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ENERGY

Natural Gas Outlook

IURC Gas Forum

October 15, 2010

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Natural Gas Outlook: Summary

The resurgence of domestic shale gas production is rapidly transforming our domestic natural gas supply and price outlook. The lack of bullish price response in the past year is due significantly to increasing shale gas production.

Indicators of this rising gas supply include:

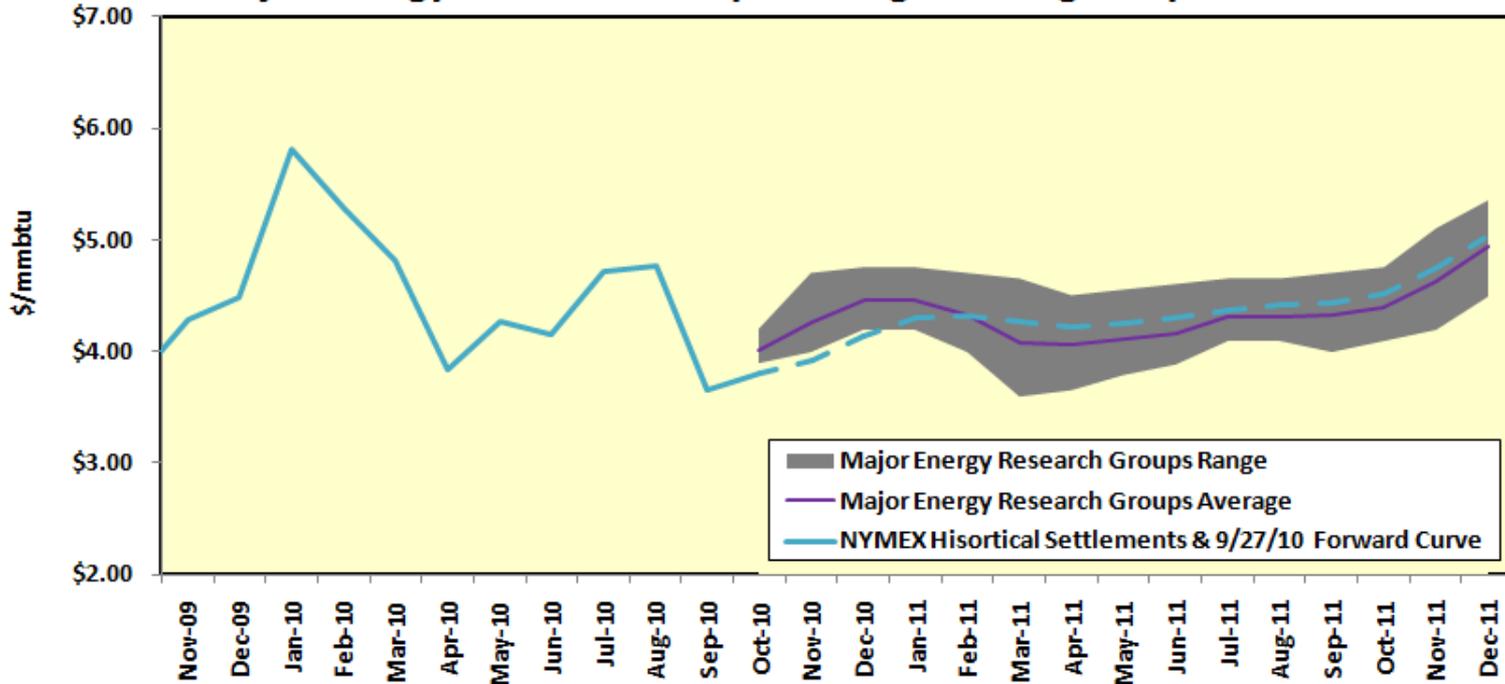
- **Winter 2009/'10:** Despite extended cold and unprecedented storage withdrawals, NYMEX peaked to only \$6.10.
- **Summer 2010:** Despite an onslaught of hot weather this summer and an early start to hurricane season, spikes in natural gas prices have been conspicuously absent. NYMEX peaked at \$5.19 in June, and has trended down ever since.
- Increased demand during 2010, due to increased power demand and industrial recovery (spurred by govt. stimulus programs) couldn't raise prices either.

Demand growth seen in 2010 is not likely to be sustained into 2011, given normal weather patterns, lack of economic stimulus and new coal fired power gen.

However, supply growth is likely to continue on into 2011, dominated by shale gas. And the price outlook is relatively flat, at least compared to the last decade.

