

**Comments on “The Accidental Hunt Brothers – Act 2,”
A paper by Michael W. Masters and Adam K. White**

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Michael W. Masters and Adam K. White have issued a new report: “The Accidental Hunt Brothers – Act 2.” In the paper, the authors examine the rise and fall of oil prices over the course of 2008. They start with the premise that speculators caused the price rise and then claim to prove the point.

Unfortunately, the authors have it all wrong. They have written a piece that is 100-percent fiction. In a phrase, they have looked for the causes of the price rise and fall “in all the wrong places.” Had they examined the market details, they would have discovered that crude prices were pushed upward by a shortage of light sweet crude. The market driver was demand for ultra-low-sulfur-diesel fuel (ULSD). As the authors of the *Financial Times* “Lex” column reported on July 30, Europe consumes more of this fuel than the United States or China. Europe’s shift to very low sulfur diesel this year has contributed to market tightness. Furthermore, European consumers pay in euros not dollars.

These facts mean the dollar price of gasoil (the European form of diesel) rose during the spring as the euro strengthened. Market supply-and-demand conditions dictated that the European diesel price must rise. The increase in the euro’s value dictated that the dollar price of gasoil increase further. Light sweet crude prices followed gasoil prices like an obedient dog.

During the spring, light sweet crude markets tightened as the available supply of this crude was reduced further by U.S. Department of Energy (DOE) actions and problems in Nigeria. DOE insisted on taking more than 60,000 barrels of light sweet crude from the market just when the supplies were needed to make ULSD. I testified to a joint Senate committee hearing on December 11, 2007, that DOE’s actions, if not stopped, would raise oil prices to \$120 per barrel.¹ As part of my conclusion, I made this statement:

¹ See “Prepared Statement of Philip K. Verleger, Jr., to the U.S. Senate Permanent Subcommittee on Investigations of the U.S. Senate Committee on Homeland Security and Governmental Affairs and the Subcommittee on Energy of the U.S. Senate Committee on Energy and Natural Resources,” *Joint Hearing*

Today, I would argue that the American economy and American consumers would be much better off if DOE changed the mix of crudes being added to the strategic reserve. If I am right, it could make the difference between \$60-per-barrel prices next summer and \$120-per-barrel prices.²

I regret to say I was correct.

Prices of light sweet crude were also pushed up by political problems in Nigeria. There is a limited supply of light sweet crude in the global market. The troubles in Nigeria could not have occurred at a worse time.

The price decline since July 14, 2008, can be explained by the reversal of these factors. Specifically,

The exchange rate between the euro and the dollar reversed. This meant the dollar price of gasoil fell even as the euro price of gasoil steadied.

Production in Nigeria stabilized.

New production of light sweet crude from the Thunder Horse field in the U.S. Gulf of Mexico began.

DOE finally stopped taking light sweet crude from the market.

The economic slowdown in Europe combined with much higher retail prices probably caused European diesel demand to decline.

The data show that light sweet crude prices continued to follow gasoil prices like a good dog. The econometrics (economic science) on the relationship is compelling. (On September 1, 2008, *International Economy* published a more detailed explanation of the phenomenon. I recommend it to readers.³)

I conclude with a simple comment: “The Accidental Hunt Brothers – Act 2” by Michael W. Masters and Adam K. White is the worst example of *junk economic analysis* published in a very long time. The authors demonstrate nothing in the article. It is devoid of *any* intelligent content. One can make a stronger case for a rooster’s crow causing the sun to rise. Their report is an utter and complete perversion of what we teach in economics.

before the Permanent Subcommittee on Investigations of the Committee on Homeland Security and Government Affairs, United States Senate, and the Subcommittee on Energy of the Committee on Energy and Natural Resources, December 11, 2007 (Washington, D.C.: U.S. Government Printing Office, 2008).

² Verleger, p. 114.

³ See Philip K. Verleger, Jr., “\$200 Oil!,” *International Economy*, Summer 2008 [http://www.international-economy.com/TIE_Su08_Verleger.pdf].