

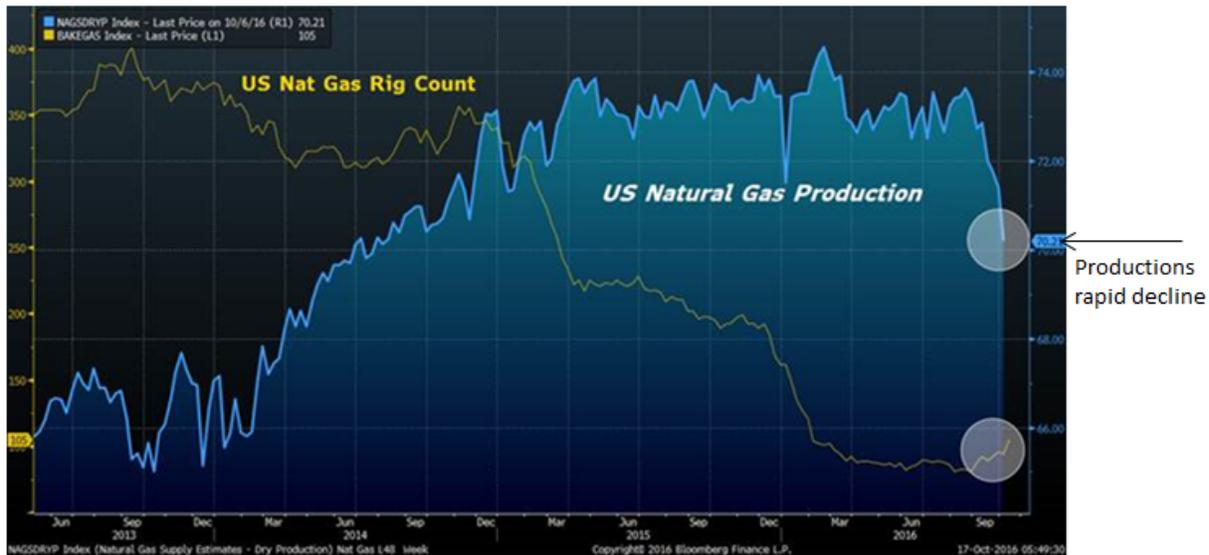


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Natural Gas

Natural gas prices have climbed steadily through 2016 largely unnoticed. Prices are currently comfortably above \$3.00 USD per MMBTU on the NYMEX for 2016, 2017 and 2018 before dipping back below \$3.00 in 2019. Even the AECO Calendar strip has poked its head above \$3.00 CAD per GJ for Calendar 2017. These are price levels that allow many producers with peer leading natural gas plays to hedge prices and deliver excellent rates of return on well-defined projects.

These prices are possible because the natural gas directed rig count has declined steadily from 2013 and has only very recently begun to show an increase in activity. The impact of a falling natural gas directed rig count and a significant drop in associated natural gas produced as a by product of many leading crude oil plays has finally begun to have an impact on natural gas production levels currently as illustrated in the Bloomberg chart below.



Strong natural gas prices are not available everywhere. There is still volatility in regional markets that are dealing with transportation related issues that occasionally result in wider than normal differentials, however the overall price level has improved significantly and should result in more drilling activity, more production being hedged at attractive prices and ultimately more production.

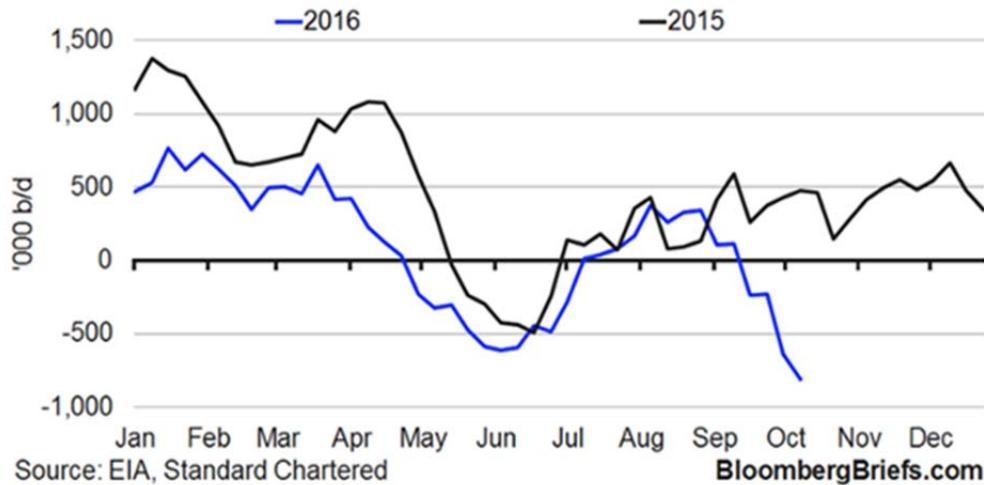
Seasonally, we could also be in for a colder than normal winter as stronger-than-expected La Niña may be brewing. Many have doubted forecasts calling for the onset of the first La Niña in almost five years, believing that its failure to materialize in convincing fashion last summer - as originally predicted - means that it may be off the table for 2016-17. That said, in recent weeks, the oceans and atmosphere have been pulling everything into place to facilitate a potentially stronger La Niña than previously thought, so those of you who follow commodities markets may want to watch to see if this weather pattern emerges. The El Niño-Southern Oscillation, with its cool phase La Niña and warm phase El Niño, is one of the most reliable long-term indicators for global climate. The ENSO phases can have drastically different impacts on commodities worldwide from energy use to grain yields. For the upcoming months, La Niña favors colder winters in the Northern United States and drier conditions across the southern tier. A colder winter would have a greater demand

for natural gas with potentially reducing current supply. Here is hoping for a little winter weather to help the potential trend up in natural gas stocks before production reverses its current trend and climb in a meaningful way with the ongoing addition of rigs with increase pricing.

Crude Oil

U.S inventories are tightening faster than the market thinks, said Standard Chartered in an Oct. 17 report. Contrary to views that suggest a normalization in inventories will take 18 months or more, it could happen within six months, it said. Over the past six weeks, the excess of crude and product inventories has fallen by 33.7 million barrels to 224.4 million barrels, representing a tightening relative to normal seasonal patterns of more than 800,000 barrels a day.

U.S. Crude and Product Draws Have Gained Pace



As mentioned in the October Issue, Saudi Arabia’s view is the only view that matters when it comes to oil production levels that in turn affects the price. Since their decision to increase market share and raise their production, the Kingdom has been working on reducing their fiscal budget in order to reduce the price of oil needed to meet their budget requirements. At current oil price levels the Kingdom continues to run large deficits. According to the International Monetary Fund, the average oil price that Saudi Arabia needs to balance its budget will fall this year by only half as much as forecast six months ago. The country’s fiscal break-even price will drop to \$79.70 a barrel in 2016 from \$92.90 in 2015. The new number released ahead of Saudi Arabia’s first-ever international bond sale, suggest that the government’s efforts to cut costs and diversify its economy away from petroleum are having less of an effect than was previously forecasted.

With key market participants such as Saudi Arabia clearly favouring higher prices we expect crude oil to continue to climb its wall of worry higher over the balance of the year.

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