



Welcome to the second issue of Fuel Focus. This report, intended for a broad audience, is a new product from Natural Resources Canada. The objective will be to provide readers with regular information on the various aspects of the gasoline market in Canada and to raise awareness of the economic drivers influencing prices. Previous issues will be available on our website at http://www.oppi.gc.ca/index_e.cfm

National Overview

Retail Gasoline Prices peak at 110.6 cents per Litre

The Canada-average retail gasoline price increased by 1 cent per litre to 110.6 cents per litre for the week ending July 18th, up from 109.6 cents per litre in the previous week.

The trend in higher retail gasoline prices followed overall wholesale gasoline prices which were approximately 17.1 cents higher on July 18th than at the same time last year.

Higher retail gasoline prices were pushed by increases in wholesale gasoline prices which were in turn driven by record crude oil prices. The recent conflict between Israel and Lebanon further contributed to increased speculation that the struggle could escalate to oil producing countries in the Middle East, resulting in potential supply shortages. These factors, along with increasing demand, are expected to continue exerting upward pressure on prices.

Diesel fuel and furnace oil prices remained fairly stable with less than 1 cent per litre variations from last week.

Recent Developments

- Statistics Canada data indicate an increase in sales of motor gasoline of 1.1%, or 38,900 cubic metres, in May 2006 compared to same period last year.
- Canadians have not yet significantly changed their driving habits despite higher gasoline prices according to a Statistics Canada survey which reported an increase in kilometers driven.
<http://www.statcan.ca/Daily/English/060717/td060717.htm> (Canadian Vehicle Survey - 2005)
- The Quebec Government plans to introduce a tax on all types of hydrocarbons to be re-directed towards climate change remediation measures.

Figure 1: Crude Oil and Regular Gasoline Price Comparison (National Average)

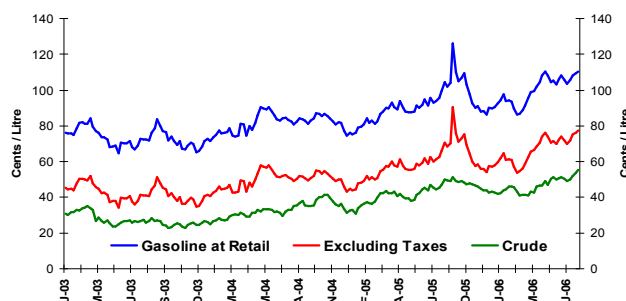
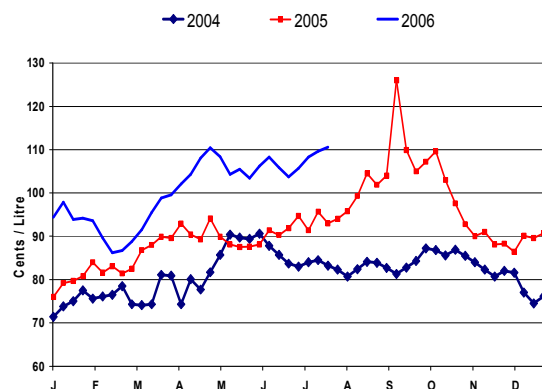


Figure 2: Weekly Regular Gasoline Prices



Changes in Fuel Prices

¢/L	Week of:	Change from:	
	2006-07-18	Previous Week	Last Year
Gasoline	110.6	+1.0	+17.6
Diesel	101.9	+0.5	+8.6
Furnace Oil	84.8	+0.3	+6.0

Source: NRCan

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Retail Gasoline Overview

The average Canadian pump price in selected cities for the four weeks ending July 18th was \$1.09 per litre, an increase of 3 cents per litre from the July 4th report, compared to 94 cents per litre during the same period in 2005.

