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1. Oil and the Global Economy

New York and London futures prices spread further apart last week as US traders focused on whether the Federal Reserve would slow bond purchases and London worried about the increasing turmoil in the Middle East. During the week NY oil fell by nearly \$4 a barrel, trading below \$104, before climbing on Friday to close at \$106.42. In London, Brent crude closed at \$111.04 on Friday, leaving the world pricing standard less than \$5 a barrel below the highs seen in 2011, 2012, and 2013.

A weaker-than-expected US housing report contributed to the Friday price surge as the dollar fell. Despite the weak housing market, analysts are still looking for the Federal Reserve to cut back on bond purchases in September.

Concerns are growing as to whether the drought in Texas will curtail fracking of new wells which can consume as much as a million gallons of water each in a very dry section of the state. The Texas Railroad Commission reports that production from the Eagle Ford shale fell by 4.5 percent between May and June.

Gasoline futures also surged on Friday to close at \$3.00 a gallon following a steep decline in US gasoline stockpiles and reports of troubles at two major refineries. This is only about 10 cents per gallon below the highs we have seen since the great 2008 price spike.

Natural gas futures settled on Friday to a low of \$3.48 per million after having traded as high as \$3.54 earlier in the week. Summer is drawing to a close, and prices around \$3.50 are too high to encourage much more switching from coal to gas by power companies. The EIA forecasts that natural gas inventories will be back to normal levels by the end of October after reaching record highs due to milder weather in the last two years.

2. The Middle East & North Africa

Syria: The use of poison gas on insurgents and civilians in a Damascus suburb has opened a new stage in the ongoing Middle Eastern turmoil. Some 3500 were allegedly subjected to the gas attack and at least 300 men, women and children died. Although most suspect that the insurgents are incapable of launching a gas attack at this scale, and have no reason to attack their own people and civilian supporters, the Assad government and their supporters in Moscow and Tehran insist that the government was not responsible. Damascus argues the attack was an insurgent provocation to bring foreign powers to their support.

In response to the attack many countries are calling on the US to retaliate as Damascus, if responsible, has crossed a "red line" set by the Obama administration. Five days after the attack the Assad government agreed to allow inspectors into the area of the attack to ascertain what happened. In the meantime the US is in a quandary as to the appropriate response.

Damascus and Tehran are already warning that any attack on Syria by the US or other outside powers would “create a ball of fire that will inflame the Middle East.” While Moscow joined in the calls to allow UN inspectors into the neighborhoods where the attack took place, they did not do so for several days thereby possibly allowing the time for definitively placing the blame to pass.

Whatever Washington decides to do in the next week could have a lasting impact on Middle Eastern developments and oil exports.

There are no easy answers for Washington which is expected to take the lead in any retaliation. Polls show that most Americans are opposed to active intervention, preferring to let the Muslims fight it out among themselves. Most US military actions ranging from missile attacks to no-fly zones would not be decisive and even the elimination of Assad and his government would likely result in a failed state in which Jihadists would be free to launch attacks on Israel or western targets.

There are many possible forms that retaliation for a direct attack on Syria could take – some of these could involve oil exports. As the Assad government’s supporters are largely confined to Hezbollah and Iran, most Arabs would be happy to see Western military intervention against Assad.

The press is reporting that some 400 tons of arms reached the insurgent forces over the weekend via Turkey, somewhat addressing the military advantage the Assad government gained when Hezbollah intervened on its behalf.

The war in Syria continues to spread into Lebanon where 47 were killed in twin car bombings in Lebanon’s northern city of Tripoli. On Thursday Hezbollah, which has come under increasing criticism for its intervention in Syria, tried to redirect attention to the Arab-Israel conflict by firing rockets at Israel in order to draw an Israeli attack on Lebanon -- which came on Friday.

Iraq: The wave of car and suicide bombings and shootings continued across Iraq last week. The northern export pipeline was blown up for what may be the 31st time this year. This bombing resulted in major amounts of oil spilling into the Tigris River which is the water supply for Baghdad and other central Iraqi cities. Water supply facilities have been shut down in several cities and water from the Tigris is being diverted into Lake Tharthar to avoid polluting Baghdad’s water supply.

The number of Syrian Kurds making their way into Iraqi Kurdistan in the last two weeks is now estimated to be 40,000. The largest refugee movements in the Syrian conflict came amidst reports of attacks by Sunni Jihadists on Syrian Kurdish villages.

