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memo w/ att.	From Schlesinger to The President (18 pp.) re:Exports of California Crude to the Bahamas and the Caribbean/enclosed in Hutcheson to Eizenstat 12/27/77 <i>opened per AAC NLC-126-10-12-1-7, 3/21/13</i>	12/27/77	A

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WASHINGTON

DATE: 18 JUL 78

FOR ACTION: STU EIZENSTAT

FRANK MOORE (LES FRANCIS)

JACK WATSON

JIM MCINTYRE

*1/10/78
7/25
8/1
8/2 - 5/12/78
K*

*nc
Handwritten signature*

STU?

INFO ONLY: THE VICE PRESIDENT

ANNE WEXLER

ZBIG BRZEZINSKI

SUBJECT: SCHLESINGER MEMO RE ANALYSIS OF EXPORTS OF CALIFORNIA CRUDE OIL TO BAHAMIAN AND CARIBBEAN REFINERIES WITH SUBSEQUENT REIMPORTATION OF REFINED PRODU

w/ Kelly

*9/18
Kelly will send short summary to say that they need not read 1002 rpt*

10/5 - Kelly will ck w/ CFR, 3 Ind. 12 NOT ready to (transmit)

*10/24 - spec w/ Kelly
* COR 10/25*

+++++
+ RESPONSE DUE TO RICK HUTCHESON STAFF SECRETARY (456-7052) +
+ BY: 1200 PM THURSDAY 20 JUL 78 +
+++++

ACTION REQUESTED:

STAFF RESPONSE: () I CONCUR. () NO COMMENT. () HOLD.

PLEASE NOTE OTHER COMMENTS BELOW:



Department of Energy
Washington, D.C. 20585

July 17, 1978

MEMORANDUM FOR:

THE PRESIDENT

FROM:

JIM SCHLESINGER 

SUBJECT:

Response to Request for Analysis of Exports
of California Crude Oil to Bahamian and
Caribbean Refineries with Subsequent
Reimportation of Refined Products

By a memorandum dated June 12, 1978, you requested the Department of Energy to undertake an analysis of the options available for exporting California crude oil to Bahamian and Caribbean refineries on the condition that the refined products are reimported to the United States. The enclosed analysis responds to the various criteria which you requested us to address.

There presently exists a potential Caribbean/Bahamian refinery capacity of 400 to 600 MBD for handling high sulfur, low gravity crudes similar to much of the crude oil produced in California. The NEPCO refinery, located in the Bahamas, has already indicated a willingness, if favorable entitlements treatment is allowed and provided they may continue to use foreign flag vessels, to purchase up to 200 MBD of heavy California crude. The refined products would be sold on the East Coast. Additional interest in a proposal of this nature has been expressed by other East Coast residual oil importers.

On June 15, 1978, the Department of Energy announced the following three-point program for alleviating the distressed market conditions for California crude:

- o More favorable entitlements treatment for California crude, based on the specific gravity of the oil. The heaviest California crudes would receive a greater subsidy under this approach. While the average benefit per barrel of lower tier oil would be \$2.38, the heaviest California crudes would receive a \$3.00 or more per barrel subsidy.

DECLASSIFIED

Per, Rac Project

ESDN; NLC-126-10-12-1-7

BY 145 NARA DATE 3/20/12

- Allowance of exports by the Department of Commerce of excess residual fuel oil, which has been in over-supply in recent months. Because of this surplus, refineries have cut back operations, requiring shipments of gasoline from outside of California to meet demand.
- Further case-by-case entitlement benefits to allow California crude to be moved to Gulf Coast, East Coast, and Puerto Rican refineries. In particular, DOE will provide increased benefits to compensate for the higher costs of using domestic rather than foreign vessels.

Conclusions

It is expected that the June 15th proposals will alleviate the immediate problems of California shut-in production. The entitlements adjustments and case-by-case transportation benefits should create economic markets for marginal supplies of heavy California crude. Recent approval of a 50 thousand barrels per day (MBD) application for transportation-related entitlement benefits suggests that these initiatives will be effective.

Any assessment of the additional benefits or the burdens associated with an export/reimport program similar to that proposed by NEPCO is highly dependent on the time frame in which such a program is analyzed. The critical question is whether the markets created by a NEPCO type proposal simply result in Alaska production replacing California production, or whether producers will actually undertake the investment to expand California production and thereby reduce oil imports and trade deficits.

