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A Note On A Proposal To Ban Heating Oil Exports

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President**

October 1996

Heating Oil And The Export Administration Act *Or Just Don't Do It**

Under the Export Administration Act, the President has the authority to ban exports of scarce materials if he believes these exports would seriously impact inflation and damage the economy. While the Export Administration Act has expired the President has apparently maintained his authorities through an Executive Order.

There has been some consideration given to banning heating oil exports. Curiously, a ban on heating oil exports might prove to be inflationary and therefore have the opposite effect that the Administration wants. Obviously, a ban on heating oil exports would initially drive prices down. However, all other things won't remain equal.

First Europe has been an important supply source of gasoline for the U.S. markets. These imports have prevented gasoline prices in the U.S. from fully rising to reflect the change in crude oil prices. These imports are responsible for the poor U.S. refinery margins (despite the fact that U.S. refiners are operating at over 95% of capacity). The gasoline is being imported in the same ships that are carrying the heating oil to Europe. This backhaul results in enormous economies since these ships would normally come back empty. If we banned exports there would be no backhaul imports. Secondly, our European allies who need the middle distillates might interpret our ban in political terms. We already have major disagreements with them over our sanctions policy and some European allies might choose to retaliate.

It's important to remember that gasoline plays a much more important role in the U.S. Economy than heating oil does. In addition, it has a much higher weighing in our inflation indices. Therefore, a ban on heating oil exports would result in some loss of gasoline imports (the size of the loss would depend upon our allies response). Weighted gasoline prices could rise under this scenario more than domestic heating oil prices might fall. The net result would be inflationary.

P.S. The government must also understand that heating oil trades in a global environment. A ban on heating oil exports might initially lower domestic prices. However, Europe would immediately try to replace these needed barrels by bidding up the price and redirecting Canadian and Caribbean supplies away from the U.S.. While the process would take a little while the end result would be somewhat higher prices for gasoline in the U.S. and no net impact on heating oils.

* The first note dealt with the proposal to exchange SPR crude for heating oil.