

The View From Washington

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Washington and the world in transition

- **Fundamental shift: the Obama Administration**
- **Despite talk of “green shoots,” the economic situation is grim**
- **Foreign policy**
- **Energy and environment**
- **Conclusions**

Fundamental Shift: The Obama Administration

- **Sea change in US politics:**
 - the end of Reaganism/Thatcherism
 - Americans looking to government for solutions
 - But they will still resist taxes
- **Significant political power**
 - Election margin confirms desire for change
 - Large House majority—and Republicans in disarray
 - On the way to 60 Democrats in Senate
- **Focused, disciplined**
- **Tight core team from Chicago**
- **Hired best Clinton administration veterans, and some non-Democrats**
- **Obama has vision; capable people to implement it**

Implementing the vision: key appointments

- **Hillary Clinton, Secretary of State**
- **General Jones, National Security Advisor**
- **Timothy Geithner, Treasury Secretary**
- **Tom Daschle, Health & Human Services**
- **Rahm Emanuel, Chief of Staff**
- **Larry Summers, National Economic Council**



Aims to govern capably from center/center-left

Obama: doing what he promised



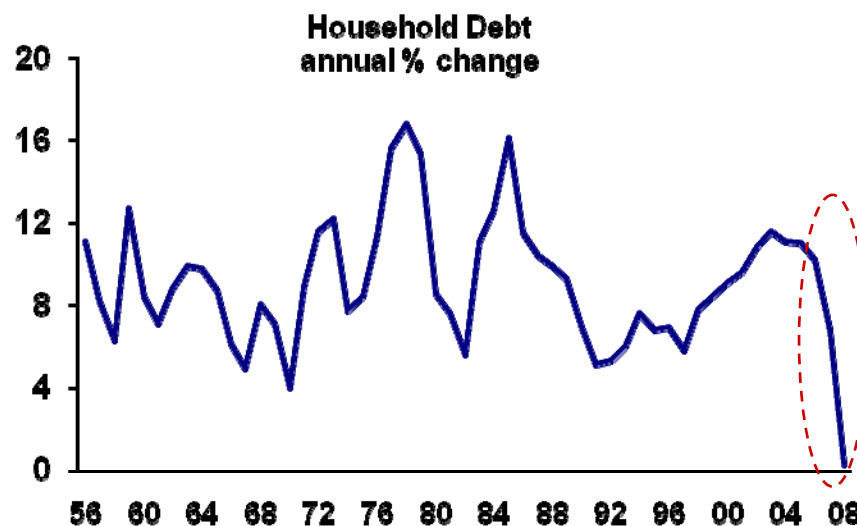
- **Very different political philosophy from prior administration**
 - Clear, long-term vision and goals: take him at his word
 - More comfortable with expanded role for state with companies and sectors
- **Result: Washington is much more important than before from political/regulatory/economic point of view**

The Economic Situation

US consumers finally stopped spending and businesses ran down inventory

- **Radical change in behavior of US consumers:**
 - Personal consumption expenditure is falling rapidly
 - Savings rate has rebounded sharply
- **One drastic response: new car sales were 17 million in 2006, 13 million in 2008, JD Power projects 11 million in 2009**
- **Inventory de-stocking appears to have ended and a modest rebuild expected in the next two quarters**
- **But, real recovery awaits an increase in underlying demand (not just inventory rebuild)**

Gross Household debt includes inflation and population growth: Q3 2008 decline the first since 1952



Stimulus package having little immediate effect

- **\$787 billion for fiscal stimulus**
 - 1/3 is earmarked for tax reduction
 - In 2008, consumers spent 20% of their tax rebate and saved the rest
 - 2009 rebate also likely to be saved, effectively moving debt from private to public sector
 - \$500 billion in direct government expenditure is spread out
 - Only \$100 billion (.7% of GDP) in 2009
 - \$225 billion in 2010, declining thereafter
 - **This may not create much stimulus in 2009**

