



2006 Annual Review

The Fuel Focus 2006 Annual Review presents this year's highlights of the domestic gasoline market. Since its inception in July 2006, Fuel Focus has provided readers with regular information on the various aspects of the Canadian gasoline markets and the economic drivers influencing prices.

In this issue we summarize the events that led to one of the more volatile years in gasoline pricing history.

Highlights

- Overall, 2006 was characterized by a gradual increase in gasoline prices in the first eight months of the year followed by a sharp decline in the latter part of the year.
- The wide price fluctuation in the gasoline market over the last two years was driven mainly by two unrelated sets of factors – the aftermath of the hurricane season in 2005; and the effect of geopolitical uncertainties in crude oil markets in 2006.
- Canadian retail gasoline prices averaged just under 98 cents per litre in 2006 compared to 92 cents per litre in 2005. A notable aspect in 2006 is the fact gasoline prices remained above the \$1 per litre mark from April to late August, the longest period at such a high level in gasoline pricing recent history. Prices ended the year on a similar trend to the last seven weeks of 2005.
- Canadian and American wholesale gasoline prices averaged approximately 60 and 59 cents per litre respectively in 2006, compared to 55 and 53 cents per litre in 2005 respectively.
- Gasoline refining margins continued to be volatile throughout the year, ranging from a high of 22 cents per litre to a low of 7 cents per litre. The average margin for the year was 14 cents per litre, an increase of 2.5 cents per litre over 2005. Nationally, marketing margins fluctuated in a much narrower range (1 to 5 cents per litre) and remained unchanged at 5 cents per litre compared to 2005.
- World crude oil prices for the three crude oil benchmarks reached a peak of \$528 per cubic metre (\$84 Can/bbl) in July, while dropping steadily, in the second portion of year, to a low of \$403 per cubic metre (\$64 Can/bbl). Crude oil prices averaged \$465 per cubic metre (\$74 Can/bbl) in 2006, an increase of \$40 per cubic metre (\$6 Can/bbl) over 2005.

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

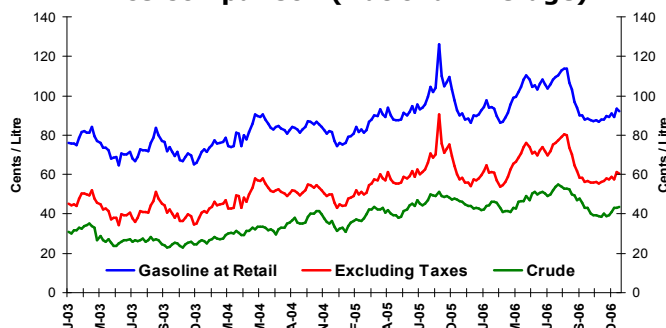
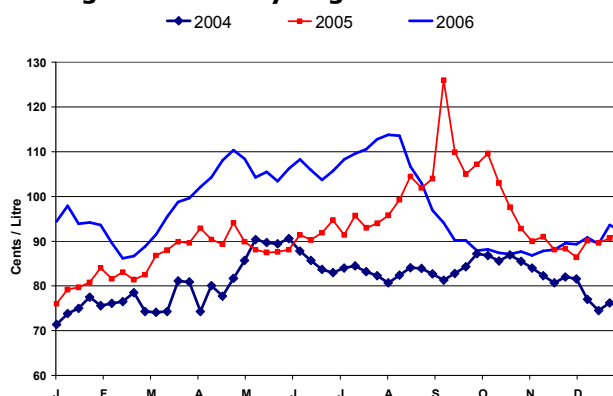


Figure 2: Weekly Regular Gasoline Prices



Changes in Fuel Prices

¢/L	Annual		
	2006	2005	Change
Gasoline	97.7	92.2	+5.5
Diesel	97.1	92.8	+4.3
Furnace Oil	82.5	79.9	+2.6

Source: NRCan

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Retail Gasoline Overview

The annual average gasoline pump price in the selected cities shown in Figure 3 was 97.7 cents per litre in 2006, an increase of 5.4 cents per litre compared to 2005.