It is unlikely producers would undertake the kind of longer term investment that would lead to increased production if any such export program were perceived as a short term relief measure. The one year duration of the NEPCO proposal, with the possibility of subsequent renewals, would appear to place it in this short-term category. It might be possible to stimulate some additional production if the ability to export were tied to incremental production. Even in this case, however, the extent of long-term commitment is critical.

As part of a longer term program involving several different initiatives for increasing California production, however, the export for reimport approach may prove to be beneficial.

The DOE is presently conducting an in-depth analysis of a wide-range of alternatives to achieve significant production increases on the West Coast, including new West-to-East pipelines, incentives to retrofit refineries, and various possible export options, including the export for reimport proposal. Since some of these initiatives involve longer lead times for implementation, it may well be that a NEPCO-type proposal, in conjunction with other longer range initiatives, will stimulate the kind of investment needed to achieve increased production. We will report back to you concerning feasibility of a NEPCO type proposal in conjunction with such a broader program.

In anticipation of the completion of the longer range analysis, the specific questions you raised were analyzed in terms of a NEPCO-type proposal standing by itself. In that context, it appears:

- The financial benefit to the refiners of this proposal provides the incentive for them to purchase this oil as opposed to foreign crude;
- While it is possible that residual oil prices might be reduced to East Coast consumers, any reduction through price discounting will be small;
- If one assumes that in the short-term no additional production would be forthcoming, a positive but small balance of payments benefit would result if total exports of California crude are less than 165 MBD. At levels greater than 165 MBD, exports of California crude will lead to an increase in the balance of payments, as expensive imports fill in behind California crude. If the program were clearly for a long-term, a greater supply response is likely, which could lead to positive balance of payment benefits.
- exports of California crude may work as a slight disincentive for retrofitting West Coast refineries to closely match regional product demand; and
- the export of substantial quantities of California crude may have some adverse impact on decisions to construct West-to-East oil transportation systems.

ANALYSIS OF CALIFORNIA CRUDE OIL EXPORTS TO THE
BAHAMAS AND CARIBBEAN

I. Introduction

There are numerous scenarios which may be postulated for the export of domestic crude oil produced in California to non-United States refineries in the Bahamas and Caribbean, and the subsequent reimportation of products refined from that crude. However, for the purposes of this analysis, a most probable scenario, closely following the proposal made by New England Petroleum Company (NEPCO) for use of its foreign subsidiary refinery (CORCO) located in the Bahamas, is used. Accordingly, the discussion below assumes that:

- o California crude oil would be purchased at the appropriate ceiling price (as stipulated in the NEPCO proposal).
- o Refined products in the same quantity as the crude exported will be reimported to the United States.
- o For the purpose of these U.S. crude export transactions only, Bahamian/Caribbean refiners would participate in the Entitlements Program on the same basis as domestic refiners, i.e., they would incur entitlement obligations and receive run credits on domestic price-controlled crude purchased and run in their refineries.
- o All transportation of exported crude oil and reimported refined products would be in foreign flag vessels.
- o Products (resid) reimported from Bahamian/Caribbean refiners would not be eligible for import entitlements, nor would they be subject to "reverse" entitlements treatment currently accorded domestic refiners.*/
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*/ Note that DOE, on June 15, 1978, issued a proposed change to its entitlements program which would eliminate the 50% "reverse" entitlements for domestic residual fuel oil shipped to East Coast markets.

II. Economic Factors

The following analysis is intended to provide some measure of the economics of a California crude export/product reimport transaction to a Bahamian/Caribbean refiner, under the above described assumptions. The analysis is based on purchase of a representative California heavy, high sulfur crude, (Kern County 16 gravity) at the lower tier ceiling price, compared to a crude oil of the type most likely to be displaced (Iranian 31 gravity). All values used in the calculations are based on most recently available information (e.g., latest residual oil price postings) and best estimates (e.g., per barrel refining cost for a large Bahamian/Caribbean refiner). It is important to emphasize that while this analysis can provide some rough gauge of the profit (loss) involved in transactions of this type, it is not, and should not be construed to be, a definitive corporate financial analysis.

As indicated in Table 1, the export proposal would reduce crude oil acquisition costs to Bahamian/Caribbean refiners by nearly \$2 per barrel, exclusive of any product import entitlements. This represents the level of benefit that would be derived through gaining access to price-controlled domestic crude, at the cost-equalized after - entitlements price. This benefit is somewhat offset by the fact that the California crude has a higher resid yield (74% vs 56%) and therefore produces lower per-barrel revenue (see Table 2). However, at current market prices for the products, the proposal would still yield a net economic benefit on the order of \$0.73 per barrel. Note that in Table 2, products refined from the representative foreign crude produce an approximate loss of \$0.57 per barrel vs. an approximate \$0.16 profit per barrel under the proposal, for an approximate net advantage (to NEPCO in this instance) of \$0.73 per barrel.

