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Engaging Encounters at the Pump



Gustav and Ike Rattle Southeastern Supply

Supply an issue, but panic an even bigger issue

BY KEITHREID

AS SERIOUS WEATHER EVENTS GO, THE IMPACT OF BOTH hurricanes Gustav and Ike were fairly minor. There was the unfortunate loss of life, property damage and a disruption of our petroleum infrastructure, but nothing on the order of what was experienced with hurricanes Katrina and Rita in 2005. However, these recent hurricanes did lead to a variety of product shortage issues throughout the Southeast. And, in some very specific ways, Katrina and Rita had a hand in that as well.



Hurricane Gustav made landfall near Morgan City, La., on Sept. 1 as a category 2 storm. Refineries were shut down in anticipation of its arrival, disrupting production. Fortunately, relatively minor damage was actually inflicted on the production, refining and distribution infrastructure in the region. Nearly two weeks later another category 2 storm, Hurricane Ike, hammered the Texas Gulf Coast on Sept. 13, once again shutting down production that was coming back on line after Gustav and causing additional damage. As the Energy Information Administration noted, both hurricanes shut in a total of 32 million barrels of crude oil and 165 billion cubic feet of natural gas production in the Federal Gulf of Mexico. Recovery is ongoing and expected to continue at least through October.

As noted, gasoline production ground to a halt with the storms, and it is slowly, but surely coming back online. As a result, the Colonial pipeline, which serves notable areas of the Southeast, had to run at reduced capacities; this, when combined with lower stocks of gasoline in general, broached the specter of a gasoline shortage in the Southeast from

Alabama to eastern Tennessee, North Carolina, South Carolina, Georgia and generally throughout the region.

“When Gustav came through it prevented waterborne deliveries from reaching Florida, and in response, people trucked in fuel from nearby states which helped create the problem we are having now,” said Ryan Mossman, vice president, general manager fuel management at Houston-based FuelQuest. FuelQuest provides on-demand, Web-based supply chain management and tax automation technologies for suppliers, distributors, buyers and traders of petroleum products and other energy commodities. “When Ike came along it impacted the refineries, which caused temporary shutdowns that are working themselves through, and you also saw some impact with the pipelines moving product at limited capacities.”

Marketers with branded supply contracts were generally put on allocation, which varied according to the market. The major brands worked to keep their wholesale prices down during the crisis. This, of course, also reduced potential political based scrutiny over price gouging concerns particularly at a time when the major oil companies have been under attack for record profits. The impact of the notably higher prices on the spot market made the period particularly painful for independent marketers.

Once the shortage specter became apparent, fueled in no small part by the local media, people with memories of Katrina began stocking up and topping off tanks. Demand increased 300 percent in some areas.

In Tennessee, the impact was felt in the mid and eastern parts of the state. “Most of the shortage was literally caused by panic buying,” said Marylee Booth, the executive director of the Tennessee Oil Marketers Association. “One of our members reported that there was an older man outside one station literally filling up empty mayonnaise jars. There’s probably as much gasoline stored in 5-gallon cans in people’s garages or the trunks of their cars today as there is at the gasoline stations.”

Booth noted that Nashville was hit hardest with roughly 85 percent of its stations closed for one weekend.

Georgia, which is still facing some spot outages, saw the same panic in the market. “There were a number of issues behind our supply shortages,” said Jim Tudor president of the Georgia Association of Convenience Stores. “First and foremost was the intensive media coverage of the event that increased anxiety levels. It was difficult for us to catch up even as supply increased. The reality is that even when we were back to 80 percent supply, we were having trouble keeping stations in fuel because of the demand.”

Tudor noted that it was only when the media coverage turned more positive that people started changing their fueling habits, and supply levels in the market caught up fairly quickly. “We were very forthcoming in dealing with the media and stated that even if there was no supply issue at all, there is never enough gasoline in the infrastructure for everybody to have a full tank at the same time. The system has never been designed for that work. We could’ve been at 100 percent supply, and the demand we were seeing would still have caused shortages.”

