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1. Oil and the Global Economy

The oil markets were driven by events in the Syrian situation last week. When it became clear on Tuesday that Washington was determined to retaliate for Damascus's use of poison gas against the insurgents and their supporters, oil prices took off out of fears that the fighting would spread and cut oil exports. New York oil futures rose as high as \$112.24 on Wednesday and London touched \$117.34. Later, when it emerged that Washington was having trouble putting together a coalition for an immediate attack, prices fell, closing Friday at \$107.65 in NY and \$113.75 in London. Over the weekend President Obama announced that he would seek congressional approval for the strikes on Syria, leaving the situation hanging until mid-September.

NY gasoline futures fell 10 cents per gallon after crude began to fall, closing at \$2.89 on Friday. With the summer driving season coming to a close next week, demand is expected to fall. Natural gas futures, which have been climbing steadily since early August, fell to a close of \$3.58 per million on Friday on forecasts of cooler weather and an EIA report that power producers are cutting natural gas use due to higher prices.

Concerns are growing that unplanned production and export outages are cutting world oil supplies. The EIA reports that disruptions in August amounted to 2.8 million b/d, up from 2.6 million in July. OPEC outages amounted to 2 million b/d, the highest since January 2011. OPEC's spare oil production capacity is now estimated to be only 2.2 million b/d as compared to an average of 3 million b/d in 2010-2012. In a recent report to Congress, the EIA shows lower output for Libya, Nigeria, Saudi Arabia, Kuwait, the UAE and Iraq. The near total shutdown of Libyan production announced last week will not help the situation.

The IEA reports that sanctions on Iran have increased the shortfall between worldwide supply and demand to 2.2 million b/d in July and August with global production averaging 85 million b/d and consumption 87.2 million. Iran produced 2.57 million b/d in August which was down about 180,000 b/d from in August 2012. Goldman Sachs notes that outages in Libya and Iraq since the start of summer have taken 33 million barrels of oil off the market which, when coupled with a 32 million barrel downwards revision in OECD inventories, completely erases the surplus cushion that was developed during 2008/2009 and that inventories should now be down to 2008 levels. Goldman's reduced their end-of-October OECD inventory forecast by a "significant" 95 million barrels.

Oil production from the North Sea is slipping due to numerous maintenance problems. The UK offshore oil operators now estimate 2013 production at 1.2-1.4 million b/d of oil equivalent, down from 1.53 million last year.

Refinery closures in Europe coupled with the Libyan and North Sea situations has caused a surge in refined products from the US Gulf Coast to Europe. A shortage of tankers is developing and exports have allowed US refiners to maintain prices in the face of weak domestic demand and increasing production of tight oil. The EIA

reports that US crude imports in June were 15 percent lower than last year due to weaker demand and increased domestic production.

2. The Middle East & North Africa

Syria: The situation continues to evolve into an ever-growing mess. When a by-now-routine poison gas attack on an insurgent-held neighborhood two weeks ago got out of hand and gassed some 3000 sleeping inhabitants, killing 1500, Washington decided it was time to retaliate. Across the globe perceptions of the event varied widely with nearly all condemning the use of gas, a few Assad supporters saying the attack was really an insurgent provocation, and most not wanting a wider war no matter what the Assad government does.

The gradual radicalization of the Syrian insurgency has led many to believe that the current situation may be better than one without Assad, hence the US attack, should it ever occur, will be carefully focused to teach the Assad government, and anyone else who might see advantage in shooting poison gas at an opponent in the future that the US will make the price unacceptably high. At the same time, the US retaliatory attack is to be so nuanced that it will not blow the Assad government to pieces, as happened in Libya, and allow Jihadist forces to take over Damascus.

Opinions as to whether a nuanced attack to deter future use of poison gas is a good idea is all over the board, with the British Parliament voting No, the French voting Yes, Israel thinking it a grand idea, and the Arab League wanting the UN involved first. The ball is now in the US Congress' court.

The key issue is whether a US strike on Syria will provoke a wider war that that will impact regional oil exports. Tehran, Moscow, Damascus, and Hezbollah are suggesting that a wider war will ensue, along with the destruction of Israel, and the kidnapping or murder of any Americans or allied westerners they can get their hands on. Most observers do not expect much of a retaliation. Hezbollah and Syria are in no position to take on the US and Europe, and the new Iranian government seems bent on negotiating itself out of the sanctions which are slowly destroying its economy. The longer run is simply too complex to foresee.

