



PEAK OIL REVIEW

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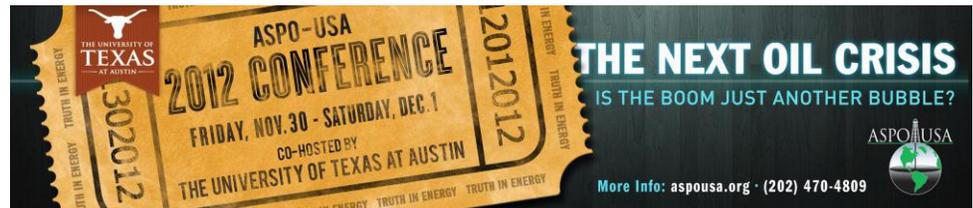
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1. Oil and the Global Economy

Oil traded in a narrow range until Friday when an accumulation of economic problems such as weak demand, growing inventories, and a seeming lack of progress at the EU summit meeting sent prices down more than \$2 a barrel. The futures market closed out the week at \$90.05 a barrel in NY and \$110.14 in London. Widespread pessimism about the global economy coupled with a lack of any immediate threats to Middle Eastern oil supplies are held responsible for Friday's decline.

US gasoline prices are finally dropping as they usually do after Labor Day with the nationwide price of regular down to \$3.67 a gallon from \$3.83 a month ago. Gasoline futures are down 25 cents a gallon in the last two weeks. In California, where they are still having refinery problems, regular is going for an average of \$4.44 a gallon. While US crude inventories are at their highest level for this time of year since 1982, gasoline and distillate inventories are pushing record lows despite weak demand. The API reported last week that US oil demand in September fell 3.8 percent from last September to 18.2 million b/d. Northeastern US distillate inventories, where most of the demand for heating oil takes place, are down to the lowest on record and weather forecasters are already talking about a colder and snowier winter ahead in the region.

US natural gas futures dropped midweek on forecasts of milder weather across most of the US in the week ahead; by Friday however, new forecasts of colder weather in November, the possibility of a cold winter in the northeast, and shrinking natural gas inventories led to a jump in futures prices. Natural gas closed on Friday above \$3.60 per million BTUs after having traded below \$2 in the spring when the gas glut was at its height and there were fears that the US would run out of storage space.

2. Middle East

The New York Times, citing administration officials, reports that Iran is willing to open direct talks with Washington on the nuclear question after the US elections. Tehran and the White House, however, have denied that any agreement for talks has been reached, but the White House says it is open to the suggestion. The possibility of talks boosts the administration's case that sanctions rather than military action is the proper way to handle the situation. Others are already saying that direct talks are merely another attempt by Tehran to stall for time as it continues to work on its nuclear weapons program.

Meanwhile the US and EU imposed further sanctions on Iran's oil and gas industries last week. Many of these new sanctions are designed to close loopholes that have arisen as Tehran scrambled to find ways around the sanctions. The EU's sanctions involve freezing the foreign assets of some 30 Iranian companies doing business in the West.

Iran is attempting to portray any strike on its nuclear facilities as a step towards a regional or "global" war with retaliation taking place against US and Israeli interests. *Der Spiegel* reports that Tehran is contemplating blocking the Straits of Hormuz with a giant oil spill. Although Iran's exports would be disrupted too, the theory is that the shutting in of most Middle Eastern oil exports would force the lifting of the sanctions.

The war in Syria continues with some 200 deaths occurring each day now. Efforts at a ceasefire appear useless and the assassination of an anti-Syrian Lebanese security official is seen as a step towards extending the war into Lebanon. The uprising is slowly engulfing Damascus with fighting in the suburbs taking place regularly and the occasional bomb going off in the center of the city. The insurgents do not have the heavy weapons to challenge government forces in the city, but do have enough manpower to hold some suburbs in hopes of strangling food and fuel supplies.

The situation is clearly going poorly for the Assad government which is unlikely to last much longer even with the support of Moscow and Tehran. The armed opposition is said to number about 100 groups of diverse political stripes. Over the longer run, the issues of where Syria's large stockpiles of chemical weapons end up and whether the Sunni-Shiite animosities spread into oil-producing countries will be critical to the future of the region. It is interesting to note that the use of twitter to discuss anti-government sentiments is spreading rapidly in Saudi Arabia despite the government's best efforts to control the situation.

In Iraq, Exxon has signed contracts to drill in Kurdistan without Baghdad's permission. The Iraqis are considering throwing Exxon out of the giant West Qurna-1 oil field and replacing them with Russian oil companies.

