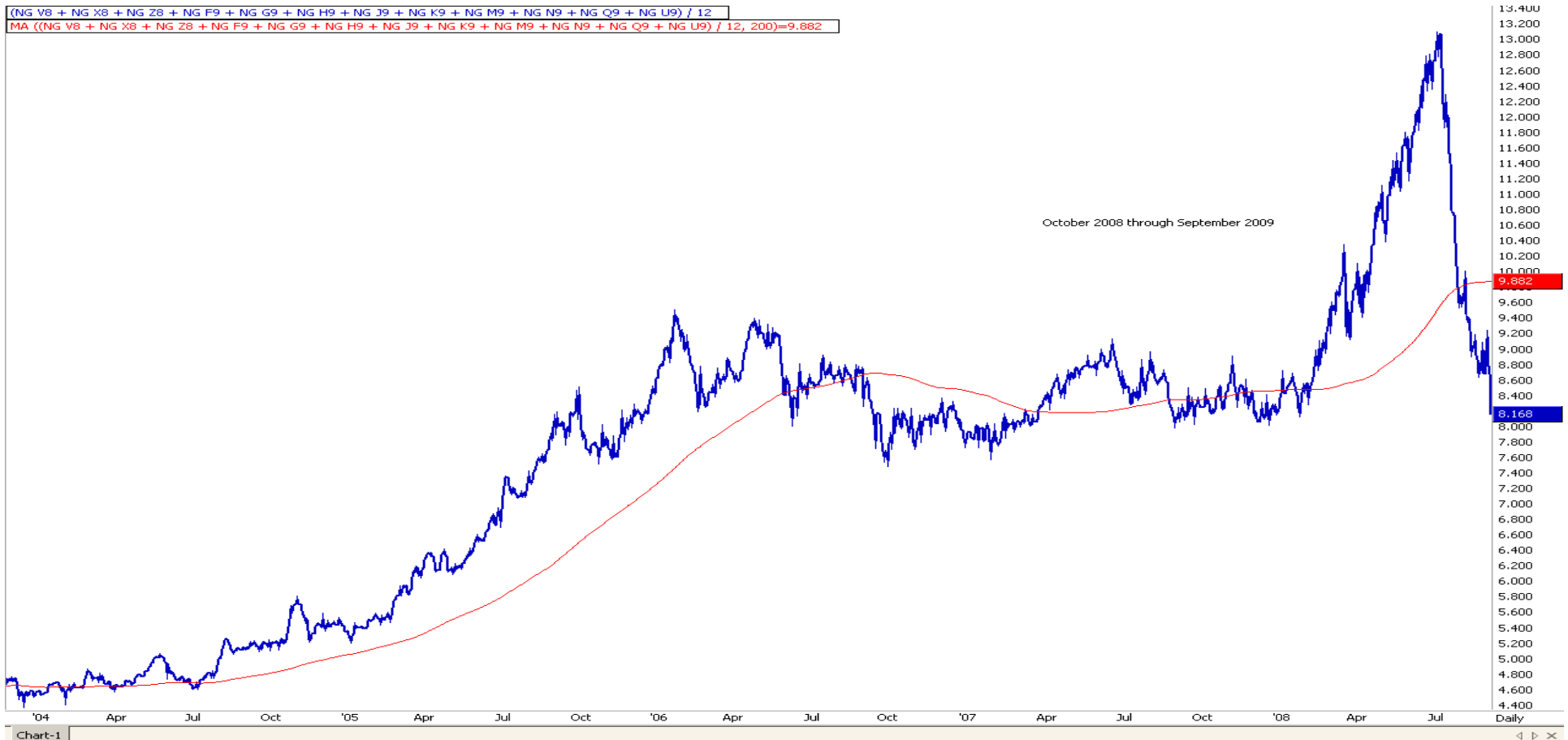
ENERGY AGENTS  
ON TOUR 08



Chart-1 | Chart-2 | Chart-3

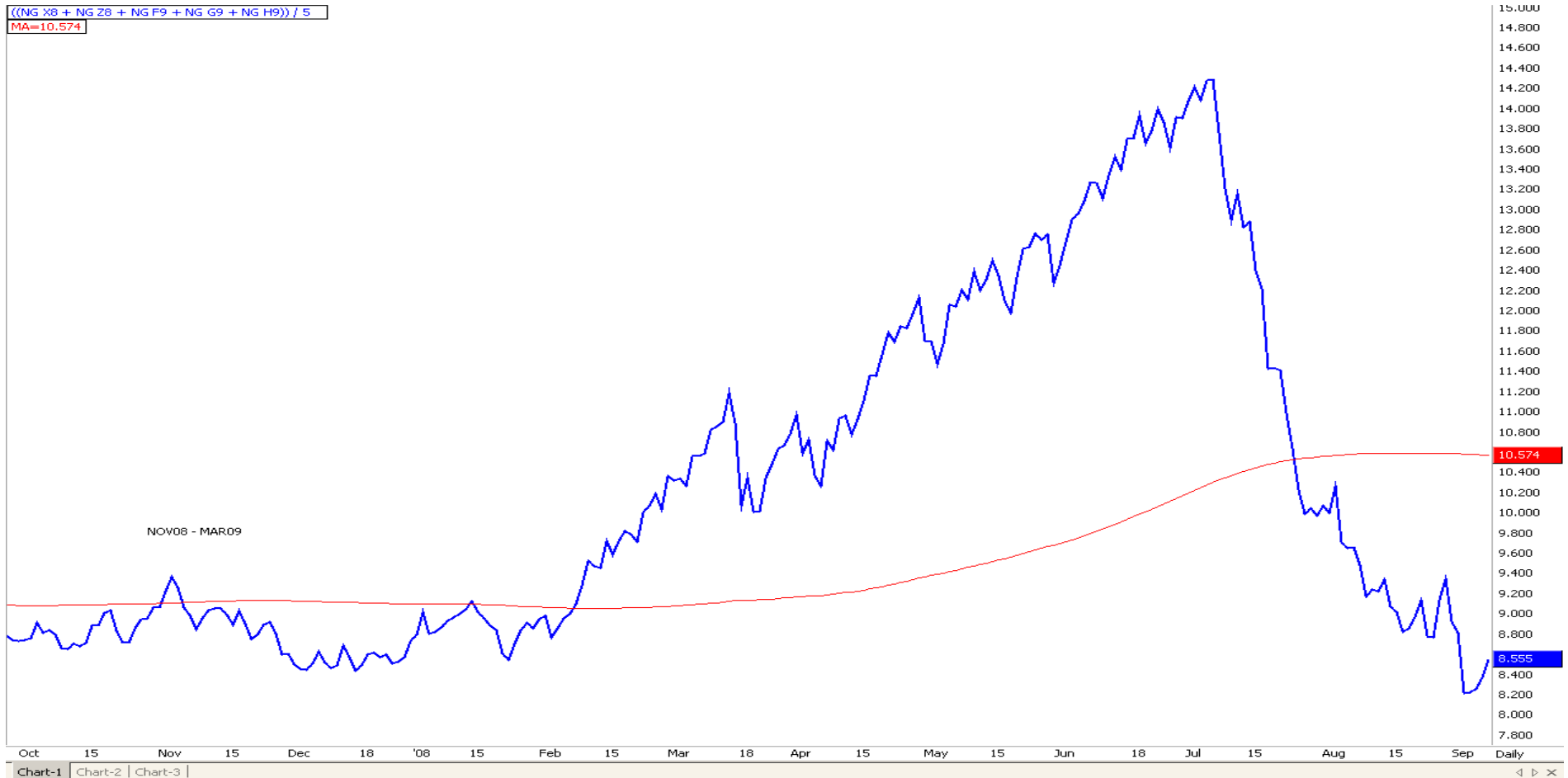
3 Daily

## Technical 12 Month Strip