Iraq: The UN reports that some 800 people, mostly civilians, were killed in a wave of shootings and bombings across Iraq in August. It is interesting that the endless bombings, mostly of Shiites by Sunnis, seems to have provoked so little response and that the much-discussed Iraqi civil war is nowhere in sight. Most of the bombings are against soft civilian targets rather than well-guarded government installations or foreigners. Large demonstrations across the country on Saturday were protesting the large salaries and lavish benefits received by lawmakers rather than the security situation.

The northern export pipeline is reported back in operation after having been blown up 31 times this year. The most recent triple bombing dumped a large quantity of oil into the Tigris River forcing the closure of several water intake facilities north of Baghdad.

Iraq is planning to reduce exports via the Basrah Oil Terminal by at least 250,000 b/d starting this week due to construction work. The IEA said last month that it expects exports to fall by about 500,000 b/d during the work. The plans call for one of the two floating Single Point Moorings to be shut for between 30 and 45 days so that work can proceed on connecting a newly installed metering and manifold platform. Projects in Iraq, however, usually take longer than planned.

The Oil Ministry has written Shell blaming it for the slow pace of work on the Majnoon Oilfield. The Ministry claims that "aggregated losses of production" now total 44 million barrels, costing the country \$4 billion in lost revenue.

Libya: Last week the terminal strikes that have been going on in Central and Eastern Libya spread to the Western oil terminals, reducing oil production to the neighborhood of 150,000 b/d from the theoretical capacity of 1.6 million. Refineries have already closed and the country faces a fuel and power shortage unless

the situation can be rectified soon. The new shutdowns were perpetrated by armed militiamen who closed the pipeline running from the desert oilfields to the coast.

The situation has been deteriorating since the fall of Gadhafi in 2011, as the new central government in Tripoli never was able to establish control over the country. Gadhafi left behind vast quantities of military equipment that has fallen into the hands of tribal groups who are now well-armed in comparison to the central government which simply does not have the forces to regain control of the oil infrastructure.

Libya is an ersatz state that was cobbled together from various tribal regions by the Italians in the 1930s. The tribes say that the \$60 billion in annual oil revenue is being stolen by corrupt central government officials and is not resulting in any benefits for the people. The regions are looking for more autonomy, less corruption, and sharing of the oil wealth.

Tripoli is resorting to negotiations to reestablish oil production and exports, but so far the situation is only getting worse. The country needs to export 400,000 b/d to pay the civil service and the national treasury will be empty by the end of the year. The only hope seems to be that when the lights go out and the gas stations run dry, some sort of compromise can be worked out. In the meantime, world oil production is down by another million b/d and the Saudis are already pumping close to capacity.

Egypt: By recent standards it was a relatively quiet week. With much of the Muslim Brotherhood's leadership in jail, last week's protest marches amounted to little. The government says it foiled a machine gun attack on a container ship that was passing through the canal on Saturday. Three men were arrested. This would be the first reported attempt to block the canal since the recent troubles began.

The army has deported three Al Jazeera journalists after the Qatari-owned channel carried appeals from the Muslim Brotherhood to stage protests against the new government.

The new government is drawing up a timetable for paying the several billion dollars it owes to foreign oil companies which have been accumulating for years. Cairo hopes the move will encourage the companies to increase exploration. US-based Apache Corps sold a 33 percent stake in its Egyptian oil operations to Sinopec for \$3.1 billion. Although Apache's drilling and production operations in remote desert regions have not been interrupted, the company is worried about Egypt's long-term stability. The Chinese, however, are willing to run bigger risks in order to obtain the oil necessary to keep their economy growing at 7 percent a year.

Iran: The current Syrian chemical weapons crisis is the first real test of Iran's new President who has vowed to patch things up with the West in order to get the oil sanctions lifted. Iran and the UN nuclear agency have agreed to restart talks focused on the Agency's efforts to probe allegations that Tehran is attempting to build nuclear weapons.

As a victim of Iraqi chemical attacks during their war, Tehran decries the use of chemical weapons in general without blaming its long-time ally Syria directly. Beyond the ritual threats and denunciations of the US for any action against Syria, Tehran seems to be saying that a mild military slap at Damascus in response to its use of chemical weapons would be acceptable. However, should the US attempt to destroy the current balance of forces in the country by significantly degrading the Assad's military capabilities, then Tehran would have to take action.