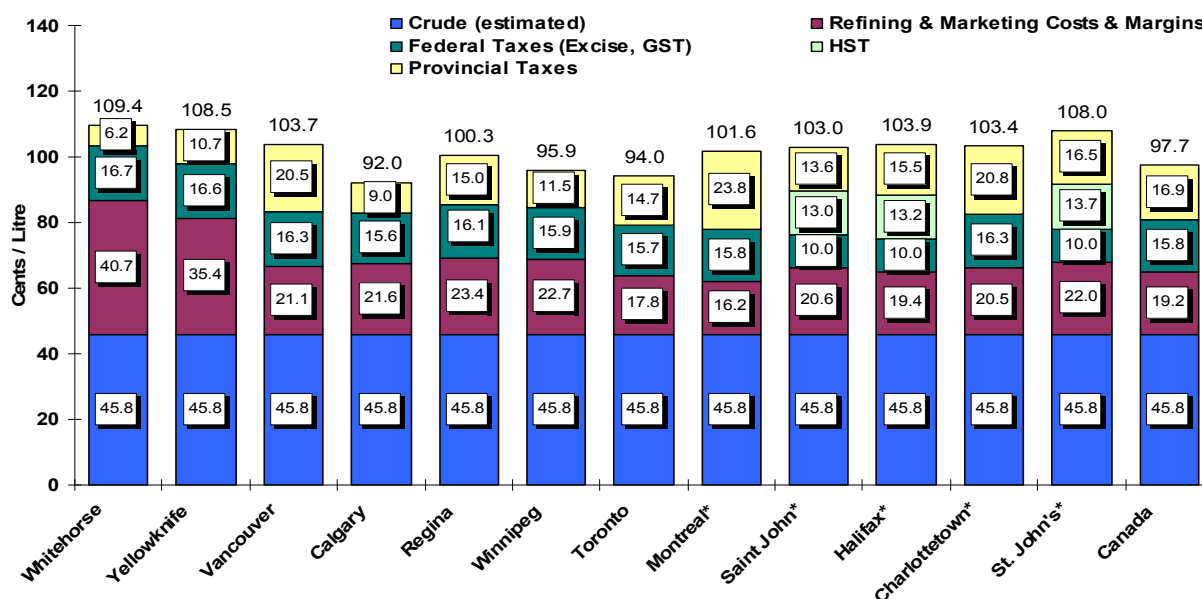
Crude oil, the main pump price component, averaged approximately 45.8 cents per litre in 2006, an increase of 2.6 cents per litre from the previous year. Along with crude oil, the refining and marketing costs and margins component of the pump price also contributed to the rise in the average retail pump price registering an increase of 2.9 cents per litre in 2006 over 2005.

In 2006, federal and provincial taxes accounted for a total of 32.7 cents per litre of the total gasoline price

at the pump, essentially unchanged from 2005, as most taxes are applied at a fixed rate and do not vary with the pump price. The exception was the July reduction of 1% in GST and its impact on the Harmonized Sales Tax (HST) in those provinces where it is applied.

Winnipeg, Regina, Calgary and Vancouver registered on average an increase of approximately 7 cents per litre in gasoline prices in 2006 over 2005 mainly due to higher refining and marketing costs and margins. Charlottetown's regular gasoline prices also ended the year at 7 cents per litre above 2005, partly due to P.E.I.'s provincial taxes. Meanwhile, Yellowknife registered the lowest pump price increase at 2.7 cents per litre in 2006 over 2005.