Since '03



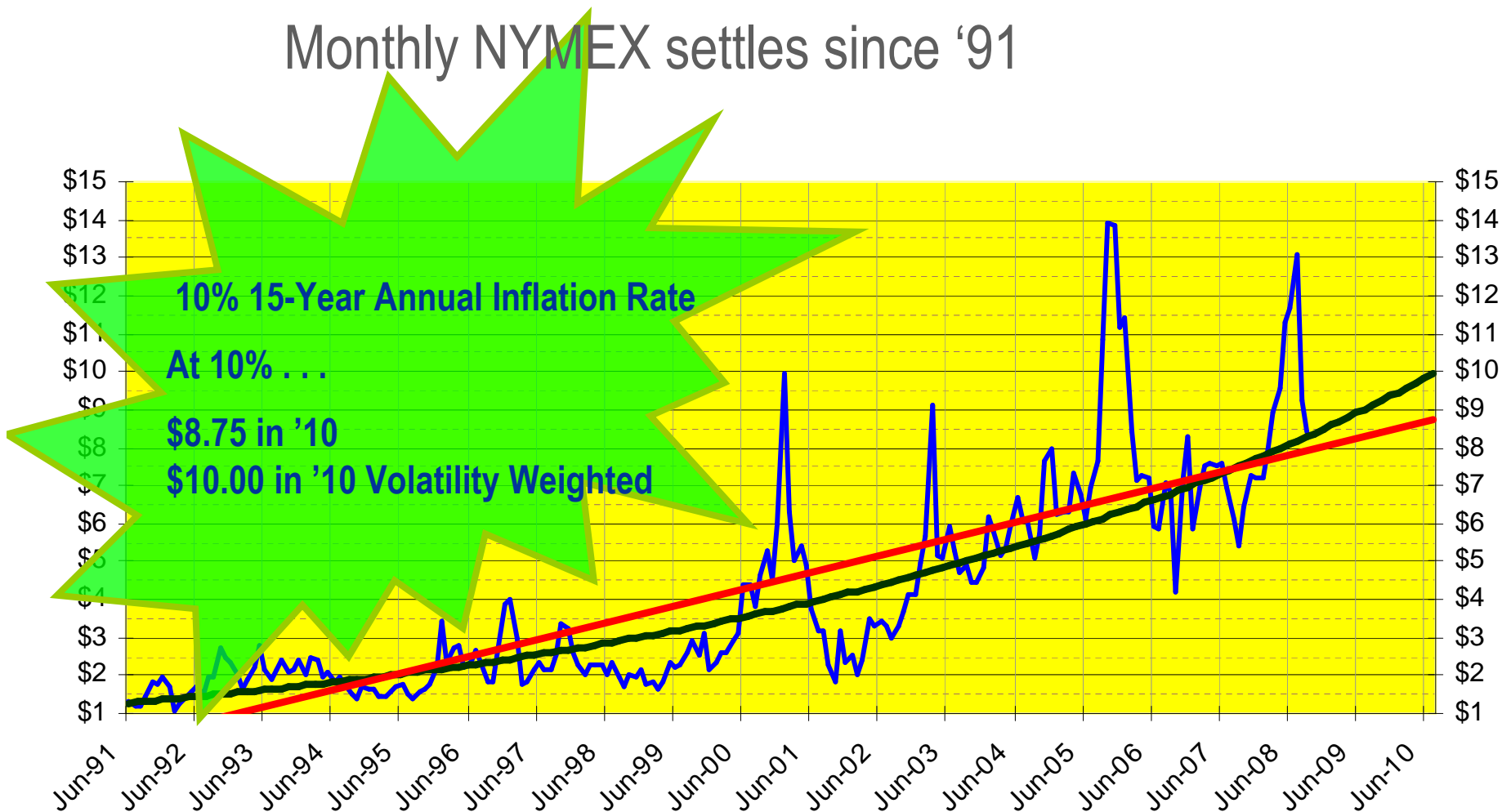
## Technical

Nov '08 – Mar '09



## Technicals

Monthly NYMEX settles since '91



## Technical

Next 5 years are “backwardated”



## Long Term Planning

### Why?

Projected Long-Term Supply vs. Demand Imbalance – Working Very Hard to “Keep Up” with Demand. Gas-fired, electric demand is scary.

