



The Daily Dish

Psst. You Want Some West Texas Crude for Mother's Day?

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Eakinomics: Psst. You Want Some West Texas Crude for Mother's Day?

Yesterday, the May futures contract for West Texas Intermediate (a particular grade of crude oil) dropped below zero for the first time in history and closed at \$-37.63. Taken at face value, this means someone will pay you \$37.63 for you to take a barrel of crude next month. While this *does* represent an unprecedented Mother's Day gift opportunity, it also raises the question: What is going on?

Fortuitously, AAF's Ewelina Czapla's newest [research](#) arrives today. As she details further, physical demand for oil has plummeted by over 20 percent with the arrival of the pandemic and the concomitant collapse of air travel, passenger auto travel, industrial production, and other demands for oil. Simultaneously, Saudi Arabia and Russia engaged in a strategic "oil war" and flooded global markets with additional supply. On the basis of real fundamentals, the price of oil has declined dramatically, enough so that the administration has talked about various interventions to raise prices. More on that later.

As it turns out, actual users of oil are not the only participants in futures markets. Lots of financial speculators purchase futures contracts in the hope of making money when prices rise or sell contracts in the expectation that prices will fall. Most important, these participants have no intention of taking possession of a barrel of oil. Yesterday was the last full day of trading for the May futures contract; it expires today. The negative price of the May contract is stark witness to how much they do *not* want to take possession of the oil. To do it would be costly – purchasing transport and storage, for example – and they would rather pay someone else to take the contract off their hands. One should fully expect that as trading switches over to the June contract the price will rebound.

But, as noted above, while prices may not be negative, they will be low. This has caused the administration to float a whole series of ideas to prop up the price – purchase oil for the Strategic Petroleum Reserve, pay producers to keep oil in the ground, impose tariffs on imported oil, and others. As Czapla notes, it's a fair question as to whether it is good policy to intervene at all. Moreover, as she walks through each of these potential policies in turn, it quickly becomes apparent (at least to me) that the proposed cures are much worse than the disease.

Not pulling the trigger on bad ideas is not the same thing as denying there is pain. There is real pain in the U.S. oil sector, as there is across the economy. That pain, along with the pain elsewhere, will diminish as the economy ramps back up. But programs now exist to help companies, including oil companies, get bridge financing until that moment.

Be sure to gift wrap that barrel.