

Natural Gas Market Update

02/20/07

Natural Gas Review and Outlook

The market is testing lower this morning as March is trading at \$7.313, as I type. The March contract remains stuck in a wide trading range from roughly \$7.00 to \$8.00 as it waits for significant news to prod it one way or the other. With plenty of storage available to get us through the remainder of winter and with the short term weather forecast turning warmer, one argument says that March is due to test support again. First support for March is at \$7.30 area. If this level breaks look for a more serious test at the large area of support at \$6.90-\$7.05. A settle below \$6.90 would likely be seen as significant and bring with it a more bearish tone to the market. With March expiring on Monday it is running out of time to break this level but I expect that it will, at the very least, give it one more attempt.

Another argument is that with the storage surplus diminished and with some cool weather in the eleven to fifteen day outlook the market may very well test the \$7.00 area but that will just be another buying opportunity. Under this scenario, the market will likely continue to be range bound for an extended time period until our end of winter storage picture is clear and possibly not until we have a better feel for what the summer may bring as far as temperatures and hurricanes. If I have to pick one outlook over the other, this is the one I'd lean toward, with the addition that the market may explore below support at \$6.90 over the coming weeks but that it is unlikely that there will be a deep sell-off for some time. I have advocated in the past couple of reports that January's settle of \$5.838 may prove to be the low settle for the year and while there is still a lot to be determined before we know that for sure, I still think that this may be the case.

The last and, in my opinion, the least likely course of action for the market in the short-term is for a renewed rally and a close over \$8.35. First resistance is at \$8.00 but a settle over \$8.35 would, from a technical standpoint, indicate that something more significant could be underway.

