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BI-WEEKLY OIL REPORT

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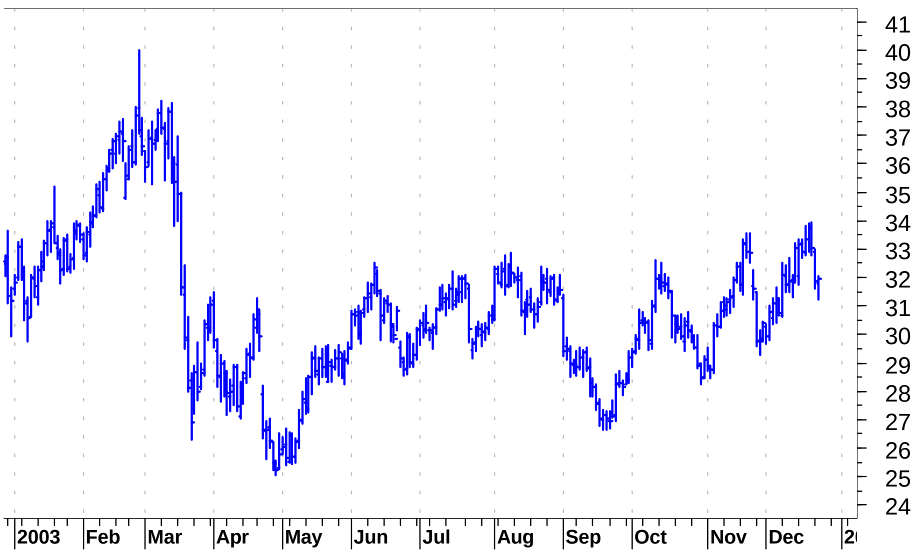
"Ladies and Gentlemen… We got him!"

Paul Bremer's, US Chief Administrator in Iraq, opening statement on the press conference regarding the capture of Saddam Hussein was probably the most characteristic way to end a year, which started with Saddam holding center-stage in world politics. His capture was treated by many with relief and joy, by some with disappointment and by many others, the oil markets among them, with indifference. The latter was probably the most unexpected reaction. By replying "so what!" to Bremer, traders showed that Saddam was old news to them long before he was actually arrested by US forces.

2003 was a year that, for petroleum, started in a spectacular way, moving from as high as $40 on March 27th, to as low as $25 on April 29th, only to climb higher again and end quite strongly, managing to retain $30's. The average yearly price for WTI reached $31.06, which is $5 or 19% higher than last year's average of $26.06.

Figure 1. NYMEX WTI daily futures prices ($/barrel)



Source: NYMEX

This spectacular rise was, as mentioned before, initially attributed to the war in Iraq and the general strike in Venezuela, but when both issues were removed, when the strike ended in February and with the quick prevalence of US forces in Iraq, others came to petroleum's rescue.

OPEC surprised everybody with its decision to cut output on September. Its members clearly stated that they want to take pro-active action against any future supply surpluses. They send a strong signal to the markets that they are not willing to see prices collapse, or world inventories grow to excessive levels. They have also showed that they would like their effective price range to remain higher than their official price band of $22-$28 basis OPEC basket prices. Venezuelan President Chavez made explicit statements supporting a higher price band, while other members indicated through their comments or actions that they tend to agree.