Natural Gas Price Outlook: 2010/'11

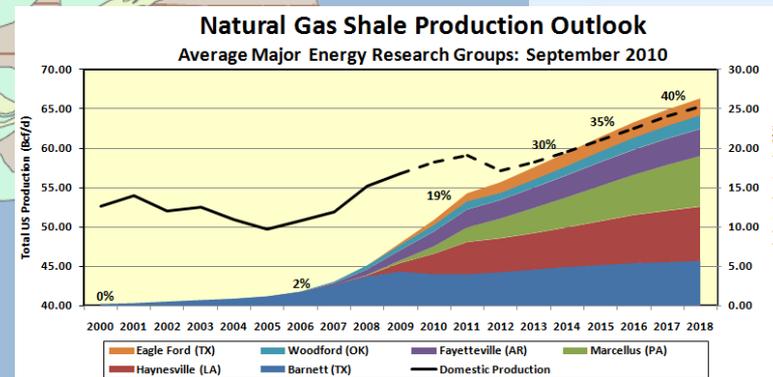
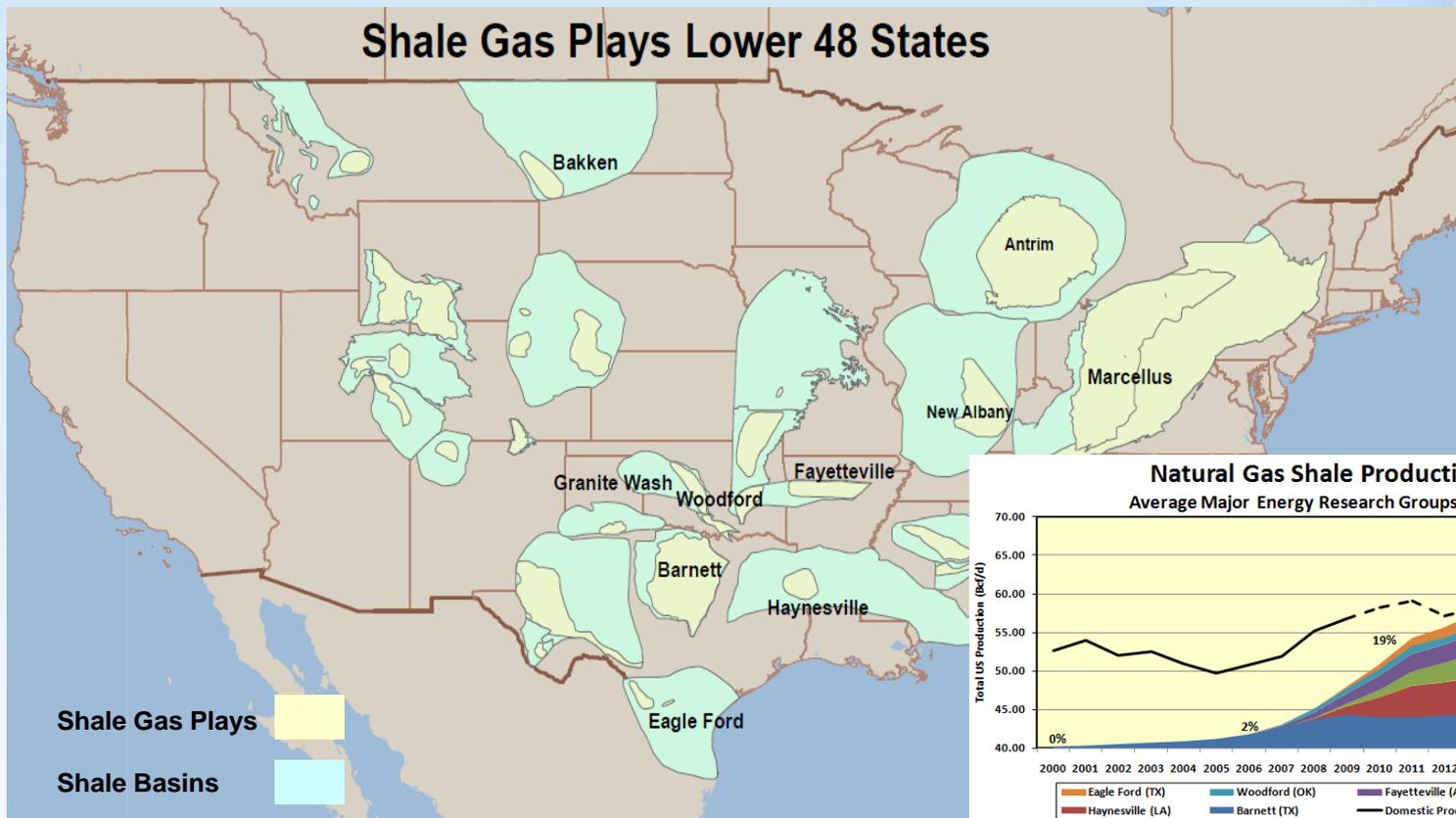
Henry Hub Short-Term Monthly Price History & Forecast
Major Energy Research Groups Average & Range: September 2010



