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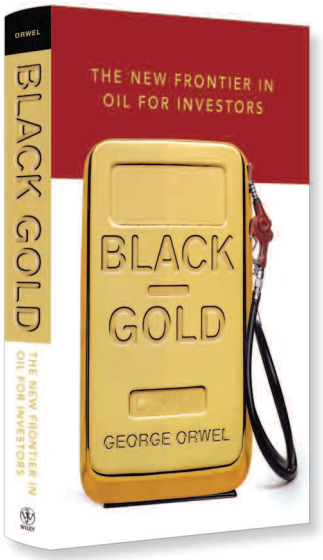
Personal Finance

The New Frontier in Oil for Investors
Black Gold



by George Orwel

THE SUMMARY IN BRIEF

Fossil fuels are the dominant energy source fueling the modern economy, and at least in the short term they will continue to shape our society in the new millennium. There are close to two trillion barrels of proven oil equivalent (boe) stored in rocks around the world, both on- and offshore. In terms of consumption, the United States uses 20 million barrels per day, or 25 percent of the world total, and imports about 60 percent of its oil needs, mostly from Canada, Saudi Arabia, Venezuela, Mexico and Nigeria, in that order.

It is essential to understand how important oil is to our way of life. Oil provides gasoline that powers automobile engines, but we depend on oil for other things as well. About 90 percent of the organic chemicals we use are made from petroleum. These include pharmaceuticals, agricultural chemicals and plastics — all byproducts of oil. As oil prices rise, so do the prices of oil products.

Oil prices started their steep climb in 2004 because of four factors: first, rapidly growing demand from China and India; secondly, the world's major oil-producing countries, mostly in the politically volatile Middle East, have almost maximized their output and have no spare capacity; third, geopolitical tensions have become common, disrupting supply from Venezuela, Nigeria, Russia and the Middle East; and fourth, oil and gas are becoming viable investment vehicles for those seeking wealth.

Major oil companies such as Exxon Mobil, BP and Valero have displaced Microsoft, AOL Time Warner and General Electric from the high table of capitalism. However, instead of mourning the tight market, investors should actually embrace it, at least for now, because there are several years ahead to enjoy the boom. Oil stocks, whether in oil exploration or refining companies, are doing so well that market analysts discount any possibility of a meltdown.

IN THIS SUMMARY, YOU WILL LEARN:

- The basics of the oil industry.
- The consequences of an oil peak for today's society.
- The possibilities that alternative fuels offer.
- Why energy is such a hot commodity.
- How to benefit from high oil prices as an investor.

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THE COMPLETE SUMMARY: **BLACK GOLD**

by George Orwel

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The End Of An Era?

With oil prices on a stratospheric flight, many traders and investors are finally taking notice. The stock market already is: Oil stocks were higher than other equities in 2006. The oil stock gains have been seen all around the world, not just in the United States. Everyone, from professional economists on Wall Street to ordinary consumers, has been wondering why oil prices are so high and continue to rise. For an answer, they should look no further than economics, geology and politics.

While oil demand is rising, supply is struggling to keep pace. The availability of cheaply exploited oil has been reduced. There are still a lot of oil reserves in some parts of the world, like in the deep waters off West Africa, in arctic Russia and in the Middle East, but there are problems as well: The cost of drilling in hard-to-reach areas like the offshore Black Sea, the Gulf of Guinea and the Gulf of Mexico is sometimes prohibitive and superior technology is required; security is tenuous in places like Iran, Iraq and Saudi Arabia; and most of the readily available oil is of the low-quality heavy, sour type, which is expensive to process into gasoline and other products. High-quality light, sweet oil, which yields more gasoline, is in short supply, and most of the old refineries in existence have not been fitted with coking units that can process the heavier crude.

Another problem is that since the early 1990s, oil companies have not invested enough in expanding their infrastructural capacity, both in oil production and in refining. Oil executives say they couldn't invest because they had no money, as oil prices were low until the shock demand of 2004 boosted prices. They say the high oil prices have given them a shot in the arm, and a number of projects are in the pipeline — however, these projects will take time to come onstream.

