



**E-illumination**  
**March 12, 2006**  
**The Peaking of World Oil Production**  
**Or Life After Fossil Fuels**  
**By Paul Krsek**  
**For K&A Asset Management, LLC**

We start this paper by assuming that most of our readers have never seriously considered that global oil production is peaking, and therefore will be declining into the future. In fact it is likely that you have never even heard of such a concept. The idea that oil production might be peaking is probably new to your lexicon. This supposition presents us with a fundamental problem. While production of oil is in danger of peaking, demand for oil is increasing at the fastest rate in history. Those two conditions do not mix well.

On February 8, 2006, Congressman Roscoe Bartlett of Maryland made a comprehensive report on the topic of “peak oil production” before the United States House of Representatives. He said, “Sometime ago our Department of Energy commissioned SAIC, Science Applications International Corporation, to do a study on the peaking of world oil production, impact mitigation, and risk management.”

“This very prestigious scientific organization took some time to complete this study; and when they completed it, they made a recommendation to the Congress and to the Department of Energy. Part of what they said in their recommendation is included here”:

“The peaking of world oil production presents the U.S. and the world with an unprecedented risk management problem. As peaking is approached, liquid fuel prices, and price volatility will increase dramatically, and, without timely mitigation, the economic, social and political costs will be unprecedented. Viable mitigation options exist on both the supply and demand sides, but to have substantial impact, they must be initiated more than a decade in advance of peaking.

Dealing with world oil production peaking will be extremely complex, involve literally trillions of dollars and require many years of intense effort.”

We are writing this paper because we think this topic is critical for all investors to consider and begin to understand. We are concerned that you will not grasp the gravity of the situation. We hope this paper will help you to understand why we have developed a significant “overweighting” to the energy sector in your investment portfolio. We also hope that we will provide you with insight as to why we have selected the specific energy related investments that are in the portfolios you entrust to us.

Let us start by telling you what the concept of ‘peak oil production’ is.

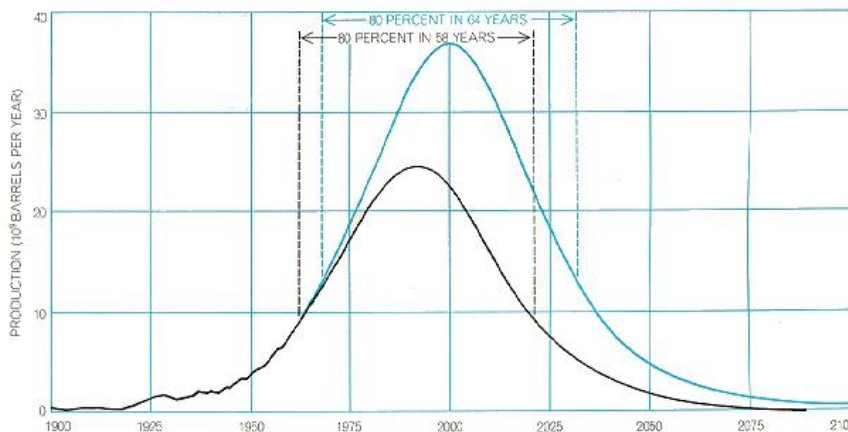
Simply stated, “peak oil production” is “the point in time when extraction of oil from the earth reaches its highest point and then begins to decline”. Oil wells tend to throw off their best production when they are new, and production declines as they age. So at “peak oil production” we are facing a future in which we have less and less oil, year after year, for the world to consume.

The question is, are we already at that point? The frank answer is that no one knows for sure. However, there is a growing body of knowledge that could easily lead a reasonable person to believe that if we have not reached “peak oil production” that it is probably not very far off. The most optimistic estimates that we can find place “peak oil production” out into the years 2025 to 2035. The most pessimistic calculate that we reached “peak oil production” six years ago.

While there may be disagreement on the exact timing of reaching “peak oil production” there is a growing consensus that this is an event that is imminent and that has ramifications that are colossal for the United States and the world.