3. Quote of the Week

- [About the pending closure of The Oil Drum website] “It should be noted just how good the site was, especially by those of us in the ‘MSM’ who have read, quoted from and linked to TOD over the years (the latter includes at least half of current and former FT Alphaville staff). You could assume that any topic raised there would be examined in some detail, and thoroughly and knowledgeably interrogated in the comments. TOD editors have written FT opeds and in academic journals. The site was, by any measure involving quality of information and discussion, a huge success.

-- By *The Financial Times* blog

4. The Briefs

- **World consumption** of petroleum products reached a record high of 88.9 million b/d in 2012, as declining consumption in North America and Europe was more than outpaced by growth in Asia and other regions, according to a recent study by the US EIA. (8/28 #5)
- **Russia** on Wednesday ordered a cut in oil supplies to Belarus and questioned the health standards of dairy imports, opening a new front in a trade and diplomatic spat after its ex-Soviet neighbor arrested the chief executive of Russian potash producer Uralkali . (8/29 #20)
- A unified **Russian-Saudi** strategy on global oil supply and price? More details of a meeting at the end of July between Russian President Vladimir Putin and Saudi intelligence chief Prince Bandar bin Sultan have emerged, with the Saudi prince reportedly having suggested the two sides come up with such a strategy. (8/27 #7)
- The news that **Saudi Arabia** is planning to employ 200 drilling rigs next year (up from 20 back in 2005) suggests that there is a recognition that future reserves may not measure up to the planned volumes needed. (8/26 #18)
- From 2005 to 2020, **China's oil imports** will rise from 2.5 million b/d to 9.2 million, according to Woods Mackenzie researchers. U.S. imports will fall from a peak of 10.1 million to 6.8 million b/d within the same period. That roughly represents a 360% increase in China's crude oil imports and a 32% decline for the U.S. during that period. (8/26 #11)
- **Statoil** said it discovered oil in the Flemish Pass Basin off the coast of Newfoundland. The discovery was made in the Bay du Nord prospect and is the second such discovery so far this year. (8/29 #17)
- India's Reliance Industries is considering expanding its presence in **Venezuela** with potential participation in more projects. Venezuela is looking for Reliance's collaboration on the construction of the \$10 billion Cabruta refinery and other oil infrastructure projects. (8/28 #14)
- One year after **Venezuela's** deadliest refinery accident, officials say they are certain that the explosion at Amuay that killed at least 42 people and resulted in more than \$2 billion in damages was the product of sabotage against the South American country's leftist government. (8/27 #10)
- Total US petroleum deliveries averaged 18.9 million b/d last month, up 1.7% from year-ago levels and hitting a 3-year high, according to API's monthly statistics. (8/27 #15).
- **US** June crude oil imports fell 15.1 percent from a year earlier amid rising domestic oil output, EIA data show, though imports were little changed from May. The drop in imports came as US oil output climbed 15.2 percent from a year earlier, to 7.20 million b/d. (8/30 #19)