An Oil Debate That May Determine Who is Top Dog

You should know from the outset that whenever experts talk of an oil peak, what they generally mean is that from then on, production will gradually slide down the slope toward the last drops at the rate of about 2 percent annually. The current oil-peak debate started around 1995 but stayed off the radar because it was drowned by the tech boom of that decade. Moreover, oil-peak theorists have warned that the decline of world oil output will force oil prices higher for good, the effects of which could be catastrophic.

However, it should be noted that the amount of oil that is recoverable under normal conditions also varies by each type of field. Some fields end up recovering as much as 65 to 80 percent, while others get as little as 10 to 20 percent recovery. The total reserves also include high-quality light sweet oil commingled with low-quality heavy, sour oil.

So, whom should you believe if world oil is really running dry? Those who reject the oil-peak theory have a lot of faith in technology; they argue that new technologies — and higher prices — are going to make it possible to suck oil out of unconventional places.

For instance, extracting oil from tar sands was once thought to be prohibitively costly, but currently oil from Canadian tar sands sells for approximately $20 per barrel. Canada puts its reserves at 300 billion barrels, higher than even Saudi Arabia, though much of that is unrecoverable.

That's why along with the debate about oil peak, there should be proposals to promote renewable fuel sources

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— green energy. However, many of these alternative fuel sources only provide supplemental solutions that have a limited impact at a time when lasting solutions are needed. Although oil is known mostly for producing transportation fuels, it's not an exaggeration to say that it literally drives the planet.

Energy Economics

Since 1972, the inflation-adjusted price for a barrel of oil has averaged $34, and while higher oil prices will depress demand, even in a classical economic model, the price of oil has to average an inflation-adjusted $60 per barrel before oil consumption/production actually declines year over year. Between 1980 and 1984, oil output declined for four consecutive years as the inflation-adjusted price averaged $69 per barrel. In 1984, as the price declined to an average of $50 per barrel, output once again began to increase and increased each year since. Demand hasn't suffered in the current situation because family incomes are just as high and energy now represents only a tiny bit of family spending in the United States. All of this makes estimating the remaining lifespan of the world's oil and equivalents supply a tricky business.

Supply and Demand

There are 38 major oil-producing countries, of which only 11 are OPEC members. These 38 producers and many other minor producers are sitting on the 1.2 trillion barrels of oil and 885 million boe of natural gas reserves. However, there is no real agreement on how large these oil reserves really are; what is uncontestable is that reserves are being found at a much lower rate than they are being consumed. Even more important is that current daily supply and demand for oil are so tightly matched that there's no room for error.

In 2003, demand from the developed world, especially the United States, was just as robust as China's, and that trend intensified in 2004, flattened in 2005 and recovered in 2006. Moreover, oil demand from the rest of Asia, particularly India, South Korea, Taiwan, Thailand and Singapore soared as well.

On the supply front, there are three things to consider:

1. The rate at which non-OPEC production capacity is growing.
2. The potential for growth in OPEC production capacity is becoming increasingly smaller. At the moment, most of the OPEC members, with the exception of Saudi Arabia, are operating at near capacity.
3. How effective OPEC has been in managing supply.

Long-Term Outlook

Over the last 30 years, daily oil consumption has risen by approximately 30 million barrels, just under one million barrels per day each year, according to the International Energy Agency (IEA). In recent years, over one-half of the growth in demand has come from Asia. Asian demand — particularly China, India and South Korea — has grown by 10 million barrels daily in the last 17 years.

The Hubbert Curve

As a framework for thinking about the world's oil production and supply, it is useful to understand the work of Marion King Hubbert, the Shell geologist who in 1956 correctly predicted that U.S. oil production would peak around 1966-1972. Oil analysts have applied Hubbert's methodology to world oil production and are predicting that world oil production will peak within the next several years, though they disagree on the precise timing. Hubbert's technique was based on the prediction that the production level for oil as it was utilized would follow a normal distribution. Thus, if the United States had 200 billion barrels of reserves when 100 billion barrels had been extracted, U.S. production would begin to decline.