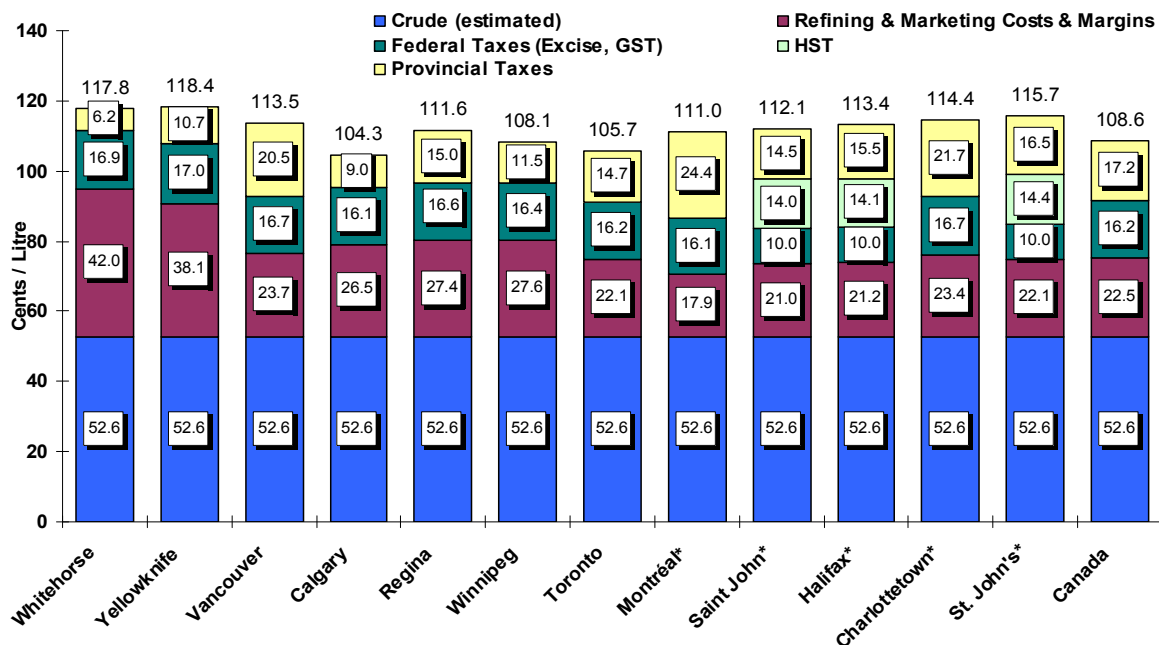
The four week average crude oil price, at 52.6 cents per litre, has risen by 2.3 cents per litre since the last report, an increase of 7.2 cents per litre from the same period last year. With all markets in Atlantic Canada regulated since July 1st, higher crude oil prices did not flow through to consumers and industry margins were reduced.

The higher combined refining and marketing costs and margins in the Territories is largely a function of the higher cost related to the transportation of the refined product and lower throughput efficiency.

The latter is a function of the lower volume of gasoline sold in northern regions and the relatively few gasoline stations which result in higher marketing costs.

As Figure 3 indicates, higher provincial taxes in the East offset the lower margins. Overall, provincial sales taxes including the provincial portion of the Harmonized Sales Tax (HST), where applicable, averaged approximately 17 cents per litre in Canada. Provincial taxes averaged 22 cents per litre of gasoline for the central to Eastern cities (Toronto to St. John's) while the similar tax component averaged 12 cents per litre in Territorial and Western cities (Whitehorse to Winnipeg).

Figure 3: Regular Gasoline Pump Prices in Selected Cities
4 Week Average (June 27 to July 18, 2006)



Source: NRCan

* Regulated Markets

Regional Variation in Gasoline Prices

Gasoline pricing generally depends on a number of factors such as taxes, local market conditions, outlet population and the number of competitors in a given region. One of the primary drivers for gasoline pricing is the average volume of sales per outlet in a particular market. This explains why prices may differ from area to area or station to station. An outlet with lower sales volume may have to charge a higher price to generate sufficient revenue to cover the fixed operating costs. Cities with low average throughputs usually require larger retail margins than those that have a large average throughput. Because the retailer with the lowest marginal cost often sets the price for a particular market, the average throughput helps to explain why outlets in small communities tend to have higher prices than retail outlets in large centres.





Wholesale Gasoline Prices

Most selected Canadian cities followed similar trends to their U.S. counterpart with wholesale gasoline prices rising in the last two weeks by 2 to 3 cents per litre. Increased demand for gasoline associated with the summer driving season and higher crude oil prices forced rack prices up across the country.