TABLE I
REFINER'S COST OF CRUDE OIL
(per barrel)

	<u>Present Case</u> (Iranian 31 ^o)	<u>Proposed</u> (Kern 16 ^o)
Crude Purchase Price	\$ 12.49	\$ 5.17 (June ceiling) ^{1/}
Pipeline and Handling	-	.60
Shipping (foreign flag)	.60	1.40
Delivered Cost	<u>\$ 13.09</u>	<u>\$ 7.17</u>
Entitlement Price (March)	N/A	\$ 8.47
California Gravity Adjustment	N/A	- 2.56
Entitlement Run Credit (March)	N/A	- 1.91
Total Cost of Crude	<u>\$ 13.09</u>	<u>\$ 11.17</u>
Refining Cost ^{2/}	.50	.50
Total Cost (to produce a barrel of refined product)	<u>\$ 13.59</u>	<u>\$ 11.67</u>

^{1/} While this calculation utilizes lower tier oil prices, the results would be essentially equivalent for other tiers.

^{2/} Refining (non-product) cost estimate includes salaries and wages, maintenance, amortization of capital, taxes, and utilities.

TABLE 2REFINER'S SALES REVENUE*
(per barrel)

	<u>Present Case</u> <u>(Iranian 31^o)</u>	<u>Proposed</u> <u>(Kern 16^o)</u>
Residual:	(2.4% S)	(2.2% S)
Yield per barrel (%)	56%	74%
Sales Price <u>1/</u>	\$11.00	\$11.05
Weighted value of resid (price x yield)	\$ 6.16	\$ 8.18
Light Products:		
(Gasoline, Naptha, Distillate)		
Yield per barrel (%)	44%	26%
Average sales price	<u>\$15.60</u>	<u>\$14.07</u> <u>2/</u>
Weighted value of light products (price x yield)	\$ 6.86	\$ 3.65
Combined sale revenue	\$13.02	\$11.83
Cost to produce	\$13.59	\$11.67
Profit (Loss)	<u>(\$ 0.57)</u>	<u>\$ 0.16</u>

* Net back to refinery, i.e., product prices F.O.B. Freeport

1/ Based on recent Platt's Oilgram Price Service New York and Boston Harbor postings, exclusive of transportation and import fees.

2/ No gasoline yield.

III. Impact on East Coast Residual Oil Prices

Average demand for residual fuel oil in PAD I (Northeast) during the 1976-1977 period was approximately 1.6 million barrels/day. If the proposed 200,000 barrels/day of California crude oil were processed in Bahamian/Caribbean refineries, approximately 150,000 barrels of resid per day, or 9.4% of average PAD I demand could be supplied from this crude stream.

Even with the favorable entitlements treatment assumed in this analysis, refineries would operate at an approximate \$.16 per barrel profit assuming current selling prices for East Coast resid. This margin offers little or no room for refiners to reduce their selling price to importers and still earn a profit. However, even if the product importer (NEPCO in this instance) were to discount resid reselling prices to consumers by \$0.20 per barrel to reflect the improved profit position of the refiner-affiliate (in other words, to reflect an approximately breakeven netback to the refinery) and to capture a greater market share, the impact on prices to East Coast consumers would be minimal. A discount of \$0.20 per barrel on this oil alone, without any price response from competitors, would reduce the overall average selling price of residual oil to East Coast consumers by \$0.019 per barrel, or \$0.0005 per gallon.

The increased resid yield of California crude over Iranian crude would give the Bahamian/Caribbean refineries the ability to increase their resid output from equal volumes of crude runs, and thus increase somewhat the supply of residual fuel oil available on the East Coast. If refineries maintain inputs at previous levels, this substitution could yield a 34% increase in resid output from each refined barrel. Increased volume output could prompt some short-term price discounting to increase market share. However, significant price cuts are unlikely, given the relatively small volume of resid involved.