3. The EU Crisis

The major development last week was another EU summit meeting, successful only in that it came up with a "timetable" for a Eurozone banking union but not the details of such a plan. Such a union is highly controversial as it would require zone members and possibly all the EU's membership to surrender some fiscal sovereignty to a central EU authority. Whether or not the goal of fiscal integration can be fulfilled in time to avoid a serious economic recession or the fiscal collapse of Greece or Spain remains to be seen.

In the meantime, Greece continues on the path towards anarchy. The country had expected to finalize last week an austerity package that would unlock a €31 billion EU loan needed before the country becomes bankrupt at the end of November. Instead the negotiations broke down once again and the EU's attention switched to the larger problem of Spain, leaving Athens hanging until sometime in November. In the meantime Greek society is coming unraveled amid strikes, massive unemployment, inflation, and shortages. Some are predicting that civil war is not far away as pro-Nazi forces square off against leftists. All this makes it

difficult to see how Greece can stay in the Eurozone despite the endless assurances from EU leaders that it wants the Greeks to remain in the zone.

The EU's austerity demands, which include the firing of many civil servants and large cuts in benefits are simply too harsh for Greek politicians to accept, so that it is doubtful they will be implemented in the immediate future. On Thursday, a second nationwide strike began.

Things are not much better in Spain where Prime Minister Rajoy is delaying asking for fiscal help from a program of bond buying approved by the EU. Spain's borrowing costs have remained below 6 percent ever since the bond-buying program was announced in early September. The delay may be partly due to pressure from the Germans who do not want to stir up their voters with more talk of another massive bailout for southern Europe using German money. Spain is caught in a trap in which austerity measures are choking off economic growth, leading to a rapidly increasing debt burden and still more problems.

With each passing week it is becoming more difficult to see how the EU can avoid a major recession or worse in some parts of the country. All this does not bode well for the EU's oil consumption in the next few years.

4. China

Beijing released data last week showing that its economy expanded by 7.4 percent in the third quarter, putting the country on course for its lowest annual growth since 1999. The World Bank recently reduced its full-year China's GDP growth rate to 7.7 percent from its May forecast of 8.8 percent. Beijing says it is confident it will achieve its goal of 7.5 percent. These numbers, of course, are well below the 9.3 percent achieved last year and the nearly 10 percent average achieved during the last 30 years.

Newly released numbers show China's electricity consumption growing by 2.9 percent year over year in September with industrial electricity consumption growing by an anemic 0.9 percent during the month, a new low for monthly growth. Consumption was so low that several thermal power plants had to shut down in southern China.

Some monthly data for September suggest that the rate of economic decline may be slowing. Most analysts see further decline halting, with economic activity growing slowly in coming quarters.

In contrast to the GDP and electricity figures, Chinese refineries processed a record amount of crude in September, up 7.0 percent from September 2011. This amount of processing, equivalent to 9.5 million b/d, was 6.2 percent higher than the crude runs in August. Custom's data shows China's oil imports rebounding from a record low in August to 4.9 million b/d.

As China's economic growth does not seem sufficient to utilize this much refined product, it is likely going into storage to replace drawdowns earlier in the year when widespread refinery maintenance closed many refineries for an extended period. It is also possible that China is preparing to increase exports of refined products in coming months.

Quote of the week

- "Mr. President, let me just see if I can move you to the gist of this question, which is, are we looking at the new normal? I can tell you that tomorrow morning, a lot of people in Hempstead will wake up and fill up and they will find that the price of gas is over \$4 a gallon. Is it within the purview of the government to bring those prices down, or are we looking at the new normal?"