Iraq’s Oil Minister confirmed that Exxon will be allowed to sell its stake in the West Qurna-1 oilfield to China’s Petro China and Indonesia’s Pertamina. The deal will be closed in the next two to three weeks.

Egypt: It was a relatively quiet week in Egypt as the Army and its hand-picked government continued to arrest prominent members of the Islamic Brotherhood and stationed troops at key locations. The crackdown was sufficient to prevent the renewal of any large pro-Morsi demonstrations last week. Several of the Brotherhood’s former leaders are due in court this week to face charges stemming from when the Brotherhood was still in charge.

For the immediate future, Egypt’s problems will be economic as the economy is in very bad shape and the curfew which, was partially eased, restricts commerce. The US has decided to continue aid to the Egyptian Army as it would be too expensive and complicated to cut the ties but to restrict economic aid. Most foreign companies have restricted travel by their employees to Egypt and many have evacuated non-essential personnel. The major Western factories seem to be reopening again, but the EU is weighing cutting off economic aid. The Gulf Arabs including the Saudi have turned out to be major supporters of Egypt’s military and have promised to increase financial assistance. Another shipment of LNG arrived in Egypt from Qatar last

week despite Qatar's position as a key backer of Morsi before the coup. Cairo has decided to forego any further talks with Qatar on LNG imports.

The upheavals have resulted in lower Egyptian oil and gas production which in turn has resulted in rolling blackouts. The oil shortage continues, and negotiations with Iraq and Libya have foundered on Cairo's inability to obtain acceptable bank guarantees for shipments. Shell says its offices were temporarily shut last week, but that the company hopes to remain in Egypt.

Texas-based Apache Corp., however, which derives about 27 percent of its revenue from operations in Egypt is considering selling out to avoid what it sees as years of political uncertainty ahead. Although its production is in the Western desert and so far has been unaffected by the problems of the cities, getting a fair price for its Egyptian assets which are worth roughly \$845 million is a major question.

Libya: On Tuesday the National Oil Company issued a force majeure at four major export terminals which cut exports to around 500,000 b/d due to strikes by terminal guards. Over the weekend, the government announced a resumption of shipments from one of the ports raising the country's theoretical export capacity to 590,000 b/d, down from over 1 million b/d before the strikes. The country is currently pumping about 700,000 b/d with the rest closed down due to lack of export capacity.

The shutdown of production has reduced Libya's refining to 150,000 b/d from its installed capacity of 380,000 b/d.

Libya is still so split along political, regional, and tribal lines that the formation of a strong central government seems impossible. Behind the port blockage is the desire of many in Eastern Libya, which contains much of the country's oil reserves, to break away and form an independent country. Getting control of the oil export revenues is the first step in realizing this goal. Given the inability to form a strong central government and the desires for autonomy or more of the oil revenues on the part of many tribal groups, the struggle may just be starting. It could be a long time before Libya's exports return to the pre – civil war level of 1.6 million b/d.

3. Quote of the Week

- "It is my philosophy that it is much better to operate with some level of uncertainty and be generally correct than to operate with dead certainty and be dead wrong."
-- Robert Rapier works in the energy industry and writes about it

4. The Briefs

- **North Sea** oil and gas production could decline by as much as 22 pct. this year - the biggest annual slump on record. Natural decline as reserves in older fields are used up is being exacerbated by increasing time lost to unintended shutdowns following accidents or for maintenance on aging infrastructure. (8/24 #25)
- The sharp decline in **UK** production of oil and gas is "worrying" industry leaders. Trade body Oil and Gas UK says there is record investment this year of £13.5bn. But its annual report on the industry's economic impact highlights the sharp fall in output of 19% during 2011 and 14% in 2012. (8/22 #19)
- **India's** production of crude oil and natural gas fell in July by 2.3 percent and 16 percent respectively. Production was hurt by well shutdowns due to technical issues. It is also hit by smaller-than-expected production from a new well and delays in commissioning some projects. (8/22 #17)
- **Iran** was once the No. 2 oil producer among members of OPEC. It's fallen to the No. 6 spot based on its 2.56 million barrels produced in July. A five-year development plan adopted in 2010 calls for an increase in oil production to 5 million bpd by 2015. (8/20 #7)
- The **Nigerian** government's gross revenue dropped 42 percent month-on-month to \$3.1 billion in July because of disruption to oil production caused by thieves hacking into pipelines. (8/23 #13)