IV. Potential of California Crude to Replace Foreign Crudes in Bahamian/Caribbean Refiners

A recent DOE report^{1/} indicates that there is a total refining capacity of 2.16 MMBD now available in the Caribbean and Bahamas, exclusive of Venezuelan and United States Virgin Islands capacity. Of this total, approximately 400-600 MBD is capable of processing heavy, high sulfur crude oil of the type assumed to be exported from California for purposes of this analysis. No additional increases to this type of capacity are indicated for at least the near-term (to 1980). Therefore, the 400-600 MBD would represent an absolute maximum physical limitation for processing heavy California crude in this region.

The actual ability of California crude to displace foreign crude in Bahamian/Caribbean refineries would depend on numerous other factors, including, but not limited to, product demand and prices, existing contractual arrangements of individual refiners, and changes in foreign and domestic crude prices. In view of uncertainties surrounding these factors, no firm estimates can be made at this time of the actual displacement potential. While quantitative conclusions cannot be reached, it can be assumed, based on the calculations in Tables 1 and 2, that no additional California crude oil would be processed in other Bahamian/Caribbean refineries unless they received the same favorable entitlements treatment contemplated in the NEPCO proposal.

V. Balance of Payments Impact

The effect of transactions of the type which are the subject of this analysis on the U.S. balance of payments is highly variable, dependent upon a number of factors. For purposes of illustration, two calculations of near-term effects are presented, within the context of the assumptions set out in Section I. The high case assumes that the full 200 MBD of California crude would be available for export and would be processed and the products reimported to the U.S., using the costs and yield factors from Tables I and II. The low case assumes a lower available near-term export volume of 50 MBD. Both cases assume that near-term

^{1/} Trends in Desulfurization Capabilities, Processing Technologies, and the Availability of Crude Oil, U.S. Refineries, Caribbean "Exporting" Refineries, December 1977. DOE/RA-005

available incremental California heavy production is 30 MBD (see discussion in Section VI), that all products refined from California crude are reimported, and that products other than resid produced by Bahamian/Caribbean refiners are not now imported into the U.S.

On June 15, 1978, DOE announced several actions specifically designed to improve the production and marketability of California heavy crudes. It is anticipated that those actions will succeed in accomplishing their desired effect, and that as a result all shut-in and distressed California production will find adequate markets.

The calculations of the balance of payments effect of an export proposal in Table 3 are made under two assumptions most favorable to the proposal: the pessimistic assumption that the recent rulemakings and residual fuel export policy would not succeed, and thus that the full increment of 30 MBD production will come back on stream directly and solely as a result of a crude export proposal. Further incremental production is considered highly unlikely for the near-term (see Section VI).

U.S. demand for crude oil and refined products should remain constant with or without this proposal. Therefore, any production displaced from California by transactions of this type must be replaced with imported barrels.

TABLE 3

BALANCE OF PAYMENTS EFFECTS
(per day basis)

I. High Case: 200 MBD California crude, resid yield 74%, displaces its volume equivalent of resid refined from foreign crude oil^{1/}

	<u>Export & In-Flow</u>	<u>Import & Out-Flow</u>
A. <u>Proposed</u> :		
200 MBD Cal. crude export at \$9.77/B ^{2/}	\$1,954,000	
148 MBD 2.2% S resid imports at \$11.05/B		\$1,635,000
150 MBD replacement crude at \$13.50/B (various foreign sources) ^{3/}		<u>\$2,025,000</u>
Net outflow		\$1,706,000
B. <u>Current</u> :		
148 MBD 2.4% S resid imports at \$11.00/B (from foreign crude)	N/A	<u>\$1,628,000</u>
Net outflow		\$1,628,000
C. <u>Net Effect</u> :		
Increase (decrease) in dollar outflow (A - B)		<u>\$ 78,000</u>

^{1/} Light product sales are not considered in the analysis. It is assumed that light products refined from California crude and reimported to the U.S. would displace other imported light products, with negligible net effect.

^{2/} Entitlements - adjusted price calculated as follows:
\$5.16 ceiling price (16 gravity) + \$8.47 (March) entitlement price - \$2.56 Cal. gravity adjustment - \$1.91 run credit + 0.60 pipeline and handling cost.

^{3/} Replacement bbls. calculated on the basis that 30 MBD of exports in incremental production and 10-20% not replaced due to higher light product yield of replacement imports.

