World Oil: Market or Mayhem?*

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Key Points

History Shows That:
- Over long run, demand has outrun supply.
- During 1980s, shrinking demand and growing non-OPEC supply squeezed OPEC out.
- Until recently, resource depletion has had no significant impact on supply.

Q: Market or Mayhem?  A: Market
- No evidence that financial speculation caused a shift in either Demand or Supply.
- No evidence that futures market traders increased price volatility.
- Ample evidence that market fundamentals caused prices to escalate… and then to retreat.

No Impact from Futures Trading and Speculators
- Every contract that a speculator buys, he sells.
- Every futures position gets unwound before the contract expires.
- Buying pressure = selling pressure = no pressure.

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America's Energy Heartland
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Oil Ranks #1 in International Trade

Global Imports, 2006

- Natural Gas
- Textiles
- Clothing
- Iron & Steel
- Food, Beverage & Tobacco
- Passenger Cars & Parts
- Chemicals
- Crude Oil & Products

Billion USD

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The Price of Oil

![Graph showing the price of oil from Jan-70 to Jan-09. The graph compares nominal and real (Jan 2009 base) prices.](image)
The 2008 Crude Oil Price Spike

Why Were Oil Prices So High?

Speculators vs Fundamentals

“the bubble will burst” vs “the shortage will persist”
What is the Cause—Supply or Demand?

What is the Cause... Supply or Demand?
How to Disentangle the Effects?
Shifts in Supply & Demand Impact the Price
Although Output Grew, Supply Decreased!
And Demand Increased Even More!
Shift in Global Supply, Holding Price Constant

Quantity Index (1975=100)

- Supply (Non-OPEC)
Shifts in Non-OPEC Supply versus Demand

Quantity Index (1975 = 100)

Demand
Supply (Non-OPEC)
OPEC Adjusts Output Accordingly...

![Graph showing the relationship between OPEC production, demand, and supply from 1975 to 2008.](image)

- **Demand** (blue line)
- **Supply (Non-OPEC)** (red line)
- **OPEC Production** (green line)

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History Shows That...

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• During 1980s, shrinking demand and growing non-OPEC supply squeezed OPEC out

• Until recently, resource depletion has had no significant impact on supply

• The 2004-2008 price spike coincided with first decrease in non-OPEC supply since 1973, plus an unprecedented surge in demand
Q: Market or Mayhem?  A: Market

• No evidence that financial speculation caused a shift in either Demand or Supply.

• No evidence that futures market traders increased price volatility.

• Ample evidence that market fundamentals caused prices to escalate... and then to retreat.
No Impact From Futures Trading & Speculators

• Every contract a speculator buys, he sells

• Every futures position gets unwound before the contract expires

• Buying pressure = selling pressure = no pressure
Thank You!

America's Energy Heartland