- In 2010/2011 prices should trade in a relatively sideways pattern with additional production providing resistance at the high end and coal/gas fuel switching giving support at the low end.
- 2010 Henry Hub price forecast: \$4.49*/mmbtu. 2011 Henry Hub price forecast: \$4.34*/mmbtu. This forecast assumes normal weather.
- Continued, but slow, economic recovery along with ample production/supply levels are the primary drivers going forward.

*Major Energy Research Groups Avg.

Natural Gas Supply Outlook: Shale Gas



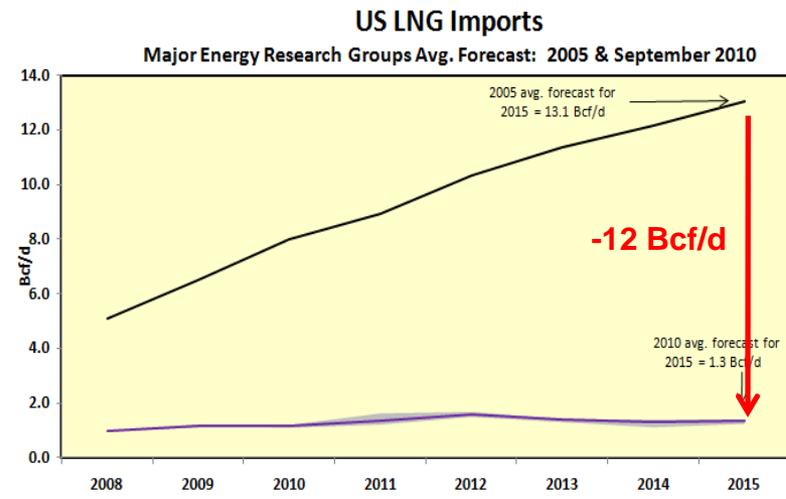
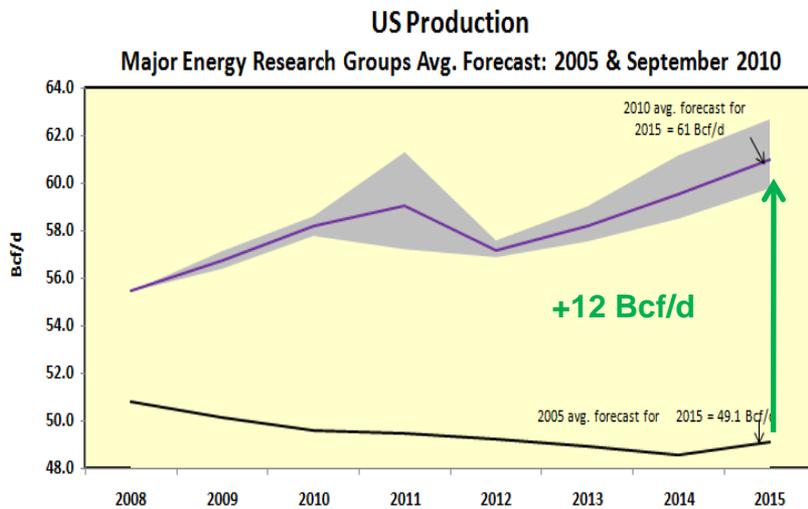
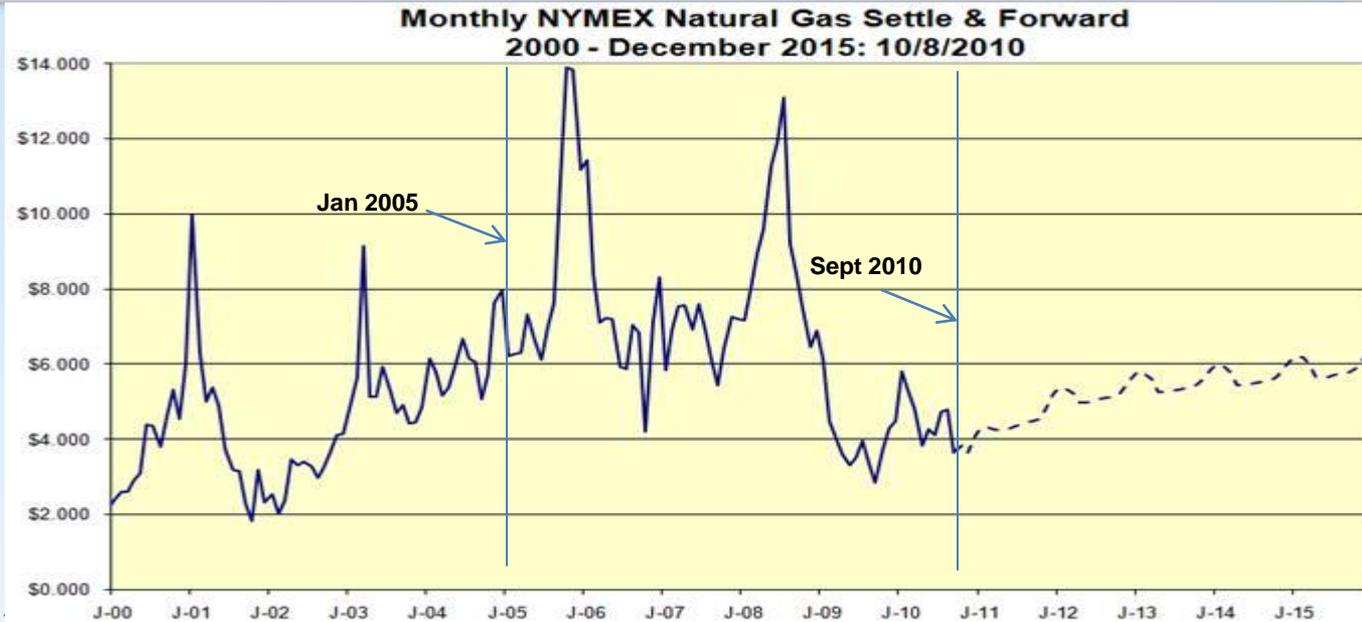
- Given current technology, estimates of recoverable reserves for U.S. shale gas currently range ~ 1,100* Tcf. Total domestic natural gas recoverable reserve est. 2,500 Tcf., ~100+ years** usage, @ today's demand level.
- The breakeven costs of shale gas are declining, with Haynesville avg. \$3.40, Barnett avg. \$4.10, and Marcellus ~\$3.10. Liquids rich Eagle Ford and Granite Wash avg. costs are well under \$3.00.***
- As shale gas technology continues to develop and improve, shale gas reserve estimates keep growing as well.