The United States reached “peak oil production” in 1970 and we have been producing less domestic oil ever since, despite massive drilling that has taken place within the territory and territorial waters of the U.S. Our remaining reserves represent approximately 2 percent of the world oil supply. Yet we produce 8 percent of the world’s current production. That means that we continue to rapidly deplete what little oil we have left. (1)

The late Dr. M. King Hubbert, geophysicist, was well known as a world authority on the estimation of energy resources and on the prediction of their patterns of discovery and depletion. He predicted as early as 1956 that the U.S. would reach “peak oil production”



CYCLE OF WORLD OIL PRODUCTION is plotted on the basis of two estimates of the amount of oil that will ultimately be produced. The colored curve reflects Ryman's estimate of  $2,100 \times 10^9$  barrels and the black curve represents an estimate of  $1,350 \times 10^9$  barrels.

in 1970. When he originally made the prediction his work was widely ridiculed. In the end his prediction turned out to be almost precisely accurate.

In 1971 Dr. Hubbert published a book called Energy

and Power. In it he included a graph that depicted two possible scenarios for the ultimate peaking of world oil production and its subsequent decline. The blue bell curve depicts the more optimistic assumption, with oil production peaking around the year 2000. (2)

Dr. Hubbert died in 1989 so he will never know if his predictive calculations for global oil peak production were as accurate as they were for U.S. peak production.

The following descriptive paragraph appears on a website commemorating Dr. Hubbert's work, "The noted geophysicist M. King Hubbert (1903-1989) was the first man to effectively apply principles of geology, physics and mathematics (in combination) to the projection of future oil production from the U.S. reserve base. The Shell employee and, later, geologist for the U.S. Geological Survey, was a brilliant scientist but was described by contemporaries as sometimes abrasive and having a short temper. He did not suffer fools gladly and was always a center of controversy." (3)

We would imagine that predicting the peaking of U.S. oil production as far back as 1956 would draw controversy, skepticism and even ridicule. In 2006 much of the general public is ignorant of the possibility that global production might be peaking. That condition exists despite the fact that Forbes, Fortune and the Wall Street Journal have all published lengthy articles on the issue. Goldman Sachs and Guinness Atkinson Global Energy Fund have issued "peak-awareness" reports. The likes of T. Boone Pickens and Richard Rainwater have spoken and written extensively on the subject. (4)

Governments around the world are almost universally oblivious to such a possibility, at least officially. The only real exception may be Sweden, which is in the process of planning to make its economy function free of dependence on oil by 2020. (5) That assumes they have that much time left. Certainly investors around the world have not yet focused on "peak oil productions" and its ramifications.

One of the most easily understood descriptions of the current state of global oil supply was published from London on Nov. 16, 2004 in the SolarQuest<sup>®</sup> iNet News Service. The entire text follows:

"World oil supplies are all but certain to remain tight through the rest of this decade, unless there is a precipitous drop in demand, according to the results of a study by the London-based Oil Depletion Analysis Centre (ODAC).

The study found that all of the major new oil-recovery projects scheduled to come on stream over the next six years are unlikely to boost supplies enough to meet the world's growing needs.

ODAC analyzed a total of 68 'mega projects' with publicly announced start-up dates from 2004 through 2010. In total, these projects would add around 12.5 million barrels a day to world oil supplies by the turn of the decade.

"This new production would almost certainly not be sufficient to offset diminishing supplies from existing sources and still meet growing global demand," ODAC Board member Chris Skrebowski said.

More than half of the estimated new supply would simply replace production declines elsewhere due to natural depletion, the study found. A modest one percent annual rise in demand over the six-year period would then leave little or no surplus capacity to cushion against unforeseen disruptions in supply.

If demand were to increase by two percent annually, available supplies could fall short of the total needed in 2010 by more than two million barrels a day – roughly equivalent to losing all of Kuwait’s current daily production.

“With most producers operating flat out to meet runaway demand increases this year, the world’s immediately available spare production capacity has virtually disappeared,” Mr. Skrebowski said. “This means that significant additional supplies in the near-to-medium term must come from new projects already in the development pipeline.”