Darker memories of Katrina and Rita also impacted marketers in the Southeast, who, like the major oil companies, had experienced price gouging accusations in the aftermath of the previous hurricanes.

A free-market principle of supply and demand is that higher prices will prolong the availability of a high-demand product when supply is notably low. A consumer might have to pay significantly more for a gallon of gasoline for the short run of a crisis, but there is also a reasonable expectation that a gallon of gasoline will be available for a critical need during that time. The consumer will buy fewer gallons and avoid driving except for critical needs, such as going to work. Gasoline hoarding becomes an expensive proposition. When supply naturally increases in the market, competition will dramatically drop prices down to normal levels.

Regulations setting emergency gasoline prices or the fear of legal action artificially limit the ability of price to rise due to natural market forces and creates an environment where panic buying empties out a station’s tanks in record time.

TOMA worked hard to stay ahead of the backlash in Tennessee. “We are fortunate that our attorney general is appointed and not elected, so it’s not such a big political thing,” Booth said. “When we saw prices going up on the spot market, we forwarded that information to the Attorney General’s office and said, ‘Listen, we’re getting ready to have a problem here.’ In general, the industry behaved responsibly. But (the Attorney General’s office) has sent out requests for information, particularly in the East Tennessee area, looking into potential price gouging concerns.”

Booth noted that one large marketer literally closed all its stations and said, basically, the stations could not afford to sell at the set price and if the prices were raised, they might be accused of price gouging.

In Georgia, the marketers were left with little choice as to their pricing policies. “Georgia was under a state of emergency starting at seven o’clock on Sept. 12, and the law is such that the retailers are hesitant to pull the trigger on price issues because of the experiences from Katrina,” said Tudor. “We had 1,500 complaints then where people thought they were being priced gouged. If the market had been allowed to price (without controls) it might certainly

ly have impacted price in the short term, but it certainly would have also impacted supply. It is what it is.”

In Florida, the major shortages were limited to the Panhandle region served by the Colonial pipeline once the waterborne terminals came back online and the costal deliveries renewed. Florida also had to operate under the restraints of state of emergency-related price gouging requirements.

“With the exception of those companies whose contracts were tied to Gulf Coast spot, you didn’t see much movement on price at all—it was minimal,” said Jim Smith, president and CEO of the Florida Petroleum Marketers Association. “We’ve had to deal with the price gouging issue long before Katrina – it was ‘04 for us. Politicians can take advantage of something that makes them look good in the media. When there is an emergency declaration, there is no such thing anymore as normal business practices in this state, and I’m sure it’s no different in others.”

At this time, recovery is well underway throughout the Southeast. Shortages and run-outs are becoming rare, though there are notable shortages of premium- and mid-grade in many of the impacted areas. The issue now with some operations is cash flow due to lost sales during the down time, both at the pump and in the store, and the high cost of inventory replacement.

What can marketers do to help insulate themselves from such local or regional supply disruptions? Mossman recommends that marketers and commercial fuel users in areas potentially vulnerable to such disruptions have on hand multiple ratable supply options, preferably set up before the interruption occurs; a transportation infrastructure or transportation partners lined up to bring product in from unaffected or less affected areas; and enhanced tankage compared to industry averages both in the ground at retail sites and at any bulk facilities that might be operated. In a broader sense, this will not only help ensure supply during times of disruptions, but will allow the marketer to take advantage of favorable volatility shifts in product price.

“In our case, because our supply network and transportation network is all over the United States and Canada, when you have a situation like we’ve seen in the Southeast, we’ve had product pulled from as far away as Ohio or Maryland going into North Carolina,” said Mossman. “If you don’t have those relationships established ahead of time, that’s not going to happen. One thing we did before this storm is we had advised our clients on tank sizes and had relationships set up and made sure customers were ratable and all of that. Just before the storm we went to more of a keep-it-full philosophy versus a just-in-time philosophy to make sure we had as much product as possible going into the situation. And even now we’re still targeting closer to keep full to prevent run-outs while things get back to normal.” **NPN**



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