WHO WANTS TO OWN AN OIL REFINERY?

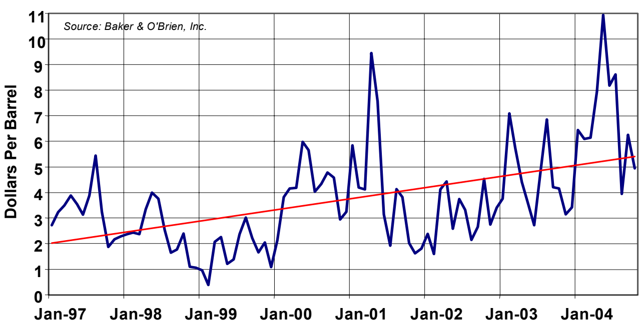
With the corner service station charging $2.00 a gallon or more for gasoline and with oil company reports of record profits, it would seem as if selling an oil refinery would be the last thing on a company's agenda.

Not necessarily so, reports John O'Brien, President of Dallas-based energy consulting firm **Baker & O'Brien, Inc.** "Many operators see today's refining margins as an opportunity to unload aging plants that may require large ongoing investments to meet new regulatory requirements and remain competitive with the integrated oil companies' flagship facilities. I expect that refineries will continue to change hands as different industry players reposition themselves for the years ahead."

WHAT'S HAPPENING TODAY?

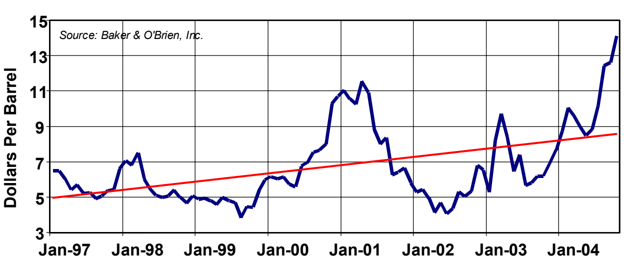
The recent improvement in refinery margins has been dramatic. For years, the crack spread—a benchmark for the difference in the value between refined products and crude oil—was barely enough to pay the operating costs of many refineries. Lately, however, with the "crack" trending higher, previously money-losing refiners have turned into money-spinners. The question is: How long can it last?

U. S. Gulf Coast Crack Spread



According to Mr. O'Brien, "Our analysis shows this year's average refinery profitability is up 25% to 35% compared to the average over the past five years. Refineries with big cokers that can process lots of heavy crude are doing even better because of the large market discount on heavy sour feedstocks compared to light sweet crudes. In particular, West Coast margins have been superlative." Can this be sustained? "Assuming that demand remains strong and there continues to be no large increase in U.S. refining capacity, both the crack and the heavy oil discount can be expected to remain attractive for refiners."

Maya Discount to WTI



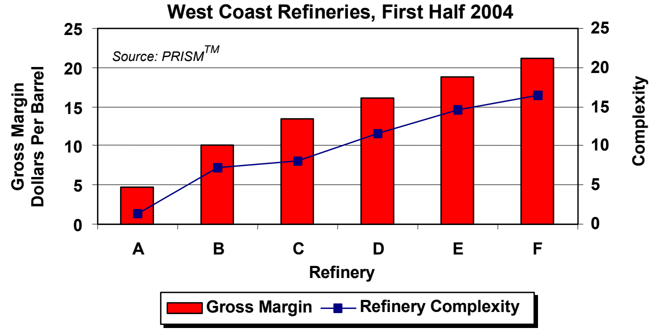
WHO WILL BUY?

If margins do remain attractive, there should be a ready market for refinery assets. Plus, financial institutions that shunned refinery investments for many years are once again funding industry transactions. Interestingly, a large segment of the refining and marketing industry is now in the hands of independent operators that have little or no crude oil production. These companies have grown rapidly by amassing assets considered to be under performing or that had to be divested for anti-trust reasons. Now, through a process of re-structuring, upgrading and cost control, these assets have been turned into highly attractive investments.

Mr. O'Brien notes, "Baker & O'Brien's proprietary ***PRISM***™ refinery industry benchmarking system is used to answer 'what-if' questions regarding refining margin trends, supply and distribution costs, competitive advantages, upgrading opportunities, and the impact of government regulations. ***PRISM*** is also used by independent refiners to uncover situations in which a refinery acquisition might make strategic or economic sense."

John B. O'Brien

Refinery Margin vs. Complexity
West Coast Refineries, First Half 2004



WHO WILL SELL?

As the refining industry adjusts to the new economics, companies will continue to focus on economies of scale, control of operating costs, heavy feedstock capability, and high quality, high complexity assets that yield a high proportion of premium products. Companies will sell refinery assets when, for whatever reason, they are unable to capitalize on these factors or are forced to sell due to a merger or acquisition. In such cases, the new owner may be better positioned to achieve long-term returns.

So, where's the action going to be? Says Mr. O'Brien: "A lot of attention has been paid to smaller, niche refineries that face large investments to meet new emissions and fuel quality standards. However, we believe that there may also be a number of larger and sophisticated refineries that will be put on the auction block in the near future."

If you are going to be in the refining business, is one location better than another? "Absolutely," says Mr. O'Brien. "Our analysis shows that the West Coast and the Midwest can be expected to provide the best returns in the future. However, attractive opportunities may also pop up in other markets as all industry players seek to optimize their returns. Despite the run-up in margins, there should still be some extraordinary buying opportunities out there."