Volatility WILL Remain High

Front-Month Prices Bumping Against E&P & Coal Floor - \$8

Near the Bottom of the Technical Market - \$7

We are IN a “Fall Dip”.

Can lock in for long-term at flat prices to '08 costs.

What are Your Energy Conservation Payback/ ROI Requirements?

Still Requiring 1 Year Simple Payback?

## Long Term Planning

### Forecast Weather Normalized Usage

| XYZ Company                |      |        |           |                |         |         |         | Thermostat            |          |
|----------------------------|------|--------|-----------|----------------|---------|---------|---------|-----------------------|----------|
| Natural Gas Usage Forecast |      |        |           |                |         |         |         | Set Back in Degrees F |          |
| 4/14/2008                  |      |        |           |                |         |         |         | 0                     |          |
|                            |      |        |           |                | Chicago |         | Chicago | Adjusted/             |          |
| Month                      | Year | Actual | Est. Base | Est. Spc. Htg. | Actual  | MMBtu   | Normal  | Normalized            | Adjusted |
|                            |      | MMBtu  | MMBtu     | MMBtu          | HDD     | Per HDD | HDD     | Spc Htg               | MMBtu    |
| Jan                        | 2007 | 6,581  | 1,412     | 5,169          | 1,291   | 4.0     | 1,333   | 5,337                 | 6,749    |
| Feb                        | 2007 | 8,129  | 1,412     | 6,717          | 1,312   | 5.1     | 1,064   | 5,447                 | 6,860    |
| Mar                        | 2007 | 4,460  | 1,412     | 3,048          | 690     | 4.4     | 858     | 3,791                 | 5,203    |
| Apr                        | 2007 | 3,937  | 1,412     | 2,525          | 543     | 4.7     | 516     | 2,399                 | 3,812    |
| May                        | 2007 | 1,679  | 1,412     | 266            | 116     | 2.3     | 141     | 324                   | 1,736    |
| Jun                        | 2007 | 1,230  | 1,230     |                | 0       |         |         |                       | 1,230    |
| Jul                        | 2007 | 1,393  | 1,393     |                | 0       |         |         |                       | 1,393    |
| Aug                        | 2007 | 1,454  | 1,454     |                | 0       |         |         |                       | 1,454    |
| Sep                        | 2007 | 1,572  | 1,572     | -              | 0       |         |         |                       | 1,572    |
| Oct                        | 2007 | 2,376  | 2,376     | -              | 234     | -       | 401     | -                     | 2,376    |
| Nov                        | 2007 | 4,333  | 1,412     | 2,921          | 763     | 3.8     | 759     | 2,906                 | 4,318    |
| Dec                        | 2007 | 6,780  | 1,412     | 5,368          | 1,153   | 4.7     | 1,151   | 5,359                 | 6,771    |
| Totals                     |      | 43,924 | 17,910    | 26,014         | 6,102   | 2.9     | 6,223   | 25,562                | 43,472   |

## Pricing Trends

### As of 9/4/08:

Oct \$7.141; Nov \$7.60; Winter – \$8.106

Possible Range for Winter prices \$7 - \$11

PIRA Forecast: Winter \$7-9

### As of 10/5/07:

Oct \$6.423 (settled 9/26); Nov \$7.25; Winter – \$7.88

Possible Range for Winter prices \$7 - \$10

### As of 9/16/05:

Oct \$11.15; Winter 12.38.