TABLE 3 (continued)

BALANCE OF PAYMENTS EFFECTS
(per day basis)

II. Low Case: 50 MBD California crude, resid yield 74%, displaces its volume equivalent of resid refined from foreign crude oil 1/

	<u>Export & In-Flow</u>	<u>Import & Out-Flow</u>
A. <u>Proposed:</u>		
50 MBD Cal. crude exports at \$9.77/B <u>2/</u>	\$ 488,000	
37 MBD 2.2% S resid imports at \$11.05/B		\$ 409,000
16 MBD replacement crude at \$13.50/B (various foreign sources) <u>3/</u>		<u>\$ 216,000</u>
Net outflow		\$ 137,000
B. <u>Current:</u>		
37 MBD 2.4% S resid imports at \$11.00/B	N/A	<u>\$ 407,000</u>
Net outflow		\$ 407,000
C. <u>Net Effect:</u>		
Increase (decrease) in dollar outflow (A - B)		<u>(\$ 270,000)</u>

1/ Light product sales are not considered in the analysis. It is assumed that light products refined from California crude and reimported to the U.S. would displace other imported light products, with negligible net effect.

2/ Entitlements - adjusted price calculated as follows: \$5.16 ceiling price (16⁰ gravity) + \$8.47 (March) entitlement price - \$2.56 Cal. gravity adjustment - \$1.91 run credit + 0.60 pipeline and handling cost.

3/ Replacement bbls. calculated on the basis that 30 MBD of exports in incremental production and 10-20% not replaced due to higher light product yield of replacement imports.

The above analysis of balance of payments impact assumes that barrels leaving California (other than new production), must be replaced even if they displace foreign crude. This replacement might occur in a variety of ways. It is however, reasonable to assume that: most of the exported California crude would be replaced by additional use of Alaskan North Slope (ANS) crude in California refineries, (resulting in substantial benefits to major ANS producers) with the balance being made up by imports (Saudi, Indonesian, or Mexican); increased use of ANS crude in California would result in decreased availability of this crude in the U.S. Gulf, where the loss would be made up by imports (mostly Saudi); although less than full replacement is assumed to occur due to the higher light product yield of replacement imports, most of the foreign crude stream "backed-out" of Bahamian/Caribbean refineries must and would re-enter the U.S. on the West and Gulf Coasts.

This analysis indicates that, giving full benefit to the ability of an export proposal to stimulate incremental production without allowing for any effect on the part of recent DOE regulatory and product export relief, for volumes of 50 MBD, the proposal would have a positive effect on the U.S. balance of payments.^{1/} However, this positive effect diminishes as export volumes increase, and for volumes at or above 165 MBD a negative effect on the U.S. balance of payments is indicated. This reflects the inability to stimulate further incremental production in the near-term, the high cost of replacement imports, and the shifting of profits to foreign centers.

1/ It should be noted that in no instance would a proposal of this type produce a positive effect remotely approximating the \$1 billion claimed in the NEPCO proposal.

VI. Stimulating Enhanced Production of California Crude

One of the presumed benefits of a California export proposal is that it would result in a favorable near-term (immediate) impact on crude production. The NEPCO proposal for instance focusses on short run transactions (one-year contracts, with four possible one-year renewals). While crude exports might stimulate production of crude now "shut-in", estimated to be on the order to 30 MBD, it would do little to stimulate the use of enhanced recovery techniques. Tertiary recovery and other advanced enhanced production technologies require considerable capital investment, involve high operating costs, and are not economic over short periods of time. A long-term commitment and adequate pricing levels are essential to the spread of tertiary recovery practices, as well as any other new investments to produce more California crude. In light of this, a NEPCO-type proposal will likely do little if anything to stimulate enhanced production of California crude in the near-term. Of course, if the Administration's current program does not reverse the current trend of shutting in marginal California crude production, this proposal could result in additional production. In addition, if the U.S. embarked on a long-term commitment to allow exports of California crude, it is likely new investments would be forthcoming. DOE is evaluating a wide-range of potential long-term options to create markets for California crude and Alaska North Slope production.

DOE has drafted a final rulemaking to provide incentive pricing for incremental production from tertiary recovery projects. At the same time, DOE plans to issue a notice of inquiry on the need for extending the incentive plan to provide for "front end" capital by "releasing" some lower tier production. Such releases would be limited, and would apply only to those which could not otherwise finance investment in a tertiary recovery project.

DOE estimates that these regulations could increase recoverable U.S. reserves by some 30-40 billion barrels, and result in a theoretical maximum of about 600 MBD of additional production in the U.S. by 1982. A DOE study entitled Research and Development in Enhanced Oil Recovery, estimates that, without current market curtailments and if the considerable environmental problems associated with emissions from steam generation can be overcome, potential enhanced U.S. production from steam drive techniques alone would be 640 MB/D by 1985. However, maximum expected enhanced

recovery for the U.S. in 1985 is about 320 MB/D. These estimates, however, are based on two very optimistic assumptions: no market constraints and the resolution of significant environmental problems.