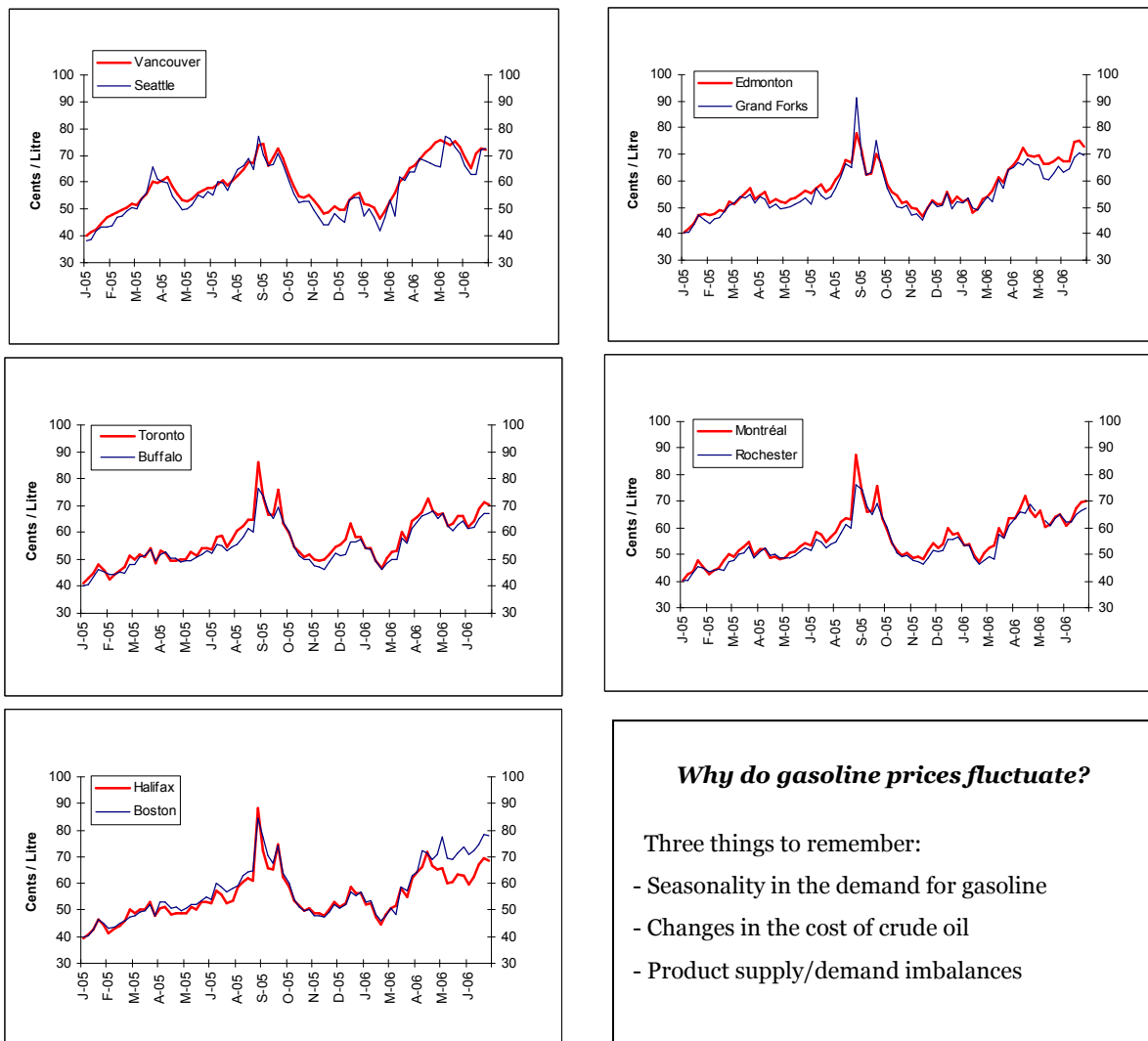
The upward trend was partially reversed the week of July 13th with most of the centres depicted below registering modest declines.

Seattle registered the largest two week increase rising by almost 10 cents per litre between June 29th and July 13th, closing the gap with Vancouver prices that had widened to almost 8 cents per litre in recent weeks.

As reported in the last issue, Boston prices continue to draw a premium over Halifax, as terminal operators adjust to the transition from using methyl tertiary butyl ether (MTBE) in reformulated gasoline. Although following similar movements in recent weeks, Boston's prices are almost 10 cents per litre higher than those in Halifax.

Figure 4: Wholesale Gasoline Prices

Rack Terminals Prices for Selected Cities on July 13th (Can ¢/L)



Sources: NRCan, Bloomberg.

Why do gasoline prices fluctuate?

