

Shut down the Strategic Petroleum Reserve

By [Jerry Taylor & Peter van Doren](#) 11:55 AM 06/28/2011

Whenever gasoline prices go through the roof, we're treated to the same, never-ending political spat that we went through last week; liberals want to release crude from the U.S. Strategic Petroleum Reserve (SPR) to help poor, downtrodden motorists while conservatives scream that the SPR is for supply emergencies only and not for domestic political gestures.

Who's right? In truth, neither side has a good argument. The SPR is worse than a waste of billions of taxpayer dollars; it's a counterproductive entity that ought to be emptied and then shut down while the emptying (selling) is good.

Let's take a [look](#) at the GOP's argument first. Republicans are right to claim that the SPR was established in 1975 to respond to "severe energy supply disruptions" (it's right there in the legislative [language](#)), which are defined in the enabling statute as "(A) is, or is likely to be, of significant scope and duration, and of an emergency nature; (B) may cause major adverse impact on national safety or the national economy; and (C) results, or is likely to result, from (i) an interruption in the supply of imported petroleum products, (ii) an interruption in the supply of domestic petroleum products, or (iii) sabotage or an act of God."

In other words, pretty much anything on the supply side of the ledger that causes prices to go up can be construed as a "severe energy supply disruption." Score one for the left.

Nonetheless, the explicit political rationale behind the establishment of the SPR was to ensure that no future oil embargo could starve the nation of crude oil as the 1973 Arab oil embargo was alleged to have done. We say "alleged" because the embargo did no such thing. All that happened during the embargo was a game of musical chairs in world oil markets. Instead of buying oil from Arab members of OPEC, we increased crude oil purchases from non-Arab producers. Imports in 1973 were actually greater than they were in 1972, and imports in 1974 were, in turn, greater than they were in 1973. There was, on balance, absolutely no reduction of imports as a consequence of the embargo.

The lesson here is that an oil embargo against the U.S. is incapable of preventing oil imports from reaching American ports. That's doubly true given today's global oil market because once oil leaves the territory of a producer, market agents dictate where the oil eventually gets refined, not the agents of the producer. The [globalization](#) of oil markets ensures that the United States will always have access to Persian Gulf oil unless the embargoing nations somehow manage to impose a naval blockade of U.S. ports. As long as we're willing to pay the market price for oil, we can have all we want.

Why, then, the gasoline lines and shuttered service stations that still haunt us from 1973; shortages that are widely attributed to the embargo? You may [thank](#) President Richard Nixon for that. In March 1973, Nixon used the power granted him in the 1970 [Economic Stabilization Act](#) to impose strict price controls on the 23 largest oil companies in the United States (a group that accounted for 95 percent of the industry's gross sales). Unable to recoup the rising costs of foreign crude, those companies reduced imports and curtailed sales of refined products to others, creating shortages. The Netherlands — which was the only other country embargoed by the Arabs — had no gasoline lines and no shortages because it did not have Richard Nixon.

Incidentally, the reason that oil imports were still, on balance, higher in 1973 relative to 1972 is because there was a major buildup of privately held oil inventories in the first nine months of 1973. Market actors (who today we might pillory as “speculators”) stockpiled crude in response to concerns about hostilities in the Middle East. In the last three months of 1973 those [inventories were drawn down](#). Things would have been even worse had these “speculators” not been on the spot.

So what's wrong with using the SPR to douse the market with crude whenever gasoline prices get out of control? Well, it's better than hoarding oil to hedge against an embargo that will never come. Still, oil economists of all stripes acknowledge that maintaining public stockpiles discourages the accumulation of private inventories and perhaps even public inventories abroad because foreign governments have an incentive to “free ride” off U.S. inventories given that a U.S. release would reduce oil prices everywhere in the world.

How much oil is displaced by the SPR is unknown, but prominent oil economists such as Philip Verleger, Brian Wright, and Jeffrey Williams suspect that the displacement is quite large. This stands to reason. It's very expensive to hold oil in storage, and market actors aren't going to be so inclined to do it if the government is going to step in and flood the market with crude whenever a nice profit opportunity materializes.

Regardless, the government shouldn't be in the commodities [business](#). Decisions about when and how much to buy and when and how much to sell are better made by businessmen, not politicians who have no expertise or comparative advantage when making those decisions. Moreover, the government shouldn't be doing what investors can do for themselves. Anyone who wishes to hedge against a supply disruption — or a rise in crude oil prices — can easily do so by buying inventories or oil futures contracts. Consumers can hedge by investing in energy efficiency or reducing their exposure to high fuel prices by, for instance, moving closer to work or adjacent to mass transit systems. Worries about the macroeconomic impact of supply disruptions might appear to justify an SPR, but even if the Reserve increases net inventory levels, notice that the SPR hasn't done anything to ameliorate the oil-related recessions of 1981, 1990 or 2008.

So let's put the SPR to use. Sell the oil off as quickly as possible while high prices promise a nice return to the taxpayer. Give consumers a gift when the economy could

certainly use a little relief. Then shut the SPR down, and end this senseless debate once and for all.

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