Figure 3: Regular Gasoline Pump Prices in Selected Cities
Annual Average for 2006



Source: NRCan

* Regulated Markets

Regular Gasoline Pump Price Components in Selected Cities													
Change in Annual Average for 2006 over 2005													
Selected Cities	WH	YK	VA	CY	RE	WG	TO	ML	SJ	HX	CH	SJ's	CA
Provincial Taxes								0.3	-0.9		1.4		
HST									0.3	0.3		0.4	
Fed. Taxes (Includes GST)	-0.2	-0.3				0.1	-0.2	-0.1					-0.1
R & M Costs and Margins	1.4	0.4	4.1	3.8	4.4	3.9	1.7	1.9	2.6	2.4	3	2.4	2.9
Crude Oil	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
Total	3.8	2.7	6.7	6.4	7	6.6	4.1	4.7	4.6	5.3	7	5.4	5.4

Note: The GST was reduced by one percentage point to 6% and the HST also by one percentage point on July 1, 2006. Empty fields means no change in taxes from 2005 to 2006. In Figure 3, for the Canada average, the Federal Taxes component includes the federal portion of the HST, and the Provincial Tax component includes the provincial portion of the HST.





Wholesale Gasoline Prices

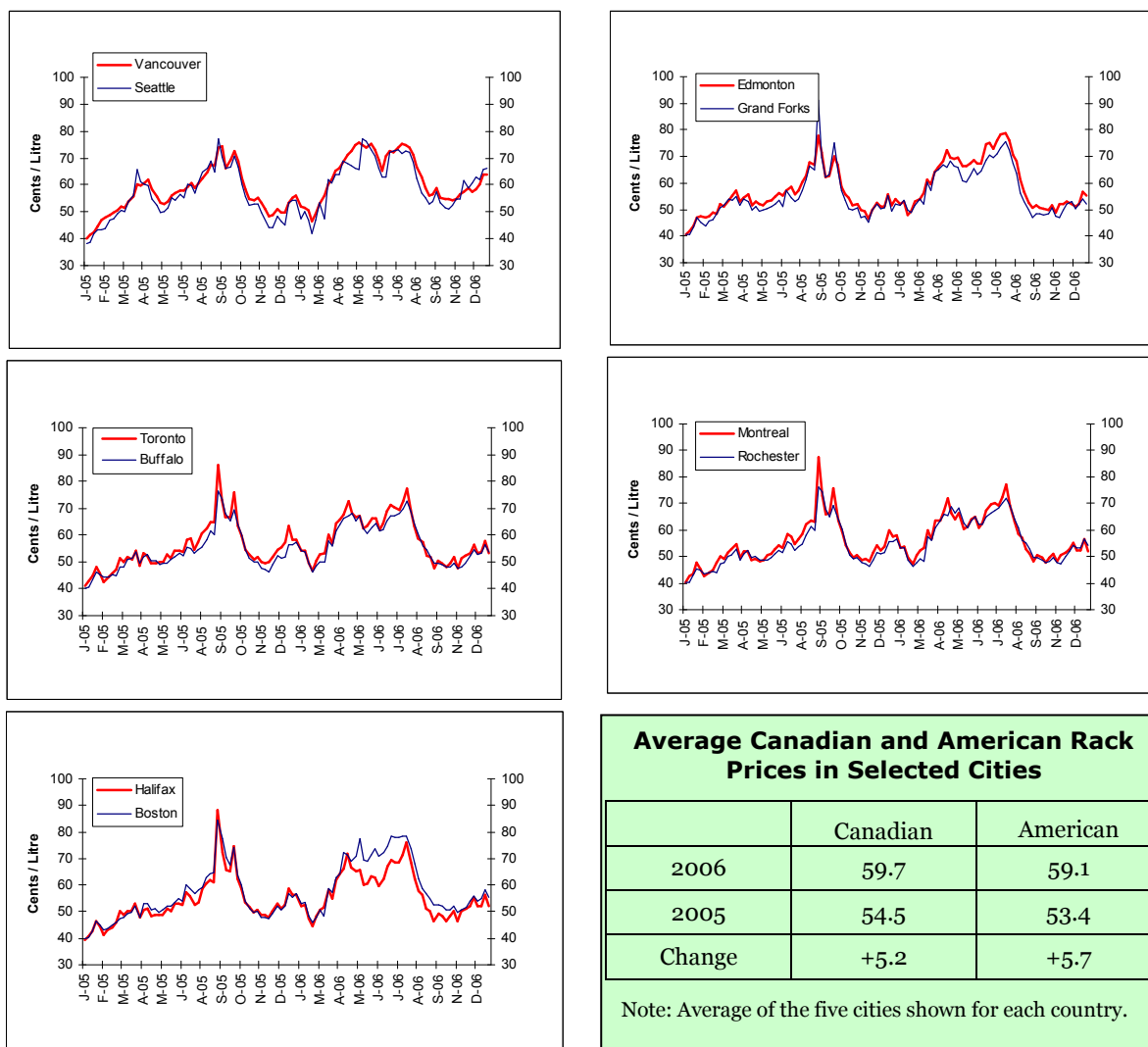
In 2006, wholesale gasoline prices in Canada and the U.S. followed similar trends with the annual average in Canada at 59.7 cents per litre slightly higher than the 59.1 cents per litre in American markets in the selected centres. Although the average Canadian wholesale price was marginally higher than in the American centres, the increase from 2006 over 2005 was slightly higher in American centres which narrowed the gap to some extent between the competing markets.