*Major Energy Research Groups Avg.

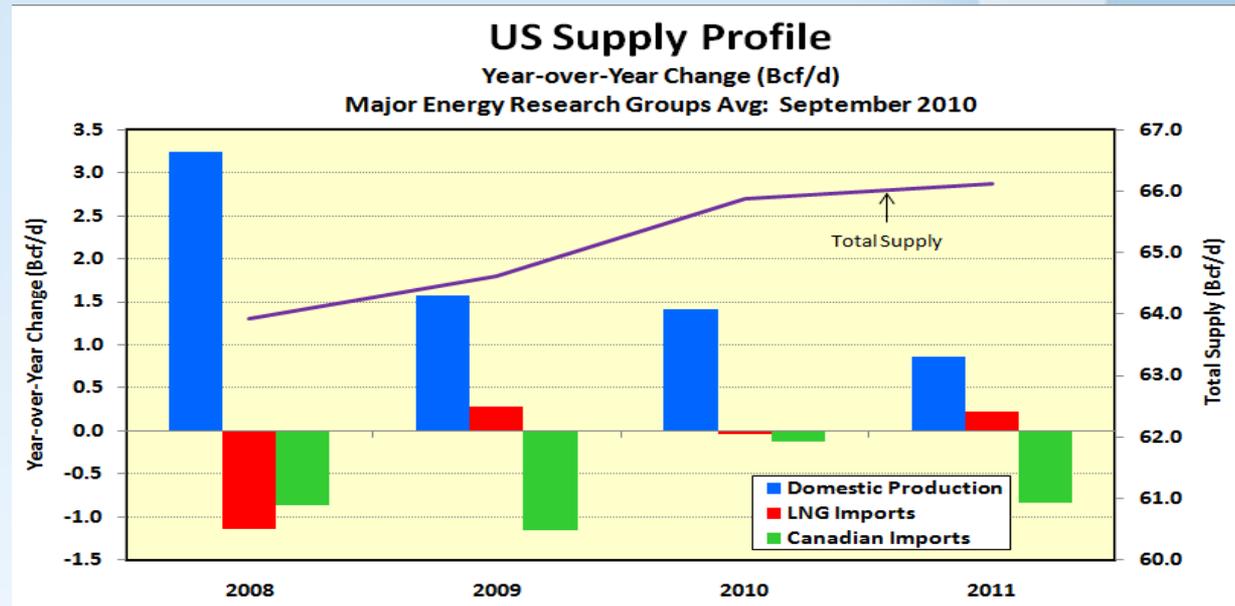
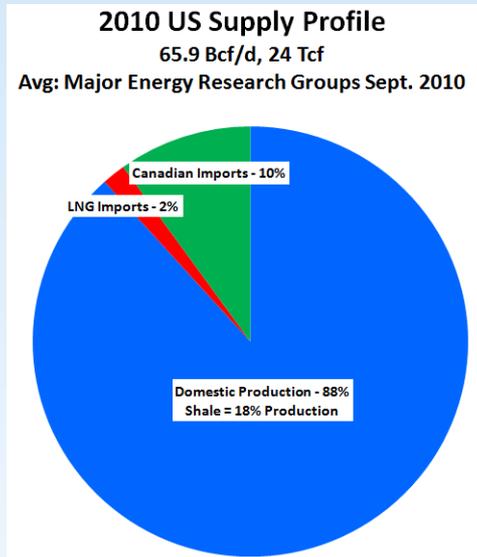
** Colorado School of Mines, Potential Gas Committee June 2009 .