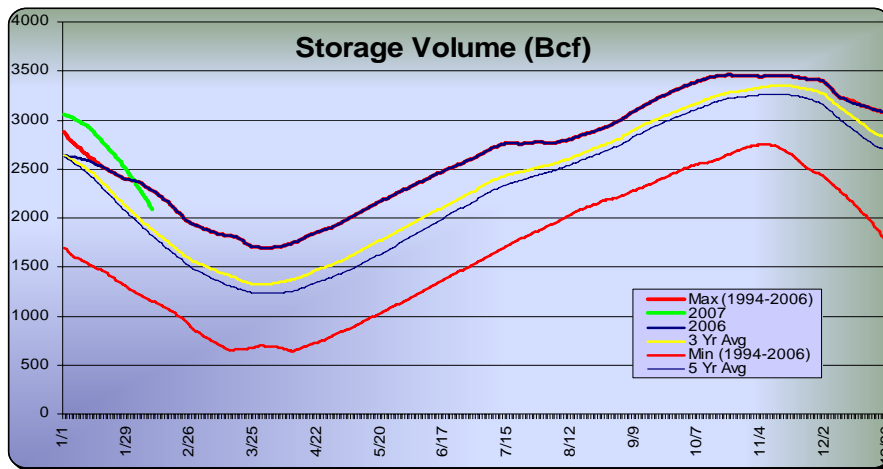


Fundamentals

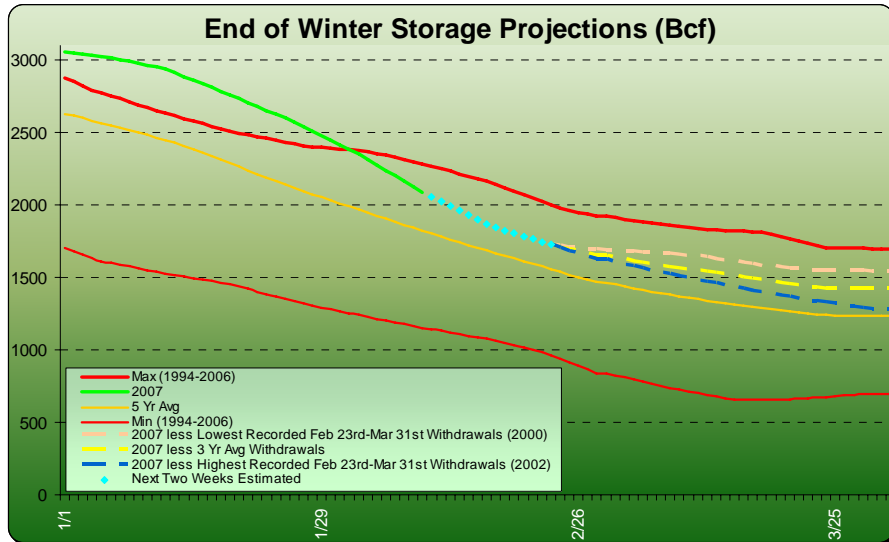
Storage

While the overall storage situation remains bearish, as there is enough gas in the ground to ensure that there will be no shortage this winter, it is not nearly as bearish as a month ago. No longer are we contemplating if a new end of season record will be set, instead the projections now show the possibility (*not probability*) of reaching the five-year average by the end of the season, see the second storage graph below. Last summer started with a higher storage level, had no extended heat and no hurricanes and it still averaged \$6.329 for the summer. So this year we are starting out the summer with lower storage levels and it is unlikely that Mother Nature will be as gentle this year as last. Will that combination result in higher summer prices this year? While it very well might, there is also a line of thinking that traders got burned being long last summer when the heat and/or hurricanes never showed up so they may be more hesitant in piling on the length this year. So while no one knows what will happen in the coming months, the lower beginning storage level may provide some basis for holding the summer curve up, at least until some of the summer season is behind us.

For the Week Ending	Total Inventory	Weekly Change	Difference – Prior Year	Difference – 3-Yr Average
01/26/07	2,571	-186	+6.3%	+18.4%
02/02/07	2,347	-224	-1.1%	+16.2%
02/09/07	2,088	-259	-8.4%	+10.9%

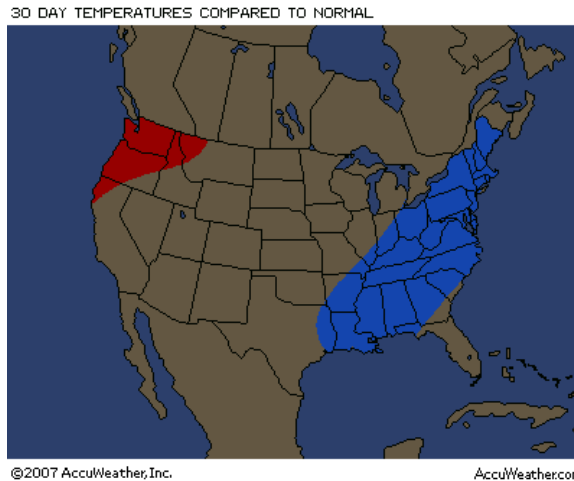


The chart below shows some possible scenarios for the end of winter storage level. The green line shows 2007, so far, extended by estimates for the next two weeks based on actual and anticipated heating degree days (denoted by the light blue diamonds). From there I took the most withdrawals ever from February 24th to the end of the winter. This scenario (dashed blue line) puts the winter ending storage just above the five-year average, while this result remains unlikely, it was unimaginable a month ago. More likely, the industry will end the season somewhere near the yellow dashed line, at about the midpoint between last year's record breaking mark of 1,695 bcf and the five-year average level on March 31st of 1,232 bcf.



Weather

Per AccuWeather: for the five day outlook, above normal temperatures are predicted for all areas east of the Rockies, except for the extreme Northeast which is predicted to have normal temperatures. Days six through ten show the area of above normal temperatures shrinking somewhat, with it being confined to the Southeast and the lower Midwest, while the eleven to fifteen day forecast shows slightly below average temps returning to the eastern third of the country. The thirty day temperature anomaly map, per AccuWeather, is included below.



Baker Hughes Rig Count			
Report Dated 02/16/07			
	Current Year	Prior Year	Increase (Decrease) over Prior Year
U.S. Gas Rigs	1,473**	1,327	146
U.S. Oil Rigs	267	215	52
Total Rigs – North America	2,382	2,263	119

** - This is a new all-time high for U.S. gas rigs.

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