Assuming that the world originally had three trillion barrels of oil reserves, if two trillion had been discovered thus far and one trillion has already been consumed, then one trillion barrels would remain to be discovered. A peaking of oil production would occur after another one-half trillion barrels had been consumed, and this would probably occur in about 15 years, according to this analysis.

It is worth noting that Hubbert's methodology is based on a purely statistical analysis of exploration and production data. It does not take into account new developments like tar sands, which could potentially prolong oil supplies for a few decades, nor does it take into consideration emerging advanced production technologies. Still, Hubbert's theory is important because it provides a road map for the oil market; if demand is set to rise to 100 million barrels per day and there isn't the production capacity to match, oil prices can only move in one direction: up. ●

Consequences Of An Oil Peak

Civilization has gotten to a point where it is almost impossible to imagine life without cars, air-conditioned

rooms, hot showers and electric appliances. And yet, there's a growing realization that such habits need to change because it takes a lot of limited resources to produce and run all the machines that make life easy and comfortable. All advances and problems are now manifested in rising fuel prices; the strain is felt at the gasoline pumps and in home heating bills.

At the moment, about 80 percent of all the energy used in the United States comes from fossil fuels — oil, coal and natural gas. Nuclear power provides 10 percent of the energy and the remaining 1 percent comes from renewable fuels — sun, wind and water, according to the U.S. Department of Energy (DOE). Oil prices, which skyrocketed from $18 to $75 per barrel in just four years, are not likely to get much lower in the long run, so we might as well get used to them.

In time, we may learn to love the aftermath of the pain. That's because as investors we are going to make money out of the situation, and in the long run we'll also find other ways of living without Middle East oil.

Neglecting Future Problems Is a Failure of Leadership

Aside from taking measures to raise the fuel-efficiency standards for vehicles as a part of a broader effort to control explosive demand growth, the U.S. government also needs to come up with a more imaginative and creative national energy policy that would not only encourage energy conservation and diversify supply, but would also jump-start a major national initiative to cut the country's dependence on foreign oil.

The federal government's inability to enact a broad energy policy to create alternative energy sources at least three decades ago has been justifiably called the biggest single U.S. policy failure of the past half-century; it has made the United States vulnerable to oil shocks from abroad.

Consumption, En Masse

Clearly, change isn't going to happen overnight for the United States. The automobile industry is one of the most energy-intensive modes of transportation ever created. Car ownership in the United States, at 217 million, is the highest in the world. Because of urban sprawl in the south and west, in places such as California and Arizona, there is a social dependency on car transportation.

The highway system, which was built in the 1950s, has only encouraged this urge to drive in a huge car alone. Millions of gallons of gasoline are being used in this process. The United States might be well-advised to start moving toward a mass-transit system even in cities that currently don't have one. The reason is simple: The need to conserve fuel is becoming greater by the year.

As for other uses of energy, according to the U.S. Energy Information Administration (EIA), residential energy use accounts for 21 percent of total national consumption, of which 51 percent is for home heating, 19 percent for water heating and meal preparation and 4 percent for air conditioning. The rest powers lights and appliances such as refrigerators.

In the developing world, most of the energy supply comes from coal, wood and dry animal waste or biofuel. Would North America be really happy with such an inefficient energy supply? That's very unlikely, especially since computers and the Internet are indirectly powered by fossil fuels. A lack of oil would shift demand away and to other sources, eventually causing the alternative fuel prices to go up. In the long run, information systems would be more difficult to expand and maintain. ●

Types of Renewable Fuels:

Solar Energy — energy that radiates to the earth from the sun; solar thermal devices concentrate it in some manner to produce heat at useful temps

Wind Energy — kinetic energy from the wind is harnessed by turbines to generate electricity

