

SPR Authorities: Adequate or Anachronistic?

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PetroStocks 2007: New Perspectives
New Orleans, Louisiana
January 30, 2007**

Authorities for Use of the SPR

- ✓ **Emergency supply disruption (unlimited drawdown)**
- ✓ **Anticipated emergency supply disruption (30 million barrel limit)**
- ✓ **5 million barrel test sale**
- ✓ **Exchange of oil to acquire oil (unlimited)**
- ✓ **Royalty-in-kind (limited by unused space in SPR)**
- ✓ **Leasing space (limited by unused space in SPR)**

Definition of “Severe Energy Supply Interruption”

“...if the President determines that –

(A) an emergency situation exists and there is a significant reduction in supply which is of significant scope and duration;

(B) a severe increase in the price of petroleum products has resulted from such emergency situation; and

(C) such price increase is likely to cause a major adverse impact on the national economy.”

Historical Uses of the SPR

Emergency supply disruption authority

- ✓ Gulf War I
- ✓ Hurricane Katrina

RIK Authority

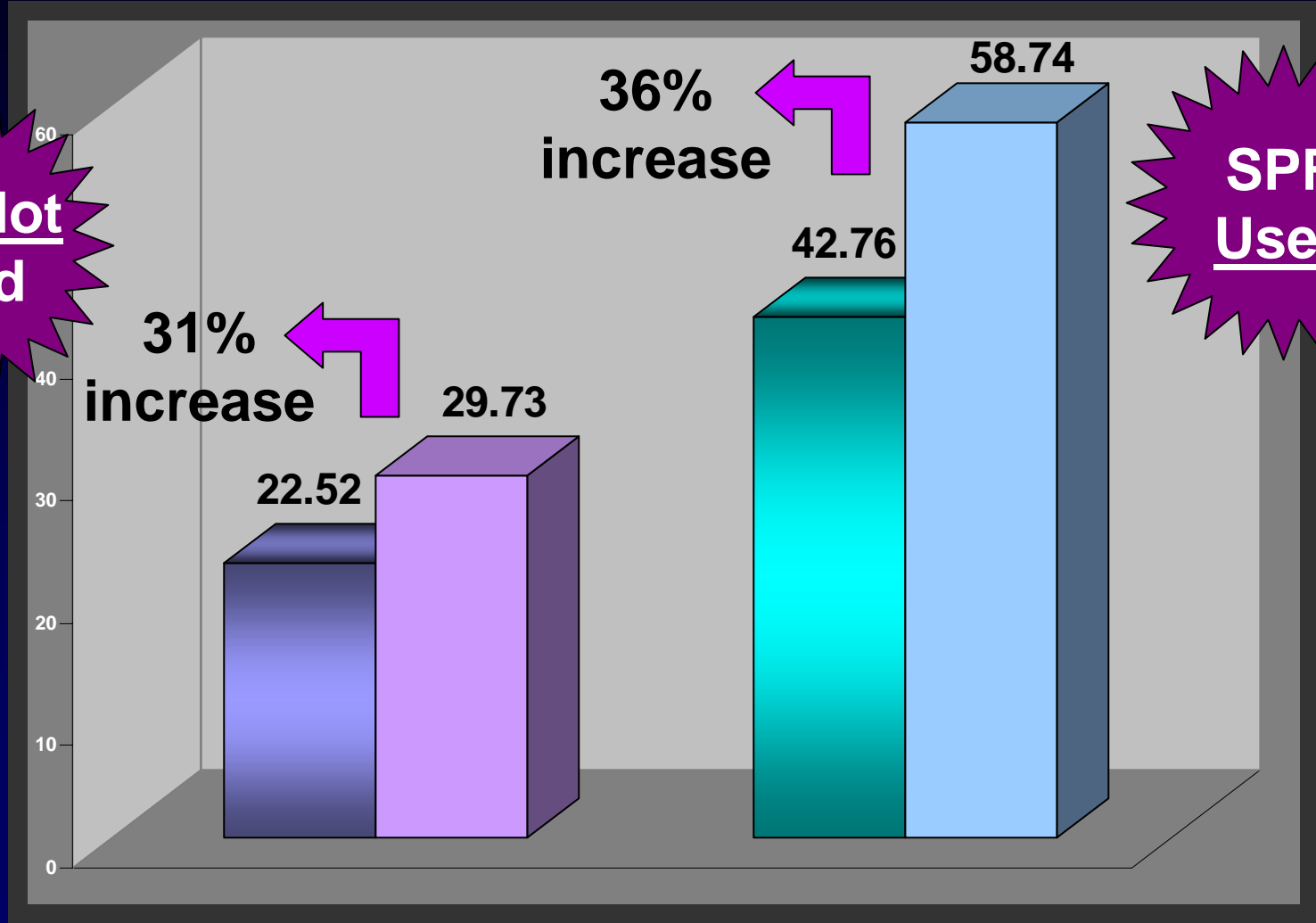
- ✓ 1998/99 to replace volumes sold at Congressional direction
- ✓ 2002-2006 to fill the Reserve to capacity

