Peak Oil Review

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1. Oil and the Global Economy

After a two week decline of nearly $10 a barrel, oil prices reversed last week and climbed a little on Thursday and Friday leaving NY oil at $92.19 and London at $112.39. Despite the steep decline in September, oil prices still registered the biggest quarterly increase this year on concerns that Middle Eastern problems could disrupt oil supplies. Higher gasoline prices also contributed to the increase.

Friday saw an unusual short squeeze on the closing October gasoline contract in NY which sent prices up 19 cents to close at $3.34 a gallon. The sudden surge was technical in nature as one or more traders scrambled to cover short positions before the contract expired. The November contract closed Friday at $2.92 up only 2.2 cents. Behind the move was the prospect of gasoline shortages in the Northeastern US as gasoline stocks in the region fell to their lowest level since record keeping began in 1990. Refinery outages in Canada, Wales, and the Netherlands have reduced shipments going into the NY area.

Higher gasoline prices are blamed for weaker US economic growth in September despite the first drop in gasoline and diesel prices in more than 3 months. The average retail price of regular gasoline was down 5 cents a gallon last week but was still 32 cents a gallon higher than at this time last year.

Natural gas prices rose more than 30 cents per million BTUs closing at $3.32 last week on reports that a “super glut” that would swamp storage capacity does not appear to be developing. A combination of a hot summer, less drilling for gas, and a switch by the power companies to natural gas kept the national stockpile at 3.6 trillion cubic feet or 84 percent of capacity, only slightly above the 80 percent at this time last year and well within the theoretical storage capacity of 4.2 trillion cubic feet. Nuclear power plant outages have contributed to the higher demand for natural gas.

Most of the US is expected to see cooler weather in the next week or two but it is too early for a solid forecast of what the winter will bring as regards to the need for heating gas.

Reuters is reporting that OPEC production in September was the lowest since January mostly because of reduced shipments from Angola and Nigeria. This may be due to shipping schedules and not indicative of falling production. Although difficult to track, Iran’s oil supply in September may have fallen by 50,000 b/d to 2.8 million. Saudi production was seen at 10 million b/d, but Libyan production was only 1.46 million vs. the 1.6 million the government was claiming. Iraqi production was up to 3.06 million b/d thanks to higher exports from the north.

2. The Middle East

Much of the action pertaining to the Middle East last week took place at the UN General Assembly meeting in NY where many of the world’s leaders gathered to air their concerns before a global

audience. Most of the major decision-makers involved in the various crises showed up and many grievances were aired. President Obama, Prime Minister Netanyahu, and President Ahmadinejad all spoke on the Iranian nuclear crisis. The upshot seems to be that the US and Israel are back in some sort of agreement as to taking action against Iran and Israel seems to be saying there is no need for an attack on Iranian nuclear facilities at least until next year – well after the US election. The Israeli government leaked a report saying that Iran is being hard hit by the sanctions.

President Ahmadinejad played down the possibility of an Israeli attack, holding that the US would be responsible if the Israelis did strike, and that Iran's economy is doing fine under the sanctions. He repeated many of his usual threats and bombast about a "third world war" and the destruction of Israel ensuing in the event of an attack.

In the meantime, the US administration told Congress that it had found that the Iranian Oil Company was so intimately involved with Iran's Revolutionary Guards that it too should be considered a terrorist organization. Any entity doing business with National Iranian Oil Company would be subject to US sanctions – thereby increasing pressure on Tehran.

Fighting in Syria is becoming more intense with bombs going off at military headquarters in Damascus and fierce fighting taking place in Aleppo, where government bombs and artillery are turning much of the city into rubble. With winter coming and the country's economy in disarray, it is difficult to see this uprising going on much longer. A major humanitarian crisis with still larger population movements seems to be in the offing.

Meanwhile, fears are rising that the Sunni/Shiite struggle in Syria is spreading into Iraq where suicide and car bombings on the rise. On Sunday some 25 people were killed in attacks on police facilities across the country raising the question of just when the increasing violence will affect oil production.

Baghdad is becoming concerned about the flow of refugees from Syria into Iraq and is said to be banning men of military age from seeking sanctuary lest they join in some sort of uprising against Iraq's Shiite government. For now Iraq's oil exports are doing nicely, but trouble may be brewing with the Kurds as Baghdad seeks to increase its control over security forces in the region.

