

NATIONAL PRESS CLUB NEWSMAKER LUNCHEON WITH JOHN HOFMEISTER,
PRESIDENT OF THE SHELL OIL COMPANY

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MR. SALANT: Good afternoon, and welcome to the National Press Club. I'm Jonathan Salant, a
reporter for Bloomberg News and president of the Press Club.

I'd like to welcome club members and their guests in the audience today, as well as those of you
watching on C-SPAN.

Please hold your applause during the speech so we have time for as many questions as possible.
For the members of our broadcast audience, I'd like to explain that if you hear applause, it is
from the guests and the members of the general public who attend our luncheons, not from the
working press.

The video archive of today's luncheon is provided by ConnectLive and is available to members
only through the National Press Club's website at www.press.org. Press Club members may also
get free transcripts of the luncheons at our website. Nonmembers may buy video tapes, audio

tapes and transcripts by calling 1-888-343-1940. For more information about joining the Press Club, please call us at Area Code 202-662-7511.

Before introducing our head table, I'd like to remind our members of future speakers. On October 25th, Senator Elizabeth Dole of North Carolina and Senator Chuck Schumer of New York, the heads of the Republican and Democratic Senatorial Campaign Committees, will discuss the 2006 elections. On October 30th, Myles Brand, the president of the NCAA, and on November 30th, David Paulison, director of FEMA.

If you have any questions for our speaker, please write them on the cards provided at your table and pass them up to me. I will ask as many as time permits.

I'd like now to introduce our head table guests and ask them to stand briefly when their names are called. Please hold your applause until all of the head table guests are introduced.

From your right, Margaret Chadbourn, a reporter for Market News International and a new member of the National Press Club. And Margaret, great to have you.

Dan Berman, senior reporter for Greenwire and the Environmental and Energy Daily; Paul Krawzak, Washington correspondent for Copley News Service; Patty Reinert, national correspondent for the Houston Chronicle; Tom Doggett, who covers energy for Reuters; Dorothy Sinclair (sp), the senior communications specialist for the Shell Oil Company; John Hughes of Bloomberg News, chair of the National Press Club Speakers Committee.

Skipping over our speaker for a moment, Ken Dalecki, a freelance reporter and the member of the Press Club Speakers Committee who organized today's luncheon. And Ken, thank you very much.

Steve Mufson, staff writer for The Washington Post; Bill Loveless, chief editor of Platt's Inside Energy; Jim Ostroff, associate editor with the Kiplinger Washington Letter; Llewellyn King, editor and publisher of White House Weekly and the host of PBS's "White House Chronicle"; and Chris Holly, a reporter for the Energy Daily and a veteran coverer of the energy industry. (Applause.)

When you leave a Washington Nationals baseball game and drive along Benning Road toward the Anacostia Freeway, you pass a unique Shell station. Along with regular, mid-grade and premium, or V-power, this station offers hydrogen. It's part of Shell's attempt to offer alternatives to the gasoline that is the mainstay of its business.

Sales of gasoline helped Shell and other oil companies post record profits this year as the price at the pump climbed above \$3 a gallon. With the cost of a gallon of gasoline dropping recently, polls show that some Americans believe that the oil industry is manipulating the price in order to keep Republicans in control of Congress. The Republicans passed an energy bill that President Bush signed into law, which gave billions of dollars in subsidies to the oil industry and did little for conservation. Meanwhile, at the Press Club last week, Congressman Chris Van Hollen,

speaking for the Democratic Congressional Campaign Committee, said that if his party wins control of Congress, they will repeal those billion-dollar subsidies.

Our speaker today, John Hofmeister of Shell Oil, has undertaken a 50-city tour to explain that oil prices are a matter of supply and demand, not market manipulation by big oil. He has called for more drilling because of the demand for oil which he says will not decline, even as efforts continue to find alternatives, such as oil shale, biofuels, or that hydrogen you can buy right near RFK Stadium.

Mr. Hofmeister became president of the American subsidiary of the Royal/Dutch Shell, the world's third-biggest oil company in 2005. He came to Shell eight years earlier, after working for AlliedSignal, Northern Telecom, and General Electric.

His visit here today is a homecoming of sorts. He was born in Cheverly, Maryland. He grew up in Pennsylvania. And he and his wife have a foundation that preserves an 18th century mill and adjacent farmland in the Amish country.

Let's welcome John Hofmeister to the National Press Club. (Applause.)

MR. HOFMEISTER: Jonathan, thank you for that introduction.

And it's very nice to be here, ladies and gentlemen, and to speak to you about a subject that is as near as our gas tank or as close as our light switch.

But as I thought about coming to speak here today, as I looked in the mirror this morning, I said: Why am I here? Why am I here in this distinguished audience representing an industry that some would say has zero credibility, selling a product that you don't want to taste, touch, smell or even see; pushing on policymakers to open up access to the Gulf of Mexico or other Outer Continental Shelf locations, which essentially irritates virtually everyone that we talk to about it; pushing alternative fuels, new technologies, like coal gasification, and other technologies which will take years to penetrate the market; promoting the notion of conservation or energy efficiency, which, if we are really good at it, will take decades to make a difference; and finally, trying to promote the notion of how do we manage greenhouse gases in a way that we have a sustainable atmosphere not only in this country but around the world, which many people dispute the technology or dispute whether there's even a problem.

