

Natural Gas Market Update

01/23/07

Natural Gas Review and Outlook

Monday saw the February contract take a bit of a wild ride before finishing up \$0.433, at \$7.319. Monday's trading began Sunday night and immediately gapped higher, up \$0.295 right off the bat and was still trading in the mid \$7.20's by the time the pit session began. During the day, February struggled to hold onto all of its gains, retreating as far as \$6.920 before regaining its traction at 1:30 in the afternoon and rocketing higher. This was important from a technical standpoint as the dip allowed the gap to be filled so there won't be any technical talk about the need for the market to fill the gap below and the settle near the high for the day was definitely a victory for the bulls. Tuesday's overnight session saw the move up extend to \$7.635 and is holding steady near \$7.60 as I type. A settle above \$7.45 would be another technical victory for the bulls, possibly signaling a move even higher and at the least signaling a significant shift in the trading range the market had been stuck in. If the market does settle over \$7.45, a big assumption for so early in the day, the next big technical target is at \$8.25, with a layer of resistance along the way at \$7.80-\$7.90. If the market fails to close over \$7.45 then it will remain first resistance until closed over. Support is at \$7.30 and the \$6.90-\$7.00 area.

Much of this move is relying on the forecasts for extended normal to below normal temps thus reducing the storage surplus to something more reasonable. If this doesn't occur the market could be vulnerable to a quick turnaround. Unfortunately, the weather forecasts have been pretty consistent and they continue to extend the duration of the cold giving the bulls some comfort in pushing the issue.

As can be seen on the chart below, while a move up of a \$1.50 is significant to our wallets, it was a short time ago that February gas was trading at \$9.06 (November 30th), so this morning's move to the \$7.60 area is only a tad above the 50% retracement of the move down from \$9.06, a common retracement level seen in this market.