Biomass — from three distinct energy sources: wood, waste, and alcohol fuels; includes biomass alcohol fuel or ethanol derived from corn

Municipal Waste — waste-to-energy combustion and landfill gas; methane is combusted for energy

Wood — generates electric power, thermal output

Nuclear Energy — from nuclear fission, which produces energy by splitting atoms

Geothermal Power — energy from the earth brought to the surface by hot water or steam Hydroelectric Power — water used by electric utilities to generate electric power

Fusion Energy — fusion reactors create energy by fusing atoms; requires 100 million degrees

Natural Gas — drilling for natural gas has surpassed oil in U.S.; net energy is equal to that of oil

Coal — enjoying a resurgence due to gasification which makes it easier to transport; coal supply is abundant yet challenges exist regarding transportation, safety and the environment.

Alternative Fuels

The Paris-based International Energy Agency (IEA), an energy watchdog for industrialized countries, estimates that over $1 trillion will be invested in non-hydro renewable technology worldwide by 2030. Though oil still has an edge due to its versatility, many activists in the environmental movement have been touting renewable fuels as the key to energy security.

One thing that must be acknowledged is that the transition to alternative fuels is necessary, but it won't be easy. It will involve more financial resources and time. Not all fuels are interchangeable, and most renewable fuels have lower fuel yields than fossil fuel. There is still no battery that can move farm machinery in the fields. Some sources of oil, such as tar sands found in Canada and heavy oil in the Orinoco Belt in Venezuela, require a lot more energy to produce, so much that in the end their net energy recovery is less.

Consumption of biofuel — which comprises ethanol and biodiesel or vegetable oil — in transport has risen in recent years; ethanol in particular is expanding in Brazil and the United States. Technologies such as wind, solar, biofuel and geothermal now provide up to 6 percent of the world's total energy, according to the EIA. ●

Is the Saudi Oil Supply Adequate?

As the world's largest producer, Saudi Arabia is the single most important oil supplier and is the major driving force within OPEC. Even more crucial, it is the only oil supplier with a spare capacity of between 1.5 million and 2 million barrels per day, which gives Saudi Arabia a small arsenal to fight higher oil prices during certain limited occasions. In an oil market where supply is very tight, having any spare capacity, as the Saudis do, is golden.

Currently the kingdom is enjoying its hugest oil boom, with revenues for 2005 at $156.8 billion, according to Saudi officials. Saudi Arabia has the capacity to produce up to about 11 million barrels per day, but actual production usually ranges from 9 million to 10 million barrels per day. Some two-thirds of Saudi reserves are considered "light" or "extra light" grades of oil, with the rest either "medium" or "heavy." Lighter grades generally are produced onshore, while medium and heavy grades come mainly from offshore fields.

Saudi Arabia's long-term goal is to further develop its lighter crude reserves. In the spring of 2005, the kingdom announced plans to increase its oil production capacity significantly. Coming at a time of tight oil supply and high fuel prices undermining economic growth, the U.S. government openly embraced the Saudi plan, but privately, they are skeptical about some of those forecasts.

U.S. leaders have always looked to Saudi Arabia to produce more oil so as to keep fuel prices from rising and becoming a political issue. But there are many within and outside the U.S. government who now doubt Saudi Arabia's ability to keep its promise of expanding capacity. ●

Why and How Oil Prices Soared

The world is experiencing its first demand crisis in more than two decades. Blame can be placed on China, OPEC, Iraq and the oil peak, but it also must be admitted that the industry has gone through structural changes that have had enormous influences on energy prices.

How the Oil Market Works

Commodity prices are a function of demand and supply; but today's market is responding to additional pressures — geopolitical tensions as well as speculative activity. Current daily oil production of about 84 million barrels globally leaves approximately two million barrels of spare capacity, hardly enough to absorb any unplanned disruptions in the supply chain. And yet there have been and will continue to be many disruptions, especially in oil-producing countries that are politically unstable.