“We now see those projects providing surprisingly limited relief in terms of incremental supply in coming years, and indeed physical shortages appear ever more likely if demand remains strong,” he said.

“Even with relatively low demand growth, our study indicates a seemingly unbridgeable supply-demand gap opening up after 2007,” he said.

Mr. Skrebowski, who is editor of the UK trade magazine *Petroleum Review*, compiles and regularly updates the details of planned major oil-development projects, as reported by the oil companies. The list contains all announced projects with at least 500 million barrels of estimated reserves and the claimed potential to produce 100,000 barrels a day or greater.

Using that list, ODAC examined three demand-growth scenarios of one, two and three percent a year to illustrate the likely range of outcomes. It also assumed that the combined annual rate of production losses from those countries where output is now permanently declining would remain constant each year, despite evidence that it appears to be accelerating and the likelihood that more producers may go into decline soon.

“The effect of depletion in mature oil-producing regions is now becoming a much more significant factor in the supply-demand equation,” Mr. Skrebowski noted.

According to data from the latest BP Statistical Review of World Energy, 18 major oil-producing countries are now past their peak production, and their combined annual output dropped by over a million barrels a day in 2003. This group of countries now accounts for almost 29 percent of total world production.

The ODAC study did not attempt to forecast when other countries would peak and tip into decline, but experts agree that several more are likely to do so within

the next few years. Mexico and China, the world's fifth- and sixth-largest producers respectively, appear to be among the likely candidates.

Mexico's national oil company, Pemex, has already announced that production from Cantarell, the world's largest offshore oil field, is expected to peak in 2006 and then decline by 14 percent a year. China, too, has confirmed that its two largest producing regions are now in decline. It achieved only modest overall production growth last year of 1.5 percent.

Of the 68 confirmed projects that ODAC analyzed, 56 are due to come on stream in the next three years. Seven are scheduled to start pumping oil in 2008, three in 2009 and just two in 2010. Since it takes, on average, six years from first discovery for a major project to start producing oil, any other new projects approved now would be unlikely to add further supplies until after 2010.

"It is disturbing to see such a dramatic fall-off of new project commitments after 2007, and not more than a handful of tentative projects into the next decade," Mr. Skrebowski said.

"This could very well be a signal that world oil production is rapidly approaching its peak, as a growing number of analysts now forecast, especially in view of the diminishing prospects for major new oil discoveries," he said.

Industry consultants IHS Energy recently reported that 85 percent of all the oil ever discovered is now in production, and only half the total produced last year was replaced by new field discoveries. Annual consumption has now exceeded new discoveries every year since the early 1980s. Overall, worldwide oil discoveries have been declining steadily for the past 40 years."

Even in the face of such comprehensive studies and data there is plenty of denial going on about "peak oil production". Last year the Saudi's suddenly announced that they had twice the reserves that they had ever previously claimed. Here is an excerpt from an article that appeared at <http://news.independent.co.uk/business/news/article315546>.

"Saudi Arabia, the biggest oil producer, and Exxon Mobil, the largest oil company, yesterday declared that the world had decades' worth of oil to come, in an attempt to calm fears about the record prices experienced in recent weeks.

Forming a powerful alliance, the Saudi oil minister Ali al-Naimi said, at an industry conference in Johannesburg that the country would soon almost double its "proven" reserve base, while Exxon's president, Rex Tillerson, spoke of 3 trillion or more barrels of oil that are yet to be recovered."

Despite such denials K&A Asset Management, LLC has reached the conclusion that “it is more likely than not” that the world has either reached “peak oil production” or will within the next few years. We have spent hundreds of hours researching this topic. We have not treated the topic superficially or lightly. We believe that “peak oil production” will have serious economic ramifications including the probability that oil prices will continue their upward trend.

We acknowledge that the trend of rising prices may be interrupted by cyclical and/or seasonal conditions that will moderate prices. However we are convinced that the long term secular trend dictates that supplies of oil will be unable to keep up with currently forecasted demand and that the price of oil will continue to rise for the foreseeable future. We would encourage all our readers to investigate this topic on their own and to reach their own conclusions.