- The US government says over \$1 trillion is required to clean-up the **Niger Delta** area impacted by the ravaging activities of illegal refineries and oil theft and pipeline vandalism. (8/19 #16)
- **Saudi Arabia**, the world's largest oil exporter, shipped less crude in June and exports also slid in fellow OPEC members Iraq, Kuwait and Nigeria, according to official data. The kingdom delivered 7.32 million barrels a day, down from 7.79 million in May. (8/19 #3)
- **Saudi Arabia** is starting to look harder for other fields. They will have increased the number of rigs employed to 170 by the end of the year (in 2005 they had about **20 oil and 10 gas rigs operating**). (8/19 #27)
- French energy services company Technip said Friday it would work on the installation of the world's deepest underwater gas pipeline—at a depth of 9,500 feet---planned for the **Gulf of Mexico** for Shell Offshore Inc.'s Stones field. (8/23 #22)
- By connecting land-locked oil deposits in Alberta and North Dakota with world markets, **TransCanada's** proposed Energy East pipeline and railways will connect those oil flows to world prices, eventually resulting in higher prices. (8/24 #24)
- Higher development costs for **Canadian** LNG export projects could make it more difficult for Canada to compete with lower-costs LNG export plans in the United States. (8/24 #23)
- **British** energy company Cuadrilla Resources confirmed it resumed drilling in the country's southeast region following major protests. (8/23 #26)
- There may be enough natural gas in the **Mediterranean** Sea—more than 40 Tcf in the Levant Basin—for future exports, though timing depends on regional issues, the U.S. Energy Department said. Insecurity in Egypt and Syria, coupled with territorial disputes between Israel and Lebanon, could complicate export plans. (8/22 #6)
- **Argentina's** state-owned energy company YPF said its next shale oil and gas partnership will be with a group including China's Cnooc Ltd. China's biggest offshore energy explorer probably will sign a definitive deal to explore and develop deposits in the Vaca Muerta formation. (8/22 #12)
- In **Mexico**, Pemex will set up a new company to explore and produce shale gas and deep-water oil in the US as part of an ambitious plan by its rookie CEO to turn around years of falling production. The proposal would force Pemex into complicated drilling techniques where it has no experience. It is a bold move for the company which has never faced competition nor ventured far beyond its borders. (8/19 #18)
- In **Ecuador**, environmental groups and indigenous lawmakers threatened over the weekend to take the government to international court over a plan to drill for oil in a protected part of the Amazon rainforest. (8/19 #17)
- For the last two years, world **liquid** energy production has grown significantly and production records have been broken on a monthly basis. However, one can see that "conventional" crude oil is on a slightly downward plateau since 2005...Supply is just one part of the equation. Demand is even harder to predict and highly volatile. Since 2005, global fuel consumption has strongly deviated from nominal levels by almost 10 million barrels per day due to the persistent high price environment and lower economic output. (8/19 #26)
- Unconventional marginal **oil supply** sources have saved the day for now; however, double digit growth in tight oil production could also mean double digit decline. No one knows how long the tight oil boom will last or how it will spread to the rest of the world. Forecasting future production capacity is more uncertain and difficult than ever as we cannot just track a set of tier one giant fields. (8/19 #26)
- The US drilling **rig count** fell 15 units from a week ago to a total of 1,776 rotary rigs working during the week ended Aug. 23. Rigs drilling for oil fell 15 units to reach 1,382, while those targeting gas also declined, falling 1 unit to 387 rigs. Compared with the same week last year, gas rigs were down 99 units, while those drilling for oil were down 26. (8/24 #22)

