Selling The Strategic Petroleum Reserve
or The Proverbial Free Lunch
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On May 21st, the House Energy and Commerce Committee voted 51 to 0 to approve a healthcare bill that would be funded in part through 8 annual sales of 8 million barrels of crude oil from The strategic Petroleum Reserve. The sale would reduce the size of the reserve by nearly 10% and according to the Congressional Budget Office would raise $5.4 billion. Since each annual sale is relatively small, Congress believes that they won't have their hand caught in the cookie jar and may in fact have discovered the "**proverbial free lunch**". We believe that this is a dangerous precedent and once you start down this oily slope there will be no way to slow it down.

One could argue that we could get by with a smaller Strategic Petroleum Reserve. Coverage for imports far exceeds our treaty obligations, and aren't we planning to get off petroleum anyway? Yet oil demand has turned around and is growing very sharply this year. Prices are down nearly 50%, rig activity has collapsed and the growth rate in domestic production is slowing dramatically and could very likely turn negative starting next year.

Certainly, how we think about the SPR should change, but we should be very cautious in making any assumptions about our current good fortunes.

If we've learned anything since the first Arab Embargo, it is that we should have a certain level of humility when looking at the future of the oil markets. It was only 5 years ago that the best and brightest analysts were forecasting inevitable declines in U.S. oil/gas production. We were planning for the import of 12-15 BCF of LNG imports. Now, we are looking to become a major exporter of LNG. Keep in mind that a supply disruption anywhere is a price increase everywhere regardless of your dependency on foreign supply. Secretary of Energy, Ernie Moniz, made this very point at a recent annual meeting in D.C. when he stated that even with our rising domestic production, a sudden loss of supply from the world market would spike world oil prices and inflict enormous damage on the national economy.

Th SPR was created in the aftermath of the 1973-74 Arab Embargo as a strategic counterweight to the then power of OPEC. A central concern among policy makers was the threat from growing reliance on insecure imports from production centers that might disrupt the flow of petroleum to the United States and its allies. Congress authorized the construction of the SPR as part of the 1975 Energy Policy and Conservation Act (EPCA). The U.S has long-standing treaty obligations to cover at least 90 days of petroleum imports. Thanks in part to hydraulic fracking, we are well in excess of that level.

However, that in itself doesn't justify selling a portion of the Reserve to fund general congressional programs. The Reserve was established as a **strategic asset** to minimize economic dislocations during supply disruptions. And we would argue that **yes, size matters** here. The SPR is both an insurance policy and a deterrent against someone wanting to disrupt supply. It not only reduces the pain of a cutoff, it also reduces the probability of a purposeful occurrence. As we look around the world today, it is hard to be complacent. A substantial amount of oil is already being disrupted, Yemen, Syria, Sudan, Libya, Nigeria, and Columbia to name a few.

We support a vigorous debate on the appropriate size and composition of the SPR, but we should have this debate before we undertake piecemeal changes in the size or use of the strategic stocks. We would do no less before making decisions on the size of our naval fleet, the number of army divisions, or our air force squadrons.