So what are we doing about “peak oil production”? As investment managers we are choosing to invest in energy related companies that are likely to benefit from the rising prices and tight oil supplies. We are also diversifying our investment choices into other energy related companies and industries. In other words we have decided to “spread our bets”. But we have done so with some specific themes and criteria in mind.

We have acquired positions the common stocks of three companies that operate specifically in oil related businesses. They are **ConocoPhillips (COP)**, **Nabors Industries Ltd (NBR)**, and **Canadian Oil Sands Trust (COSWF)**. We have also acquired shares of the exchange traded fund **Energy Select Sector SPDR (XLE)**. The XLE offers investors the opportunity to own one security that offers broad representation of the oil and gas business. On March 11, 2006 its top ten holdings included:

BURLINGTON RESOURCES	<a href="#">BR</a>	4.13%
CHEVRON CORP	<a href="#">CVX</a>	10.97%
CONOCOPHILLIPS	<a href="#">COP</a>	7.83%
DEVON ENERGY CP (OK)	<a href="#">DVN</a>	3.54%
EOG RESOURCES INC	<a href="#">EOG</a>	3.62%
EXXON MOBIL CP	<a href="#">XOM</a>	15.75%
HALLIBURTON CO	<a href="#">HAL</a>	4.79%
OCCIDENTAL PET	<a href="#">OXY</a>	4.51%
SCHLUMBERGER LTD	<a href="#">SLB</a>	4.47%
TRANSOCEAN INC	<a href="#">RIG</a>	3.58%

In addition we have acquired shares of two companies that are businesses primarily related to natural gas. They are **Chesapeake Energy (CHK)** and **Kinder Morgan Partners (KMP)**. and **Encana Corporation (ECA)**

More recently we have also started to acquire shares of one company that is in the solar energy panel business, **Evergreen Solar (ESLR)** and one company that is a uranium mining company, **Cameco Corporation (CCJ)** which provides uranium as fuel for nuclear power.

It is clear that as supplies of oil have tightened and that the price of oil has gone up and that the prices of the oil related stocks have gone up as well. Therefore if one believes as we do that “peak oil production” is either upon us or imminent, it makes sense to have “oil” in your investment portfolio.

As we are drafting this newsletter oil stocks are actually in retreat after rising rather steadily for over two years. All of the oil stocks mentioned in this letter are significantly off their highs, and at least temporarily trending downward, in response to the cyclical perception that oil inventories are sufficient and therefore oil prices are dropping around the world.

If you accept the proposition of “peak oil production” you can’t help but look at the current retreat in prices as a short term cyclical event. The decline in oil stock prices begs the question of whether or not K&A wishes to try to “time the market” and therefore sell any or all of these stocks as they break down through technical support at their 200-day moving averages—or hang on and wait out the probability that they will recover in price and even go higher in the next cycle.

We have already sold Chesapeake Energy and Encana Corporation once before and booked significant profits for our clients who owned them. We have since bought them back. We will be monitoring the stocks on a case by case basis as this portion of the cycle plays itself out.

However, we are committed to these specific stocks for the secular move in oil prices for a variety of reasons.

### ConocoPhillips (COP)

ConocoPhillips is an international, integrated energy company. It is the third-largest integrated energy company in the United States, based on market capitalization, and oil and gas proved reserves and production; and the largest refiner in the United States. Worldwide, of non-government controlled companies, ConocoPhillips has the eighth-largest total of proved reserves and is the fifth-largest refiner. (copy from ConocoPhillips website)

We chose ConocoPhillips over several other large integrated energy companies because we believe they are doing a better job than most of replacing reserves in both the oil and gas arenas. It is our perception that they have outperformed some of their peers in oil and gas exploration; they appear to have solid relationships with foreign partners throughout the world; and they are aggressive and perceptive about strategic combinations to keep their business growing, such as the recent acquisition of Burlington Resources, which

should be completed in the first half of 2006. Burlington Resources ranks among the world's largest independent oil and gas companies, and holds one of the industry's leading positions in North American natural gas reserves and production. Headquartered in Houston, Texas, the company conducts exploration, production and development operations in the U.S., Canada, the United Kingdom, Africa, China and South America.

