



# Special Report: An Unusual Short-Term Profit Opportunity In Oil

by Dr. Kent Moors, Editor, *The Oil & Energy Investor*

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Dear Reader,

You don't always need to pump, transport, or sell oil to make a profit. Sometimes you just need to hold it.

What follows should be good news to the commodities side of **Goldman Sachs Group Inc. (NYSE:GS-A)**. Unfortunately, this has not been a good two weeks for the company. First a fraud charge. Then the release of damaging internal E-mails. Too bad, because their oil traders may have just hit the jackpot.

Goldman is one of the leading traders in commodities in general and crude oil in particular. The trading side of the house has been betting heavily on oil in storage, and that is soon to pay off nicely. I'm about to explain why those profits are shortly going to flow.

Please, feel free to join in on the action. This will be a quick in and out.

It's all about what is taking place in a somewhat dull little town in north central Oklahoma. No, that's not really accurate – it is an *extremely* dull little town. Believe me, I know, having spent two of the most boring years of my young life there. Not much to commend it – except for the fact that this little community of barely 8,000 people just happens to be where Gulf Coast oil supplies meet northern refinery needs.

As it turns out, that is a very big deal.

This is the town of Cushing, Oklahoma, the most important U.S. oil hub representing a major intersection of pipeline systems. Here, oil prices for West Texas Intermediate (WTI) benchmark crude rate deliveries are set, the same ones quoted on NYMEX in New York City.

The boys at Goldman are on to it. And in about 750 more words, you will be too...

## Oil Storage Points the Way to Contango Profits

Four things are happening right now, making for an unusual situation in Cushing.

First, crude oil prices are moving into a concerted “contango” market – a market in which prices for later month futures contracts are higher than the prices in spot sales for immediate delivery. This is becoming a classic contango example. The longer one moves from the front month to six-months-out futures contracts, the wider the pricing spread.

Second, we have approached the end of the trading month – the front month has become deliveries in June rather than May.

Third, refinery usage continues to be well below capacity, averaging less than 85% last week, but barely 80% for the past several months.

Fourth – and this is the real kicker – the spread margin is very large. At the open of trade on Monday, April 26, the spread between June and July contracts was approaching \$2... *a barrel*.

If you are a trader at Goldman, you acquire volume now that will not be released until July. If the contango effect continues into the high summer, you just roll over the contracts. The prices at redemption on the more distant month’s contracts will continue to increase, but you are also trading into that environment from cheaper consignments. That simply continues the profit wagon. If the market starts moving in the opposite direction (into a backwardation scenario), simply liquidate the actual crude (wet barrel) underlying asset position and carve out a nice little return.

Most of you reading this have neither the interest nor the stomach to be trading futures contracts.

You could straddle the action by pairing ETFs weighted to future crude oil prices against crack spreads (providing the difference between the prices of crude oil versus the prices of products, like gasoline, made from it). I am having some of my grad students (mostly those without a social life) run six-month models on this as we speak.

But even this is not necessary for the average investor. You can play this one with simple equity trades. You need to know only three things:

1. Who controls the storage facilities at Cushing;
2. Which trading companies have the best capacity to store crude oil, along with refineries having the ability to wait on processing it into finished products; and
3. When to pull the plug.

The first two points to know are the companies that will profit from what is unfolding in Cushing. The storage companies can collect the crude and release it later, when the prices are higher. The refineries can buy the crude now more cheaply than in July (and probably later), store it themselves, and utilize capacity restrictions to push retail prices higher moving forward. At minimum, they have reduced the single greatest cost component in processing, the crude oil, and that will certainly increase their bottom line.

And here they are (drum roll, please)...

Most of the storage facilities at Cushing are owned by four companies: oil major **BP** (NYSE:BP); **Enbridge Energy Partners LP** (NYSE:EEL); **Plains All American**

**Pipeline LP** (NYSE:PAA); and **SemGroup Corp.** (currently privately held; coming out of a nasty bankruptcy and series of court litigations; will list shortly).

On the refinery side, two stand out as direct beneficiaries. One is again **BP**, while the other is **Valero Energy Corp.** (NYSE:VLO).

Among those able to store considerable crude oil in transit, **Vitol** is the primary player. This large, multi-faceted, international trader is rumored to have been a main actor in withholding some *150 million* barrels of crude (equal to almost *two days* of total global demand) from the market in 2009, when a similar contango took place. Retail investors cannot reach Vitol directly but can participate in its upside by trading in Vitol's strategic partner **Arturus Capital** (AX:AKW) on the Australian Stock Exchange.

Now for point three: When do you exit?

Easy: You simply go to the **NYMEX prices**, click on Crude Oil, and hold your position until ALL of the next five forward months (now June through October 2010) dip below \$0.50 in the green AND ALL of the first three (June through August) are below \$0.20. That should still give you about a 5- to 10-day trading window before the ride is over.

The adventurous among you may ride this one to an even narrower pricing differential, but it will be difficult to estimate what the price swings will do to the inventory by that point. Remember, you are making a profit here off of *oil in storage*, not oil sold. Once it moves, your upside is over.

Don't fret if you miss this one. With the volatility coming fast, there will be multiple upcoming occasions to ride this roller coaster and make some money. Stay tuned to your inbox...

Kent

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*Dr. Moors is the Editor of The Oil & Energy Investor and has been advising the "Big Boys" for 31 years now, including six of the world's top 10 oil companies and leading natural gas producers throughout Russia, the Caspian Basin, the Persian Gulf and North Africa. For his latest energy opportunity report, visit [www.oilandenergyinvestor.com](http://www.oilandenergyinvestor.com)*



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