Why am I here? Well, there are two main reasons I'm here. I believe in the brand that we represent. The Shell brand that we represent has brought affordable energy to the American people for nearly a hundred years. It has brought credible technology to an industry that has continued to evolve and has supported the economic well-being not only of this country but the world for more than a century.

And secondly, I really do represent what I consider the myths of big oil. And let me penetrate that myth for a moment because what big oil represents are really the tens of thousands of people, everyday Americans in this country who get out of bed every day to go bring energy to the American people, who work hard, who do what they do, who create against the odds, who

work in the extremes of weather, whether it's the Arctic Circle or the Gulf of Mexico, and try turning around a refinery near the Gulf of Mexico in the month of July or August wearing all of your safety gear and coveralls and realize how difficult a job that is to perform.

So those two reasons say, yes, come and make your comments. And the comments I'd like to make are the fact that we can achieve energy security in this country by working on it. By doing the things that can be done, all within the realm of human possibility, all within the realm of technology, we can do these things. And we start by continuing to do what we've been doing, and that is bringing conventional oil and gas to market. Bringing conventional oil and gas means continuing to exploit the Gulf of Mexico, continuing to develop the resources that are there, prolific as they are, but needing the access to go do it.

We've recently seen an announcement in the lower tertiary region of the Gulf of Mexico where Chevron and Devon made a big announcement a couple of weeks ago, and we're very pleased that they made that discovery. Shell is on both the east and the west side of that discovery called Great White and Stones, and we are working very hard to develop that form of energy, which is in unprecedented deep water and at unprecedented depths below the surface of the Earth. It will be a technically challenging project, but it is what we still consider conventional oil and gas. We're hopeful that the Congress, when it returns, will pass the legislation that would open up additional Outer Continental shelf to try to get access to even more of the Gulf of Mexico.

Of course we'd like to see Outer Continental Shelf developed in other parts of the nation, and particularly off the coasts of Alaska, and even off the East Coasts, if those are one day to be developed.

But the conventional oil and gas, the "easy stuff," as we call it in the industry, is running out. It is more difficult to find prolific reserves in this country of what we consider conventional oil and gas. And so we've come to a conclusion that that's not enough. So what will be enough, what will be enough to provide energy security in this country?

Well, we can start by developing the oil shale of Colorado. The estimates are that more than a trillion barrels of oil and gas sit within the basin in Colorado, which was once a sea -- we may not know that -- that was once a sea. And so there are a trillion barrels of immature oil and gas in rock called shale, which can be developed. We know in the 1970s there were efforts made to mine and extract and use retort methodology to heat the rock to take out the oil and gas. That was given up on in the 1980s, or mostly given up on. Shell, however, stayed; we stayed in Colorado to try to test a different technology for developing the oil shale. We're still testing that technology, but we're getting closer and closer to a financial investment decision, hopefully by 2010, where we use an in situ technology -- "in situ" means "in place" -- where we would drill holes rather than mine huge quarries, we would drill holes down into the oil shale and place heaters in the oil shale, which would then accelerate the maturation of the oil that's already there to where it drips off of the rock, and then it can be pumped out in conventional fashion. We hope that the technology works. We're testing now a freeze wall to see if the freeze wall technology, in which these wells would be drilled, can contain the water. We believe that sometime in the next few -- three or four years, we should be far enough along on our research to make an investment decision.

And so if we develop the oil shale and we have the conventional oil shale -- oil and gas, is that enough to provide energy security? Shell doesn't think so. We think not. We need some additional supplies of energy.

This nation has abundant coal. We believe the technology has moved coal to the point that coal can be developed in what people are now calling "clean coal." IGCC technology is what it's called; that's a technology in which it's an Integrated Gas Combined Cycle gasification of coal, which instead of using pulverized coal which is burned, we would, rather, gasify coal powder in a gasifier which explodes the molecules, resulting in a far more efficient use of the coal.

And with the appropriate membrane technology associated with the gasifier itself, we can capture the emissions. One of those emissions is natural gas. The natural gas moves to a gas turbine. The gas turbine creates electricity.

Another emission is natural gas liquid, which can be used as a clean-diesel fuel, no sulfur, because the sulfur is also captured and the sulfur can be managed. And what about the CO₂? The CO₂ can be captured as well, and that CO₂ can then be managed. Rather than simply emitted into the atmosphere, that CO₂ could be captured and sequestered or it could be captured and piped for enhanced oil recovery purposes to the old remaining oil fields in this country, which may have as much as half of the oil still remaining in the conventional oil fields -- and the mercury and the sulfur, all of which can be managed through the IGCC technology.

If we develop that and utilities put that to work, is that enough? Not yet. We don't think so. We use prolific amounts of natural gas in this country, but ladies and gentlemen, we have a problem: The demand for natural gas is over the next 10 years going to exceed the supply of natural gas. The supply of natural gas today comes from the Gulf of Mexico, Texas, Oklahoma, Colorado and other states -- Montana, Wyoming, et cetera -- but that supply of natural gas is at risk for two main demand purposes.

One of those demands is American industry. American industry needs natural gas and its production processes as a fuel source. It is a clean, efficient use of fuel in the factories of America, particularly petrochemicals, fertilizers, other agricultural industries, but also most other industries such as steel, et cetera, use massive amounts of natural gas and power generation.

