US export ban has oil producers over barrel

By Ed Crooks

October 14, 2013

Only five years ago, the US ban on crude oil exports looked about as relevant a piece of legislation as an ordinance against riding unicorns.

Today, it is rapidly becoming one of the US oil industry's most worrying issues: a regulatory restraint that is affecting business decisions, and is likely to create increasingly severe distortions in the next few years.

It is particularly troubling because although the prohibition is an artefact of a very different time, it is likely to prove difficult to remove.

As Maria van der Hoeven, executive director of the International Energy Agency, put it in an article for the Financial Times this year: "Washington will need to address this misalignment, lest the great American oil boom goes bust."

Until very recently, US crude oil exports seemed a purely theoretical proposition. After steady decline since its peak in 1970, US crude production hit a low point of just 5m barrels a day in 2008, and seemed to be heading inexorably lower. Domestic production provided just two-thirds of the crude used in US refineries.

Half a decade later, the position has been turned on its head.

Booming production and weak demand have sent America's oil imports plunging, to the point that it has fallen behind China as the world's largest net oil importer.

Some analysts believe that by the end of the decade, US net oil imports, which are about 6.2m b/d today, may be negligible.

Gushers of light and sweet oil are flowing from the Eagle Ford shale of south Texas and the Bakken shale of North Dakota, creating a flood of crude in the storage tanks and refineries of Oklahoma and the Texas coast.

If, as many analysts expect, production from those shales continues to grow, and production from newer growth areas such as the Permian Basin of west Texas also rises strongly, the US is likely to be left with a glut of oil in the Gulf of Mexico region that has nowhere to go.

The US ban on crude oil exports dates from the 1975 Energy Policy and Conservation Act, reinforced by the 1979 Export Administration Act. In the energy crisis-conscious 1970s, with US oil production in steep decline, these seemed sensible measures to protect domestic crude for American consumers.

Crude oil can be exported with a special licence, but very few have been granted. Exports from Alaska were approved in 1996, although no crude has actually gone to a foreign market since 2004.

A few licences for exports to Canada that have a special dispensation making approvals easier were sought by oil companies last year. A single cargo of oil left the US for China this year, apparently foreign crude that was being re-exported. In general, though, crude is trapped in the US.

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Gas exports face similar restrictions under the 1938 Natural Gas Act, but the Obama administration has been moving to relax those restraints. More than 20 projects have been approved to export liquefied natural gas to countries that have a trade agreement with the US, and four have been approved to export to countries without such agreements.

Licences for oil exports, however, are more difficult to obtain. As Scott Lincicome of the Cato Institute, the free-market think-tank, puts it: "With natural gas, the law is 'export unless', but with crude oil the law is 'ban unless'."

As the build-up of crude in the US began, it drove down West Texas Intermediate and other onshore benchmarks relative to internationally traded crude. Last November, the spread between WTI and Brent prices widened to $26 per barrel.

Since then, added pipeline capacity has come on-stream to carry oil to the Gulf of Mexico coast, and more is coming, including the lower section of the controversial Keystone XL project, now known as the Gulf Coast Project, which is set to be in use before the end of the year.

The effect of that has been to close the WTI-Brent spread down to about $7 per barrel, but promises merely to shift the glut down to the gulf region.

Already, refiners have been saying that they no longer use any imported light and sweet (low-sulphur) crude in their gulf coast refineries, because those varieties are in plentiful supply from US production.

Many refineries in the region, however, have been designed to work best with heavy and sour (high-sulphur) crude, and have relationships with parent companies in Saudi Arabia and Venezuela that mean they will want to continue importing.

It would be tough even for a Republican from Texas to [allow more oil exports]. For the Obama administration, it's even more so

- Scott Lincicome of the Cato Institute, the free-market think-tank

As a result, Mr Lincicome says, the problems of excess US oil in the gulf region will become critical long before oil imports actually drop to zero.

Companies have been getting around the ban by exporting more refined products, including very lightly refined oil that requires further processing. US refined products exports have trebled since 2005.

Other expensive workarounds are being used, including transporting more oil by train and tanker to the east and west coasts.

Before much longer, however, the export ban risks creating an artificial glut of US oil, forcing down prices and choking off production.

For both President Barack Obama and the US Congress, there is little political capital to be gained from allowing more oil exports, pushing up domestic oil prices to help foreign consumers and the oil companies.

"It would be tough even for a Republican from Texas to do it," says the Cato Institute's Mr Lincicome. "For the Obama administration, it's even more so."

As the tensions mount, the oil industry can be expected to become increasingly vocal.

The impact of the export ban may be a problem that comes with success, but it is nevertheless a serious threat.