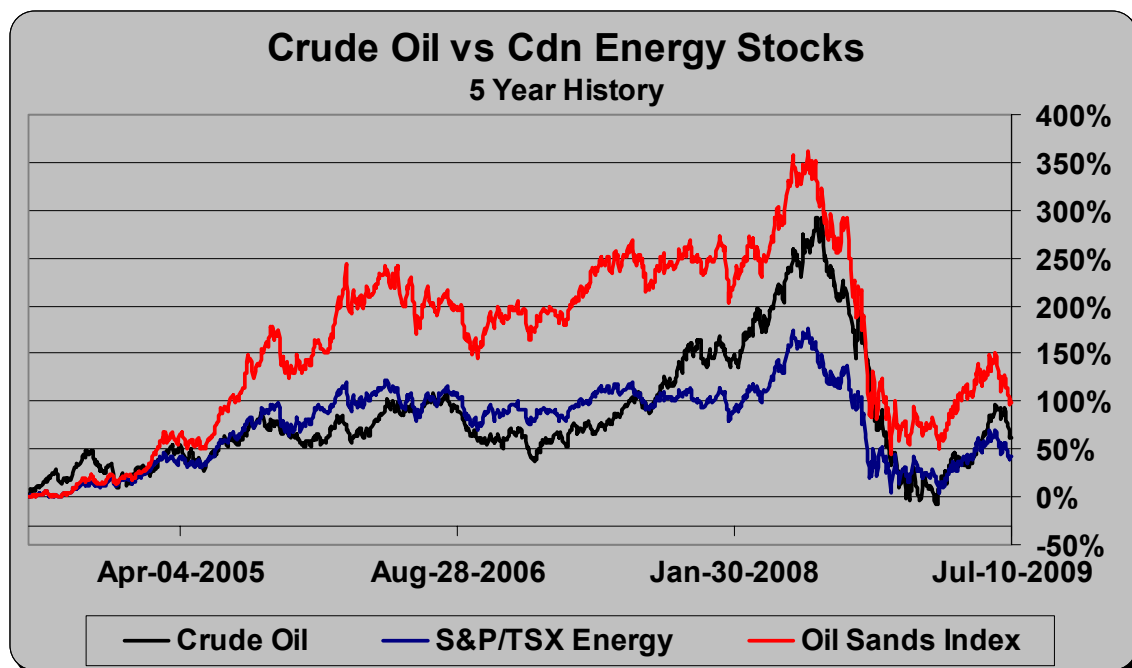




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Sustainable Oil Sands Sector Index™ (SOSSI) July 2009 Commentary Oil Sands Index Celebrates 5 Year Anniversary

The oil sands stock index has reached a major milestone, its fifth anniversary. I continue to believe, as I did 5 years ago, that Canada's oil sands will be one of the greatest investment opportunities in the global energy sector. What makes me confident enough to make such a bold statement? Historical evidence is a good place to start (see chart below).



The chart clearly shows that the oil sands index consistently outperformed both crude oil prices and the benchmark Canadian energy index. I am delighted with these results since I had taken a major risk basing the index on fundamental, sector specific factors over the traditional market capitalization based index methodologies. I think a lot of the success of the oil sands focused stocks over conventional oil and gas producers is related to the tremendous operating leverage they enjoy in a rising crude oil price trend. As I look forward another 5 years, I see the cost of finding and developing new oil resources going much higher and froth with unpredictable geopolitical risk. Environmental and government regulatory changes suggest to me that operating costs in the sector will increase and preference will shift to non fossil fuel energy sources. Energy demand in North American and Europe might be on the decline however the



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mass of humanity is just now beginning to increase their own energy usage as they develop into modern economies. Major crude oil exporters such as Norway, Mexico, and most OPEC members (save Saudi Arabia) have reached a production plateau or have clearly peaked years ago. These factors and dozens more support a rising price environment for many years to come.

In the short term the results were poor in June for energy stocks while natural gas prices were flat and crude oil had a healthy 5% plus gain. After last month's 16% gain we should have anticipated a retreat however the downtrend has continued into mid July. This makes it uncomfortably similar to last years devastating collapse that began in the summer months. However, I don't see this year repeating the same pattern (more on this later).

Index	Symbol	Region	June 2009 Return
NYMEX Natural Gas	NGAS	US	0.0%**
NYMEX Crude Oil	OIL	US	5.4%**
Oil Sands Sector Index	SOSSI	Canada	-5.9%*
S&P/TSX Capped Energy	TTEN	Canada	-3.3%*

* Return in Canadian dollar terms.

**Return in US dollar terms.

OPTI Canada was hammered in June as they announced the issuance of a huge amount of new shares significantly below the current market price. Clearly, speculators that had more than doubled the price of the stock in the prior two months took a major hit. The anxiety extended to other small players that have been hit hard by the downturn such as Oilsands Quest and Connacher Oil and Gas which both failed to qualify for the index this year due to a failure to reach minimum market capitalization requirements. I look forward to welcoming them back to the index if and when their fortunes turn around.

Top Performing Stocks June 2009

Worst Performing Stocks June 2009

Imperial Oil	1.7%	OPTI Canada	-40.5%
Baytex Energy	1.3%	Connacher Oil & Gas	-15.6%
Ivanhoe Energy	0.0%	Suncor Energy	-7.5%
Cdn Oil Sands	-0.8%	Petrobank	-7.3%
UTS Energy	-1.3%	Oilsands Quest	-5.9%

Last month I discussed how Saudi Arabia just added over 1.2 million barrels of production from their new Khurais field, equivalent to the current total oil sands production. Why is this important? It provides us with clues on the development cost of conventional oil projects and the potential problems with



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increasing production. The new Khurais field is claimed to be the fourth largest producing oil field in the world (a claim I have not verified but do not doubt). It cost \$10 billion US to get to its 1,200,000 boe/day production rate which is an incredibly economic \$9,000 per flowing barrel of production. Compare this to the recently completed Horizon project by CNQ that cost \$8.5 Billion US (\$9.7 Billion Cdn) which has initial production of only 110,000 barrels per day with a maximum potential production of 500,000 barrels/day in the future. On the surface the Saudi field seems like a bargain compared to the \$77,000 per flowing barrel cost of the Horizon project however I think we should investigate further. The Khurais field was discovered in 1957 and was brought on to primary production in the 1970s and mothballed in the 1980s. This new reincarnation is based on a massive water injection project that requires almost 4 barrels of water for each barrel of oil produced. Water is scarce in Saudi Arabia so seawater is used at great expense. The Khurais field is expected to produce for 20 to 25 years however I expect production will peak early and extraction costs will increase in the future (research SPE reports on the Khurais field for details). Horizon could produce for over 150 years at the current production level, eventually recovering 6 to 8 billion barrels of synthetic crude oil similar to the Khurais field. The difference will be very profitable to investors. If I am correct, crude oil prices will be substantially more expensive in the future. The Saudi field will hit its maximum production when prices are relatively low and face a rising cost curve. The Horizon cost curve will decrease on a per barrel basis as it expands its production capacity and new technology will help reduce environmental impact and operating costs. The majority of Horizon production will occur during my anticipated high price environment and be extremely profitable for investors.

I am envious of how quickly Saudi Arabia can add production capacity compared to our oil sands projects however I think as an investor I will stick to my oil sands tortoise over the Khurais hare over the long run.

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