The media is starting to grasp that much of Saudi Arabia's much ballyhooed increase in oil production last summer went into domestic consumption to keep air conditioning working during the hot months and did not go for export. Concerns of systemic instability in Libya are also rising.

3. Slowing Economies

Hardly a day goes by without a pessimistic economic report from one or another of the world's developed countries. In the US, consumer spending stagnated in August with purchases increasing by only 0.1 percent after adjusting for inflation. Higher gasoline and food bills, which preempt spending on other goods and services, are seen as responsible for the decline. Retail regular gasoline averaged $3.83 a gallon through September 27 as compared to $3.70 in August and $3.42 in July. The financial press is beginning to make the connection between high gas prices and weak consumer spending.

Concern is increasing about the gridlock in Washington over the deficit and the $600 billion in expiring tax cuts and government reductions that are scheduled for 2013. Any relaxation of the cuts will have to await the outcome of the November election. Until a new policy is set, businesses will have to plan for the worst by holding back on hiring and investment decisions and in some cases preparing for major reductions in force.

In Europe most of the activity centered on Spain, although demonstrations in Greece came in for a share of the attention. With borrowing costs rising sharply and capital fleeing the country, Madrid announced a series of reforms and cost cutting measures before formally requesting a bailout from the EU. The situation was further confused by a call for an early election in Catalonia, Spain's most powerful economic region, which could turn into an unofficial referendum on splitting from the rest of the country. In Germany, business sentiment has dropped for the 5th consecutive month as did

sentiment among EU-wide businesses and consumers. All this is interpreted by financial analysts that the EU is slipping into recession.

China's manufacturing contracted for the 11th consecutive month as export orders continue to fall. With Beijing in the midst of its once-a-decade leadership transition, there is concern that the government may not be able to take the decisive action necessary to head off more serious problems in the future. Most observers agree that Beijing failed to anticipate the rapid fall in export orders that is currently taking place. The dispute with Japan over claims to some islands is also affecting China's exports.

The oil markets are clearly aware of the simultaneous slowing of most of the world's major economies and this is leading to frequent assertions that oil prices will be falling soon. The key question for the immediate future is how much the demand for oil will slow in response to reduced economic activity and the level of the perceived threat to Middle Eastern oil exports.

Quote of the week

- "Oil on Greenland would be a disaster."

  - Christophe de Margerie, Total's chief executive

The Briefs (clips from recent Peak Oil News dailies are indicated by date and item #)

- **OPEC** crude oil output has fallen in September because of reduced exports from Angola and Nigeria, and as Iranian output slipped back to its lowest in more than two decades. (9/29, #5)
- Japan's crude oil imports from **Iran** in August fell 66 percent from a year earlier to 100,000 b/d. (9/29, #6)
- Total expects to pump crude from its **Ugandan** oil fields in 2017, a year later than previous estimates had suggested, as the firms developing the country's oilfields work on issues that have delayed the start of operations. (9/29, #12)
- Japan's industry minister said the country must give up **nuclear** power plants as soon as possible because they pose too much risk in one of the world's most earthquake-prone countries. (9/29, #15)
- The **US** imported more oil from OPEC producers in the first six months of 2012 than for the same period last year. (9/29, #21)
- **India** is becoming more interested in Canadian energy assets. "Discussions have been initiated," said Indian Consul General Saran in an interview. Her comments follow reports this week that Indian companies were exploring potential purchases of Canadian oil sands assets of ConocoPhillips. (9/29, #24)
- **India** is determined to increase nuclear power. An adviser to Indian Prime Minister Singh, acknowledged "apprehensions" raised in the wake of Japan's Fukushima disaster. "There are safety challenges but India has adequate capabilities to meet those challenges," the advisor said. (9/26, #11)
- President Obama blocked a privately owned Chinese company from building **wind turbines** close to a Navy military site in Oregon due to national security concerns. The company said it would challenge the action in court. (9/29, #27)
- Energy Minister Bassil says economically battered **Lebanon** is "technically ready" to start drilling for natural gas in the eastern Mediterranean, an assessment industry insiders say is overly optimistic. (9/28, #12)