US economy starting to bottom out, but a bounce is not a recovery

- **Idle manufacturing capacity is at the highest rate since 1951, when measures started; business investment will continue to decline but not at the same rate**
- **New housing starts fell for the 13th consecutive quarter, or some 70% since the peak. This may be the bottom**
- **Consumer credit total is still shrinking. Minor uptick in Q1 was a bounce, not a recovery**
- **The rundown in inventories is emptying the pipeline, so some upturn is inevitable**
- **The \$787 billion stimulus package will help but limited impact in 2009**

First quarter US GDP was (6.1%) although rate of decline is slowing

US GDP % Growth				
2000	3.7%			
2001	0.8%			
2002	1.6%			
2003	2.5%			
2004	3.6%			
2005	2.9%			
2006	2.8%			
2007	2.0%	PFC Energy Scenarios		
2008	1.1%	Evolutionary	Protectionist	Transformative
2009	~ (3.5%)	(2.0%)	(4.0%)	(5.0%)
2010		0.5%	(3.0%)	(2.0%)

- Prior US recessions were not as long or deep
 - 1982 US GDP (1.9%); rebounded to 4.5% in 1983
 - 1991 US GDP (0.2%); up to 3.3% in 1992
- In the Great Depression, US GDP fell (30%) from 1929 to 1933

Economic/financial crisis competes for attention with key long-term policy challenges

- Iraq/Afghanistan
- Middle East
- Health care
 - expensive, mediocre, unfair
- Immigration
- Funding Social Security
- Energy/environment
- Education

The National Debt is **\$11.3 trillion!**



Foreign Policy

Obama Administration has a more realistic foreign policy

- **Avoiding disruptions with China, Russia**
- **Raising human rights, but not as #1 priority**
- **The outstanding foreign policy challenge is Afghanistan/Pakistan:**
 - Obama has not changed policy as much as hoped/expected
 - If nothing changes, there will be failure
- **Israel-Palestine (and Iran)**
 - A grey swan to convulse oil markets would be Israeli raid on Iran
 - US-Israel relations have been driven by the US conservative Israel lobby allied with sympathetic evangelicals
 - Obama is so strong politically that he has more leeway

Energy and environment

- **Energy/environment is one of three key domestic policy initiatives, together with health care and education**
- **Campaign promises:**
 - Reduce dependence on foreign oil
 - Regard solving energy/environment challenges as an opportunity; invest \$150 billion over 10 years to create 5 million green jobs
 - Take climate change seriously:
 - Establish national Low Carbon Fuel Standard
 - Begin serious transition to renewable power: 10% by 2012, 25% by 2025
 - Establish cap and trade system for CO₂ with 100% auctioned permits
 - Clean coal: Invest to create five commercial scale power plants with CCS
 - Re-engage internationally on climate change
 - Eliminate all oil and gas tax loopholes
- **Major changes:**
 - EPA restored to power—and will act if Congress does not
 - Staffing of Energy, Interior, EPA, etc.
 - Henry Waxman replaces John Dingell as Chair of House Energy and Commerce Committee