- The **North Dakota** government said it welcomed the announcement of pipeline and railway expansion projects meant to facilitate the export of crude oil from the state. (8/22 #18)
- The decline rate for oil wells in the **Bakken** formation is ferocious. Therefore they must keep bringing more and more wells on line each month just to keep production stable. If they keep adding wells but at the same rate each month, then production will likely increase but at a declining rate until it stops increasing at all. How long will it be before the mainstream media figures that out? (8/23 #28)
- The story of **oil limits** is one that crosses many disciplines. It is not an easy one to understand. Most of those who are writing about peak oil come from hard sciences such as geology, chemistry, and engineering. (8/20 #23)
- The **US's** biggest oil refinery is largely out of service after several fires over the past two weeks damaged equipment at Motiva Enterprises' plant in Port Arthur (TX). The fires are the latest in a series of mechanical failures at the refinery, which doubled in size last year after a \$10 billion expansion paid for by co-owners Royal Dutch Shell and Saudi Aramco. (8/24 #18)
- Petroleum trade associations in the United State said federal proposals for **regulating hydraulic fracturing** undermine state authorities. (8/24 #20)
- The investigation of an alleged conflict of interest by a U.S. State Department contractor reviewing the proposed **Keystone pipeline** won't be complete until January. (8/24 #21)
- **US fuel consumption** in July reached the highest level for the month in three years, the API said. Total deliveries of petroleum products climbed 1.7 percent from a year earlier to 18.9 million barrels a day. Year-to-date consumption has averaged 18.6 million barrels a day, up 0.6 percent from 2012. (8/24 #16)
- **US** crude oil imports in July dropped to 7.7 million b/d, the lowest level in 17 years, the American Petroleum Institute said. The 7.7 million b/d was a 10.5 percent decline from July 2012. Domestic crude oil production, meanwhile, rose 17.4 percent from July 2012 to 7.5 million bpd. (8/24 #17)
- **U.S. gasoline prices** gained on speculation that unplanned refinery shutdowns and slowdowns will crimp supply as the nation nears the Sept. 2 Labor Day holiday. (8/23 #20)
- The recapture of power generation demand from coal and expectations for an early start to the heating season could prompt a pre-winter rally for **US natural gas** prices by October, BNP Paribas said Friday. (8/19 #21)
- **US railways** carried nearly 20 percent more petroleum and petroleum products in the week ending Aug. 17 than last year. (8/23 #21)
- **Goldman Sachs** has played a leading role in financing the expansion of nearly a dozen specialized railway terminals that can quickly load and unload massive, mile-long trains carrying crude oil and ethanol across the United States. (8/22 #17)
- Hydraulic fracturing operations in **California** represent a clear danger that requires "urgent attention," according to environmental advocate NRDC. Energy companies are using hydraulic fracturing, known also as fracking, to get oil from the state's Monterey shale play. (8/22 #18)
- **China** is expected to surpass the US as the world's largest oil importer by 2017, and the opposing trend of growing crude oil imports by China and falling imports by the US will affect inter-regional trade flows and the cost to both countries, according to consultants Wood Mackenzie. From 2005 to 2020, China's oil imports will rise from 2.5 million b/d to 9.2 million b/d, while US imports will have fallen from a peak of 10.1 million b/d to 6.8 million b/d within the same period. (8/20 #4)
- A gap in US. law has allowed **China** to import nearly \$500 million of additional oil products from Iran this year while avoiding U.S. sanctions, demonstrating Washington's challenge in designing effective measures to target Tehran. (8/22 #3)

- **China's** manufacturing sector picked up steam in August, a further sign of stabilization in the world's second-largest economy that reduces the chances Beijing will shift policy into stimulus mode. (8/22 #13)
- Record temperatures in **China** have boosted energy use. At the peak of the heat earlier in August, power generation was 15 per cent higher than last year. Add to that a drought in the south: previous dry years have added about 3 per cent to coal demand to replace the fall in hydropower. (8/21 #12)
- **China's** renewal of its carbon reduction targets, as well as reports that it is clamping down on coal production, has led analysts to turn bearish on the outlook for coal, claiming that peak demand for the fossil-fuel could be behind us. (8/20 #17)
- **India's** tumbling currency and the possibility of slower growth are adding to the challenges confronting companies in India—just as some multinationals already were having second thoughts about investing. Overburdened infrastructure, serious power shortages, difficulty obtaining land and government red-tape pose significant hurdles for business in India. (8/21 #14)
- The operator of **Japan's** tsunami-hit nuclear power plant sounded the alarm on the gravity of the deepening crisis of containment at the coastal site on Friday, saying that there are more than 200,000 tons of radioactive water in makeshift tanks vulnerable to leaks, with no reliable way to check on them or anywhere to transfer the water. (8/24 #1)
- **Kenya** is set to become East Africa's first oil exporter, after Tullow discovered oil there last year, starting shipments in 2016, overtaking neighboring Uganda, where Tullow found crude more than seven years ago. (8/20 #16)