PARALLEL

LETTER TO STOCKHOLDERS

This year Parallel celebrates 20 years of operations. As a new millennium begins, your company is better positioned to benefit from a strong oil and gas industry than at any other time in its history.

What a difference a year can make. In late 1998, crude oil prices were at record lows and industry recovery was uncertain. In early 1999, oil and natural gas prices collapsed to 20-year lows of $10 per barrel and $1.50 per mcf. This year, however, we have seen oil prices as high as $31.00 per barrel and natural gas prices reach $3.40 per Mcf.

1999 HIGHLIGHTS

- **Through participation in a major acquisition in the Permian Basin of West Texas, our year-end proved reserves increased from 6.1 million EBOs to 15.5 million EBOs, on a combined basis.**
- **We continued adding to and high-grading our drilling inventory of 3-D natural gas prospects in the Yegua/Frio/Wilcox Gas Trend.**
- **Bank debt was reduced, increasing financial flexibility.**

Many small independent oil and gas companies did not survive the protracted period of low oil and gas prices and are not around today. Others were forced to sell properties at the bottom of the pricing cycle. We are proud to have survived the aftershock of 1998 and early 1999. Our low-cost structure helped us survive these tough economic conditions.

A REVIEW OF 1999

When reviewing 1999, it is important to remember that this was a year of recovery for the oil and gas industry, and for Parallel. During the year, we lived within our means. Because of capital constraints, we focused on meeting our drilling commitments and protecting our undeveloped leasehold position in the Yegua/Frio/Wilcox Gas Trend. We continued our drilling program, albeit at a slower pace, while protecting our upside in this trend.

The Form 10-K included with this annual report provides detailed financial and operational information. Instead of repeating this information, following are key statistics comparing 1999 and 1998 results:

- The average sales price we received per EBO increased 19%, from $12.31 in 1998 to $14.59 in 1999.
- 1999 revenues were basically flat when compared with 1998 revenues, despite a 16% decline in production volumes in 1999. This production decline was a result of normal production declines and curtailed drilling activities, which affected our ability to replace reserves.
- Operating cash flow declined slightly, from $4,627,312 in 1998 to $4,478,043 in 1999.
- EBITDA was basically flat when comparing 1999 with 1998.

Having weathered the worst, we are now benefitting from a recovery in the oil and natural gas sector. Strong oil and natural gas prices are providing excellent cash flows.

A NEW DIMENSION IS ADDED

Downturns in the oil and gas industry can result in opportunities to acquire producing properties, as can corporate mergers and consolidations. In early 1999, we were presented with the opportunity of a lifetime. We learned that Fina Oil and Chemical was marketing all of its producing oil and gas properties in the Permian Basin of West Texas, an area where we have operated for the past 20 years.

On June 25, 1999, we joined with three other oil and gas companies and formed First Permian, L.L.C., a Delaware limited liability company, to acquire the oil and gas properties from Fina Oil and Chemical Company. The owners of First Permian are Parallel, Baytech, Inc., Tejon Exploration Company and Mansefeldt Investment Corporation and affiliates. Baytech, Tejon and Mansefeldt are privately held oil and gas companies.

The Fina properties were considered among the best in the Permian Basin. Production is from shallow formations, primarily the San Andres, Glorietta and Clearfork, from 2,500 feet to 7,500 feet. Long-lived with low to flat production decline rates, the properties will be producing for many years to come.

The transaction included producing wells, proven development projects and other associated assets. In addition, secondary and tertiary recovery programs on key properties had been implemented and proven to be effective and costly production infrastructures were in place and paid for. These were added benefits.

We also believed the properties had significant upside potential that had not been exploited. Since there had not been an active program to develop additional reserves on the properties for the past three years, we believed infill drilling could add substantial reserves. In our opinion, there could be as many as 300 low-risk infill drilling locations on the First Permian properties.

The transaction was completed on June 30, 1999 when Fina transferred all of the oil and gas properties to a wholly owned subsidiary of Fina that was then merged into First Permian. As of December 31, 1999, Parallel and Baytech each owned a 35% membership interest in First Permian. Tejon Exploration, Mansefeldt Investment and affiliates of Mansefeldt owned the remaining 30% interest. Parallel and Baytech manage the day-to-day operations of First Permian.

WHAT FIRST PERMIAN MEANS TO PARALLEL

The First Permian transaction came at an opportune time for Parallel. Like other small exploration and production companies, our cash flows had declined substantially and access to other capital resources was difficult. However, for an initial cash investment of $3,500 and a loan guarantee of $10 million, we now own a 35% interest in a company with significant growth potential.

Noting that we completed the First Permian transaction in a down oil market is important. When we started negotiating the terms of the transaction in March 1999, oil was selling for about $12.50 a barrel. When we closed the transaction in July 1999, oil prices had increased to approximately $17 a barrel, an almost immediate increase in the value of our investment. Since then, oil prices have continued to rise to the $28.00 range.

Our ownership of First Permian strengthens the company in many ways.

- First, the First Permian properties complement our existing Permian Basin production and reserves and provide certain synergies of operations and technical expertise.
- Second, the properties are long-lived with low production decline rates. This helps offset the higher production decline rates of our reserve base in the Yegua/Frio/Wilcox Gas Trend, which is primarily natural gas. Given the higher decline rates of natural gas reserves, a company must work very hard just to hold production flat, much less to grow it significantly. Couple a high production decline rate with reduced drilling activity in the recent past and you can easily see why Parallel's production volumes and proved reserves did not increase during this period.
- Third, our share of First Permian's proved reserves provides us with reserve stability. At December 31, 1999, the reserve life of First Permian's properties (total estimated proved reserves divided by the prior 12 months production) was approximately 35 years. This compares with the reserve life of Parallel's proved reserves, on a stand alone basis, of approximately six years. After including our 35% share of First Permian's oil and gas reserves, at December 31, 1999, the reserve life of our properties increased to approximately 16 years.
- Fourth, because the First Permian properties are primarily oil producing, we are now leveraged to both oil and natural gas

markets. On a combined basis, at year-end 1999, oil reserves comprised 73 percent of Parallel's proved reserves and natural gas reserves comprised 27%. We are positioned to benefit from both strong oil and natural gas prices.