### Canadian Oil Sands Trust (COWSF)

It is estimated that the oil sands of Canada hold as much oil as can be found in all of Saudi Arabia. The problem is that the oil is actually mixed in the sand and it is extremely expensive to extract. However, recent escalation in the price oil makes the oil sands an economical source of reserves. Canadian Oil Sands Trust is the only public investment vehicle that provides non-diversified ownership in Syncrude, the largest oil sands project in the world. The Syncrude asset offers investors:

**Long-life resource:**

Total resources of 9 billion barrels of Syncrude Sweet Blend. Proven and probable reserves would allow us to produce for more than 35 years at post Stage 3 productive capacity of 128 million barrels annually.

**Production growth with no decline:**

The Stage 3 expansion, scheduled to begin production in mid 2006, is expected to result in a 50% increase in productive capacity to 350,000 barrels per day. Syncrude's future expansions have the potential to increase productive capacity to more than 500,000 barrels per day.

**High-quality, synthetic light oil production:**

Syncrude Sweet Blend is valued by refineries and receives a price in the market that approximates West Texas Intermediate. Following the Stage 3 expansion, Syncrude is expected to improve the quality of its entire production to Syncrude Sweet Premium, which should help North American refiners meet more stringent environmental requirements. (copy from Canadian Oil Sands Trust website)

All of Canadian Oil Sands production comes from Canada, therefore K&A believes that the assets are strategically safer than much alternative production throughout the world. We also believe that the Canadian government is much more able to deal with environmental issues related to exploration for oil than the governments of many third world countries.

### Nabors Industries (NBR)

If you are going to find new reserves, you have to drill. K&A believes Nabors is the class act of the drilling companies. Nabors is the largest drilling contractor in the world, conducting oil, gas and geothermal land drilling operations in the US Lower 48 states, Alaska, Canada and internationally in more than 20 additional countries.

Nabors is also one of the largest well-servicing, workover and production services contractors in the US through Pool Well Services Co., in Canada through Nabors Production Services and in select international markets.

Nabors also provides offshore workover and drilling rigs in the Gulf of Mexico and international markets.

The Nabors companies own and operate almost 600 land drilling and 970 land work over and well-servicing rigs worldwide. Offshore, Nabors operates 44 platforms, 17 jack-ups, and three barge rigs in the domestic and international markets. Nabors markets 30 marine transportation and support vessels, primarily in the US Gulf of Mexico. In addition, Nabors manufactures top drives and drilling instrumentation systems and provides comprehensive oilfield hauling, engineering, civil construction, logistics and facilities maintenance, and project management services. Nabors participates in most of the significant oil, gas and geothermal markets in the world. (copy from Nabors website)

### Chesapeake Energy (CHK)

We became aware of CHK while following insider trading statistics, not while doing specific research on the oil or gas businesses. The single largest shareholder of CHK publicly traded common stock is Aubrey K. McClendon, Chairman of the Board. Mr. McClendon buys CHK stock like many people buy groceries—that is all the time. We are not aware of any other insider buying the stock of his own company as aggressively as Mr. McClendon does.

The second largest shareholder is Fidelity Research and Management, which owns the stock in several of their mutual funds. The third largest shareholder is Tom L. Ward, President of Chesapeake. He buys the stock almost as often as McClendon does.

McClendon and Ward put their money where their mouth is, and then some. The current issue of Forbes Magazine has this to say about Chesapeake, and we couldn't agree more:

“The market's once ardent view of energy stocks has cooled a bit of late. That makes domestic natural gas producer **Chesapeake Energy** (nyse: [CHK](#) – [news](#) – [people](#)) (32, CHK), down from its \$40 12-month high, a decent buy at 13 times trailing earnings. That's only a little more than you pay for BP or ExxonMobil.