Obviously, such a tight market causes oil and natural gas prices to soar, as seen in 2004. When you add unexpectedly destructive natural disasters like Hurricanes Katrina and Rita, the pain becomes almost unbearable. Since 2004, oil prices have spiked in a manner that hasn't been seen since the last oil shock in 1979.

Hedging Against High Prices

Crude oil and its products, such as gasoline, heating oil, diesel and kerosene/jet fuel are traded both on a spot basis and on the futures contract basis. The futures market is basically a market for risk management, where traders sell contracts for crude cargoes that will be delivered at a later date, typically two months to many months out, through 2011. As oil prices become more volatile, those whose business involves producing, mar-

keting or using oil, gasoline and other types of energy use have resorted to managing their financial risks by buying contracts for oil and product deliveries many months or years in advance.

Tight Refining Capacity Will Keep Prices High

If there's anything to remember from Hurricanes Katrina and Rita, besides the human toll in New Orleans, it's the impact they both had on the nation's oil-refining capacity. Much of the price spike that was witnessed was due to the fact that up to a quarter of U.S. refining capacity was wiped out for several weeks. The country was able to deal with the shutdown of offshore oil production, but was unable to deal with a large reduction in refining capacity. The reason: Since the oil shocks of the 1970s, the U.S. government has always kept about 700 million barrels of oil in underground salt storage in Louisiana for emergency supply, known as the Strategic Petroleum Reserve. But the country can't import gasoline from everywhere because of strict environmental regulations.

But even before Katrina, the United States already had a refining capacity problem. There have not been any new refineries built in the last 30 years. In 1980, there were about 425 refineries; currently there are only 147. Many refineries failed in the intervening years when refining wasn't a profitable business. Those 147 refineries can process only 17 to 20 million barrels a day of crude into gasoline. That's not enough for the 217 million automobiles registered in the United States, so about one million barrels of gasoline has to be imported every day, or 30 million barrels a month, to get along. ●

Murti and the Super-Spike

In the spring of 2005, Arjun N. Murti, an analyst with Goldman, Sachs & Co., released a report forecasting a "super-spike," with prices rising to $105 per barrel. It was a shocker to the oil community since oil was trading at $54 at the time; many analysts condemned it as far-fetched.

But that was before Katrina, which sent oil prices up 20 percent to $70 per barrel within five months. So, it turns out after Katrina that Murti may have been right after all. Murti has become something of a prophet in the industry. Murti's super-spike theory was based on an assumption of a continued tight balance between global supply and demand, plus the likelihood that a supply disruption could occur anytime overseas, upsetting the market. It only missed one thing: that the disruption occurred in the United States.

Bumper Harvest For Oil Majors

At the end of January 2006, Exxon Mobil reported profits of $36.13 billion and revenues totaling $371 billion for 2005, up 40 percent over 2004. To put it into context, it's more than what Coca-Cola Co., Intel Corp. and Time Warner, Inc. together earn in an entire year.

To put everything into perspective, from a stock price of $12 per share in 1990 to about $60 a share 15 years later, Exxon Mobil has grown fivefold, compared with Coca-Cola's share price, which rose from $11 to $42 a share during the same 15-year period, while Time Warner's share price rose from less than $1 [in 1992, after the merger with AOL] to about $17 a share.

Smaller oil companies haven't been left behind either, especially refiners. Among these, Valero Corp. and Sunoco Inc. represent different business approaches.

Valero Corp.

Valero specializes in refining dirty low-grade oil — heavy sour crude — that is found mostly in Latin America and the Middle East. Sour crude has the advantage of being easy to get and cheaper for a refiner to buy in the market, but it is also very difficult and costly to refine. The refiner's stock price, which was trading at $104 a share in December 2005, has roughly doubled since January 2006 and has increased about seven times during a five year period.

Sunoco Inc.

Sunoco specializes in refining the pricier high-grade oil — light sweet crude — found mostly in the U.S. Gulf of Mexico, Canada, West Africa and Europe. Sweet crude is very expensive to buy and also difficult to find, but it is very cheap to refine and yields a lot more gasoline, kerosene and jet fuel.