The combined cycle turbine has been well developed in this country and makes efficient use of gas for electricity purposes, and the construction cycle over the last decade and into this decade will put such a demand on natural gas that it's doubtful that with the reserves we have we can meet the demands.

An augmentation of that supply chain can come from liquefied natural gas. There are vast deposits of gas in different parts of the world called stranded gas, such as off the coast of Australia, or such as in Nigeria and Ghadir and other parts of the Middle East. This gas can be liquefied and brought by ship to this country and regasified. Shell is actually quite well positioned already in this country for liquefied natural gas -- Cove Point, Maryland; Elba Island, South Carolina, where we have gasification -- regasification terminals -- and we're proposing to build several more.

There is an issue with siting liquefied natural gas terminals.

There is a problem in this country called NIMBY -- Not In My Back Yard. And the people who don't want a regasification terminal near them have rights to protest and to protect what they consider to be their environment, their security, their neighborhood. This is an issue we have to face for liquefied natural gas to come into this country.

But we believe it's possible. We believe it's doable. It's already happening. Will this be enough? No, we don't think so. We think there's more that needs to be done. There's the whole field of alternative fuels that needs to be worked on. Shell is a major investor in second-generation ethanol. What is second-generation ethanol? It's cellulosic ethanol. And we're pleased that today in the audience is the president and CEO of Iogen, a company in which Shell is investing to which produces cellulosic ethanol from straw. Brian Foody is here. And that second-generation ethanol, we believe, is an excellent way to extend the fuels market of this country. We're already putting ethanol in cars, as you know. There are some states that have a 5 percent, up to a 10 percent mandate to put ethanol in gasoline. It stretches the gasoline supply. There are some who advocate E85, which is 85 percent ethanol. I'll come back to that in a moment.

But here's the issue that we face in the ethanol development phase of this new alternative fuel industry: should ethanol come from corn and sugar? Or should ethanol come from cellulosic matter, such as the cornstalk -- as the president has referred to, switchgrass, or other forms of biomass such as wood chips?

The issue with corn-based and sugar-based ethanol from a Shell point of view is that if we as a company are already being blamed for high gasoline prices, we really don't want to be blamed also for high food prices. And corn-based ethanol affects the food chain. Sugar-based ethanol affects the food chain as well. And there are stories beginning to build in this country about what farmers are now paying for chicken feed because the price of corn, as you know, has gone up significantly in the past month not only because of the demand for ethanol but because of a relatively poor harvest this year. The consequence of that will be felt by all of us in our pocketbooks; thus, the concentration of our investment dollars on second-generation ethanol or cellulosic ethanol.

Will that be enough? Well, let me just cover the E85 for a moment. To get E85 to market, two things have to happen.

One of those is the fleet of automobiles in this country has to be large enough to create a market. Today, about 2 to 3 percent of America's cars can use E85. Now, we know the automakers are trying to build them as -- build flex-fuel automobiles as fast as they can.

But then we run into the second problem; that is, there isn't a supply of ethanol to satisfy a large market of E85 requirements.

So while we can talk about E85, the reality is there's no market and there's no supply. That can change, of course, over the next 10 or 20 years, but it's not an instant turn-on the ethanol switch and all of a sudden it's at your local station, because in addition to that, an infrastructure would

have to be built to distribute and sell that ethanol. We cannot put E85 ethanol into a regular gas station gas tank, storage tank, because the alcohol will eat right through the fiberglass storage tank or it will corrode the pipes which we currently have in the gas stations because they were never designed for ethanol. So we need a whole new infrastructure if we're going to sell E85 ethanol.

Shell is piloting E85 ethanol in Chicago. We hope to test the market to see if people like it. Procuring it is very difficult because the supplies of ethanol are so tight, and then building the infrastructure is really just a matter of paying for it. But before we go invest millions or hundreds of millions in an infrastructure, we need to find out if the market will accept it.

One of the reasons the market may or may not accept ethanol is that it gets 75 percent of the mileage that gasoline gets. In other words, it has 25 percent less miles per gallon than we see with gasoline. Will customers pay the same price to get 25 percent less if ethanol is priced at the price of gasoline? Throughout most of this year, ethanol has cost more than gasoline.

So it may not be these solution that some think it is, although we're investing money in making it and we are investing money in testing the market to see if it will be accepted.

If that goes forward, is that enough? We still don't think so. We still believe that there are other forms of energy that need to be developed, such as wind. We started construction in the last few weeks in Mount Storm, West Virginia, to build a very large wind farm which produces CO2-free electricity. And the good news about this country, ladies and gentlemen, is we do have a lot of wind. (Laughter.) And that wind can be used to make CO2-free electricity.

I was in Maui recently, where we announced a wind farm for the back side of Maui, out of sight of most of the visitors so the issue of observing wind turbines is not at stake. But it takes away the need for a common pulverized coal-generating plant in Maui. They've run the limit of the current generation of electricity. They need another plant. Instead, they will have a wind farm, which Shell will provide.

Is that enough? Not yet.