Exchange of Oil to Acquire Oil Authority

- ✓ Arco
- ✓ Maya Crude
- ✓ Citgo/Conoco (2)
- ✓ To Establish Heating Oil Reserve
- ✓ 2000 Heating Oil Shortage
- ✓ Hurricane Lili
- ✓ Hurricane Ivan
- ✓ Hurricane Katrina

What is the Trigger ??????

**SPR Not
Used**



SPR Used

PDVSA Strike

Hurricane Katrina

1973 Oil Markets vs. Today's

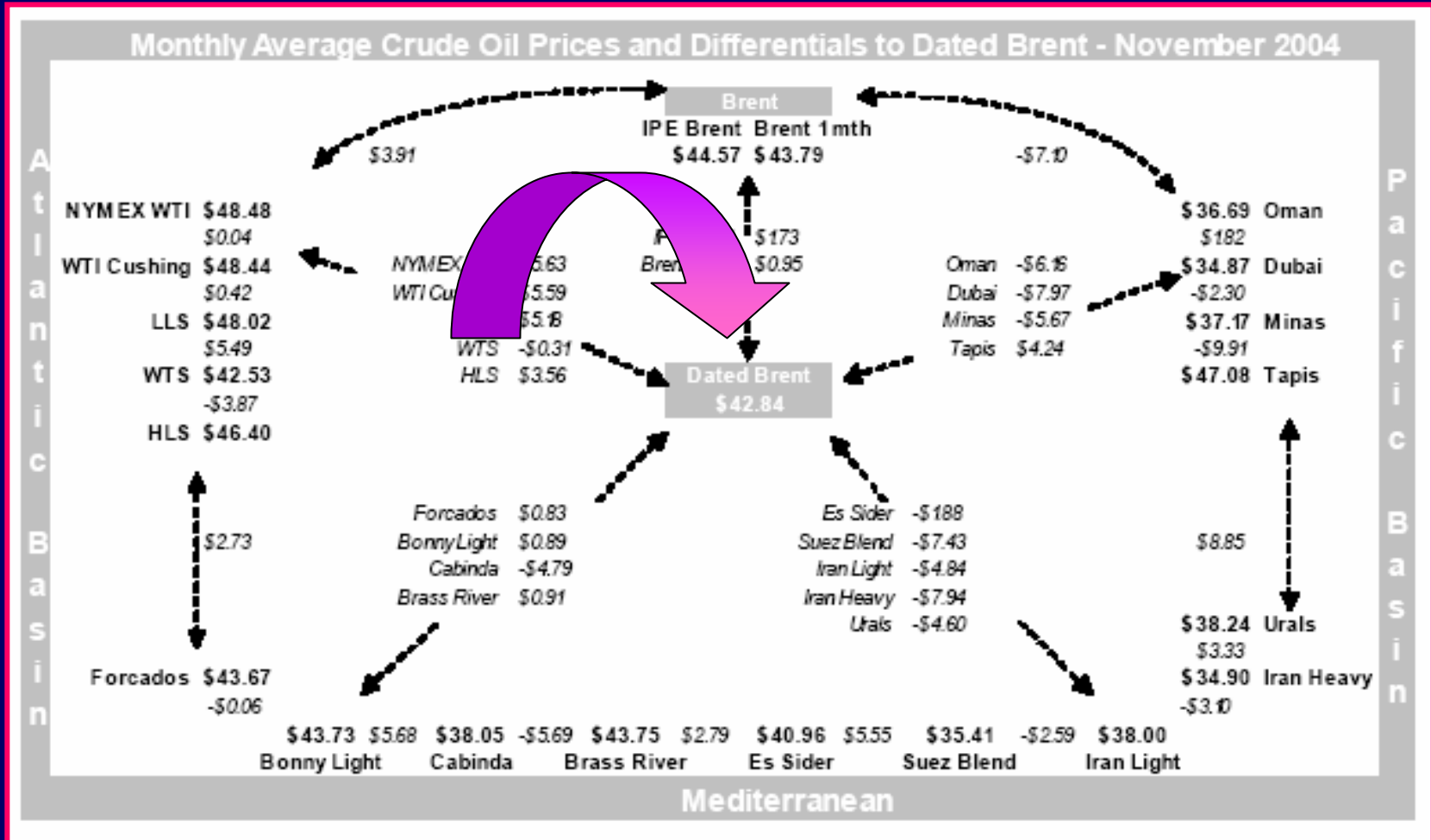
1973

- US crude and product prices were controlled during the Nixon Administration
- Greater working stocks were required because controlled markets were inherently inefficient
- Disruptions were measured by number of barrels lost
- No futures markets
- High energy intensity
- No spare capacity
- No IEA
- No SPR
- **Real threat: Supply Disruptions**

Current

- Oil markets are deregulated, markets are deemed most appropriate to manage scarcity
- Competitive markets have discouraged the holding of inventory
- Disruptions in long term are ineffective as oil supply is managed by markets e.g. tight supplies raise prices, high prices reduce demand
- Supplies are diversified and there is some excess capacity
- Improved energy intensity
- We have IEA, the SPR
- NYMEX and IPE help manage risk
- **The real threat: price spikes.**

World Oil Markets: Price Spikes Anywhere = Price Spikes Everywhere