Oil Companies Raise Capital Spending to Increase Capacity

In 2005, oil companies spent about $86 billion on capital expenditures in the United States, up from $81 billion in 2004 and $76 billion in 2003, according to the American Petroleum Institute, the industry's lobby in Washington.

Nonetheless, there are other reasons why capital spending should continue to rise. Oil companies are valued on Wall Street in most part by their oil and natural

gas reserves. As long as earnings remain strong, the companies will be forced to replace the crude they pump out of the ground, because they'll go out of business if they don't. That requires taking some risks — financial, logistical, political and marketwise.

Analysts See Upside in Booming Oil

Convinced that there's more upside in the booming oil industry, Prudential Equity Group has initiated coverage of major oil companies with a favorable overall rating, based on the strength of the underlying energy market. Among market trends pointing toward sustained growth are the resurgent U.S. demand for refined petroleum products, and the likelihood of continued strong natural gas prices. Similarly, Morgan Stanley forecast an upside to earnings in 2006 for several European oil companies, driven by refining margins. The firm favored Poland's PKN Orlen, MOL Hungarian Oil and Gas, Spain's Repsol and the Anglo-Dutch giant Royal Dutch Shell for their exposure to margin gains from refining. ●

The New Frontier In Oil Investments

There's been a great deal of talk about the energy crisis. You should by now be aware of the gloom and doom forecast by some very smart people for the end of oil. Also, you've heard the opposing view that some kind of solution will come through, either in the form of additional oil supply or an alternative to oil. These are both very simplistic ways of looking at the issue and virtually guarantee that nothing will be done to alleviate the problem.

However, the question you should be asking yourself is whether you are going to take advantage of the situation to save or get rich through various energy investments. Here's one important thing to know as an investor: It's a good thing to gamble, but it's even better to be sure about which market you intend to gamble in. Currently, there is no better market to invest in than energy, and it doesn't matter whether you want to invest in small cap or big cap energy stocks.

To understand why energy is such a hot commodity, look at industry trends starting in the summer of 2004, when Chinese demand hit the market and Hurricane Ivan ravaged the Gulf Coast. Then came the summer of 2005 when Hurricanes Katrina and Rita blew ashore a new energy crisis, sending crude prices to record levels above $70 per barrel, and gasoline, heating oil and natural gas prices followed higher, increasing the cost of almost everything from filling your car's tank to heating your home.

The Basics of Investing in Energy

First, the most fundamental reason for investing is to make more money than you get from your day job; however, buying an oil stock or two will not necessarily make you any richer instantly, nor make up for your gushing energy bills.

The type of investment you should be interested in is discretionary investments; however, like any venture, this type of investing involves risks. These risks can be dealt with though.

The first thing that you need to do is study the industry trend. Pay attention to news, both business and other types of news, because company decisions are informed by many issues, including legislative politics and technology. Currently, a useful avenue for investing in the energy industry is through an index fund like Vanguard Energy Index Fund (VENAX), which replicates a basket of stocks in a given industry. In 2005, VENAX grew nearly 40 percent, far more than Standard & Poor's 500 Index's gain of nearly 3 percent during the same period.

As an investor, don't get worried about high oil prices and the fact that they cause inflation. Let other people get anxious about such things; your job should be to use the opportunity to make money for yourself.

Don't Panic — The Boom Will Last, But Have a Plan

It's also important to time the market very well, usually before it gets red-hot, as the energy markets are now. But if you are late, don't give up; no one ever gets anything for doing nothing, so you'd be better off late than never investing in energy stocks.

Stocks are important to successful investment plans because, historically, their annual returns are double what you can get in bonds. With the U.S. inflation rate at about 3 percent, you are left with a 7 percent rate of return per year when you invest in stocks, as opposed to 2 percent when you invest in bonds. Stock investments grow faster, almost doubling every 10 years, but they are also very volatile, and you could lose money if the market goes south.