## Pricing Trends

### Winter Price Concerns

**This Winter Holds “Price Volatility” Potential.**

**We are in a very good “Fall Dip”. Make Hay.**

**Cold Early Winter is the Worst Thing for the Market.**

**Volatility is Here to Stay. Fear, Financial Trading, Electric Generation Demand, Natural gas going more “Global”... Bring This to Light**

## Pricing Trends

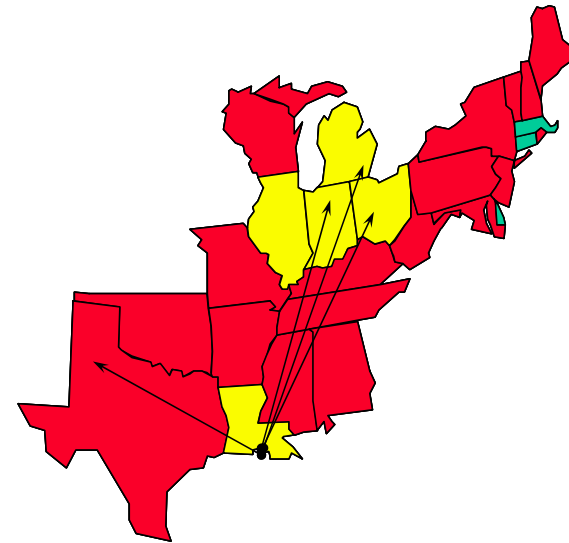
### The Trend is Your Friend!

|         | Jan    | Feb   | Mar   | Apr   | May    | Jun    | Jul    | Aug   | Sept   | Oct    | Nov    | Dec    | Average |
|---------|--------|-------|-------|-------|--------|--------|--------|-------|--------|--------|--------|--------|---------|
| 1990    |        |       |       |       |        | 1.554  | 1.510  | 1.426 | 1.426  | 1.555  | 1.970  | 2.380  | 1.689   |
| 1991    | 2.046  | 1.538 | 1.395 | 1.391 | 1.350  | 1.336  | 1.167  | 1.195 | 1.426  | 1.800  | 1.772  | 1.987  | 1.533   |
| 1992    | 1.695  | 1.046 | 1.249 | 1.418 | 1.596  | 1.685  | 1.517  | 1.939 | 1.987  | 2.743  | 2.499  | 2.332  | 1.809   |
| 1993    | 2.003  | 1.634 | 1.906 | 2.224 | 2.758  | 2.119  | 1.918  | 2.121 | 2.401  | 2.066  | 2.153  | 2.385  | 2.141   |
| 1994    | 2.022  | 2.470 | 2.418 | 1.981 | 2.076  | 1.851  | 1.966  | 1.789 | 1.482  | 1.611  | 1.611  | 1.611  | 1.901   |
| 1995    | 1.639  | 1.416 | 1.428 | 1.566 | 1.672  | 1.757  | 1.532  | 1.385 | 1.575  | 1.631  | 1.771  | 1.941  | 1.636   |
| 1996    | 3.448  | 2.340 | 2.746 | 2.779 | 2.214  | 2.361  | 2.646  | 2.322 | 1.853  | 1.828  | 2.652  | 3.001  | 2.591   |
| 1997    | 3.998  | 2.986 | 1.780 | 1.807 | 2.122  | 2.346  | 2.145  | 2.161 | 2.515  | 3.346  | 3.266  | 2.577  | 2.587   |
| 1998    | 2.309  | 2.001 | 2.286 | 2.300 | 2.262  | 2.017  | 2.358  | 1.942 | 1.672  | 2.031  | 1.972  | 2.149  | 2.108   |
| 1999    | 1.765  | 1.810 | 1.666 | 1.852 | 2.346  | 2.226  | 2.262  | 2.601 | 2.912  | 2.560  | 3.092  | 2.120  | 2.268   |
| 2000    | 2.344  | 2.610 | 2.603 | 2.900 | 3.089  | 4.406  | 4.369  | 3.820 | 4.618  | 5.312  | 4.541  | 6.016  | 3.886   |
| 2001    | 9.980  | 6.293 | 4.998 | 5.384 | 4.891  | 3.738  | 3.182  | 3.167 | 2.295  | 1.830  | 3.202  | 2.316  | 4.273   |
| 2002    | 2.555  | 2.006 | 2.388 | 3.472 | 3.319  | 3.420  | 3.278  | 2.976 | 3.288  | 3.686  | 4.126  | 4.140  | 3.221   |
| 2003    | 4.988  | 5.660 | 9.133 | 5.146 | 5.123  | 5.945  | 5.291  | 4.693 | 4.927  | 4.430  | 4.459  | 4.860  | 5.388   |
| 2004    | 6.150  | 5.775 | 5.150 | 5.365 | 5.935  | 6.680  | 6.141  | 6.048 | 5.082  | 5.723  | 7.626  | 7.976  | 6.138   |
| 2005    | 6.213  | 6.288 | 6.304 | 7.323 | 6.748  | 6.123  | 6.976  | 7.647 | 10.847 | 13.907 | 13.832 | 11.180 | 8.616   |
| 2006    | 11.431 | 8.400 | 7.112 | 7.233 | 7.198  | 5.925  | 5.887  | 7.042 | 6.816  | 4.201  | 7.153  | 8.318  | 7.226   |
| 2007    | 5.838  | 6.917 | 7.547 | 7.558 | 7.508  | 7.591  | 6.929  | 6.110 | 5.430  | 6.423  | 7.269  | 7.203  | 6.860   |
| 2008    | 7.172  | 7.996 | 8.930 | 9.578 | 11.280 | 11.916 | 13.105 | 9.217 | 8.394  |        |        |        | 9.732   |
| Average | 4.311  | 3.844 | 3.947 | 3.960 | 4.083  | 3.947  | 3.904  | 3.663 | 3.734  | 3.694  | 4.169  | 4.208  | 3.979   |