***Bentek June 2010

Natural Gas Price/Supply: History/Outlook



US Supply Growth Driven by Domestic Shale Gas Production

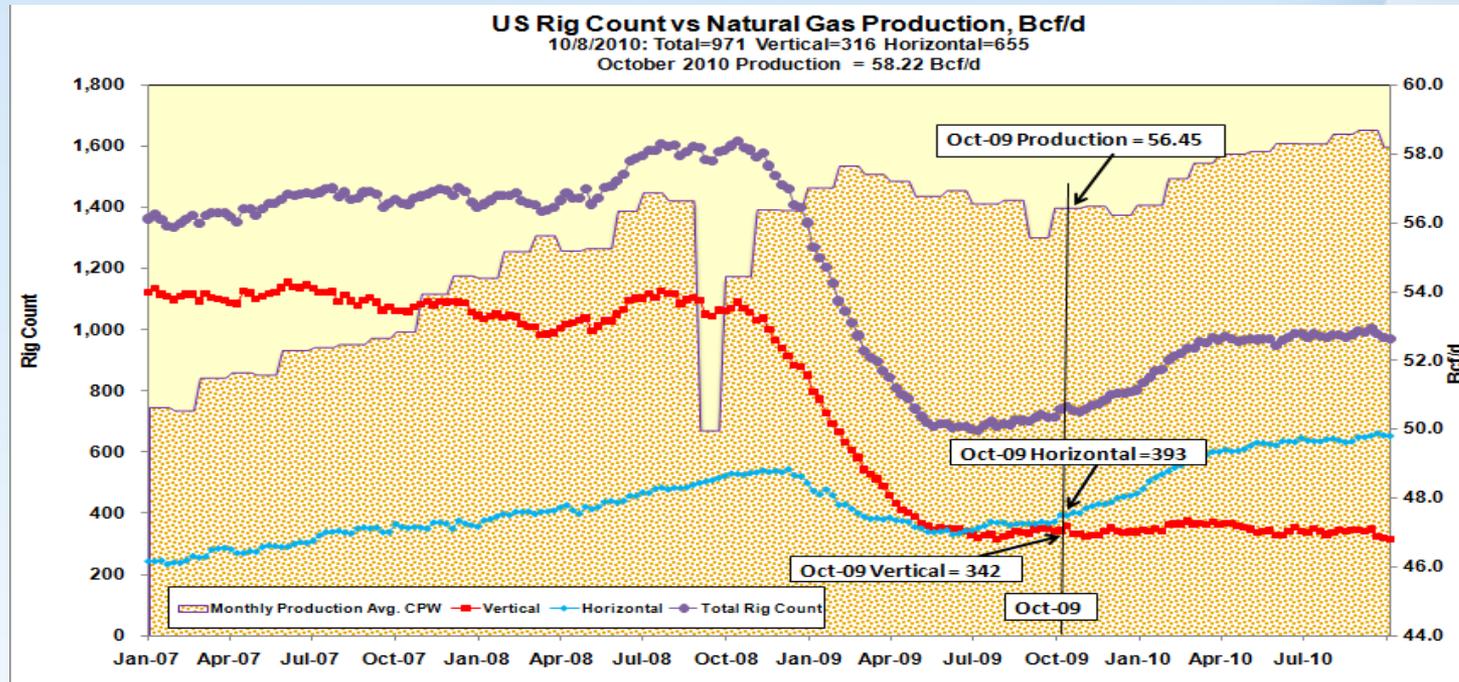


- **2010 Supply:** Est. 65.9 Bcf/d*, up 2%; Canadian imports down .1 Bcf/d*, LNG imports flat* and domestic production up 1.4 Bcf/d*.
- During the last 12 months, US domestic production outlook for 2010 has grown by 11.5%, or up 6 Bcf/d, to 58.2 Bcf/d, as shale efficiencies improve, JV's increase and drilling grows.
- **2011 Supply:** Est. 66.1 Bcf/d with
 - Domestic Production: Up 0.9 Bcf/d*, driven by continued shale drilling.
 - Canadian Imports: Down 0.8 Bcf/d*.
 - LNG Imports: Up .2 Bcf/d*.

*Major Energy Research Groups Avg.