The graphs show the seasonal variations and the impact of unpredictable supply constraints during the summer driving season. In 2006, prices fluctuated between approximately 47 and 77 cents per litre in the Canadian markets and between 46 and 75 cents per litre in the competing U.S. markets.

Overall, Canadian and American average wholesale gasoline prices followed each other closely. The notable exception was the Halifax / Boston spread from May to August 2006 when Boston terminal operators were adjusting to the transition to ethanol-blended reformulated gasoline.

Most of the selected centres ended the year between the 52 and 55 cents per litre, except for Vancouver and Seattle which saw prices hover above 60 cents per litre. Higher prices on the West Coast, during the latter part of 2006, were mainly due to tighter supplies of gasoline and more limited access to supplies from other regions.

Figure 4: Wholesale Gasoline Prices (Weekly Average)
Rack Terminals Prices for Selected Cities ending December 28th (Can ¢/L)



Sources: NRCan, Bloomberg





Refining and Marketing Margins

Refining margins for gasoline continued to be volatile throughout 2006. Nationally, margins ranged from a high of 22 cents per litre to a low of 7 cents per litre, similar to the 22 and the 5 cents per litre in 2005. Overall, the average refining margins have gradually increased from 9 cents per litre in January 2002 to 13.9 cents per litre in December 2006.