Best time to buy is late winter/early spring – before April 1st... But, watch for "fall dip"

### Pricing / Buying Basic Equation

**Basis = Financial Transportation  
Difference in Value Between  
Henry Hub and Delivery Point**



**NYMEX = Commodity**

**New York Mercantile Exchange – Price at the Henry Hub, LA**

**NYMEX + Basis = Locational Pricing**

**Can Be Purchased Separately or Together**

## Pricing / Buying

### Developing a Price Strategy

**Establish a Ceiling Price**

**Develop a Portfolio of Options**

**If you “layer in” hedges (25%, 33%, 50%, etc), assuming you are under budget with the first layer(s), you can get more aggressive with the later hedges**

**Determine Level of Risk Tolerance**

**Monitor Market & Act – Change targets if market dictates, but don’t change your buying philosophy**

**Pricing / Buying**  
**Price Options**

**BASIC PRICING TOOLS**

**Daily/Monthly Market Pricing - Floating**  
**Fixed Pricing – NYMEX & Basis (Transport)**  
**Peaking/Storage Services**

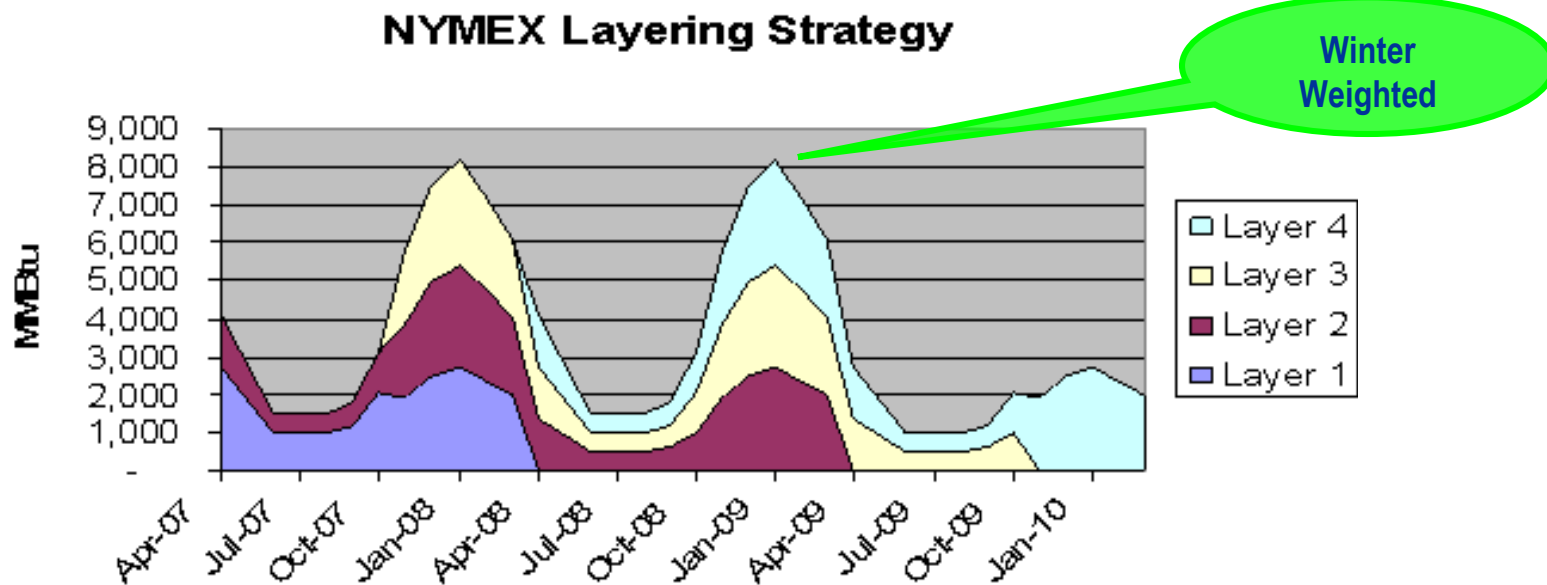
**ADVANCED PRICING TOOLS**

**Ceiling/Floor Pricing - Options**  
**Guaranteed Savings vs. non-Transport tariff**  
**Burner-tip Pricing**

## Pricing / Buying Layering

Strategies are end-user specific.

Example of a 4-layer strategy – 50,000 MMBtu/yr



## Pricing / Buying Options on Futures

Date: 9/05/08

Winter '08/'09-NYMEX

Current Market cost

\$8.40

Option Cost

\$7.50 floor/put

-\$0.40

\$8.00 floor/put

-\$0.60

\$10.00 ceiling/call

\$0.40

\$9.00 ceiling/call

\$0.60

\$11.00 ceiling/call