Early mention was made of the Benning Road hydrogen station. Shell is pleased to have a partnership with General Motors working on hydrogen fuel cell vehicles. I had the good fortune of being here three weeks ago for a day-long meeting at the Energy Department with the undersecretary, Garman, working on hydrogen fuel cell technology, where the three major American automotive manufacturers were there and the five major oil companies were present, to talk about how do we develop a hydrogen infrastructure to support a hydrogen fuel cell vehicle. And I invite you as you leave today to either take a look or take a ride in the GM vans downstairs powered by Shell hydrogen and see how they operate.

It can become a commercial reality, probably not next year or the year after, but within five to 10 years, we should be seeing commercially available hydrogen fuel cell vehicles on America's highway, and Shell wants to be the distributor of choice for the hydrogen fuel that this car will use.

Is that enough? No. Three more areas to touch on, ladies and gentlemen, to make all of this real and to deliver U.S. energy security.

First and foremost of the remaining three, we must recognize that energy efficiency is a field of endeavor that we must pursue. Four and a half percent of the world's population does not have the right, the inalienable right, to use 25 percent of the world's oil and gas. And that's the formula today in the United States. The rest of the world wants that oil and gas as well, and they would like their fair share. And if that is to occur, then something has to give in the balance, or the price will simply skyrocket from where we've seen it. Four and a half percent using 25 percent of the world's oil and gas is simply a formula that has to change.

And so energy efficiency -- and ideas coming from the Department of Energy are very useful, but I think we have to go farther. I think we have to go into the culture of America to make a change felt. And people say this is too soft to say, but I'll say it anyway. The hearts, the minds and the behaviors of Americans need to change to where we teach our children energy efficiency, and then those children grow up and become technicians and technologists, and then they design differently than we have known in the past, our homes, our offices, our factories, our vehicles, to be designed with efficiency in mind as a priority, because the last 50 years of enjoyable mobility that we've had in this country are not to be repeated in the next 50 years if we don't do something very different, and energy efficiency is one of those differences that must change.

Secondly, it's Shell's belief that we have to deal with greenhouse gases. From a Shell point of view, the debate's over. When 90-plus percent of the world's leading figures believe greenhouse gases have impacted the climate of the earth, who is Shell to say that let's debate the science. We're not going to debate the science. When the policymakers decide it's a problem, it's a problem. And so there are good ideas coming from the White House that will address this, but we believe there needs to be more.

Shell was involved in discussing AB 32 in California. At the end of the day, we didn't support the bill, because of its ambiguity, but we want to be involved in the debate. We want to be involved in the rule writing that will now occur in California. But ladies and gentlemen, we can't have 50 state policies on greenhouse gas emissions. We believe, Shell believes we need a national approach to greenhouse gas management and how that would work across our industries, not only the gas and oil industry.

And then, finally, in some parts of this country, children are taught about energy. They are taught about gas and oil. They are taught about the social implications of CO₂. They are taught about the kind of use and applications of energy.

It's Shell's belief that all children should be taught about energy. Here we are in the capital of the nation, having a huge debate about the direction -- future direction of energy in this country, and the debate at some times sounds like a squabble. And I personally irritate both sides of the aisle when I express my own views on it.

The fact that we are having such a debate when other countries have a straightforward direction that they are following is due to the fact that I don't think we fully understand, as Americans, where energy comes from, how hard it is to produce it and how challenging it is to sustain that level of production. And we should be having a debate that is informed by people knowing more than they know today, starting with schoolchildren and moving through the generations. I think the time has come for the Education Department to recommend to the state school superintendents of the nation that energy become a part of the curricula in our nation's schools in the same way that history and science and civics and math are part of our curriculum, because, ladies and gentlemen, we have developed a lifestyle that is predicated on energy. We've developed an economic capability in this country and a desire for economic growth that again is predicated on energy, but yet we're not teaching ourselves how precious and how important and how challenging and difficult energy is to produce and to bring to the American people.

The combination of conventional oil and gas; unconventional oil and gas; liquefied natural gas; coal gasification; alternative fuels, such as ethanol, wind, hydrogen and solar, which I didn't mention but which Shell is investing in, in terms of a new technology called copper indium diselenide technology; coupled with greenhouse gas management, energy efficiency at the core of how we behave and how we think, and an education of our nation's population that are growing up and learning about this precious commodity -- all of those together, we believe, ladies and gentlemen, will deliver energy efficiency and energy security to this country.

Thank you. (Applause.)

MR. SALANT: You talked about this a lot in your speech, but this questioner would like to get a little bit more -- for you to respond to the argument that U.S. reliance on imported oil poses a significant threat to economic and national security.

MR. HOFMEISTER: We are aware that some people call for energy independence. We frankly think that's naive. Energy independence, when you think about the fact that 60 percent of today's oil comes from abroad, there really is not sufficient capacity in this country to make up for those 60 percent of our daily oil supply. That's more than 10 million barrels a day. We're having arguments over whether or not to open up the Eastern Gulf of Mexico, which we don't know if there is actually oil and gas there until we get in and explore. And to think that we can somehow find another 10 million barrels a day and sustain economic growth, we just don't think that's possible. We think imports are here to stay, but perhaps not at the level at which they are today.

MR. SALANT: What is your message to other oil companies who continue to fight the science and consensus on global warming?

MR. HOFMEISTER: For us the debate is over, as I said. I think that each company will have to take its own view, and we will simply express our view in the fullness of the arguments that we make, and others will either listen or not.

