Biggest Oil ETF Halts Creations

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The shoe continues to drop for the world's biggest oil fund.

This morning, the **United States Oil Fund LP (USO)** suspended creations of new shares, due to an incredible spike in investor demand that has resulted in the fund actually running out of registered shares to issue.

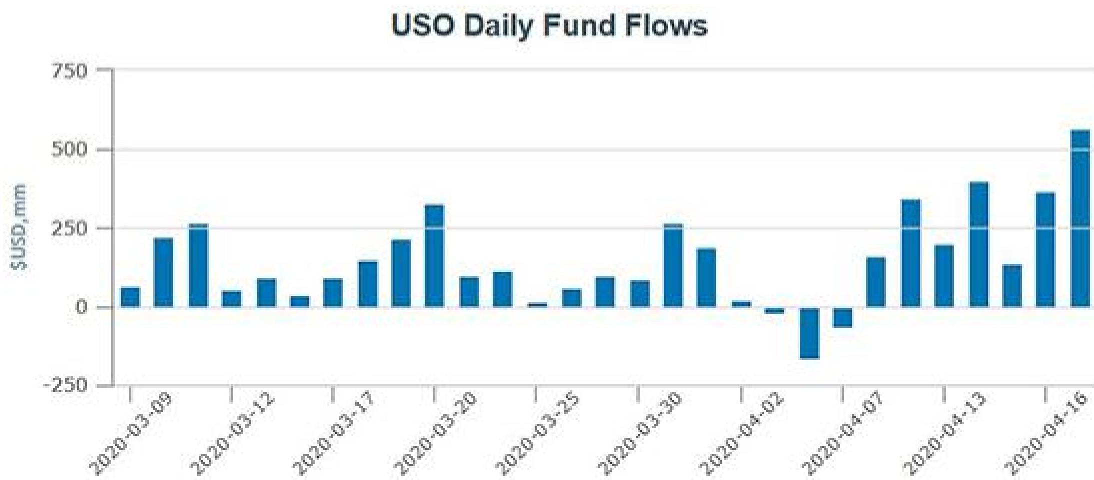
As a result of the halt, no new shares of the fund can be created by authorized participants (APs), but the fund will continue to trade as normal in secondary markets (i.e., the NYSE Arca).

Investment Deluge For USO

USO has seen a massive spike in investor demand, with $4.3 billion in new net cash pouring into the fund since crude oil's troubles first began on March 9. (This figure doesn't yet include yesterday's numbers. We'll update this story as soon as we receive them.)

Before yesterday, USO had registered 1,136,200,000 outstanding shares. Due to this increased demand, however, only 299.9 million of those shares, or 26%, were left available for APs to use as of yesterday afternoon.

The pace of inflows being what they were, USO appeared likely to run out of shares very quickly: On Friday alone, $564 million entered the fund.



(For a larger view, click on the image above)

Source: ETF.com; Data as of April 20, 2020

Therefore, yesterday afternoon, USO's issuer, U.S. Commodity Funds (USCF) filed with the Securities and Exchange Commission to raise its outstanding shares to 4 billion, giving the fund more wiggle room.

The SEC has yet to approve or disprove the registration, however, thus necessitating the creation halt when available shares ran out this morning.

USO Holds No May 2020 Contract

USCF made its filing yesterday, just hours before the expiring May 2020 NYMEX WTI oil contract went negative, settling the session at -$37.63/barrel on collapsed demand and vanishing storage (read: "Stunningly, Oil Prices Crash Below Zero").

To be clear, USO does not hold any May 2020 NYMEX WTI oil contracts. As we covered on Friday, it currently holds an 80%/20% blend of second- and third-month contracts, meaning the June and July 2020 WTI NYMEX contracts (read: "Biggest Oil ETF Shakes Up Structure").

USO had adjusted its portfolio in part to accommodate regulatory limits; as more and more money entered the fund, the ETF exceeded position limits, preventing any one investor from owning more than 25% of deliverable supply in a given futures contract.

As of yesterday's close, USO owns 23.5% of June 2020 oil contract, coming perilously close to once again exceeding position limits.

What's Next For USO

If and when the SEC approves an increase in shares, USO will reopen to new creations; until then, creations will remain suspended.

One immediate consequence of the creation halt will be a rise in trading costs for investors.

When ETFs suspend creations, the arbitrage mechanism that usually keeps a fund's price in line with its underlying net asset value (NAV) is disabled. As a result, premiums to NAV often develop in the fund, as investors chase after a limited amount of shares.

In addition, bid/ask spreads for the ETF often widen as well, in order to compensate APs for the inability to effectively arbitrage.

Investors—especially retail investors who may not understand the mechanics of oil markets or futures-based ETFs—are advised to tread with extreme caution when trading USO.

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