\$0.30

Costless Collar sample

\$10/7.50 or \$8/9

\* Price based on  
underlying  
Futures price.  
\* Priced and  
expire monthly.

## Placing an Order

### Clearly Describe Your Plan

**Limit Order**      “No Higher Than “x” ”  
Hardest to execute, especially with “odd lots”.

**Market Order**    “Execute at Current Price Now”

**Market-if-Touched Order - Execute at Current Price if...**  
“My Target Price is Touched”

## Placing an Order

One Cancels the Other Order

Current NYMEX Market Cost for 11/08 – 03/09 - \$8.40

|                     | Bottom | Top    | Activation |
|---------------------|--------|--------|------------|
| Conservative Buyer: | \$8.00 | \$8.75 | Now        |
| Moderate Buyer:     | \$7.85 | \$8.35 | \$8.05     |
| Aggressive Buyer:   | \$7.50 | \$8.00 | \$7.75     |

Also, Consider “Trailing Stops” to Follow Market Down. Though, at this time, Trailing Stops are somewhat impractical since we are so near the bottom. They did work very well this July/August.

## Placing an Order Strategies

Place Lower target price “just below” “support point”.

Place Upper target price “just above” “resistance point”.

NO “bottom feeding” orders without a “stop the bleeding” order,  
unless you can handle the “upside pain”.

Hi/Low Range - Set Upper and Lower target price of “x/y”

Upper and Lower Limit should be near equidistant from current  
market. Example... \$8.50 market - \$8 low / \$9 hi

Can move target range down if market is moving down and Lower  
target price isn't hit. But, this takes more monitoring.