Stocks typically move up and down in five-year cycles, so long-haul investors are cushioned from market volatility. Someone who has 10 years ahead of him is different from another person with a much shorter time before he has to start spending his money. If you have a longer time frame in which to invest, look for high-return

energy stock — mostly smaller or midsized stocks — because you have time to play the market. But remember also that they are some of the most vulnerable to short-term swings. Still, you can load up most of your money in small to medium-sized company stocks. If you don't want to risk your money because you are just a few years from retirement, then consider investing in large caps and steady performers like Exxon Mobil.

One thing you should do as an investor is to develop some spine, because you are going to be taking big chances. But don't panic. The trick to smart investing is minimizing risks, while expanding opportunities for success. One sure way of doing that is by diversifying your investments. If you diversify, some of your funds will be better than others, and you'll also be cushioned from a hard landing if the market begins to dip.

Check Out Top Companies With Low P/E Ratio

The current oil boom is creating a cash-flow windfall for oil companies and that improves their fundamentals. It plays a part in the upward movement of a company's stock. You should ask yourself a few questions: "What's the health of the company and that of its stock?" "Has this company been discovered?" and "Is it an undervalued stock?" Put all of these things together and if the answers to most of these questions are positive, then you are in luck.

As an investor, don't wait it out for long once you have successfully gone through the vetting process. Look for such a company, especially one with large enough quantities of oil and gas reserves. The best ones are those with most of their reserves in North America and Europe, where political risks are low. Also, look for stocks trading at a fairly low price/earning (P/E) ratio, such as company stocks that are cheap but have high returns, because such companies have low risk, and if oil prices come off, they are more likely to profit from stock buybacks or restructuring. Such companies are also more likely to be the target of mergers and acquisitions, which increases their stock value.

The most profitable companies now happen to be refiners because the margins are so high. This means that for every barrel of crude that a refiner buys and processes into petroleum products — gasoline, diesel, jet fuel and others — the refiner gets more than $20 in profit. The reason is that there are fewer refineries in the United States — just 147, down from 425 about 25 years ago.

Business Outlook and Balance Sheet: The Devil's in the Details

There's a broad range of oil and oil-services companies that can suit anyone's investment strategy. But you have to know first if there is growth of earnings and sales, both of which tell you whether the business is financially sound. Look at the balance sheet of each company you want to invest in and see if there's too much debt and what is the collateral for that debt, whether they are doing accounting right, whether the company has pending litigation or labor action or less insurance coverage. These are red flags for potential trouble, unless thoroughly explained.

However, if you find that you are too busy to invest in stocks on your own, then here are additional strategies to consider:

- **Mutual funds** — Try to find out what kind of managers are running the funds. The two best known commodities indexes, the Goldman Sachs Commodities Index and the Dow Jones AIG Commodities Index, are both heavily weighted toward energy, 30 percent to 40 percent. Investors who prefer small-cap companies could check out Brandywine Advisors Fund, whose portfolio is 21 percent energy stocks.
- **Exchange-traded funds —** These are low-cost funds that have become popular with investors, although they are less well understood. Like traditional funds, exchanged-traded funds (ETF) hold baskets of securities and other investments, but rather than get priced once a day, like traditional funds, they trade throughout the day like the stock market or futures market for commodities.
- **Hedge funds —** These are investment firms that try to profit by making bets on commodity and exchange futures. They buy financial instruments, or contracts, today and sell them later at higher prices and pocket the difference. They generally trade on arbitrage, or the price difference of contracts.
- **Superfunds —** Great for the smaller investor because managers charge less, typically 8.75 percent, in brokerage and management fees.
- **Private Equity —** For the wealthy investor that invests large sums of money in all manners of sectors; currently the hottest investment tools in the energy markets.

The bottom line is this: The world needs a lot of energy, but supply is getting tighter; an "uberspike" in oil prices is in the making and the potential rewards for the savvy energy investor are huge.