



FUTURES \$ OPTIONS

“Beware the Ides of March”

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

At this time of the year, most oil dealers are starting to look forward to the end of the heating season, and to assessing how it went. Most of the season’s surprises are usually out of the way, and many forward-thinking marketers start to look towards the next heating season—with an eye towards starting their hedging.

Rules of thumb in oil hedging seem to change as quickly as they become rules. For a while, buying in the spring for the following winter was the way to go. Then, for a while, buying during the winter—for the following winter—was the way to go. While we have always preached buying hedges only when you know what, and why, you are hedging, there is a school of thought that likes to ratably buy over the spring and into the summer months. The main reason that it is hard to argue with that logic is that **NO ONE KNOWS WHAT PRICES ARE GOING TO DO**. They also don’t know when the best time to buy is—until after the season. Monday morning quarterbacking is fun, but you cannot run a business that way. The “new reality” that we see with oil prices makes it quite believable that “the bar has been raised”—prices no longer seem to have the ability to get too low. Yet, they do seem to have the ability to rise. Timing seems to be getting real important.

We are (through the middle of February) in the first winter that has not seen prices (Spot–New York Harbor, #2 Oil) below 70 cents per gallon, even once, during the season. The realities of the oil business have changed over the last few years, and the plans to lock-in wetbarrels at 50 cents per gallon have gone the way of the PG-rated half-time show. Cap offerings keep growing in popularity, and while more and more oil dealers are capping their own costs, there is still a stubborn group who “know better”. The reality is that price SWINGS, not price DIRECTION, are what make predictable profits elusive for some. In the last five years, the AVERAGE range (spread between the high price of oil and the low price of oil) is about 60 cents per gallon. Picking the bottom of a market that can swing almost 100% in price is quite a trick to do even once. Yet, there are those who believe that they can call the bottoms each and every year. With the “new reality” here, there can be a tendency towards just buying some oil now, and betting that prices will go up from here. Great if it works, terrible if prices drop by 20 cents be-

fore your competition starts their buying. The 60-cent range we spoke of is not always a market moving up throughout the winter. Often, prices start high, and just drift lower and lower and lower.

There is also the “it can’t happen again” group. Those groupies cannot fathom that OPEC can keep control over prices, and that prices will have to fall. In a vacuum, with an infinite time horizon, that might be accurate. But when programs are offered to customers, they are offered for the coming season. Homeowners don’t care about concepts, market trends or technical analysis. They want to stay warm, to be treated well, and to pay a fair price. They don’t want to overpay because the oil company that made them a promise didn’t protect themselves well. Bad purchases can’t always be “mixed in with the rest of my oil”. If you own a little oil, and it drops by 20-cents, you still lost 20 cents on that oil—regardless if you “mixed it in” with the rest. The goal of a proper hedge program is to not put yourself in a position where you CAN lose the 20 cents.

Where does this take us? Back to the March uncertainty. Prices are high, and there is no doubt about it. They have been high for a while, and might stay that way for a while. So, what do you do? Buy now (wet, paper, both....) and hope that prices go up? Wait till prices fall, and risk that they don’t? Much is said about the “new reality”, but much was said about oil staying at 30 cents per gallon, when it hit those levels five years ago.

We have a tendency to assume that everything that we have seen for the past year or two will just continue indefinitely. That belief usually changes right around the time when something totally unexpected happens. The notion of proper hedging is not to expect the unexpected, but to be prepared in the event that the unexpected happens. Short of being prepared (hedged), you are speculating.

We have now had business relationships with over 400 different heating oil companies, and can say that we have just about “heard it all”. Our expertise is not in selling, but in listening to what the client wants—and that is not always what they say they want. It’s a very harried, rushed world—why else buy oil 10 months ahead of the time you need it? Sometimes, you just have to take a small step backwards, to make great leaps forward. From our small part of your world—the profit-protection part—that means taking the time to formulate a plan. If you need help making the plan, call us. If you don’t need the help, at least take the time to make the plan. □

*President of Angus Energy, Inc., 1-800-440-0472; fax: 1-954-564-7045; e-mail: pbaratz@angusenergy.com.