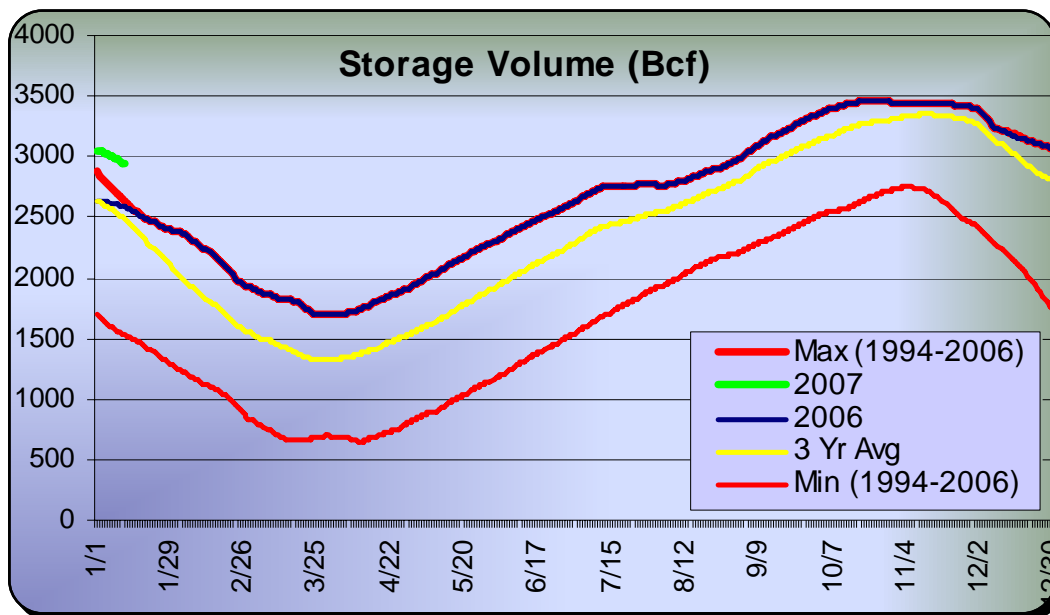
Fundamentals

Storage

The overall storage situation remains bearish, with last year's end of winter record level of 1,695 Bcf having a shot at being broken. In order to *not* set a new record 1,241 Bcf will need to be withdrawn from storage during the January 13th – March 31st time frame. More than 1,241 Bcf has been pulled from storage during that time period in three out of the past four years, last year being the exception with only 887 Bcf withdrawn. It all comes down to the weather, a normal or below normal last half of winter and last year's record will stay intact, otherwise it looks likely to fall. It is also important to remember that economics as well as weather will help dictate the amount of gas withdrawn. If the spreads between months in the forward curve is great enough it may pay people to leave the gas in the ground and buy spot month gas, not to mention average storage costs which may be higher than current market prices, again giving storage owners incentive to leave the gas in the ground and buy flowing supply.

EIA Weekly Natural Gas Storage Report

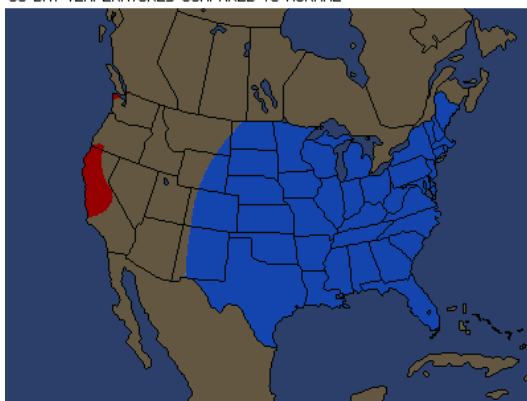
For the Week Ending	Total Inventory	Weekly Change	Difference – Prior Year	Difference – 3-Yr Average	Difference – Record High
12/29/06	3,074	-47	+16.4%	+15.6%	+3.8%
01/05/07	3,025	-49	+15.3%	+16.9%	+9.2%
01/12/07	2,936	-89	+13.7%	+18.1%	+11.6%



Weather

Per AccuWeather: for the five day outlook, normal temperatures will prevail for most areas east of the Rockies, with the Northeast predicted to have temps below normal. The forecast for days six through ten indicates that temperatures should average below normal for all areas east of the Rockies. The eleven to fifteen day outlook is more of the same except for the Southeast where average temperatures are predicted. The thirty day outlook from AccuWeather appears below:

30 DAY TEMPERATURES COMPARED TO NORMAL



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Baker Hughes Rig Count			
Report Dated 01/19/07			
	Current Year	Prior Year	Increase (Decrease) over Prior Year
U.S. Gas Rigs	1,466**	1,222	244
U.S. Oil Rigs	275	247	28
Total Rigs – North America	2,351	2,147	204

** - This is a new all-time high for U.S. gas rigs. The previous record of 1,450 was set on September 22, 2006.

Crude Oil

Crude oil continues to flounder as the same story lines that were the reason (or excuse) for setting records a year ago now are regularly shrugged off. Iran is still an issue, as are the problems of rebels in Nigeria. If anything they are more of an issue now, I suppose you can only trade on hype for so long before actual disruptions have to take place to make them real. The market appears to have shifted into a mode of 'I'll believe it when I see it'. Even shrinking inventory levels, as compared to last year, due to an apparent supply/demand imbalance resulting from production cuts aren't garnering the headlines and price reaction of a year ago. Speaking of production cuts, OPEC is expected to reduce their production again in the coming months in order to help stabilize prices. February crude oil gave up \$0.86 yesterday to expire at \$51.13, the lowest settle for a prompt month contract since the June 2004 contract expired at \$46.80 in May of 2005. With the test of \$50.00 last week and considering how far crude oil has fallen recently, it is overdue for an extended correction to the upside. First resistance is at \$53.50, although, it would not be surprising, or particularly bullish, if the market were to correct all the way to the \$55.30-\$55.80 area. A correction to this level would be considered normal and would likely meet some resistance at that point. First support is at the \$50.00 level. For the market to get and settle below \$50.00 would be a big blow to the bulls, and the area will likely be met with good buying. I believe this move lower is likely over. Below is the daily perpetual chart for crude oil with first support and resistance marked.



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