**Buying Pools**  
Disciplined Dollar Program

**Dollar Cost Averaging**

**Buy a Fixed Percentage of Your Needs Every Month for 12 Months**

**Purchased on a Set Day of Each Month Rolling Forward**

**Three Pools      Conservative 8.25% Purchase Each Month**

**Balanced 5.5% Each Month for 2/3 Total**

**Speculative 2.75% Each Month for 1/3 Total**

**Remaining Balance Allows Market Participation**

**Four Month Initial Phase In – 100%, 50%, 33%, 25%**

**Better in a “Bull” Market than in a “Bear” Market**

## Buying Pools

### Weekly EnergyUSA Buying Pool Recommendations

| EnergyUSA Target Pricing for 09.12.08 |              |                  |                 |                 |                          |
|---------------------------------------|--------------|------------------|-----------------|-----------------|--------------------------|
|                                       | NYMEX Settle | Conservative     | Moderate        | Aggressive      | CHANGE SINCE<br>09.05.08 |
| Oct'08                                | \$7.366      | \$7.00 - \$7.50  | \$6.95 - \$7.40 | \$6.75 - \$7.25 | \$ (0.083)               |
| Nov'08 – Mar'09                       | \$8.075      | \$8.00 - \$8.30  | \$7.85 - \$8.25 | \$7.75 - \$8.15 | \$ (0.307)               |
| Apr'09 - Oct'09                       | \$8.188      | \$8.10 - \$8.50  | \$8.00 - \$8.40 | \$7.85 - \$8.35 | \$ (0.300)               |
| Calendar 2009                         | \$8.321      | \$8.20 - \$8.50  | \$8.10 - \$8.45 | \$7.95 - \$8.30 | \$ (0.309)               |
| Nov'09 - Mar'10                       | \$9.093      | \$9.050 - \$9.25 | \$8.75 - \$9.10 | \$8.65 - \$8.95 | \$ (0.310)               |
| Apr'10 - Oct'10                       | \$8.297      | \$8.50 - \$8.85  | \$8.30 - \$8.60 | \$8.15 - \$8.50 | \$ (0.253)               |
| Nov'10 - Mar'11                       | \$9.064      | \$9.25 - \$9.65  | \$9.00 - \$9.45 | \$8.75 - \$9.15 | \$ (0.254)               |

**Action Plan**  
**Strategic Thoughts**

**October Near \$7 – This feels like the bottom of the market**

**Winter at \$8 - \$8.50, seems like a great buy**

**Put this Winter to Bed and Consider Longer Term Strategies**

**Emphasize Short to Medium Coverage & Long-Term Initial Layer.**

**At this point, a conservative/moderate buyer should be 75-100% hedged for winter '08-'09.**

**Construct a Supply Portfolio with 3-4 Layers of 25% to 33%, each.**

**As always, if it Meets/Beats Your Budget...Buy It!**

**Are You Conserving Where You Should?**

## Action Plan

### “Drop Dead’ Dates

Now – If You Don’t Have a “2<sup>nd</sup> or 3<sup>rd</sup> Layer” for the Winter. Since the Winter is Trading Near its Lows, putting the winter to ‘bed’ can be justified for a Conservative or Moderate Buyer.

October 15th – Optimism on Storage Levels; Before Market’s Attention Turns to Winter; Before an Early Cold Blast – Worst Possibility for Gas Prices.

Thanksgiving – Last holiday before ‘brunt’ of winter. Early Winter Self-Assessment Opportunity – Supply, Demand, Storage; Only for Aggressive Buyers or Aggressive Layer.

## Action Plan

### Tracking Action

Because Second Guessing is Rampant:

Keep Track of...

Why You Did

What You Did

When You Did It

## Action Plan

### Evaluating Success

Were Objectives Met?

Did We Beat Budget ?

Did We Beat Tariff ?

Costs Trending Lower ?

Did Vendor Deliver High Quality Service ?

Remember . . .

Success does not equal “beating the market”

## Summary

**Risk is Unavoidable – But CAN be Managed**  
**Like other Business Risks**  
**Without being a Trading/Supply/Tariff Expert**  
**If Objectives are Clearly Defined**  
**Establish Plan, Budget, Price Forecast**  
**Determine Level of Risk Tolerance**  
**Monitor Market & Act – Revise Plan if Needed**

**Once you act, Don't Look Back!**