Three things to remember:

- Seasonality in the demand for gasoline
- Changes in the cost of crude oil
- Product supply/demand imbalances





Refining and Marketing Margins

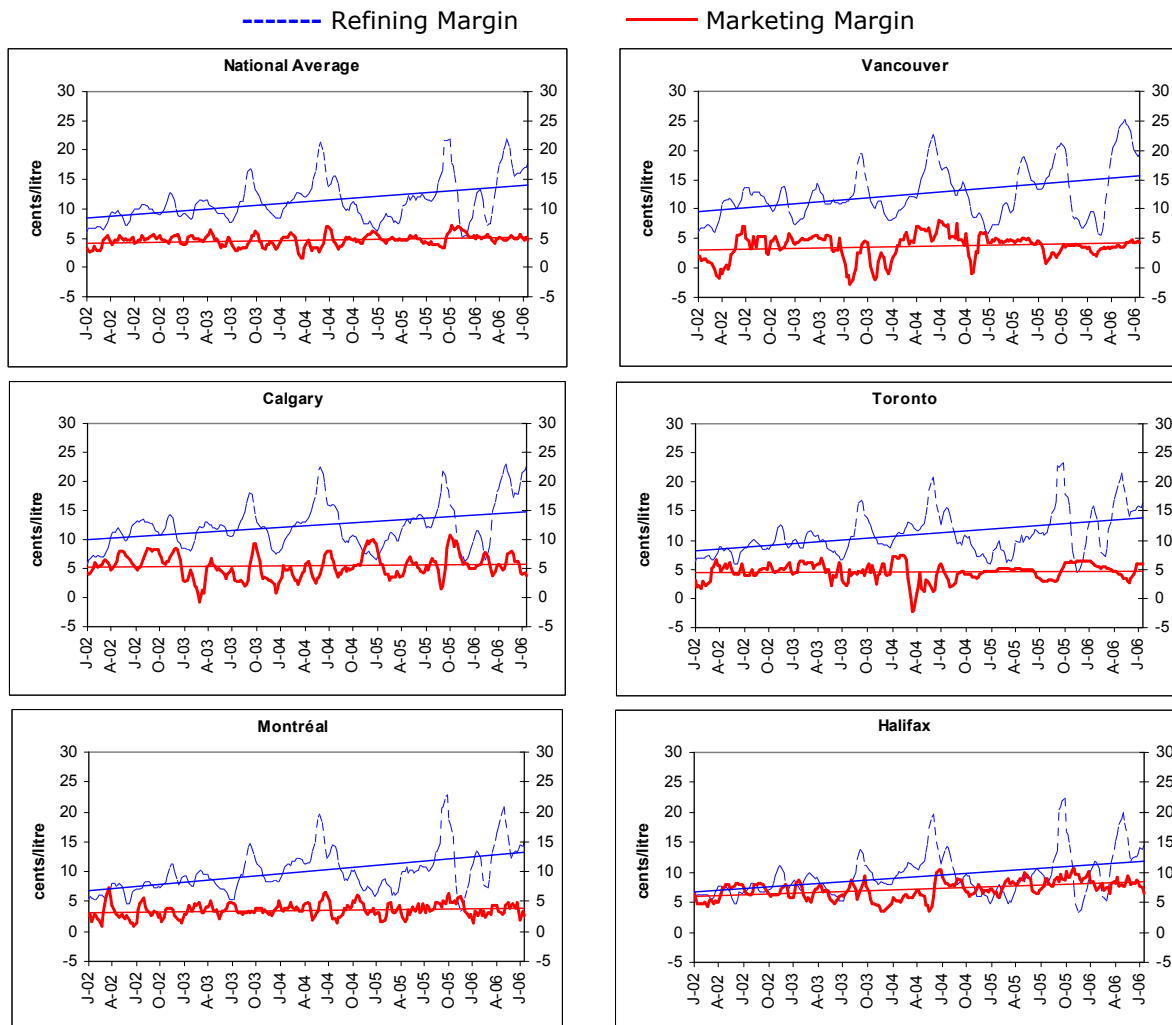
Marketing margins continue to be fairly stable over the last few weeks across Canada while the refining margins tend to fluctuate more widely in response to the specific supply and demand market constraints of each region.

For the purpose of this report the refining and marketing margins calculations are based on a four week rolling average of crude oil prices, gasoline prices excluding taxes and gasoline rack prices. Usually, refining margins show more volatility on a day-to-day basis depending on the gasoline supply and demand in specific regions. These variations tend to last for short periods of time making it difficult to derive any significant correlations. Therefore, the methodology used in the analysis has the advantage of eliminating the wide variability that can be sometimes observed on a daily or weekly basis in favour of a more meaningful trend.

Factors such as the transportation to the demand centres, refinery utilization rates, and concerns over tight supplies in the face of rising demand for gasoline can cause the refiner margin to vary considerably over the short term. More recently, some of these increases in the refining margins are also attributed to the higher costs associated with producing lower-sulphur fuels.