What makes Chesapeake special, notes analyst Brian M. Gibbons of CreditSights, is its voracious acquisition program: 66 buyouts since it began in 1989. Focused on drilling in the nation's midsection and Gulf region, the company has built its gas reserves to a comfortable 13-year life. With gas prices likely to stay high, earnings prospects are rosy.”

## Encana Corporation (ECA)

When we started buying Encana's stock they were a much more diversified company than they are today. They could easily have been described as a diversified energy company. Today they are in the latter stages of slimming down to a company that specializes in developing "key resource plays" primarily around natural gas reserves. Encana is currently focused on eight natural gas and two oil "key resource plays". They are all on the North American continent.

At Encana, key resource plays capture huge accumulations of hydrocarbons trapped in unconventional reservoirs. For natural gas this means they must be of the size to be able to ultimately recover greater than one trillion cubic feet of reserves and to grow

In 2005 Encana targeted between 54,000 and 56,000 bbls per day from their two oil resource plays.

Steady, reliable and highly-profitable production growth year after year, is Encana's goal.

Large, known sources of oil and gas are trapped beneath the earth's surface in what Encana calls resource plays. The resource exists over a large real expanse and/or thick vertical section and was long considered uneconomic or a challenge technically. But by bringing together innovative technology and large scale exploitation programs, these resource plays are providing the foundation for long-term, low-risk, predictable and profitable production growth.

Encana's focus on resource plays in North America is fundamental to its target of delivering an average 10 percent per share growth in reserves and production per year for at least five years. (copy from Encana's website)

## Kinder Morgan Energy Partners (KMP)

Kinder Morgan Partners is one of three entities that make up the Kinder Morgan family of companies. The other two are Kinder Morgan, Inc. and Kinder Morgan Management, LLC.

Kinder Morgan Energy Partners, L.P. (NYSE: [KMP](#)) is one of the largest publicly traded pipeline limited partnerships in America. KMP owns or operates more than 25,000 miles of pipelines and approximately 145 terminals. Its pipelines transport more than 2 million barrels per day of gasoline and other petroleum products and up to 8.4 billion cubic feet per day of natural gas. Its terminals handle over 80 million tons of coal and other dry-bulk materials annually and have a liquids storage capacity of approximately 65 million barrels for petroleum products and chemicals. KMP is also the leading provider of CO<sub>2</sub> for enhanced oil recovery projects in the United States. (copy from Kinder Morgan's website)

KMP appeals to us for a lot of reasons, not the least of which is that it operates pipelines that transport more than 2 million barrels per day of gasoline, natural gas, diesel and jet fuel through over 25,000 miles of pipelines. Its revenue stream is fixed to transporting the product, which it does day in and day out, every day of the year. Frankly, KMP doesn't care if oil is selling for \$50 per barrel or \$70 per barrel. It doesn't care if natural gas is trading for \$5 per mcf or \$17 per mcf. Its revenue stream is not tied to the price of the commodity. The revenue stream is merely produced by transporting the commodity.

All of its assets are in North America. Richard D. Kinder is the Chairman and CEO of the three Kinder Morgan companies. His salary is \$0.00 per year. You read that correctly. His total compensation is tied to making the stock price and dividends go up for his investors. We like that. We can't think of another Chairman of the Board whose personal interests are so aligned with his shareholders.

### Evergreen Solar (ESLR)

Evergreen Solar, founded in 1994, develops, manufactures and sells solar power products, primarily solar panels that provide reliable and environmentally clean electric power throughout the world. The three markets the Company serves are: wireless power, rural electrification and grid-connected applications. The Company expects to exploit its proprietary and patented technology to produce distinctive products, to reduce manufacturing costs through lower materials use and streamlined processes, and to manufacture internationally for global market penetration.

The solar panels produced by Evergreen Solar incorporate proprietary crystalline silicon technology known as String Ribbon wafer production, which uses approximately half the silicon and avoids the sawing of conventional approaches.

The whole arena of solar power manufacturers is made up of unprofitable companies including ESLR. While "solar" has been around for many years it has eluded becoming a profitable industry and a significant source of reliable cost-effective energy. That is still true. But federal, state and even local subsidies are increasingly available to entice end-users to install solar power systems. The government is forcing this market to grow. ESLR is one of the most technologically innovative companies in the solar power business.