Natural Gas Supply: Drilling & Production

Drilling Cutback not Reflected in Production

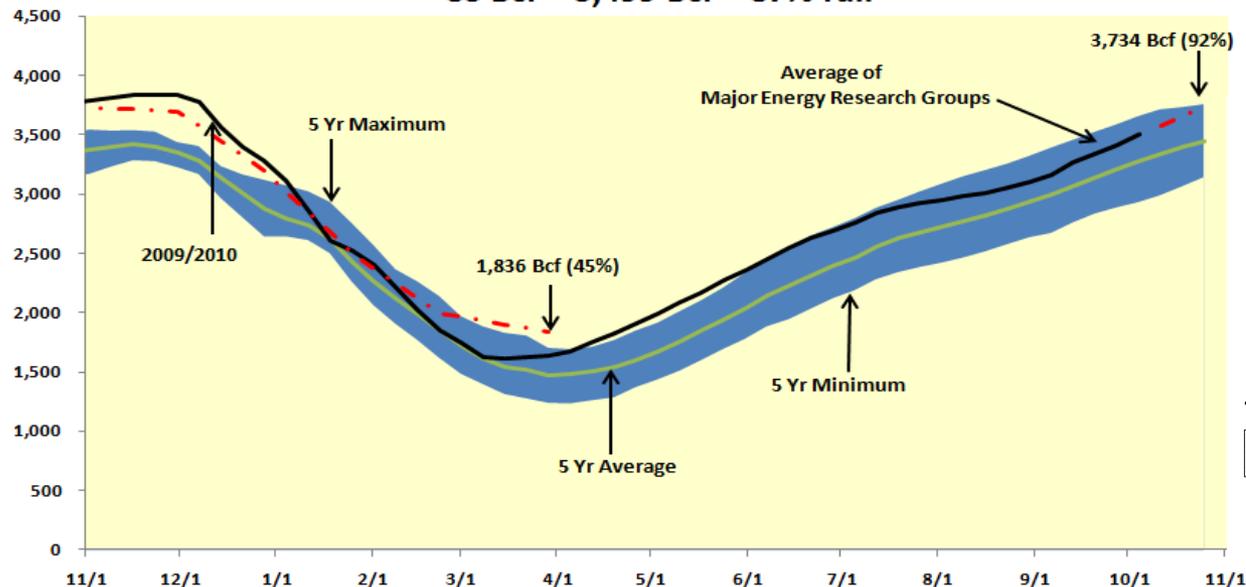


- Natural gas rig counts hit a new high of 1,620, September 2008, then plunged to 675 in July 2009, as natural gas prices fell. To date, rigs have recovered only one third of the loss, to 988. Almost exclusively, the growth has been in horizontal, shale drilling.
- However, 2010 production is projected to be 58.2 Bcf/d*, up 1.4 Bcf/d or +2% * from 2009.
- October 2010: Total drilling is up 32% y/y. Vertical (conventional) drilling is down 8% y/y, and horizontal (unconventional/shale) is up 67%.
- Producers may be calibrating activity based on weather extremes ytd, leading to future over supply.