The above projections also assume realistically that significant enhanced production from tertiary recovery will not begin until 1982; a two-year lead time is minimal in realizing results from such projects. This difference in timeframe therefore makes it exceedingly unlikely that the NEPCO proposal - a series of short duration near-term transactions - will contribute to or stimulate tertiary recovery in California.

VII. Effect on Decisions by West Coast Refiners to Retrofit Their Facilities

California air quality standards presently require consumption of low sulfur fuels, and place serious restrictions on the emissions of stationary sources, such as refineries. Other characteristics of the West Coast market result in refinery slates which emphasize gasoline production rather than residual or heavy fuel oils. As a result of these conditions, most West Coast refineries are designed to process light, low sulfur crude. Since many indigenous California crudes are heavy, high sulfur oil, West Coast refiners tend to meet market requirements by importing low sulfur foreign crudes to which they have ample access and which have a greater range of product yield, as well as using Alaskan North Slope crude.

As long as these conditions prevail, there is little incentive for West Coast refiners to retrofit their facilities to process heavy, high sulfur crude oil. The world supply of light sweet crude is dwindling rapidly, and retrofitting cannot be delayed indefinitely. However, retrofitting is a costly process in terms of both capital and down-time. Refining heavy high sulfur crude requires both emissions control equipment and sophisticated desulfurization, coking and cracking facilities. Substantial investments in this equipment and facilities are required for each additional barrel of heavy refining capacity. Without sufficient price incentives and assurances of a long-term favorable return on investment, refiners have little inducement to retrofit their facilities now. In 1978, only one West Coast refiner is scheduled to increase its ability to process heavy crude oil. This refinery will increase its capacity by only 10 MBD.

One factor which currently does exert pressure for retrofitting is the surplus of residual fuel oil in the California market. With storage facilities full of unmarketable product, refiners have reduced their runs, resulting in the need to ship gasoline into PADD J from other sources. Exporting California crude to the Bahamas would relieve some of the market pressures for retrofitting and would thereby serve as a further disincentive to retrofit West Coast refineries.

VIII. Effect on Decisions to Construct West-to-East Crude Oil Transportation Systems

The export of substantial quantities of California heavy crude could adversely impact decisions to proceed with one or more of the West-to-East pipeline systems that have been proposed. Very little indigenous California crude, other than the Elk Hills production, is likely to be pipelined to Texas via the PACTEX line or to the northern tier and other inland states by other proposed West-to-East transportation systems. Physical problems associated with pipeline shipment of heavy crude, and the availability of better quality crude from other sources, make it unlikely that California crude itself would be shipped by pipeline outside of PAD V.

However, the current West Coast oil surplus is projected to increase as ANS crude shipments increase. The additional ANS crude could be shipped via one of the proposed West-to-East pipelines. Such a diversion of ANS crude could stimulate increased production of California crude by effectively removing some of the ANS competition.

Alternatively, California crude now being backed out of the market could be exported, either to Japan or to the Caribbean. This option would relieve the current market pressures for improved West-to-East transport facilities, and thus serve as a disincentive to their construction. It should be noted, however, that the amounts of crude involved in the NEPCO proposal are probably not sufficient in themselves to affect a decision on the development of West-to-East distribution systems.



EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

July 20, 1978

MEMORANDUM FOR THE PRESIDENT

FROM:

JIM McINTYRE

*W. Brown - Clark
C/pt*

SUBJECT:

July 17 Schlesinger Analysis of California Crude Exports
to Bahamian and Caribbean Refiners

We have reviewed Jim Schlesinger's July 17 memorandum which provides answers to your questions on the proposal to export heavy California crude oil to Bahamian and Caribbean refiners, with subsequent reimport of the resulting refined products.

We agree with Jim's conclusions that (1) as a short-term initiative, the proposal would have only slightly favorable, and possibly adverse, impact on the balance of payments and little or no favorable effect on the price or supply of East Coast residual oil; and (2) further action on the California crude surplus problem is not now warranted in view of the Energy Department June 15 initiatives which are expected to relieve the situation.

As a longer term proposition which might result in net favorable impacts on balance of payments and import levels, this approach (including a variation which would focus more directly on new production) should be studied, as Jim suggests, in the broader context of other initiatives to achieve substantial increases in California crude production. We would hope that the results would be forthcoming by year end.