If current trends related to increasing subsidies and increasing demand continue ESLR should become a profitable company, while continuing to lead technologically in their industry.

## Cameco Corporation (CCJ)

Cameco is the world's largest, low-cost uranium producer accounting for 20% of the world's uranium production. Our mining and conversion facilities in North America provide fuel to the western world's nuclear power plants. Through a partnership, we also generate clean electricity with our share of about 1,500 MW from a nuclear facility in Ontario.

Growing demand for electricity and concern over greenhouse gas emissions is fuelling a rediscovery of nuclear as a clean, reliable and affordable source of base load electricity.

Existing uranium supply is expected to fall short of demand over the next decade demonstrating a need for new primary mine production which will require higher sustained prices. World demand is predicted to outpace existing supply by more than 400 million pounds, between 2005 and 2014. Cameco is positioned to benefit from this shortfall through our control of more than 60% of known new uranium production. (copy from Cameco's website)

### Summary and Wrap Up

K&A believes that oil is going to continue to get scarcer and costlier in the foreseeable future. "Peak Oil Production" is a reality, sooner than later, in our opinion. We only hope that for the sake of society as we know it that we have some transition time available to us before the situation gets absolutely critical.

If you haven't surmised from reading this paper, we will explain to you that it will not take much of a decline in oil supply, given rapidly increasing demand, to shoot the price of oil through the proverbial roof. The total supply available today is approximately 84 million barrels per day. We frankly do not believe that significant excess capacity exists beyond that number. We have seen reliable decreases in the estimates of reserves of companies and whole countries for that matter. We are not aware of any reliable data that would demonstrate a significant increase in global reserves. Therefore, if we are correct in our assumptions, any significant interruption in supply could cause a major increase in oil prices.

The implications for investors in oil companies are obvious. Stock prices will go up. The implications for society as a whole are less obvious and probably not so rosy. The global economy could suffer a blow if prices were to rise significantly from current levels.

We believe the shift to other sources of energy will accelerate as the price of oil increases. We also believe that governments around the world will be spending money and providing incentives to convert to other forms of energy including gas, clean burning coal, nuclear, wind, hydro and solar.

Therefore we have constructed an “energy” portfolio for our clients comprised of the stocks and ETF’s listed in this report. It is our intention to continue adding to the portfolio.

The choices we have made so far include companies whose assets are primarily based in North America. This was a conscious choice that seemed to us to be geopolitically less risky for our investors than other choices we could have made. All of the companies in the portfolio are leaders in their specific fields. They all have management teams that are friendly to shareholders. Even though our portfolio is North America ‘centric’, we have attempted to pick companies and enterprises that minimize exposure to Gulf Coast drilling. We see changing weather patterns in the Gulf to be a greater potential danger to these assets than terrorism. We have also tried to focus on companies that understand the importance of renewing and expanding their reserves. The companies in the portfolio have proven to be quite astute at doing so.

We are trying to insulate our client’s portfolios against the shock of rising energy costs and frankly to take advantage of the phenomena. Readers of this report should note that K&A does not purchase individual stocks in client portfolios of less than \$240,000, so clients with smaller portfolios do not own the assets described in this paper, with the possible exception of the ETF Energy Select Sector Spider (XLE).

If energy prices become too expensive that condition could contribute to a hostile environment for other stock prices and the economy in general. We are constantly monitoring the situation

Paul Krsek

For K&A Asset Management, LLC

March 12, 2006

Footnotes:

(1) Congressman Roscoe Bartlett, Congressional Record, THE PEAKING OF WORLD OIL, House of Representatives, February 8, 2006

(2) See Page 39 of Energy and Power by Dr. M. King Hubbert

(3) See <http://www.hubbertpeak.com/hubbert/>

(4) See page 9, **The Post-Oil Bulletin, Issue #3: Investing in Peak Oil: Strategic Considerations, March 2006, by Adam Cohen**

(5) See The New York Times on the Web, February 5, 2006