The Senate on price gouging

Posted by Yankee on September 7, 2005 - 8:33am
Topic: Economics/Finance

Update [2005-9-8 9:17:14 by ianqui]: John Whitehead of Environmental Economics has a post called "Gas price politics" on his personal blog Hypothetical Bias. He discusses why both Republicans and Democrats are getting it wrong with respect to high gas prices.

(Original post) Yesterday, Super G opened up a discussion about what level is the biggest cause of the rising price of gasoline. Our source, who helped explain how the industry works, suspects that price gouging is most likely to be found at the retail level—the people who own gas stations. He also explained that oil companies *are* doing well right now, but it's because the oil futures market has bid the price up to $70/barrel for oil that was originally priced at $15-20/barrel.

If only the government understood how the market works. This morning, NPR had a story about yesterday's Senate Energy and Natural Resources Committee meeting. This meeting had been scheduled even before Katrina hit, and the Senators were already intent on sticking it to Big Oil.

At the meeting, Dianne Feinstein (D-CA) gave profit numbers for the first 6 months of this year for several companies: Exxon $31 billion, Conoco $12.1 billion, BP $20.9 billion. "Price of oil will bankrupt airlines...and it's just a question of time before it begins to destroy the economy," Feinstein said.

Other senators, like Lisa Murkowski (R-AK) noted a concern for farmers and ranchers, while Byron Dorgan (D-ND) wants to introduce a bill that imposes a windfall profits rebate on big oil. He asked, "Will you do nothing when you have an industry that will reap a windfall of $80b?"

The direction that Feinstein, Murkowski, and Dorgan are going in troubles me. If I understand our previous post, it's merely coincidental that Big Oil is reaping windfall profits right now. The fact that oil is $70/barrel, which is the biggest contributor to high gasoline prices, has to do with the world futures market, not because Big Oil is free to set the price of crude at whatever they want. This seems crucial, and it seems dangerous for the Senate not to understand it. Taxing Big Oil is not going to bring down the price of gas.

The New York Times also had an article on the meeting. In light of prices, it's been suggested that environmental controls on different types of gas and additives be relaxed, and drilling in Alaska comes up again:

> Several others argued for expanding domestic oil drilling in Alaska and offshore. Pointing the finger at environmental regulations he blamed for constricting domestic oil supplies, Senator Larry Craig, Republican of Idaho, questioned his colleagues stern words for the oil companies and other energy producers.

But there were also some positives (though perhaps only symbolic):

> Senator Domenici and Senator Jeff Bingaman, who is also from New Mexico and the ranking Democrat on the committee, agreed to send a letter to President Bush asking him to require government agencies to begin conserving gas in their vehicles, saying that would set an example for consumers.

Up until now I've been optimistic, but maybe I should rethink my belief that the government will have to be involved in helping us find solutions to the US's ever-increasing demand for oil.

Update [2005-9-7 14:13:15 by ianqui]: Our industry insider emailed me to say that refiners are not the ones causing a quick rise of prices at the pump:

> Refiners are NOT the guys raising prices instantaneously—they cannot due to contract agrements. Refiners could not engineer a price increase across all brands in a matter of days—their deliveries are contracted. Gasoline isn't pooled up in tanks and then auctioned off—gasoline deliveries are planned by dates and CONTRACTED....
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> Oil and gas and everything else in the petroleum stream are based on contracted delivery. Failure to deliver and failure to accept delivery each have financial consequences.
>
> This leaves distributors (who are notoriously greedy and secretive) and retailers (who have a lot of profit at stake even at pennies a gallon due to high corporate volumes) as the guys possibly gouging.
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> But as I said yesterday, the point is—NOT oil companies.

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