- Crude oil production in **Texas** has increased 16 percent during the first six months of 2013 over the same period in 2012, creating an economic tidal wave throughout Texas. (8/26 #16)
- Dennis Coyne predicts that **shale oil production** from the Bakken will peak in late 2016 or early 2017 at just over one million barrels per day and that Eagle Ford will peak in mid 2015 at just over 1.2 million barrels per day. (8/28 #23)
- A recent wave of small **earthquakes** in and around the Eagle Ford formation in Texas was probably the result of extracting oil and in some cases water used for hydraulic fracturing, according to a study the University of Texas' Institute for Geophysics. (8/28 #19)
- In 2010 and 2011, the farming town of Greenbrier, Arkansas, was rattled by more than 1,000 **minor earthquakes**, the largest hitting 4.7 on the Richter scale. Then came another surprise: University of Memphis and Arkansas Geological Survey scientists said the quakes were likely triggered by the disposal of fracking wastewater into deep, underground wells. (8/27 #18)
- More **US crude oil** is moving around on trucks, barges and trains than at any point since the government began keeping records in 1981, as the energy industry devises ways to get around a pipeline-capacity shortage to take petroleum from new wells to refineries. (8/26 #15)
- The head of a **US rail safety** group compared a widely used oil tank car to the recalled Ford Pinto in urging regulators to require upgrades that would prevent railroad accidents like a Quebec derailment that killed 47 people. (8/29 #16)
- Europe's utilities are replenishing **natural gas reserves** at the fastest pace on record, risking a surge in prices as the region's winter heating season looms. Inventories in eight European countries were 14 percentage points below the year-earlier level on Aug. 26. (8/29 #18)
- **Iran** said it was frustrated with the pace at which China National Petroleum Corp. was working on Phase II of the South Pars gas complex and replaced it with domestic firm Petropars Ltd. CNPC took over in 2009 at South Pars after French energy company Total and its Malaysian counterpart Petronas failed to live up to the terms of their contractual obligations for development. (8/28 #7)
- A green advocacy group said the Dutch government should be mindful of protests in Great Britain as it gives its consent to shale **natural gas** development. Dutch Minister for Economic Affairs Henk Kamp told the Dutch Parliament risks associated from hydraulic fracturing, or fracking, campaigns in shale natural gas formations could be overcome. (8/28 #22)
- **US natural gas** production during June in the Lower 48 states appears to have set a record. Figures from the EIA show estimated June gas output averaged 73.62 billion cubic feet a day. That figure would top the November 2012 revised figure of 73.54 bcf/day. (8/31 #14)
- **Natural-gas use** by the US power-generating sector fell 16.9% in June from a year earlier, amid a 52% rise in prices. (8/31 #15)
- August is about to end without an **Atlantic hurricane** for the first time since 2002, calling into question predictions of a more active storm season than normal. (8/31 #18)
- The closing of the Vermont **Yankee nuclear plant** could be indicative of more shutdowns to come, experts say. It is the fifth such announcement in the nation's nuclear energy sector this year. San Onofre's two reactors in California, Kewaunee in Wisconsin and Crystal River 3 in Florida are also being retired. (8/31 #19)
- Japan's **Fukushima** Daiichi nuclear facility made headlines again this week, when some 305 tons of radioactive water leaked from a storage tank at the complex. This prompted Japan's Nuclear

Regulation Authority to upgrade the situation from 1 to 3 - a "serious accident" on the 8-point International Nuclear Event Scale. (8/26 #13)

- The Japanese government will provide money and personnel to help cope with the ever increasing amount of contaminated water at the **Fukushima** nuclear power plant after losing confidence in Tokyo Electric Power Co.'s ability to handle the situation by itself. (8/27 #14)
- **China's** environmental watchdog has suspended approvals for new oil-refining projects after two of the country's largest refiners missed pollution targets last year. (8/29 #15)
- The worsening Syria conflict has exposed an uncomfortable truth behind **China's** cherished policy of non-interference: Beijing cannot do much to influence events even if it wanted to. With weak and untested military forces unable to project power in the Middle East, China can only play a low-key role in a region that is crucial for its energy security. (8/28 #17)
- Mohammad Javad Zarif, one of **Iran's** most accomplished diplomats is the country's new foreign minister and seems virtually certain to lead Iran's delegation in nuclear negotiations with the West - further indications, analysts say, that Mr. Rouhani is serious about reducing tensions with the United States and other Western countries. (8/27 #6)
- **China's economy** is showing clear signs of stabilization, helped by policy support and some improvement in global demand, and is on track to meet the government's 2013 growth target of 7.5 percent, the state statistics bureau said on Monday. (8/26 #10)
- **India** is making progress with Iran in resolving a dispute over an Indian oil tanker that was detained by Iranian naval authorities more than two weeks ago. Iran detained the ship carrying crude oil from Iraq to India on Aug. 13, saying it was polluting Iranian waters. (8/31 #9)
- **India's battered rupee** was on track for its worst one-day fall in more than two decades on Wednesday, plunging 3.4 per cent in morning trading to breach Rs68 to the US dollar for the first time in a downbeat reaction to a government plan to rescue the floundering economy. (8/28 #15)
- A brewing scandal over missing government files related to coal mining blocs allocation is unsettling **India's** government. In an effort to defuse the situation, the Indian government is preparing to give an explanation about the furor, dubbed "Coalgate" by the media, to the Supreme Court. (8/28 #16)