

- By Leah McGrath Goodman
- Of DOW JONES NEWSWIRES

¶ NEW YORK (Dow Jones)--Last year's high energy prices made for some surreal events: fuel giveaways to the U.S. by Venezuela, lawmakers' grilling of Big Oil on Capitol Hill and energy-saving adjustments to daylight savings hours by Congress.

¶ But prices don't appear to be heading any lower, according to market forecasts. While projections range widely, market watchers on average expect oil prices to consolidate in the neighborhood of \$55 to \$60 a barrel this year. Still, that is good news for the cash-strapped consumer after last year's \$20 leap and the prior year's \$10 gain.

¶ A brave few also continue to point to the possibility of "superspike" - a jump in prices that could send oil prices barreling toward \$100.

¶ "The main question underlying prices is this: At what price does oil start to slow down world demand?" said Jacques Rousseau, senior vice president and energy analyst at Friedman Billings Ramsey in Arlington, Va.

¶ Evidence of a slowdown in demand last autumn, when oil prices touched a record high above \$70 a barrel and hurricanes ravaged the oil-rich Gulf Coast, could offer the best marker yet of consumer intolerance, Rousseau said.

¶ "The high prices lowered demand, and that was witnessed even ahead of last year's hurricanes," he said.

¶ Others said the drop in demand established a new floor.

¶ "Demand has already bottomed," said Joseph Terranova, director of trading for MBF Clearing Corp. in New York. "Crude is going to \$90."

¶ A report this week from the federal Energy Information Administration, the statistics and analysis branch of the U.S. Department of Energy, backed the notion that demand may be on the mend.

¶ Though the EIA's preliminary annual data showed U.S. oil demand fell 60,000 barrels a day to 20.668 million b/d in 2005, demand closed out December at a record-high monthly average of 21.619 million barrels a day, up 1.8% on year.

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· Fund Reversal

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¶ Crude oil futures in New York got off to a galloping start this year amid signs of rising demand in the first week of January, despite mild winter weather in the Northern Hemisphere.

¶ The February crude contract settled near a 12-week high Friday, surging \$1.42 to \$64.21 a barrel on the New York Mercantile Exchange. Market participants attributed the rally to a sharp reversal by well-financed commodity funds who largely shorted the market late last year.

¶ Lackluster returns in the U.S. stock and bond markets drove investors to higher-growth commodities this year, economists said.

¶ "In the search for higher rates of return, hedge funds and institutional investors have brought a lot of people into the game right now," said Nariman Behraves, chief economist for Global Insight Inc. in Lexington, Mass.

¶ Though Behraves said the influx of cash doesn't raise any immediate concerns of "unreasonable, irrational speculative behavior," he noted the oil-investing community has grown at a rapid pace.

¶ "Commodities in general are prone to more volatility than many other kinds of assets, and this kind of speculative activity could push prices up in the near term," he said.

¶ Such a boost could set the market up for a tumble later this year, Behravesh said, but global economic growth likely will keep prices taut.

¶ An economic consulting firm to Fortune 500 companies, Global Insight expects oil prices to average at \$58.20 in 2006, but doesn't buy into any superspike theories.

¶ "Whenever we go through one of these energy scares, the real gloom and doomers come out," Behravesh said. "They are usually wrong."

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· Refining Key

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¶ Renewed fund interest aside, continued strains in U.S. and worldwide refining capacity also will keep energy markets on a bullish course.

¶ Efforts are underway to build new refineries outside the U.S., and within its borders, a handful of refineries plan to boost production capacity. But with no projects slated for completion until 2007 at the earliest, the situation is likely to get worse before signs of improvement appear, said Rousseau.

¶ "Some people think that new refining investments are going to overwhelm the industry and bring a correction in prices, but we think supply will remain tight and prices high," he said.

¶ In a report released Friday, Rosseau noted that the Paris-based International Energy Agency posted a 2% increase in crude oil and refined product inventories for member countries of the Organization for Economic Cooperation and Development in October. That leaves little wiggle room on the heels of an 8% jump in consumption over the past five years.

¶ Friedman Billings counts 12 projects underway - mainly in Asia and the Middle East - to build new refineries, but most aren't scheduled to begin processing until much later in the decade.

¶ In the U.S., a homegrown twist will keep prices high: Tougher fuel standards for gasoline and diesel will take effect this year, putting more stress on the nation's fuel-supply system.

¶ The stricter standards will whittle down the number of foreign refiners able to meet U.S. fuel specifications, and distributors will need to keep cleaner-burning fuels separate from other petroleum products moving through pipelines - something most lines aren't designed to do.

¶ That could leave prices on volatile footing in the months ahead, analysts said.

¶ "We're gradually working our way back up to high historic trend levels," said Jim Ritterbusch, who heads energy consultancy Ritterbusch & Associates in Galena, Ill.

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¶ -By Leah McGrath Goodman, Dow Jones Newswires; 1-201-938-2062; Leah.Goodman@dowjones.com