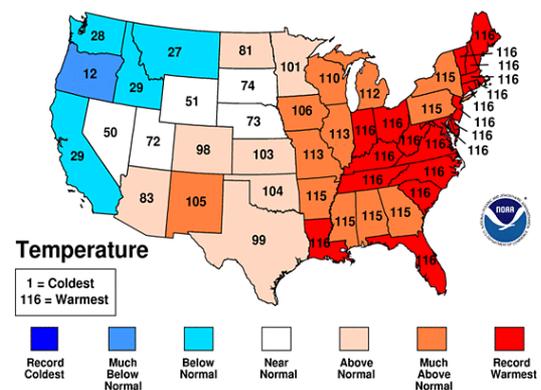
*Major Energy Research Groups Avg.

Repeat of Last Fall's 10/31 Record Storage Unlikely

EIA Inventory thru 10/1/2010
 +85 Bcf = 3,499 Bcf = 87% full



April-September 2010 Statewide Ranks
 National Climatic Data Center/NESDIS/NOAA

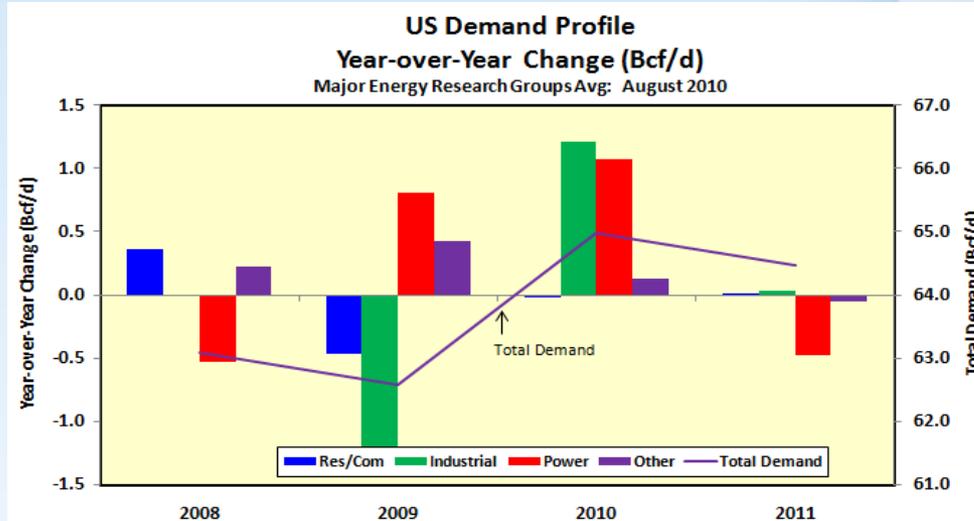
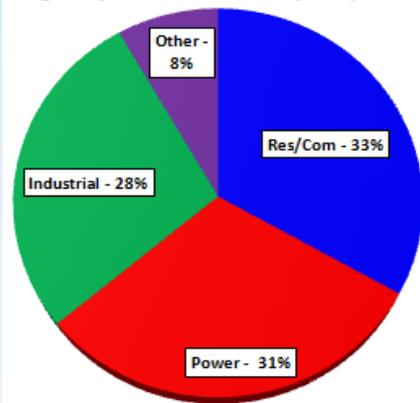


- Natural gas storage inventories were at record highs from early June 2009 to January 1, 2010. Then, as severe cold gripped much of the nation for Dec'09 - Feb'10, inventory surplus was eliminated, as we drew more gas from storage than in any other year since NYMEX started trading in 1990.
- Extended extreme heat over summer put additional pressure on storage fills.
- Projection of storage level at the end of injection season, 10/31/2010, ~3,734 Bcf*, 92% full, not at last year's record (3,807 Bcf).
- Assuming normal weather, storage could test record by end of winter, 3/31/2011.

*Major Energy Research Groups Avg.

US Economic Recovery Could Face Headwinds in Balance of 2010, Followed by Continued Slow Growth in 2011.