- Chevron and drill-rig operator Transocean have 30 days to stop operating in **Brazil** after a local court served the two companies with an injunction for their roles in an offshore oil spill last year. (9/28, #13)
- **Ecuador** plans to process 84% of Ecuadorean crude oil and 16% of Venezuelan crude in the $13 billion planned Refineria del Pacifico, a refining and petrochemical complex project run by state oil companies of Venezuela and Ecuador. (9/28, #15)
- The US Interior Department said it approved the construction of electricity lines from a 139-megawatt solar power project in southern **California**. Secretary Ken Salazar gave consent for the construction of transmission lines that cross federal and public land in southern California. (9/28, #23)
- The Environmental Protection Agency said new government tests of **groundwater** near Pavillion, Wyo., have yielded results similar to data it released last year, when it suggested chemicals in the water were linked to hydraulic fracturing. The EPA's contention was dismissed by Encana, the natural-gas company operating in the area, which said the EPA was still offering a "flawed" interpretation of test results. (9/28, #25, #26)
- **US oil production** surged last week to the highest level since January 1997, reducing the country's dependence on imported fuels as new technology unlocks oil trapped in shale formations. Crude output rose by 3.7 percent to 6.509 million b/d in the week ended Sept. 21. (9/27, #12)
- **Natural gas pipelines** coming into service by year end may boost deliveries from the Marcellus shale deposit in the Northeast by 30 percent, extending a supply glut that helped send prices to decade lows. (9/27, #14)
- **BP** may get less than half the $2.85 billion it planned for selling its Texas City refinery, the third-largest in the U.S., as values for U.S. plants haven't kept pace with profits. The average price of U.S. refineries sold since 2009 indicates the plant should sell for $1 billion, data compiled by Bloomberg Industries show, a valuation that would be among the lowest in two decades. (9/27, #16)
- Northern Plains Nitrogen is developing plans for a billion-dollar **fertilizer plant** in North Dakota to extract better value from the state's abundant natural gas. If launched, the plant would help reverse a long-term decline in U.S. nitrogen-fertilizer output, reflecting the competitive advantages conferred on U.S. fertilizer makers by cheap gas. (9/27, #17)
- **Nigeria**'s crude oil exports are due to hit a six-month high in November as almost all its oilfields pump near peak levels. Africa's biggest oil producer is due to sell around 2.12 million b/d of crude oil in November, up from 2.05 million b/d scheduled to load in October and 1.84 million b/d in September. (9/25, #19)
- **Brazilian ethanol** is coming back into the US after a three-year ebb, drawn less by the severe drought that has inflated corn costs than by biofuel regulations that could more than triple next year's shipments. (9/24, #12)
- Reaction to the announcement by the Cuomo administration that **New York** State must review potential public health effects before deciding whether to allow fracking is split along fairly predictable lines. Gas industry officials and landowners who want to lease their properties for this kind of natural gas drilling said they were disappointed because the move means that fracking won’t start anytime soon. (9/24, #15)
- The US drilling **rig count** fell 11 units during the week ended Sept. 28, with the total number of rotary rigs in the US reaching 1,848. This compares with 1,990 rigs working in the comparable week last year. (9/29, #23)

Reader Survey: Oil and Growth: What are the Key Economic Questions?

One of the highlights of the upcoming ASPO-USA conference at The University of Texas at Austin (November 30- December 1) will be the economics "debate." Three leading economic thinkers will wrestle with fundamental questions about the role of energy in the economy and the effect of changing realities for oil on economic growth. Featured guests will be:

- **James Kenneth Galbraith** - notable professor of economics and government at the Lyndon B. Johnson School of Public Affairs of The University of Texas

- **Jason Schenker** - chief economist and president of Prestige Economics; guest host of *Street Smart* on Bloomberg Television

- **Charles Hall** - distinguished professor at the SUNY College of Environmental Science and Forestry of the State University of New York; co-author of *Energy and the Wealth of Nations: Understanding the Biophysical Economy*

Scenarios for common economic indicators such as GDP, employment, and inflation will be explored, while underlying assumptions and the very foundations of conventional economics will be questioned and debated. Our three speakers come at these issues from very different perspectives and we can hardly wait to see what will come out of this "joust" of ideas.

The audience will be an important part of the conversation and will essentially fill the fourth seat at the table. We expect the discussion to be lively and spontaneous; however, it also will be helpful to identify key questions in advance. So tell us:

What do you think are the central economic questions that need to be addressed regarding oil and the economy?

Please send us your suggested questions and we will incorporate them into our preparation for the session.
While you can send us as many suggestions as you would like, we will distill the list down to the most critical questions and issues, so put your thinking caps on and focus on honing one really good question.
Please send via email to info@aspousa.org with “Economics Question” in the subject line.

Thanks for the help, see you in Austin!

Jan Lars Mueller
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