MR. SALANT: What's the best way to reduce greenhouse gas emissions -- a carbon tax, cap-and-trade, technology?

MR. HOFMEISTER: At the end of the day, it's probably a combination. There are other parts of the world which are already working on this. Europe, of course, has a cap-and-trade system. We think cap-and-trade is possible. The information management system that supports a cap-and-trade is available. The electronics are there. We think a national cap-and-trade system would be a good idea. It could also become ultimately a global cap-and-trade system, because just as we trade oil globally, we could probably trade carbon globally. A carbon tax probably fits in there somewhere, but again, if it's going to be a tax, the one request we would make as a company is that it be a level playing field so that all would be participating in it, not just a few.

MR. SALANT: Do you think it's possible to link international efforts to reduce global warming to the emerging U.S. market? And what will Shell see for itself in that business?

MR. HOFMEISTER: Well, we would certainly be a spokesperson for dealing with it. We do think there are lessons to be learned from around the world that we should pay attention to, and I do think that particularly in the developing world we have to lead by example for the developing world to follow. And one of the arguments that of course we all hear is that, Well, China can pollute too much, and the U.S. is, you know, just not going to be able to do anything about it." Well, I do think leadership by example is a good way to get followers to follow.

MR. SALANT: There has been talk about a huge gasoline tax, as much as 50 cents a gallon. I know in California there's a proposal on the ballot in November that would tax oil taken from California's shores and use that money to be spent on -- to fuel advanced energy research and technology and alternatives to fuel. What's your position on that type of a gasoline tax?

MR. HOFMEISTER: Shell's basic position on any kind of tax that it be a decision made by policymakers, not by companies. Policymakers have the duty and the responsibility to set the taxes. Our request only is that it be a level playing field, as I said earlier.

With respect to Prop 87 in California, that's the effort by -- on a ballot initiative to try and tax gas and oil at the wellhead in California to pay for renewables investments. Shell's taken a very strong position, through our Aera joint venture, which is a partnership with Exxon, very much against Prop 87, not because we're against alternative fuels or biofuels. We're investing heavily. It's our view that the investments in biofuels will happen regardless, and what California doesn't need in its industrial base is a new tax on anything, frankly, but particularly on oil and gas, which is very much a part of that whole society. We think that the increased costs will ultimately lead to more imports into California and quite possibly the loss of investment in future gas and oil development in California, which we don't think is good for the state.

MR. SALANT: What effect will OPEC's decision last week to cut its oil production by 1.2 million barrels a day have on available oil supplies for Shell's refineries and for all American refineries? And do you see the OPEC cut reducing heating oil supplies this winter?

MR. HOFMEISTER: Well, the good news is that in the short term, there is quite a bit of crude available in the world, and that has been the case really since last winter. When the Gulf of Mexico was shut in, because of the hurricanes, for most of last fall and was still continuing to open up in the first quarter of this year, we could already see that crude supplies worldwide were

building, which was a reflection of the fact that around the world, both OPEC and non- OPEC producers were actually having a very good year of it. The industry, after all, has been putting billions and billions of dollars into new production over the last four or five years. Ever since that low oil-price era of the late '90s, we have stepped up the investment. Shell's at \$19 billion this year, \$21 billion next year. That's a lot of money going into new production opportunities.

The cutback of 1.2 million I think is really OPEC's business about how they manage their affairs. The reality is there's a lot of crude out there. The issue around available supplies of crude is one that is less pronounced today, in part because of what some people consider -- two things, actually. The height of tension in the geopolitical environment seems to have diminished some, in the view of oil traders.

And then there are probably some financial traders who buy and hold various lots of oil who seem to be unwinding their positions, and therefore, we've seen some decrease in the global crude price.

But I don't think that overall we are going to see any surplus of crude lasting. The reason is the world economies continue to grow -- China, India and other developing nations, as well as the United States -- let's not forget, our demand for oil and gas continues to increase. We're pumping all the crude we can pump, and over the next 10 years, the predictions are that we'll need another 25 percent more crude oil into the market, and by 2020, we probably will need about 120 million barrels a day against today's 85 million barrels per day of production. So while this may be a temporary cutback, I don't see it as a long-standing position.

MR. SALANT: You talked about oil and gas. What's Shell's long- and short-term outlook for the U.S. natural gas industry?

MR. HOFMEISTER: In the very short term, there is -- the good news is there's record storage taking place. This is, in part, because last winter was mild across the nation, so a lot less gas was used than was predicted to be used, and this summer, we did not have damaging hurricanes that shut down production in the Gulf of Mexico. So in the short term, we've been able to store as much as gas as we've ever stored. Not knowing what the winter may be like, that storage could be used up quite quickly if, in fact, it's a cold winter.

The longer-term outlook is one of a very thinly stretched supply chain against an increasing demand curve. And over the next probably 10 years, we actually see a gap between the supply and the demand, where the demand exceeds the supply, which is why we're strong supporters of liquefied natural gas coming into this country.

MR. SALANT: As you know, polls have shown that many Americans believe that the oil industry is manipulating the price of oil to keep the Republicans in control of Congress. How do you respond?

MR. HOFMEISTER: I really respond with a smile on that kind of a conspiracy theory.