- Fifth, our 35% interest in First Permian improved our year-end reserves dramatically. On a stand alone basis, Parallel's oil and gas reserves at December 31, 1999, totaled 1.0 million barrels of oil (Mmbl) and 17.3 billion cubic feet of gas (Bcf), or 3.9 million equivalent barrels of oil (Mmebo). This compares with 1.7 Mmbl and 26 Bcf, or 6.1 Mmebo, at December 31, 1998. The pretax present value, discounted at 10%, of Parallel's 1999 estimated proved reserves was approximately $25.5 million compared with $26.8 million in 1998.

As of December 31, 1999, First Permian's proved reserves totaled 29.2 Mmbl of oil and 23.4 Bcf of natural gas. Based on our 35% interest, this represented 10.2 Mmbl of oil and 8.2 Bcf of natural gas, net to Parallel's interest, or 11.6 Mmebo. The pretax present value, discounted at 10%, of Parallel's 35% share of the 1999 estimated proved reserves of First Permian was approximately $73.7 million. On a combined basis, Parallel's proved reserves totaled 15.5 Mmebo of oil with a pretax present value of $99.2 million.

- Last, our ownership in First Permian provides us with a more diversified drilling portfolio through our exploratory natural gas drilling activities in the Yegua/Frio/Wilcox Gas Trend and through participation in First Permian's program of low-risk infill drilling to develop proved undeveloped oil reserves in the Permian Basin.

THE FUTURE OF THE OIL AND GAS INDUSTRY

The energy industry is changing daily. Technologies keep emerging and advancing, changing the way we do business both in the field and in the office. Consolidation and mergers continue, increasing competitiveness in the industry. But the importance of energy to the world's economic growth remains unchanged. North American drilling activity has increased healthily in recent months, suggesting a belief in the stability of oil and natural gas prices. This rebound has been driven primarily by an increase in drilling for natural gas reserves.

Demand for oil remains strong, with global demand expected to grow approximately 2.4% this year. Many oil analysts predict that the price of oil will not fall below $20 a barrel and will average between $20 and $25 per barrel for the next several years, particularly in view of the recent cooperation of OPEC regarding production output and price stabilization.

The positive trends in natural gas supply and demand and recent price increases are also encouraging. One important factor driving natural gas demand is the rapidly increasing demand for electricity generated using natural gas. This may have downplayed the effects of another record-breaking warm winter and suggests that cold weather may no longer be the driving force in determining natural gas prices. For example, natural gas storage levels are at all time lows despite three years of record warm winters. Other factors influencing strong natural gas demand include increased cooling needs because of warmer weather, environmental concerns and increased industrial usage because of fuel switching.

Another important factor that bodes well for a strong natural gas market is the time lag between an increase in drilling activity and meaningful production increases. Decline rates of natural gas wells are steep, particularly in the Gulf of Mexico, which produces most of the domestic natural gas supply. The decrease in drilling activity in 1998 and 1999 means that fewer natural gas reserves have been replaced.

PARALLEL

LETTER TO STOCKHOLDERS

GROWTH STRATEGY

Our growth strategy for the immediate future will focus on:

- **Accelerating the drilling of high impact, lower-risk natural gas prospects in the Yegua/Frio/ Wilcox Gas Trend.**

  Ideally, an exploration company should have a large pool of prospective drilling opportunities relative to its annual projected drilling activity to be able to invest capital dollars efficiently. Since we have a large inventory of drilling prospects to choose from, the odds of drilling successes are greater because we can high-grade our inventory and selectively drill the lowest risk, highest reward prospects.

- **Benefiting from accelerating the drilling of low-risk infill oil wells through our interest in First Permian.**

  As a condition of obtaining bank financing to acquire the Fina properties, First Permian was required to hedge a substantial portion of its oil production. While this limits First Permian's ability to benefit from current high oil prices, it does provide downside price protection. In July 2001, the current oil hedge will expire.

  However, any new barrels First Permian adds through infill drilling activities during the remaining period of the hedge contract in excess of the required hedge volumes are not subject to hedging. Therefore, in this time of high oil prices, a key part of First Permian's 2000 business plan is to accelerate its infill drilling program.

- **Managing risks.**

  We manage drilling risk by using leading edge 3-D seismic technologies to delineate drilling locations. Our historical drilling success ratio of 73% illustrates the effectiveness of these technologies. To manage financial risk, we reduce our interests in selected higher-risk, costlier prospects.

- **Monetizing our investment in First Permian.**

  As management, it is our responsibility to ensure that the investment in First Permian is viewed as a meaningful component of Parallel's overall value. A key part of our long term growth strategy is to evaluate options that will allow us to monetize our interest in First Permian.

OUTLOOK

As we enter the year 2000, we are excited about the future of Parallel. With our 35% interest in First Permian, we have provided for the long term reserve stability of the company and added a new dimension of growth.

We believe the energy industry has a bright future, as does Parallel. By investing in First Permian, we have moved aggressively to make your company stronger. We are prepared to participate in the exciting period of growth that lies ahead.

Sincerely,

Chairman of the Board

President