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Debunking Democrats on Drilling

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House Speaker Nancy Pelosi last Tuesday dismissively referred to pro-oil-drilling demonstrators chanting "Drill here! Drill now!" as the "2-cents-in-10-years-crowd." She may have to revise her insult strategy, since it seems that some mere pro-drilling posturing by President Bush has already helped reduce the price of gas.

The "2-cents-in-10-years" slam refers to the anti-drilling environmentalists' primary argument that even if we expanded domestic oil production, it would have only a marginal impact on gasoline prices far into the future.

Increased worldwide oil demand, a weak dollar and increased oil futures speculation are among the leading factors that have caused crude oil prices to rocket upward since last summer, reaching a peak of about $136 per barrel in mid-July. Since then, the price of oil has backed off to about $110 per barrel, a decline of almost 20 percent. Gasoline prices have also fallen from mid-July's national average of $4.11 per gallon to late-August's $3.73 — a decline of more than 9 percent.

Why have the prices of oil and gasoline declined so much since mid-July? It's hard to know for sure, but let's consider the factors that caused the price to spike in the first place.

Americans, who drive about 3 trillion miles per year, do seem to be driving less and reducing demand for gasoline, according to the latest figures from the Federal Highway Administration.

Americans drove 4.7 percent fewer miles in June 2008 than June 2007, and 53.7 billion fewer miles between November 2007 to June 2008 than over the same period a year earlier — a time when gasoline prices rose from $3.06 to $4.13. So if less driving leads to lower oil and gas prices, the data don't show that relationship.

How about the dollar's 8 percent rally against the Euro since mid-July? Historically, the relationship between the dollar and the Euro has been only weakly correlated with the price of oil. That is, higher-dollar/lower-Euro and lower-dollar/higher-Euro movements have correlated only about 20 percent of the time with decreases and increases, respectively, in the price of oil. Recently, however, this correlation has increased to 57 percent, indicating "a reasonably high level of common movement," according to David Gaffen, who writes the Wall Street Journal's Marketbeat blog. So it is possible that the dollar's rise against the Euro may have helped reduce oil prices somewhat — but to what extent is unclear.

The remaining factor is oil futures speculation — which can be gauged by so-called “open interest” in crude oil, the number of futures contracts open on a given day. Since mid-July, crude oil open interest has declined by 100,000 contracts, a sign of heavy liquidation, the president of an energy risk management firm recently told the Associated Press.

So what happened in mid-July to cause oil speculators to bail out of oil? Could it have been Bush’s July 14 announcement that he was lifting the 1990 executive order barring the Department of Interior from issuing leasing rights to explore and drill for oil offshore? If Bush’s announcement was the trigger — and there doesn’t appear to be any other significant event during that time that might have caused speculators to rethink their positions — then it’s all the more remarkable since Bush’s action itself will not lead to more drilling or a major infusion of new supply.

Not only is there a separate moratorium on offshore drilling that Congress renews every year — and, so far, the Democrat-controlled Congress has given little indication that it is seriously considering lifting it — but there’s “only” an estimated 18 billion barrels of oil in the offshore areas subject to the leasing prohibitions. At current consumption rates of 7.5 billion barrels of oil annually, that’s less than a three-year supply of oil for the U.S.

Getting back to Pelosi’s derogatory “2-cents-in-10-years-crowd” comment, it seems as if it was debunked before she uttered it. Bush’s revocation of the executive order — which without similar congressional action amounts to little more than a political statement in favor of increasing the oil supply — has possibly already reduced the price of gasoline by 38 cents in 30 days.

The mere prospect that the U.S. might get serious about increasing the supply of oil has sent speculators scurrying for cover. Imagine what would happen if we actually explored, drilled and produced some of that offshore oil — which, by the way, could be way more than 18 billion barrels. The U.S. Minerals Management Service estimated in 2006 that the quantity of undiscovered technically recoverable oil in the outer continental shelf is between 66.6 to 115.3 billion barrels of oil.

In any event, even if the offshore drilling only reduced the price of oil 2 cents over 10 years, as Pelosi would have us believe, isn’t that better than the alternative her no-drill policy offers — ever-increasing prices?

As reported by Politico.com, Pelosi’s retort to the protesters’ chant was, “Right here? Can we drill your brains?” House Majority Leader Steny Hoyer then chided the protesters that “sophomoric chanting” won’t solve the energy crisis. That may be true as long as we allow petulant Democrats to run Congress and our energy future.

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