The oil industry has been one of the most sensitive industries that I've ever worked in -- and I've worked in several -- with respect to the antitrust issues. We simply do not talk to each other about issues like pricing. We would not talk to the White House about pricing. Pricing is set by market, and all we have are our own ideas, our own supplies to bring to market. Ultimately, prices are set by the market. The current rundown in prices is due very simply to the fact that we didn't have hurricanes this summer that shut down production facilities. And in anticipation of the hurricane season, we both built inventory for our own storage and we incentivized dealers along the Gulf Coast to keep their tanks full.

So there actually is a surplus of gasoline in the country for now, and it's also the end of the driving season.

Now, somebody's going to say, well, does that mean the prices go back up again after the election when the heating season comes onstream? Well, we don't know that. If the current demand situation prevails -- and demand right now, ladies and gentlemen, is about 5 percent greater than a year ago -- if the current demand situation prevails, we could see the current surplus of inventory being worked off, which would get us right back into the tight supply-demand relationship we had prior to the end of the hurricane season. So we don't predict prices. Our job instead is to try to address the supply situation.

In the case of Shell, we're working with our Motiva partner, a joint venture with Saudi Refining, to add 300,000 barrels a day capacity in our Port Arthur, Texas, refinery. That, along with some other industry moves, will go a long way towards easing some of the supply-demand crunch that we've been in the last couple of years.

MR. SALANT: What changes in energy environmental policies do you expect if the Democrats win control of both houses or one house of Congress?

MR. HOFMEISTER: I'm not sure that there's clarity yet on what the Democrats would do, and I think we would very much like to be involved in the debate. We have some experiences from around the world we'd like to share with members. We've already been sharing with members on both sides of the aisle. We'd like to be involved in discussing that. We have experience in cap and trade. We have experience with carbon taxes. We have experience with a number of different mandatory policies and regulations in different parts of the world. And so whatever policies they would propose, we'd simply like to be involved in the discussion.

MR. SALANT: This questioner notes that the Center for Responsive Politics reports that donations from the oil industry and its employees are running 83 percent for Republicans. Why is that?

MR. HOFMEISTER: (Pause.) (Laughter.) I don't know. (Laughter.) I can assure you that my contributions -- my own contributions are fully bipartisan, 50-50. And I watch that very closely, and I keep the list of who I give to religiously in a file in my assistant's drawer, so that I'm never going to be accused of being partisan. I really am promoting America, as an executive, promoting the democratic process, and I think both parties are important to this country.

MR. SALANT: Your industry works closely with the railroad industry to ship thousands of loads of oil and chemicals around the country. Shell has complained about rail service in the past. What is the current state of railroad market power, in your view? And are you considering moving manufacturing plants offshore as a result of rail rates that are too high or rail service that is inadequate?

MR. HOFMEISTER: I think the rail infrastructure suffers from the same reality that the oil infrastructure suffers from, and that is, nobody wants a train track in their backyard.

I do think that the nation's rails are stressed. I think that the availability of rail cars, limited by rail tracks, are a very serious problem for the country. We see huge investment requirements in places like Chicago and other major cities, where I think we need a huge infrastructure improvement. And just as the oil infrastructure needs to be developed in terms of more refining capacity and more off-shore and more on-shore development of assets, I think the rail industry faces the same.

And here's a more philosophical view. We like very much the lifestyle of the post-industrial information age that we live in, but ladies and gentlemen, we rely upon an industrial infrastructure to be able to enjoy that post-industrial life. And what we have to come to grips with as a nation, whether it's the oil industry or other industries, is developing that infrastructure, that industrial infrastructure which is the price we must all pay to enjoy the quality of life that we come to know.

MR. SALANT: With 100 percent control of Shell Canada, does Shell plan to send more Canadian oil to U.S. refineries?

MR. HOFMEISTER: As -- people may not realize, but this morning Shell announced that it was seeking to acquire minority shares that are currently in the Canadian market, and Shell Canada, which is a publicly listed company in Canada, would, if we acquired their shares, become a wholly owned subsidiary of Royal Dutch Shell, as Shell oil is in the United States. That offer was simply put forward today. There's still a long way before -- between making the offer and closing the deal and making the transaction come to place.

But as we said in the announcement, it does enable us, if it's a successful transaction, to look at North America as -- in terms of how we support both Canada and the United States. It enables us to look across. So whether that's the movement of product, whether that's development of natural resources, those things would happen across the continent as opposed to each country perhaps doing its own thing.

MR. SALANT: What does Shell and other firms doing to catch energy from the tar sands of Canada?

MR. HOFMEISTER: Shell Canada is currently heavily invested in the oil sands of Alberta, and we're producing somewhere well in excess of 100,000 barrels a day with plans already announced by Shell Canada to expand that to at least double the current capacity. And those plans are plans that were agreed to by the shareholders and would continue under this

transaction. We see the development of the oil sands as a great boost to the economy of Canada and a great new supply source for the United States and actually the global market for crude oil. And what we've demonstrated is the ability to produce oil efficiently and cost effectively as part of a national strategy in Canada, where the federal government got behind the project and the Alberta province got behind the project, and where the policymakers made it happen, it happened.

And part of my talk today, I hope you will see, is a message to policymakers that if we can get behind the policy to make it happen, the industry can then make it real.

