Survey of energy plan shows

Profits must increase with risks

By TRICIA BRUNHART

An analysis of the national energy plan conducted at Texas A&M University has found that oil company profits must increase along with any increases in investment risks.

Dr. Peter S. Rose, a professor of finance at Texas A&M and author of the study, said the more uncertainty in industry profits, the more risks to stockholders. Consequently, investors are only willing to take on added risks if the oil companies pay higher interest rates. Therefore the companies must earn a greater return on their product to afford the higher interest rates.

The study states that the costs of energy exploration, development, and transportation are rising and *since petroleum resources are available* only in more remote locations, the risk of investment is greater. Rose said remote locations are such places as offshore drilling areas and Alaska's north slope.

"The risks include not only technological and economic factors, but also political forces," Rose said. The government makes the "rules of the game" he said, and changes in these rules can be a risk to investment. For example, there could be changes in permissible prices, or in promoting competition.

The study also found that capital needs for the petroleum industry have increased greatly since the mid-1960's. An estimate by the Energy Economics Division and Chase Manhattan Bank places "total capital requirements for oil and gas production and exploration in the free world at 1.3 trillion between 1976 and 1985."

Oil companies in the United States rely in part on borrowed funds to meet their capital needs and have done so since their beginnings, Rose said. These funds come from commercial banks in the forms of short- and medium-term loans, or from selling bonds.

Petroleum firms enjoyed the greatest profitability during the early 1950's for several reasons, said Rose. One reason is that costs were below any legal price ceilings, which makes it easier to make a profit. Another reason is that during *this time* there was a relative quiet in the economy and interest rates were low. A third reason is that demand grew faster than the cost of production, which boosted revenues.

During the oil embargo of 1973-1974, profits of oil companies were greater because there was a rise in the value of inventories of oil, said Rose. The Arabs raised the price and the oil which was stored in tanks increased in value, he explained. With the increased value of oil, petroleum firms found their net worth rising.

The study suggests solutions for the financial situation in the oil industry. "One possibility is to institute more flexible pricing policies for both oil and natural gas in order to allow industry revenues to keep pace with rising costs," Rose said. A sudden lifting of price controls would not be advisable, he said. Instead, these controls should be a phased out as quickly as possible.

Another suggestion is "to encourage greater diversification into new product lines and geographic regions." By spreading out into many markets, oil firms would be able to hold down their cost of capital and reduce their financial and operating risks.

Rose, who once worked for the Federal Reserve Bank of Dallas as a financial economist, researched the 121-page study for four months.

campus activities

Monday

Student "Y", applications available until Feb. 17, 216 MSC

Women's Leadership Workshop, 6:30 to 8 p.m., 145 MSC

Killeen Area Hometown Club, 7:30 p.m., 350 MSC

266 G. Rollie White

Tuesday

Student Teachers, for those going through EDCI for certification, 6 to 7:30 p.m., 108 HECC

College of Business Administration Student Council, 6 p.m., Dean's office, old Engineering Building

Lambda Sigma, 7 p.m., 108 Harrington

Biomedical Science Association, 7:30 p.m., 201 VMS

Nautical Archeology, 7:30 p.m., 140A MSC

TAMU Collegiate FFA, 7:30 p.m., 209 Harrington

Recreation & Parks Club, 7:30 p.m., Goodwin Hall, basement

Phi Delta Gamma, Dr. Nanetter Bruckner, 8 p.m., 205 MSC

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