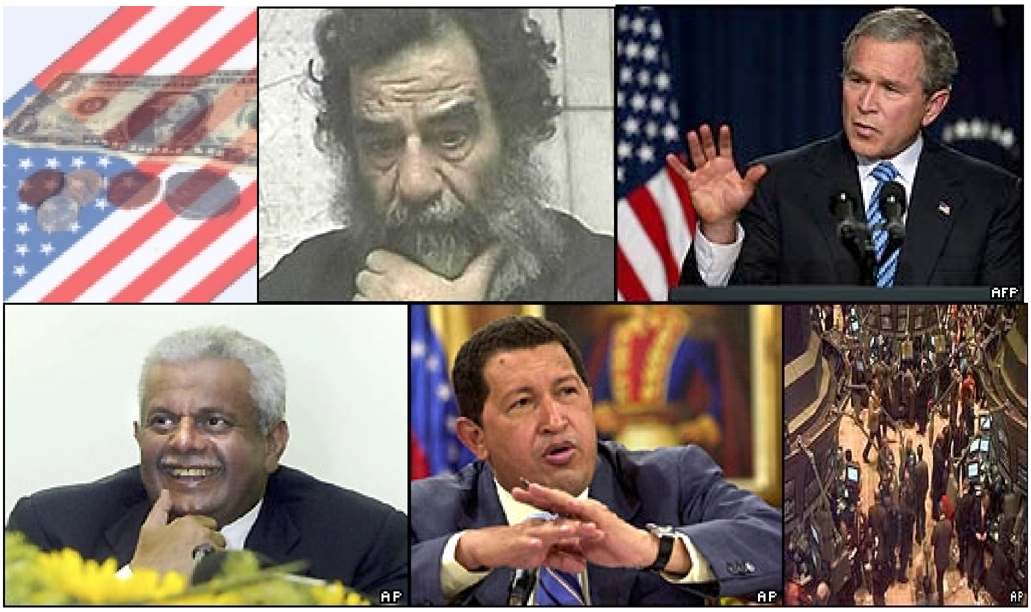
When pressured to comment if they share the concerns of oil consumers regarding high oil prices OPEC members pointed to our next "hero" of 2003 the US dollar; or rather the **weak US Dollar** (The euro and the yen gained 18.5% and 11.7% vs the USD respectively). OPEC blamed the weakness of the currency for the overall rise in prices, noting that their increased expenses in other currencies offset any rise in their dollar income. The comment did not ease the concerns of the largest consumer, the US, which had to carry all the burden of high dollar denominated petroleum prices. US Energy Secretary Abraham bluntly stated that prices are "too high" during the recent price rally in December.

Not that the **US Administration** did not play its role in underpinning prices. The Bush Administration's decision to refill the **Strategic Petroleum Reserve** led to the removal of more than 35 million barrel of crude away from the US markets. This represents an almost 100,000 barrels per day outflow, which although was meant to serve US's strategic interests, it also helped crude prices retain their strength.

In a more subtle and quiet way, emerged another sponsor of higher petroleum prices; **economic growth**, which led to higher **petroleum demand**. It seems that US demand will surpass the 20 million bpd level for the first time ever in 2003 and this could be attributed to the improvement of economic conditions. EIA predicts a 310,000 bpd rise in US demand for the year, bringing it above 20 million bpd for the first time ever, while at the same time the S&P index posted a 16.7% rise after three consecutive years of losses. European equity market recovered even more strongly, supporting the view that a worldwide recovery effort is taking place. There is clearly a direct link that connects economic growth and robust petroleum demand, which can become even stronger if recovery accelerates next year.

In summarizing, Saddam and Chavez at first, OPEC, the US dollar and stronger economic growth all assisted in raising average crude oil prices by $5. During the course of this year the most dominant factor –Saddam-disappeared, while another –Chavez- is waiting on the sidelines, maybe to emerge again next year. As for the remaining ones, their fates cannot be easily determined.

Figure 2. US$, Saddam Hussein, G.W.Bush, Al-Attiyah, H. Chavez, NYSE



While we can easily determine this year's star actors, many conflicting views have appeared regarding next year's actors in the global petroleum scene. It is extremely hard to see which predictions hold more merit and which are likely to be vindicated. Many of this year's "heroes" will most likely dominate the scene in 2004 as well, but it is also clear that some will disappear and be replaced by new. Real life seldom agrees with analysts' assumptions, choosing to make gurus out of some while ridiculing others, not always on the basis of merit, but rather based on a twisted sense of humor.

We would like to wish all of you a happy and prosperous 2004.

[The report will be issued again on January 8th.]

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