MR. SALANT: Shell has had problems with overstated reserves. What is your position today?

MR. HOFMEISTER: We did a couple of years ago announce a write-down of some of our proven reserves, and it was as a consequence of having found through our own audits that some of the requirements to meet the SEC rules and regulations were not being followed by some of our subsidiary operating companies.

We've addressed that problem. We now have a clean bill of health on our reserves. But now we have to get more of our probable reserves, which excess well in excess of 50 billion barrels of probable reserves -- we need to move those into proven reserves. Thus, the heavy investment level, the 19 billion I mentioned for this year, the 21 billion for next year -- this is intended to get more of our probable reserves into the proven category, which means we are prepared to and ready to produce that oil and have built the infrastructure in place to produce that oil. We do think over a period of time that our reserve position, given that very, very large probable reserve position, will return to good health.

MR. SALANT: Jet fuel prices in some recent months rose to record levels. What do you think of the idea of a jet fuel reserve similar to the Strategic Petroleum Reserve that could be tapped in time of need?

MR. HOFMEISTER: One of the good aspects of the Strategic Petroleum Reserve is that we can lock up crude for as long as we want to lock it up.

One of the challenges, however, on a finished product reserve is that finished product degrades over time. And so a finished product really needs to be cycled through its end use as rapidly as we can so it doesn't degrade. And as a consequence of that, we would rather see the supply and demand balance achieved. We don't think there's really a need for the cost of creating such a reserve, and in any event, we would need to turn that reserve on a periodic basis to make sure the product was ever fresh.

MR. SALANT: I have a lot of questions about Shell operations overseas and in foreign countries, even in this hemisphere.

The first one dealt with Mexico. What role do you see for Mexico as a future supplier of more oil and gas to the United States? And will Mexico ever privatize its energy industry?

MR. HOFMEISTER: Well, the nationalization and management of oil in Mexico, of course, is part of the constitution of Mexico, and so any change would have to come as a consequence of a constitutional amendment for a Western oil company or any oil company other than PEMEX to operate in Mexico. That we would have to leave to the politicians in Mexico City to make something like that happen.

Shell, however, is a partner with PEMEX in the United States where we have a 50/50 joint venture and a refinery in Houston, Texas. PEMEX currently delivers a lot of oil to the United States and is likely to continue to do so in addition to meeting its own needs. We would very much welcome partnerships with PEMEX in the area of technology and other operations, but it would probably have to come at the price of a constitutional amendment, which is for the -- as I said, for the Mexican politicians to decide.

Shell has, however, been operating in the liquefied natural gas arena in Mexico. So we have a Baja re-gasification facility in partnership with Sempra, and we have a wholly owned -- or a partially owned -- where Shell is the majority holder -- of a facility in Altamira, Mexico, to bring natural -- liquefied natural gas into Mexico. And in addition, we're in the lubricants business in Mexico. So we are making some inroads.

MR. SALANT: Is Shell engaged in bidding for production sharing arrangements in Iraq? And if so, what fields?

MR. HOFMEISTER: Our current work in Iraq is limited to field analysis, where we have a contract with the Iraq Ministry of Oil to analyze in particular the northern oil fields.

Before we can actually participate in the oil industry activities in Iraq, we really have internally set three conditions on it, one of which is security, in which our employees could work safely; the second is the requirement that the rule of law, the adjudication system around contracts and so forth, would be such that disputes could be reconciled through a court of law; and thirdly, that we be actually invited into the country. None of those three have yet occurred, but we stand ready, willing and able.

MR. SALANT: Do you see Russia's huge oil and gas reserves as a possible solution to dwindling supplies of oil and gas in this country? Are you investing in development of Siberian oil reserves?

MR. HOFMEISTER: Shell has been involved in developing of reserves in Russia for a number of years. The largest project that we have is a -- in a -- on Sakhalin Island, which is actually one of the largest investments Shell has ever made in its history. It will come in at something like \$20 billion, when all is said and done.

In addition, we're working in a number of other projects throughout the country of Russia, and we'd like to do more.

MR. SALANT: In February 2006, a federal high court in Nigeria ordered Shell to pay \$1.5 billion to local communities in environmental damages. Shell has appealed. What's the status of that case?

MR. HOFMEISTER: It is still under appeal. We believe that the act is punitive by design, and we believe that under appeal our arguments will be heard, hopefully favorably. But for us, for a company like Shell to operate in Nigeria, we need to know that the rule of law is fair, that it is level playing field, and this particular bill passed in ways in which we question the process and in ways in which we think, a corporate citizen of Nigeria, we should be allowed to protect ourselves.

MR. SALANT: Does Shell get oil from Venezuela? And if so, are you worried about President Chavez?

MR. HOFMEISTER: Shell's been involved in Venezuela for nearly a hundred years. And we have been working there successfully under a variety of presidential administrations and different political regimes. Shell was one of the first companies in recent -- in the past year to renegotiate its contracts with Pedvesa, the national oil company of Venezuela, in a way in which it works in our business model, it works under the new constitution of Venezuela.

And because we are in it for the long term, we work very hard to work with all of the parties that may come to power in virtually any country around the world, provided that we can defend one important quality of Shell, and that is our business principles. And under the new contracts in Venezuela, we can protect our business principles, and we have a business model that we believe works economically. And as a consequence, we're quite pleased with the new contracts we have in Venezuela.

