



FUTURES \$ OPTIONS

by Philip J. Baratz, C.T.A.*

“Tools of the Trade”

Within the first week of June, we saw both the highest prices ever recorded in crude oil, and the lowest prices since April. We saw gasoline prices move by more than 20 cents per gallon, and heating oil by “only” 12 cents per gallon. No real surprises on the news front—more attacks by insurgents in Iraq, OPEC agreed to “officially” produce what they were producing anyway, and on the demand side, just some lazy June days.

What made the first week of June more tense than it needed to be was not the fact that oil dealers were coming to grip with having to offer prices that were a lot closer to \$2.00 than to \$1.50—despite gasoline prices well above \$2.00. What was causing the tension was simply not knowing what to do on the hedging front. We have all become familiar with the need to have a plan, AND to execute the plan, but too many oil dealers have their “plans” in their heads, without enough commitment to those informal plans, let alone a clear path to executing them. Prices might rise 50 cents in the next half-year, or they might fall 50 cents. The weather might be unseasonably cold, like '01-'02, or it might be bitter cold, like '02-'03. If you can't predict what you are going to pay, and you don't know how much oil you are going to sell, it is understandable why “the plans” have been slow in forming, and even slower in being acted upon.

We have been working with a number of our clients in trying to create a product for them to use when putting their pricing programs together. The goal of the product is for them to use it to:

- Figure out what price levels are acceptable (both to the dealer and the customers).
- Include all the anticipated costs in the purchase of oil (supply, basis, price protection, etc.).
- Run several “what if” scenarios to get a handle on what their real margins will be “if” something happens.
- To help to determine which approach best achieves the STATED margin goals.
- Choose from the mix of available products the best fit—in all situations

The goal was to help the client figure out for him or herself how to meet their margin needs regardless of where prices go. Once purchases are made, tracking the purchases, and the related margins, becomes much easier. There are many tracking tools that will tell you the value of what you already have done, but not that many that will help you plan what you should be doing. Hindsight is always 20/20, but foresight is harder to come by.

There seems to be uniform agreement that ratable buying is the simplest way to stay out of trouble. We agree with that wholeheartedly. The swings that we have seen in the markets over the past year only seem to be getting worse. There are so many facets of your business that do not relate to the price of oil, but this one issue seems to take up the most amount of time. The tools exist to make that part of your life easier. You just have to ask for them.

Rest up, the fall is right around the corner. □



Not the best tracking tool...

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