

CAPITALISM MAGAZINE

Stop Oil Speculation Now: The Airlines Disgraceful Political Agenda

by [Paul Blair](#) (July 11, 2008)

Today I received a [message](#) from United Airlines pushing a particularly misguided political agenda. It is one of the most disgraceful public displays of incompetence and evasion by American business in recent memory.

According to the airlines, speculators are to blame for high oil prices, and should be squelched. This ignores a number of obvious facts:

- Every time someone buys oil or oil futures, someone else is selling them. That person has expectations too.
- If someone buys up a lot of oil now to sell later, that person is eventually going to have to sell the oil. The degree to which that person's bidding drives the price up now, is the extent to which selling will drive the price back down later. The fact that the futures markets aren't expecting such a drop is a good indication that this isn't the cause of rising oil prices. In fact, there isn't a whit of evidence anywhere that someone is sitting on a cache of millions of barrels of oil they're holding off the market. (Well, except for the U.S. government's "strategic petroleum reserve" and similar ones in other countries.)
- It works just the same way with futures contracts. If a person buys an oil contract now for delivery later, then when the contract expires, that person either has to take delivery of the oil, or sell the contract. There is no net effect on the supply of oil.
- The airlines express shock that "a barrel of oil may trade 20-plus times before it is delivered and used; the price goes up with each trade." But if the market were going down, the price would go *down* with each trade. The number of trades proves nothing about whether speculation is causing prices to rise.
- It also doesn't prove that speculation amplifies price changes. In fact, it does the opposite--speculation brings today's prices in line with what people expect tomorrow's prices to be. If people buy today in order to sell tomorrow, this has the effect of making today's prices more closely approximate what tomorrow's prices are expected to be. Today's prices will be higher than they otherwise would have been, and tomorrow's prices will be lower than they otherwise would have been. And that also means that *today's expectation* of tomorrow's prices will be lower than it would be without the speculators.

Speculators are one class of buyers in the market whose action acts to *counter* the expectation of higher prices in the future. The fact that speculators are acting based on the expectation of higher prices in the future does not mean that their actions are the cause of that expectation.

The reason speculators are buying oil is that they want to lock in today's price because they forecast that prices will be even higher in the future. If they are wrong about that, they will lose a lot of money.

The airlines also buy oil futures, because they too want to lock in today's price to avoid the impact of prices getting higher in the future. What the airlines are saying is that *they* should be allowed to benefit from locking in today's price, but that *other people* shouldn't be allowed to. Why not? Because those other people are "greedy speculators," whereas the airlines

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And that's what the whole sorry thing boils down to. There isn't any valid evidence that speculation is what's causing the price of oil to rise. But since "everybody knows" that greed is the source of all the world's problems, then it must be the source of this problem too, and the easiest scapegoat there is "those greedy speculators."

The idea that speculation is causing higher prices just boils down to the idea that prices are going up because certain greedy people want them to go up. But if people could raise prices just by wishing, why weren't prices already skyrocketing ten years ago? Why aren't they always skyrocketing in every market? Why don't the speculative short sellers greedily lower the prices simply by wishing them to go lower?

If the airlines manage to persuade people that their misguided ideas are true, they're going to get exactly what they deserve. For if speculation is curtailed, who is going to sell them the oil futures contracts they use to hedge against future price increases? If it becomes harder to find a seller, what will that do to the price of those contracts?

Maybe they only want speculative *buyers* to be restricted, but not speculative *sellers*. Just imagine what *that* would do to the price of oil--could there be anything that would better serve to create market panic at the prospect of higher prices?

Anyone who owns airline stock owes it to himself, if no one else, to make sure that anyone who was a part of this shameful campaign, from the UA CEOs on down, gets sacked. These people are the real-life incarnations of James Taggart, the businessman-villain of Ayn Rand's *Atlas Shrugged*.

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