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Open The Spigot

In late June, the International Energy Agency(IEA) announced plans to release a small portion of its petroleum reserves, providing an additional 60 million barrels to global crude oil supplies over a one-month period. As a significant part of this program, supplies from the US Strategic Petroleum Reserve will contribute half the oil. The stated rationale for this move is to replace supplies lost to the war in Libya. The immediate market response was a five percent drop in oil prices, with US-crude falling to $90 per barrel.

Initial thoughts include a simple observation: US administrations have developed a pattern of opening the Strategic Reserve for less than strategic reasons. In 1990-91 the reserve was opened during Desert Storm, our first war in Iraq. Six years later, the spigot was opened again, without much reason. The Reserve was tapped again in 2005, after Hurricane Katrina shut down much of our Gulf-based production. And now, six years later, we have a new and improved excuse to flood the market with oil. Add it all up, and the last four administrations have tapped into our Strategic Reserve, often providing unneeded oil.

Unneeded you say? Well yes. In this case, oil prices had already dropped 17% from their April highs, and were basically flat for the year. Saudi Arabia just a week prior announced plans to unilaterally increase production, filling much of the void from Libya's shortfall. But our economy is struggling -- fiscal stimulus is out of bullets, the Federal Reserve will accommodate, but QE2 is completed and QE3 is not even half baked. So, short of reverting to capitalism, what is a meddling administration to do?

Political expediency aside, is there more to it? Perhaps. There are two possible targets with nothing in common other than oil itself. First are the energy traders, those evil speculators, whose only motive, according to the narrative, is to profit at the expense of the US economy. Sure they are only a small part of an $8 billion per day oil market, and sure they may position for declining prices just as easily as rising prices, and sure they have their own capital at risk, but no matter. They play the villain so well. Oil traders should heed the warning: drive prices too high and the government will raid your party.

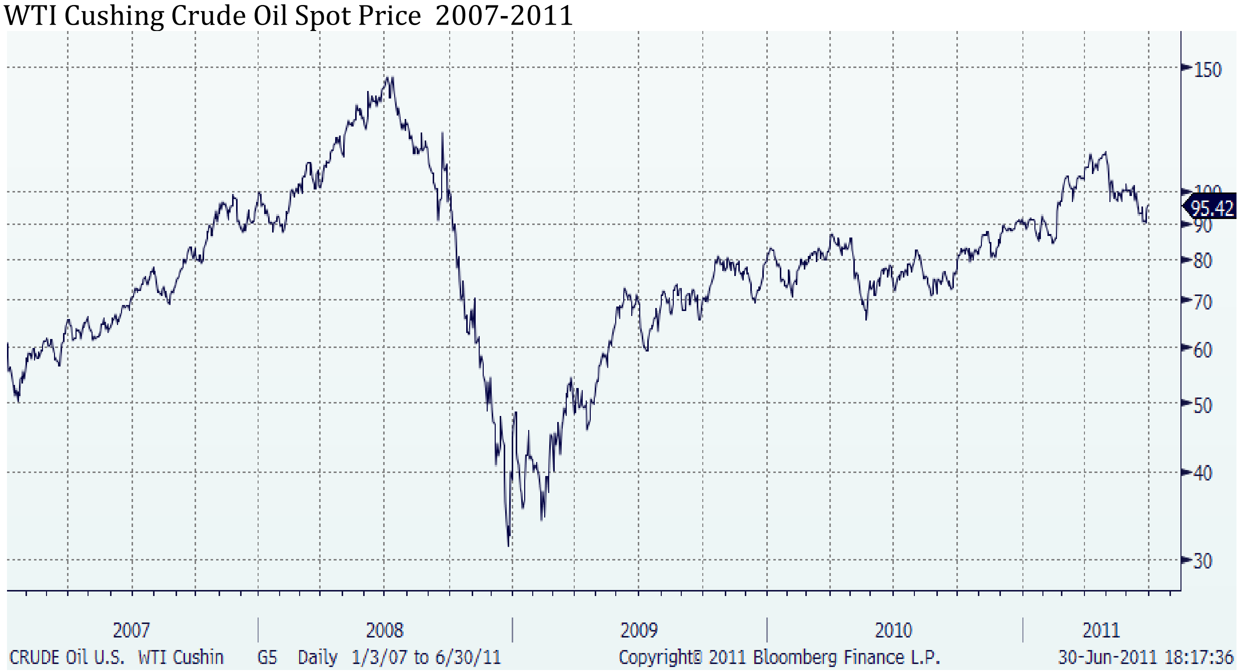
The second target is much more intriguing, as it plays into geo-politics. The US and Saudi Arabia have a common enemy, one that is stirring up far too much trouble in the Middle East -- Iran. The Saudi's may earn the same or greater oil profit by raising production, but Iran, lacking spare capacity, suffers from a drop in oil revenues whenever prices fall. The reserve release may be a stopgap measure to immediately pressure Iran, with increased Saudi production coming online in the months ahead. From this standpoint, who doesn't love a geo-political thriller with Iran as the target?

Given so many plot twists, what are we to make of this plan? From a broader perspective, there is too much fodder for the cynics. Years ago we banned drilling in oil-rich portions of Alaska's North Slope. Off-shore production has long been restricted. Last year we imposed a moratorium on drilling in the Gulf of Mexico. Congress recently voted against plans to expand domestic output. The EPA has initiated actions to de-commission a number of coal-fired power plants. Nuclear power is again seen as too risky. Anything that does not rhyme with 'green energy' is becoming taboo. With every chance, we increase our reliance on foreign oil. At the same time, we find the rising price of oil to be an ongoing irritation.

Somewhere, somebody needs a basic economics lesson.
Let's try this one: restricted supply and rising demand = higher prices.

The sad reality is this: For decades the US has had no coherent policy for energy independence. No short term tactical strike against market forces -- or traders, or big oil, or whomever the bad guy is supposed to be -- will change that fact.

WTI Cushing Crude Oil Spot Price 2007-2011



Tidbits..

Zillow report says 28% of home mortgages in US are under water.
Case-Shiller Home Price index drops to eight-year low level.

Five years in and still no relief for the nationwide housing disaster.

Galleon Group hedge fund tycoon Raj Rajaratnam convicted as leader of insider trading ring.

Nobody likes a cheating billionaire.

Medicare on path to insolvency in 2024, five years earlier than prior estimate.

For government spending, the real elephant in the room.

Federal debt ceiling is reached, officials warn of financial apocalypse.

Bond market, all-knowing, lets out collective yawn.

Networking site LinkedIn goes public, attains $8 billion market value.

Let the newest IPO craze begin.

US Senate drills oil executives, then nixes plan to expand domestic drilling.

In Washington, the search for intelligent life continues.

EPA exempts dairy industry from rules designating milk as oil, subjecting farmers to oil-spill regulations.

Can't make this stuff up.

Federal Reserve lowers US economic growth forecast, yet again.

How many guesses do they get?

Congress, New York investigators turn up scrutiny of Goldman Sachs.

If losing money in a crisis is not a crime, then making money must be?

News Corp to jettison MySpace for $35 million, take 94% loss on investment.

A real trick: turn social networking and market leadership into financial disaster.

White House floats idea of 56 miles per gallon fuel economy target for autos.

Why stop the fantasy at 56? Go for 100!

Federal Reserve Chairman Bernanke receives 30% approval rating in public opinion poll.

And 10% of the public knows what the Federal Reserve does.

Misery Index, combining unemployment and inflation, reaches 28 year high.

No wonder it feels so bad.