2010 US Demand Profile
65.2 Bcf/d, 23.8 Tcf
Avg: Major Research Groups Sept. 2010

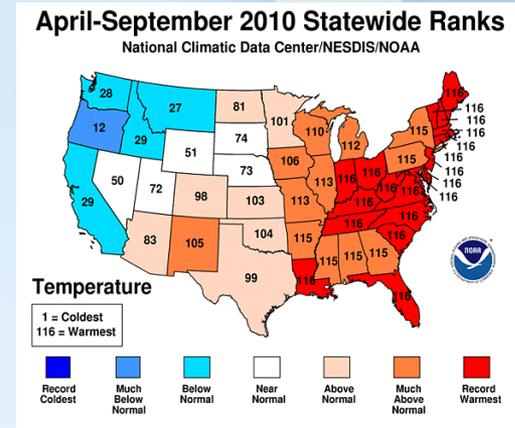


- US GDP Outlook: 2010= 2.6%* & 2011=2.2%*.
- 2010 US Demand: Est. 65.2 Bcf/d*, up 4%; with power demand @ 20 Bcf/d*, up 1.2 Bcf/d, residential and commercial flat @ 21.7 Bcf/d* and industrial demand @ 18.1 Bcf/d*, up 1.3 Bcf/d.
- Expiring government stimulus programs, weakening global demand and new coal fired power generation are expected to pressure demand through 2011.
- 2011 Demand: Est. 65.0 Bcf/d with
 - Power Demand : Down .3 Bcf/d*.
 - Industrial Demand: Flat*.
 - Res/Com Demand: Will remain weather driven and continue to be a wild card going forward.

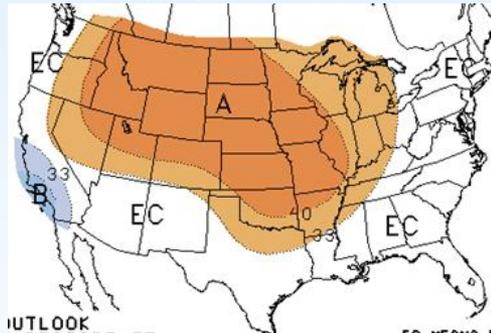
Natural Gas Demand: Weather

Weather is Always a Wild Card

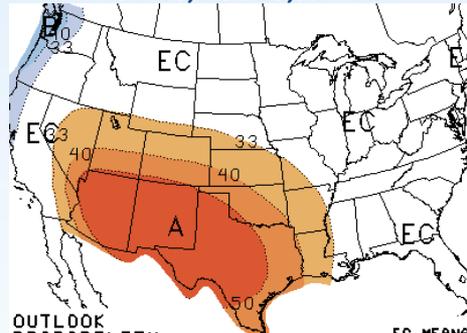
- Winter 2009/2010 was much colder than normal. Summer 2010 has been much hotter than normal. La Nina conditions have developed. Summer seasons that feature a swing from El Nino to La Nina conditions tend to average hotter and drier than normal.
- The longer-term weather forecast thru winter is expect to average normal temps Winter 2010/'11 in major heating regions.
- Latest NOAA Forecasts: September 16/30, 2010:



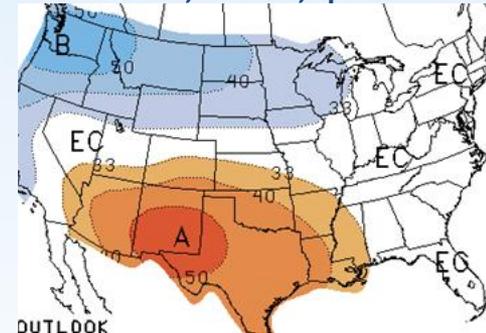
Oct'10



Nov'10, Dec'10, Jan'11



Feb'11, Mar'11, Apr'11



- Hurricane season is winding down with 16 named storms and 9 hurricanes to date, but none impacting the GoM. Drivers include transition from El Nino to La Nina and unusually warm tropical Atlantic sea surface temps.

Major Drivers Through 2010/2011

- Further impact of the economic recovery, or additional economic weakness/strength on demand, particularly in the industrial sector.
- Storage: Current end of injection season (10/31/2010) est. @ 3,734 Bcf, 92% full.
- Storage Withdrawals: Current end of winter (3/31/2011) est. @ 1,836 Bcf, 45% full.
- Winter weather: Forecasts/actual, as well as remainder of season hurricane activity.
- Timing of further shale drilling recovery/pullback, and its impact on US production.
- LNG Imports, as new global capacity comes on line. Potential of “dumping” in US remains low.
- New coal fired power generation coming on line 2010/'11, displacing natural gas.
- Speculative activity, with net speculative short positions near record highs. Abrupt closing of positions could be bullish for prices.

*Major Energy Research Groups Avg.

Thank You

**Further Questions?
Please contact**

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