What we need is a $5 gallon of gas

In 1970 we had a wake up call, the OPEC oil embargo. At that time we were importing about one third of our oil or about 483,293,000 barrels of oil annually. In 2007 this has increased to 3,656,170,000 barrels of oil, about 60%, while our domestic production has been dropping about 1.8% per year since 1985. As a nation we have not taken any significant action since the embargo to become energy independent.

There has been a lot of smoke and mirrors about increasing the mileage of our auto fleet. The three major auto manufacturers, already under stress at the time, sent their lobbyist to Washington to plead their case. They could not compete with the Asian auto manufactures as the US manufactures made large low mileage cars compared to the small high mileage cars of the Asian manufactures. As a result the SUV was born and the average mileage of today’s car has not changed since 1981 about 25 miles per gallon.

Our need for oil has involved us in foreign entanglements and dealings with unfriendly nations. You do not see us sending 140,000 troops to Africa to save people or promote democracy. Just think, we have not built a new refinery in the United States in over 30 years and environmentalists have prevented the drilling for oil in the Artic National Wildlife Refuge (ANWR), off the Pacific and Atlantic coasts, and the Gulf of Mexico.

Energy independence does not mean that we produce all our energy needs within the continental United States. What it means is that we need to reduce our consumption and produce enough energy so that we only have deal with friendly and stable nations such as Canada and Mexico and stop dealing with the likes of Saudi Arabia (1.5 million barrels a day), Nigeria 1.2 million barrels a day), and Venezuela (0.75 million barrels a day).

One difference between 1970 and today is there is no shortage of gas at the pump. What you see is high prices. Today's high oil prices have been caused by a decline in the dollar. First, oil is priced in dollars, so OPEC needs to raise the price of oil to maintain its profit margins and second from emerging countries. World oil consumption is projected to grow by 1.2 million barrels per day in 2008. Almost all of the growth in 2008 is expected to come from the non-Organization for Economic Cooperation and Development (OECD) countries, led by China, Middle East oil producing countries, and Russia, as well as Brazil and India.

What Americans need to be concerned about is not only OPEC’s obvious control of our oil supply but a new threat that is more insidious and potentially damaging to our national security, the development of Sovereign Wealth Funds (SWF). SWF is a state-owned fund composed of financial assets such as stocks, bonds, property or other financial instruments. SWFs have gained world-wide exposure by investing in New York Harbor and several Wall Street financial firms including Citigroup, Morgan Stanley, and Merrill Lynch. As a result of the price run up of oil, OPEC countries have been accumilating large sums of dollars. The expanded activities of the SWFs over the past several years as well as the increased amounts available to the funds have created concern that the SWFs can destabilize financial markets and the global economy if their investments are motivated by political rather than economic considerations. Remember a large percentage of our negative balance of payments is due to the transfer of dollars to the OPEC countries.

We can achieve oil independence if we have the will to accept change and compromises. Long term we need to increase our domestic oil supplies by drilling in the continental United States and in ANWR. We must build refinery capability to meet our needs.

In the short term a shift in focus is required away from the politically motivated approaches towards a major conservation effort. In a capitalistic society this means cost and thus the $5 per gallon gas. As we have seen, the $4 gallon has started the process. The difference is that the additional revenues collected would be used to encourage the shifting of the fleet to 35 mile per gallon vehicles.

As the Wall Street Journal pointed out, oil is still the most cost effective energy source available. Alternate fuels must be subsidized to be competitive. The U.S. Energy Information Administration (EIA) did an independent study and found that ethanol and bio fuels receive a $5.72 per British thermal unit subsidy, while solar receives $2.82 and refined coal $1.32. This is in comparison to three cents for petroleum liquids.

The bottom line of all this is that fossil fuels will continue to dominate the American economy and we had better learn to use it efficiently. If we don’t, it will be at our own peril.