Changes planned/underway on many fronts

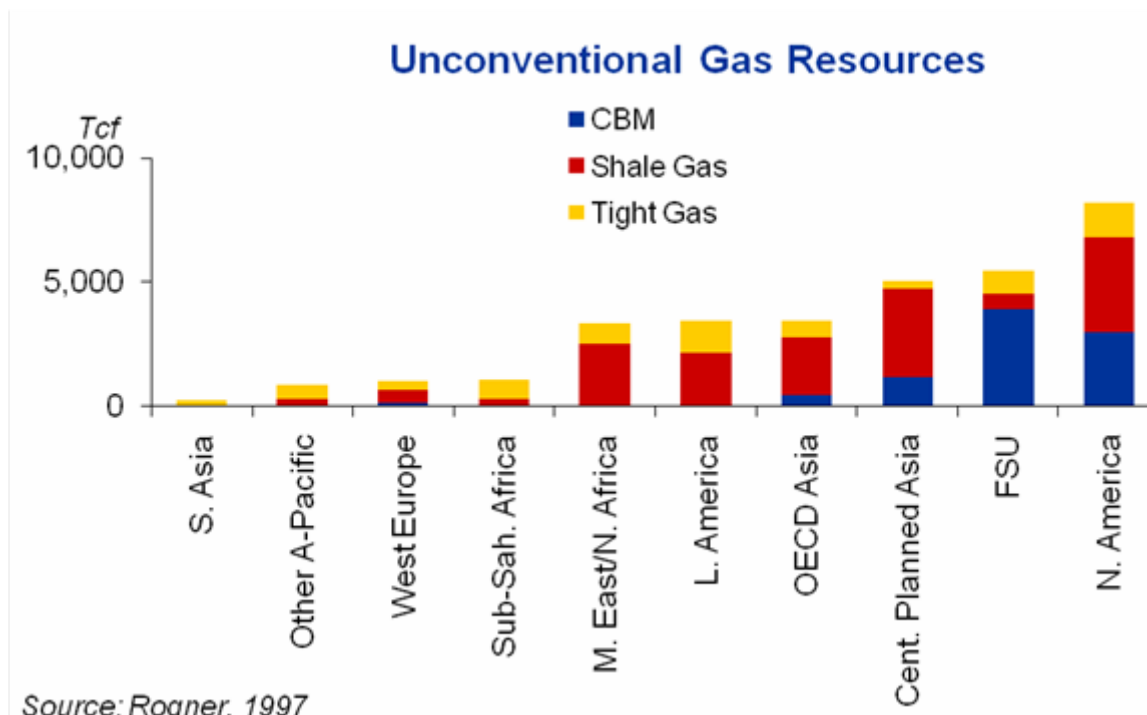
Action/Policy	Challenges	Mitigating factors
Accelerate CAFÉ standards to achieve 35.5 mpg and 250 mg per mile by 2016	Design/build/adoption of flex fuel and hybrid vehicles	Bankrupt auto companies in no place to resist
Continuing push for alternative fuels	Technology and cost of cellulosic ethanol, flexfuel vehicles	As the “marginal barrel” alternatives can influence oil price
Waxman-Markey CO ₂ cap and trade bill	Increasing costs for consumers, utilities	Generous free allowances to start
Renewable fuels standards for utilities	Technology, scale, cost, reliability of wind/solar	Nuclear?
Green jobs, “turning inspiration into innovation”	Cost per job, displacement of (more?) old jobs	Political support from rust belt, labor
Efficiency, smart grid	Up-front cost, technology	
Clean coal	Time, money, technology	

The energy/environmental policy outlook

- **Most serious US companies believe carbon constraints are coming and want a stable, predictable regime**
- **But the US' advocacy system of government means that the vested interests with lobbyists tend to drive policy:**
 - Pushing technologies rather than outcomes
 - Excessively focused on interests of farmers, utilities, others with strong advocacy
- **Carbon cap and trade bill will probably pass the House, in 2010 if not in 2009, BUT**
 - Rural/agricultural lobby may oppose it in senate
 - Senate will want to see China/India engaged in limiting climate change
- **Convergence between transportation and power will come—but major impact will take 20 years; cannot afford to overlook short/medium term**

So much focus on distant future that we may miss an important energy story: unconventional gas

- US has an enormous resource of unconventional gas (shale, CBM, tight gas)—resources of 8,000 tcf, equivalent to the world's total proven oil reserves
- Small, independent companies have found efficient ways to drill and produce it, which significantly changes the US energy picture for gas (and LNG)



Conclusions

- **Americans now look to Washington for solutions for the first time since Ronald Reagan. First watershed since 1980**
- **They elected Barack Obama because they liked his vision**
- **He is a very smart man and surrounds himself with capable people**
- **Most Americans really want Barack Obama to succeed**
- **The financial crisis and Afghanistan/Iraq distract to some degree from important long-term policy goals, but it is vital to get these right**
- **Energy/environment policy driven by some unrealistic hopes, but more dynamic than in many years**
- **US advocacy system of government has not changed, so implementing policy is a messy and often uncertain process**



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Main regional offices are shown in blue.

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