STATEMENT OF
FADEL GHEIT
Managing Director and Senior Oil Analyst
Oppenheimer & Co. Inc.

Good morning ladies and gentlemen

I would like to take this opportunity to thank Senators Levin, Coleman and all members of this panel for inviting me to share my views on the role of speculation in the recent run up in oil prices.

I am a Managing Director and Senior Oil Analyst with Oppenheimer & Co. Inc. I have over 30 years of energy industry experience, including 21 years on Wall Street as an oil analyst. I would like to emphasize that my comments today reflect my own personal views and not those of Oppenheimer & Co. Inc.

Oil is a commodity, but unlike any other, it is critical to global economic growth and our national security. It impacts our lives, influences our national policies, both domestic and foreign, and is likely to play a key role in shaping our future.

Over the last 40 years, oil prices fluctuated from under $3/barrel to a record of more than $98/barrel a few weeks ago. Oil traders and the media were cheering the rise in oil prices and hoping for oil to break the $100 mark. Some analysts even predicted that oil prices are heading for $120 by the end of this year and that prices could exceed $150 or $200 in the next two years.

I don't know where the price of oil will be a month from now or a year from now, but I believe the current high oil prices are inflated by as much as 100%. I don't think industry fundamentals of supply and demand justify the current high prices, which I believe, are driven by excessive speculation. Based on various press accounts, others who share this view include our Energy Secretary, most OPEC ministers, and the heads of major international oil companies.

Oil prices were close to $60 in August and rose sharply to almost $100 in November, although there were no changes in world oil supply or demand. The price surge, in my view, was a result of excessive speculation about potential supply disruption in the event of military strikes against Iran. The passing of the Senate resolution regarding the Iran Revolutionary Guard as a terrorist organization seem to have been the catalyst speculators needed to fan the fire. The drop in the value of the US dollar against major currencies as a result of the Fed decision to lower interest rates, also contributed to the sharp rise in oil prices.

No one has been able to accurately and consistently forecast oil prices—not oil companies, governments, or the Wall Street investment community. This lack of reliable oil price forecasting has created a vacuum that has been filled by financial players with very short investment horizons, which significantly increased oil price volatility.

The globalization of the financial markets, ease of trading, rapid movement of large sums of capital, information overflow, and increased global tension, have created an ideal environment for excessive speculation in the world oil markets.

Oil price volatility has attracted a large and growing number of speculators seeking the highest profit in the shortest time. Volatility, however, has an adverse impact on the oil industry because it increases uncertainty, and distorts market fundamentals, which could result in poor investment decisions in securing adequate reliable supply to meet global energy demand. The oil industry operates in an environment driven primarily by factors it does not control.

Global economic growth increased world oil demand and reduced OPEC spare production capacity to historically low levels. Non-OPEC production is hampered by project delays, rising costs and technical problems. These factors increased the risk of potential supply tightness.

I believe that the oil markets need assurances from leaders of both major exporting and major importing countries as well as the oil industry. People need to know that the world is not running out of oil, that supplies are adequate, and that global stockpiles are sufficient to make up for any potential supply shortfall or demand surge.

It is worth noting that the current global oil inventories of more than 4 billion barrels exceed the oil volume exported from Iran for more than two and a half years, from Saudi Arabia for 15 months, and from the entire Middle East for six months.

I believe that oil speculators use the weekly petroleum data published by the Energy Information Administration to manipulate oil prices for short-term gain. Speculators have used declining inventory levels to spread fear about potential shortages, when in fact it indicates exactly the opposite. Reducing inventory levels improves capital efficiency, especially in a high price environment. In addition, oil price backwardation makes it even more prudent for the oil industry to reduce inventories further. But, more importantly, declining inventories, in my view, underscores that the industry is less concerned about shortages and is more confident about supply availability.

While oil trading helps protect long-haul crude shipments against price volatility, I believe it should be regulated, to ensure transparency, discourage excessive speculation and prevent potential conflict of interests and abuse by traders. Several measures should be considered to regulate oil trading by financial players, including major investment banks, commodity traders, hedge funds, and private equity funds. These include:

- Raising the current margin requirement to 50% of the value of the trade,
- Setting limits on the number of oil contacts by each account,
- Establishing minimum holding period,
- Preventing conflict of interests by financial institutions.
- Imposing stiff penalties on violators, including minimum jail sentences.