100% Domestic Oil Sufficiency Will Not Protect US From Price Spikes

United Kingdom

- ▶ Produced 2.38 MMB/D, Consumed 1.69 MMB/D, Net Exports 0.69 MMB/D

Norway

- ▶ Produced 3.18 MMB/D, Consumed 0.264 MMB/D, Net Exports 2.92 MMB/D

In 2000, when oil prices rose, prices in UK and Norway rose like elsewhere



UK protests trigger fuel shortages



SPR Exchange, September, 2000

Situation

- ✓ August, 2000, Northeast heating oil stocks down 42% over 1999 levels, New England down 72%
- ✓ Market severely backwardated
- ✓ Oil prices hit \$37 per barrel
- ✓ OPEC increased production 4 mbpd since 2/2000
- ✓ OPEC hitting productive capacity

Action Taken

- ✓ 30 million barrel exchange
- ✓ Utilized authorities to “exchange oil to acquire oil”
- ✓ Did not utilize emergency authorities

SPR Exchange 2000: The Result

- ✓ **10 million barrels refined in US**
- ✓ **20 million barrels backed out to Europe**
- ✓ **Arbitrage between Europe and US reverses, stopping US heating oil exports to Europe**
- ✓ **4.5 million barrels ultimately added to SPR at no cost to the taxpayer**
- ✓ **No heating oil shortages in winter 2000/2001**

Are SPR Authorities Adequate or Anachronistic?

In today's global oil markets,
oil price volatility is the
equivalent of yesterday's
supply disruptions