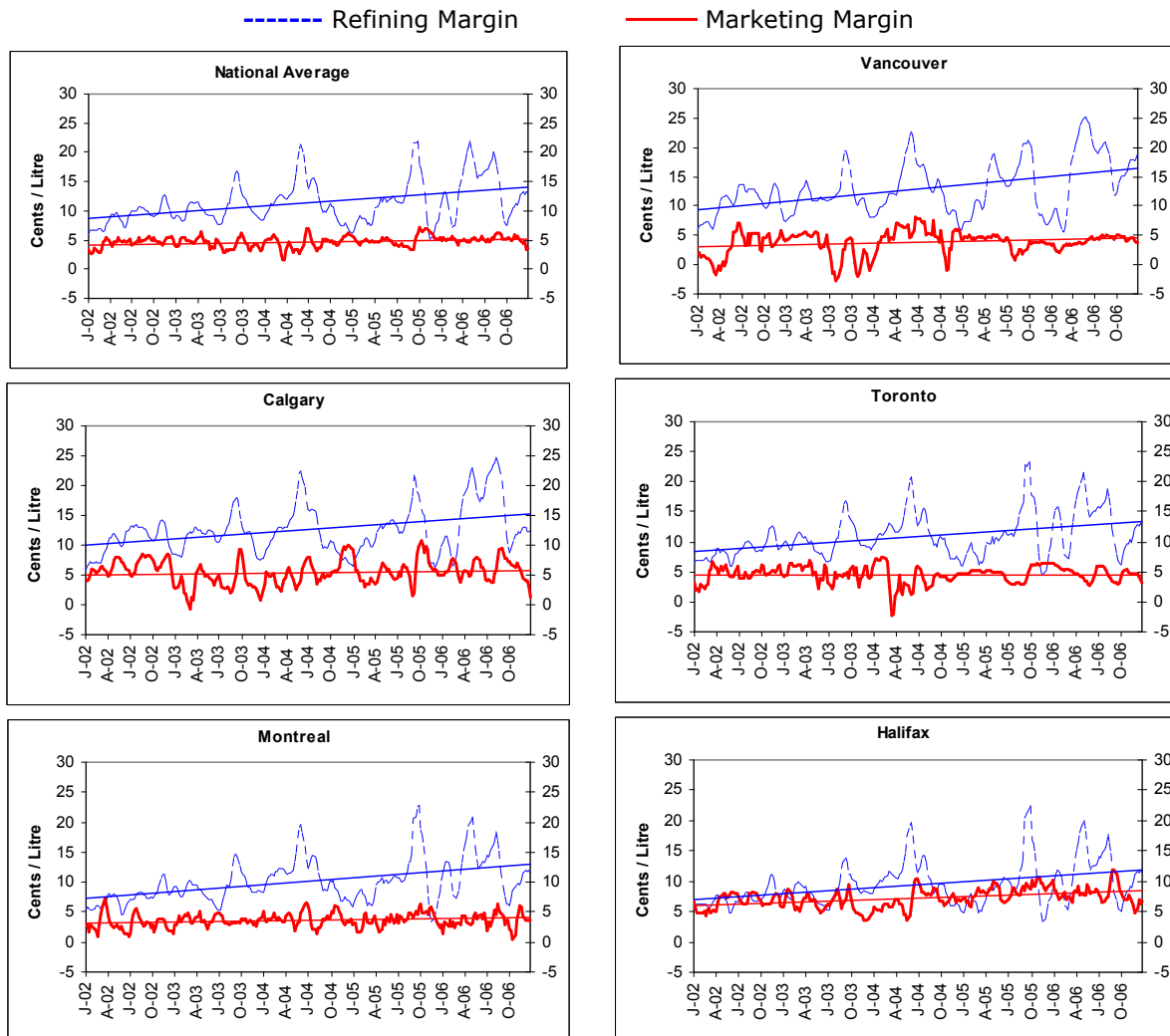
This increase is the result of higher operating costs associated with new fuel quality standards and tighter supply and demand balances for gasoline. On average the refining margins in 2006 were about 2.5 cents per litre higher than in 2005.

With most of the Canadian refineries operating at full capacity, markets have become increasingly vulnerable to even small supply disruptions.

When a short-term supply problem arises, prices will spike dampening demand which helps re-balance the market. This year refiners had to deal with a number of issues ranging from refinery fires, construction delays, electricity supply interruptions due to summer storms and short-term shutdowns to install new equipment.

In general, marketing margins are less volatile than refining margins fluctuating over a much narrower range. At the national level, the average margin remained virtually unchanged from last year at 5 cents per litre. Among the five centres featured in Figure 5, Calgary demonstrated the widest fluctuations with margins moving over 8 cents per litre in 2006, or 1 cent per litre below 2005. Marketing margins in Vancouver, on the other hand, moved within a much narrower range with values of 1 to 5 cents per litre over both years.

Figure 5: Refining and Marketing Margins (Four Week Rolling Average)



Source: NRCan





Crude Oil Overview

The average world crude oil prices, for the three crude oil benchmarks shown in Figure 6, started the year at a relatively high level (\$465/m³ or \$74 Can/bbl) following the aftermath of the hurricanes' devastation of oil producing infrastructures in the U.S. Gulf Coast in the fall of 2005. Following a moderate decline in the first two months of 2006, prices started to increase by the end of the first quarter buoyed by anxiety over supply disruptions and a possible larger than anticipated increased demand for crude oil in the U.S. and China.