On June 1, 2006, Ultra-Low Sulphur Diesel Regulations were adopted in Canada. These regulations target on-road vehicles using diesel fuel and require companies to clean out the higher sulphur product from the storage tanks before replenishing with new supplies. The new regulatory measures and associated implementation costs also partially contributed to the higher refining and marketing margins affecting all refined products.

Figure 5: Refining and Marketing Margins



Source: NRCan





Crude Oil Overview

Crude Oil Prices Continue to Rise

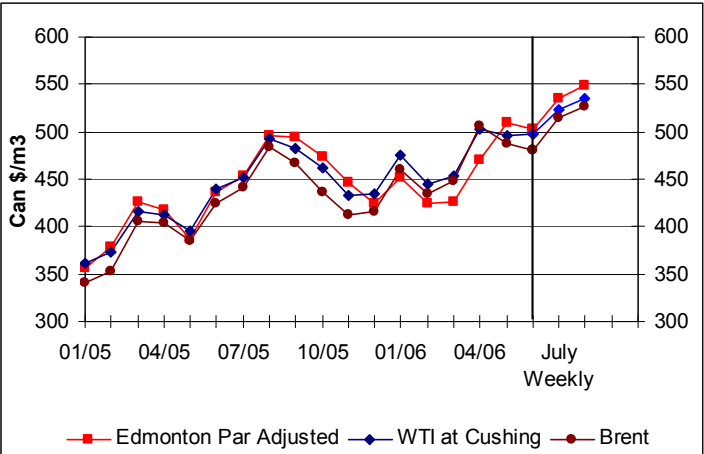
The recent unrest between Israel and Lebanon, although neither is a significant oil producing country, provoked fear that the struggle will spread to nearby oil rich and volatile regions, causing short term oil contracts to close at record prices. In addition, the civil unrest in Nigeria and Iran's refusal to respond quickly to incentives to postpone their uranium enrichment program continue to have a major impact on the petroleum market.

On July 14th the average weekly Edmonton Par crude oil price increased by more than \$2 per barrel (bbl) from the previous week. As shown in the table below, crude oil prices reached \$548 per cubic metre (\$87/bbl) for Edmonton Par compared to \$457 per cubic metre (\$73/bbl) last year.

Meanwhile, the benchmark crude price for West Texas Intermediate (WTI) was \$535 per cubic metre (\$85/bbl), an increase of almost \$12 per cubic metre (\$2/bbl) from the previous week, and \$86 per cubic metre (\$14/bbl) higher than last year.

The Brent crude oil benchmark rose to \$527 per cubic metre, nearly \$91 per cubic metre higher than last year. It is expected that on-going concerns over the potential supply constraints from key crude oil producing countries will continue to keep upward pressure on oil prices.

Figure 6: Crude Oil Price Comparisons
(NRCan data on crude oil prices available on July 14th)



Changes in Crude Oil Prices

Crude Oil Prices (\$Can)	Week ending: 2006-07-14		Change from:			
			Previous Week		Last Year	
	\$/m3	\$/bbl	\$/m3	\$/bbl	\$/m3	\$/bbl
Edmonton Par	548.17	87.15	+13.03	+2.07	+91.53	+14.55
WTI	535.47	85.13	+12.11	+1.93	+86.03	+13.68
Brent	527.09	83.80	+12.16	+1.93	+90.83	+14.44

Source: NRCan

U.S. Federal Trade Commission Report on Gasoline Prices

On May 22, 2006, the United States Federal Trade Commission (FTC) issued a report entitled "Investigation of Gasoline Price Manipulation and Post-Katrina Gasoline Price Increases." The report details the results of an intensive, Congressionally-mandated Commission investigation into whether gasoline prices nationwide were "artificially manipulated by reducing refinery capacity or by any other form of market manipulation or price gouging practices" and into gasoline pricing by refiners, large wholesalers, and retailers in the aftermath of Hurricane Katrina.

In its investigation, the FTC found no instances of illegal market manipulation that led to higher prices during the relevant time periods. In the 15 examples of pricing at the refining, wholesale, or retail level that fit the relevant legislation's definition of evidence of "price gouging", it concluded that other factors such as regional or local market trends, appeared to explain these firms' prices in nearly all cases. Further, the report reiterated the FTC's position that federal gasoline price gouging legislation, in addition to being difficult to enforce, could cause more problems for consumers than it solves, and that competitive market forces should be allowed to determine the price of gasoline drivers pay at the pump.