MR. SALANT: Speaking of Venezuela, CITGO is providing low-cost heating oil to poor communities in the U.S. Will you undertake a similar initiative?

MR. HOFMEISTER: It's Shell's position that the LIHEAP program, which is the Low-Income Heating Energy Program that Congress has passed, is a good program for the nation and should be fully funded. We think that it is better to apply contributions through government, through tax regime, through a general tax in which the lower-income people of the nation benefit from something like a heating-oil program. We think that a unilateral action by a particular company, while it may be politically popular in the city in which they provide fuel, becomes actually unpopular in the next-door city because people aren't getting what they're getting in the other city. So we'd rather see a uniform, level playing field in that arena as well, preferably through the tax system.

MR. SALANT: What is Shell's policy on conducting business operations in countries with serious human rights violations?

MR. HOFMEISTER: We take that very seriously. And as a consequence, we do not have operations in Burma. And we take that seriously around the world. We have a social responsibility agenda, and that includes human rights protection. We are part and parcel of the

United Nations in this area, in which we support actively the United Nations work in this arena. And we, I believe, are behaving according to our principles.

The debate over human rights, of course, is one that is a wide-ranging debate with many views on various sides of it. But we believe that by being in the game, in the discussion and in the debate and being -- and having ourselves monitored by third parties as we produce each year our sustainable development report which judges us across a wide range of factors, human rights being one of them.

MR. SALANT: What are some actions that each American can take to reduce the amount of gas and other energy we use without unduly affecting our lifestyles?

MR. HOFMEISTER: Boy, that word "unduly" could throw a lot of people. I remember being asked that question on the "Today" show when prices were much higher than they are today, and my response to Katie Couric was to say we could all slow down.

Now, that could unduly compromise a lot of people. A lot of people enjoy the speed at which they travel, and some would say that if they slowed down to the speed limit, they'd be run over by the people behind them.

I do think that there are steps that we can take, and in every Shell station across the nation is a list of helpful hints. This is to encourage you to go to your local Shell station and go get those helpful hints! (Laughter.) But there are helpful hints around inflating your tires, changing your oil, driving at lower speeds, stop the rapid acceleration or the rapid deceleration. There are some -- this is in transport fuels.

In terms of home management, well, each person chooses for themselves how they use electricity or how they use power in the home. I think there are a lot of individual actions that can be taken.

MR. SALANT: Is there anything that can be done to retrofit autos and other vehicles to run on E85 or other alternative fuels?

MR. HOFMEISTER: Not really. I think some people will try, and that's one of the great qualities of this country is the innovators who are out there. But the reality is as an engine is designed, it is designed around the fuels that it is expected to burn, and the kinds of metals that are chosen, the kinds of valves and seals that are used are very clearly designed with a fuel in mind. And by introducing a new fuel, it causes consequences that one might not be anxious to see. The Wall Street Journal recently ran an article on marine engines and the introduction of ethanol and the damage it was causing to older marine engines.

So engines are designed for a particular type of fuel, and I don't think add-ons will make a good difference.

MR. SALANT: How close are you to reaching a deal with the Interior Department over royalty price relief in the Gulf of Mexico drilling contracts?

MR. HOFMEISTER: I think we reached agreement in principle back in September. And the new secretary, Secretary Kempthorne, properly so, as a new Energy secretary -- or Department of Interior secretary, wanted to take his own look, fresh look at the issue of the '98-'99 leases. So essentially, he's assigned his new undersecretary to take a fresh look at that, and that may take some time.

But from Shell's point of view, as I testified in the House of Representatives back in June, we recognize that a mistake was made. We're prepared to try to correct the mistake going forward. We think that we had a contract up until the time that the mistake was made that should be honored, which means we should not go back retroactively and try to do something or the sanctity of contracts is amiss.

But on a go-forward basis, hey, we make mistakes as a company; others in the government can make mistakes. Let's fix the mistakes and move on. And so we reached agreement in principle with how to fix it. But, of course, the secretary is due his desire to take a fresh look, and we'll see what happens when he comes back.

MR. SALANT: Well, thank you very much for coming today.

Before we ask our last question, I would like to offer you the official National Press Club coffee mug. (Laughter.)

MR. HOFMEISTER: Thank you. Thank you.

MR. SALANT: And a certificate of appreciation for appearing here. Thank you.

MR. HOFMEISTER: Thank you, Jonathan. (Applause.) MR. SALANT: Our last question, in 15 years when you drive up to the Amish country to look at the -- your farmland, what kind of fuel will be powering your car? (Laughter.)

MR. HOFMEISTER: Why not a bicycle? (Laughter.) I would hope that it is a mixture of ethanol and gasoline or a hydrogen fuel cell alternative. That's what I would like to drive.

Thank you. (Applause.)

MR. SALANT: I'd like to thank everyone for coming today. I also would like to thank National Press Club staff members Melinda Cooke, Pat Nelson, Jo Anne Booze and Howard Rothman for organizing today's lunch. And thanks to the Eric Friedheim National Journalism Library at the National Press Club for its research. Research is available to all club members by calling 202-662-7523. Good afternoon. We're adjourned. (Sounds gavel.)

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