The persistent rise in crude oil prices in the first half of the year was influenced by a series of international events which caused significant market instability. These included, amongst others, the Israel / Hezbollah conflict which threatened to disrupt crucial supplies of crude oil from the Middle East; the civil unrest in Nigeria and the closure of important oil producing wells; the Iranian impasse with respect to the postponement of their uranium enrichment program and concerns that any actions against the country might cause havoc in oil market; and concerns over a possible repeat of the 2005 weather-related events in the U.S. Gulf Coast.

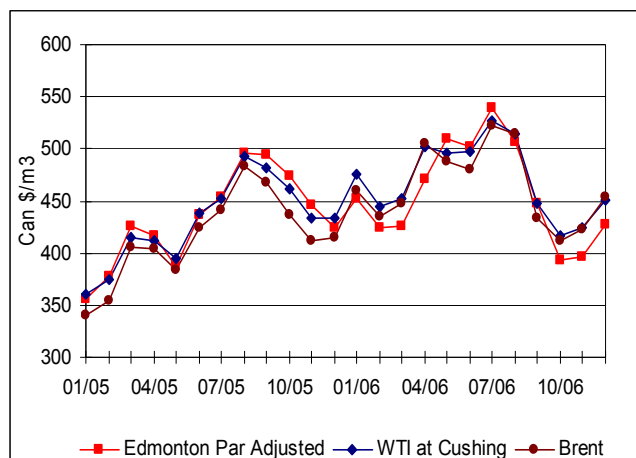
Interestingly, 2006 can almost be divided in half with respect to crude oil prices. After an initial drop in February and March, prices increased at a steady pace in the first half of the year to a peak of \$528 per cubic metre (\$84 Can/bbl) in July, followed by a steady decline to a low of \$403 per cubic metre (\$64 Can/bbl) in the second portion of year. Towards the end of the fourth quarter prices rose again amid speculation that the Organization of Petroleum Exporting Countries (OPEC) would move ahead with their proposed production cuts in February 2007, in an attempt to support crude oil prices.

Prices for the three crude oil benchmarks ended the year in the \$458 per cubic metre (\$73 Can/bbl) to \$471 per cubic metre (\$75 Can/bbl) range, an increase of \$25 to \$41 per cubic metre (\$4 to \$7 Can/bbl) from the average crude price of last year.

Despite ongoing geopolitical and oil supply concerns, global oil reserves continued to grow and world oil markets remain well supplied with crude oil. OPEC had to act to restrain production since global oil inventories continued to rise, reaching record levels. Higher inventories and OPEC's spare capacity provided a safeguard against any disruptions. World oil demand growth in 2006 was somewhat weak at 0.9 million barrels per day (MMB/D) – less than one-third the strong growth of 3.1 MMB/D in 2004, when prices averaged \$41 US/bbl.

World crude oil markets continue to experience a conflict between rising prices and the very strong supply and demand fundamentals of the market (supply is running ahead of demand and crude inventories and stocks are growing). Fears of potential supply outages and speculative investments in oil and other commodities have, in turn, led to upstream exploration and development cost increases that in turn fed back to higher crude oil prices. One other factor keeping crude oil prices rising over the past four years is that although growth has moderated back to more normal levels, demand has not fully responded to higher prices. This is in part due to the growing service component of most developed economies and is evidence that these higher prices may be sustainable in today's global economy.

Figure 6: Crude Oil Price Comparisons



Changes in Crude Oil Prices

Crude Oil Prices (\$Can)	Annual					
	2006		2005		Change	
	\$/m3	\$/bbl	\$/m3	\$/bbl	\$/m3	\$/bbl
Edmonton Par	457.93	72.80	432.49	68.76	+25.44	+4.04
WTI	470.86	74.86	429.40	68.27	+41.46	+6.59
Brent	464.66	73.87	414.19	65.85	+50.47	+8.02

Source: NRCan