- Candy Crowley, moderator of the second presidential debate

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

- **Saudi Arabia** plans to become 100 percent powered by renewable and low-carbon forms of energy, according to an influential member of the royal family. But the process is likely to take decades and some observers are skeptical as to whether it is any more than window-dressing. (10/20, #7)
- **Egypt** increasingly views Ethiopia's plan to build a massive 6,000-megawatt hydroelectric dam on the Nile River as a threat to its national security because it will seriously cut the Arab state's water supplies. Egypt depends on the Nile for virtually all of its water and is mounting a major diplomatic and economic campaign to stop the plan. (10/20, #9)
- **Shell** has been in talks with the US government over extending its leases for oil development in the Arctic seas north of Alaska after its drilling program was held up by legal actions and objections from regulators. (10/20, #14)
- **Canada** blocked Petroliaam Nasional Bhd.'s \$5.2 billion takeover of Progress Energy Resources, saying the bid by Malaysia's state-owned oil company wouldn't advance national interests. (10/20, #19)
- Most Canadians surveyed said they didn't support the proposed Chinese takeover of oil and gas company **Nexen**. China National Offshore Oil has offered to buy Nexen for \$15 billion. Around 90 percent of the Nexen shareholders voted in favor of the deal last month. (10/18, #25)
- **Goldman Sachs** has called an end to the oil price super-cycle, reversing years of bullish recommendations, citing a rise in unconventional oil supplies in the United States and Canada. Goldman has been the highest predictor among major oil price forecasters but said "long-dated" or five-year forward Brent crude may be anchored at about \$90 a barrel. (10/19, #5)
- Israeli business daily Globes said there are signs suggesting Russian natural gas company **Gazprom** is set to take on a stake on the giant offshore Leviathan gas field. (10/19, #13)
- **South Sudan** has ordered oil companies to restart production immediately, ending its dispute with Sudan. It halted production in January in a row over oil transit fees. (10/19, #14)
- **China's** effort to shut down dozens of small, privately owned oil refineries is making them grow bigger instead, threatening Beijing's plans to regulate an industry that the International Energy Agency says is already overheating. (10/19, #15)
- Construction has started on what Royal Dutch Shell calls its "game-changing" **Prelude FLNG** (floating liquefied natural gas) project. The firm reported that first steel was cut on the project's substructure at Samsung Heavy Industries' Geoje shipyard in South Korea. (10/19, #17)
- The coming **winter** will probably be cooler in the US than a year ago, boosting demand for heating fuels such as natural gas. While December will be warmer than normal, temperatures will drop through February, increasing natural gas use by 13 percent over the same period from last year. (10/19, #18)
- Mitsubishi will acquire a 20-percent stake in Star Energy Geothermal, a holding company that manages Indonesia's largest geothermal power station on Java. The deal represents Mitsubishi's first operation of a geothermal power plant as well as its first entry into the **Indonesian** power sector. (10/19, #27)
- **Reliance Industries** is in talks with Venezuela's PDVSA to produce heavy oil in the South American OPEC nation. (10/18, #14)
- The ball is in **New Delhi's** court in terms of a natural gas pipeline planned from Iran. Iran has pressed ahead with the development of a gas pipeline from the South Pars field in the Persian Gulf despite a lack of guarantees from downstream partners. Iranian Deputy Foreign Minister for Asia Araqchi called on New Delhi to make a decision on the project in order to expedite development. (10/18, #21)
- The Obama administration has issued the most **deep-water oil-drilling permits** for the Gulf of Mexico this year since 2007 as high crude prices revive exploration slowed by the 2010 BP spill. The pace of issuing permits drew criticism from Mitt Romney and energy lobbyists during the campaign who say the policies slowed oil and gas production on federal land. (10/18, #23)
- **Halliburton**, the world's largest provider of hydraulic-fracturing services, said third-quarter profit decreased 12 percent as customers negotiated cheaper rates because of the glut of fracking equipment. (10/18, #24)

- Crude oil production in **Russia** will hit a record high of about 517 million tons in 2012, about 1.2 percent up from last year. (10/18, #27)
- A British energy official said the government was warming to the development of **shale gas** but warned it won't be a panacea for cheaper energy. British Energy Secretary Davey told *The Daily Telegraph* the government is expected to give the nod to shale when it unveils plans for more gas-fired power plants in November. (10/17, #18)
- China National Petroleum Corp.'s gross production from its **Iraqi projects** has now reached 1.64 million b/d of crude, the company said on its website. This is slightly higher than CNPC's last update in mid-August, when it said its Iraqi output hit a record 1.6 million b/d. (10/16, #8)
- Kuwait Energy Co. and its main partner, the Egyptian General Petroleum Corp., said they made a new oil discovery at Ahmad-2 well, located in **Egypt's** Gulf of Suez. (10/16, #10)
- **India's** emergency oil stockpile storage is facing a year's delay because of geological surprises encountered in construction of underground caverns that will be used to cushion the country against supply disruptions and price fluctuations. (10/16, #13)
- The global energy industry faces downward pressure on **demand** while the supply of fossil fuels has risen sharply but there is no risk of a price collapse, Saudi Aramco CEO Khalid al-Falih was quoted as saying. (10/16, #4)
- The number of **natural-gas drilling rigs** working in the US rose by five this week to 427, according to Baker Hughes. The figure is down 500 from a year-ago level of 927. The **oil-rig count** fell by one to 1,410 in the week. The number of working oil rigs is up 331 from a year ago. (10/20, #15)