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In the late spring and early summer of 2004, the U.S. economy is in new territory vis-à-vis energy prices. While media attention has focused primarily on U.S. crude oil and retail gasoline prices, the more important change in energy prices relates to long-term natural gas futures.

Today, NYMEX crude oil prices are over \$40 per barrel — up from about \$31 per barrel last year. Clearly the rise in oil prices has implications for the growth in the world economy. High petroleum prices emerge as a tax on consumption in industrial countries and place added cost pressure on manufacturing and services suppliers. But oil price trends exist in a global market and the competitive burden is largely spread evenly — China, Brazil, India, Japan, the EU and the United States are equally disadvantaged by these trends.

### NATURAL GAS FUTURES AND U.S. GROWTH & COMPETITIVENESS

Much more important to U.S. growth and competitiveness is NYMEX natural gas futures prices — at \$6.28 per million BTU and 6 year futures prices at the same level. Two years ago, prices were at \$3.65/mBTU and in July 2000 at \$2.55/mBTU. Not only are natural gas prices high today, but also long term prospects are for them to stay high.

This is new. The U.S. has managed the specter of rising oil prices at various points, but rising natural gas prices have implications for the de-industrialization of the country, capital investment in the manufacturing sector, and overall economic growth and competitiveness.

In April 2004, Federal Reserve Chairman Alan Greenspan warned of the long-term danger to the U.S. economy, noting that the “shift in expectations” on energy prices has been “substantial enough and persistent enough to influence business investment decisions, especially for facilities that require large quantities of natural gas.” Not only is the U.S. now open to a new

competitive disadvantage that will affect investment patterns, but also there is little prospect that the U.S. will return to previous levels of natural gas supply and prices.

What sets the U.S. apart in this dynamic is that rising natural gas prices are a problem unique to North America. U.S. supplies are drying up and the expanding U.S. economy is making increasing demands. Other industrialized nations in Europe and Asia have more than adequate supplies of gas originating from Africa, the Middle East, and Russia. Over time, overseas competitors will claim increasing market share in a higher cost production environment. This could affect U.S. competitiveness over time.

### KEY IMPLICATIONS:

- ✓ U.S. industries dependent on natural gas will be more likely to move offshore or simply reduce output as competitive imports take their place. The U.S. chemical, plastics, and fertilizer industries are directly dependent on natural gas feedstock. But many industries like steel, aluminum and automobile manufacturing are dependent on access to low priced natural gas for basic production processes.
- ✓ In 2004, pressure on U.S. electricity prices brought about by sustained increases in natural gas input costs, could for the first time affect U.S. competitiveness on a broader scale than chemicals and steel. With natural gas accounting for 22% of U.S. energy consumption and supplying virtually all the incremental U.S. electricity capacity, declining supplies in a rebounding manufacturing sector means it is realistic to expect upward pressure on wholesale electricity prices in the summer months. This would affect most industrial production across the U.S.
- ✓ Companies in the energy sector, as well as major industrial energy users should be moving now to both assess their dependence and risk exposure and, if appropriate, develop a strategic plan to protect the company, its customers and its shareholders against this contingency.