Peak Oil Review

Tom Whipple, Editor
Sharon Astyk, Commentary Editor

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1. Oil and the Global Economy

A perfect storm of bad economic news, increasing inventories, falling sales, and a relatively quiescent Middle East assembled last week to send oil prices down $8 a barrel. By Friday's close NY oil was down from $106 to $98 a barrel and London was down to $113 after falling below $112. Gasoline futures in NY at one point were trading below $2.95 a gallon after having been above $3.50 in late March. As could be expected technical factors contributed to the precipitous drop as various support areas were taken out.

The major impetus for the decline on Thursday and Friday was a weak US jobs report coupled with increasing economic and political problems across the EU. Signs of slower economic growth in China did not help the situation.

MasterCard reports that US gasoline consumption fell the week before last for the 35th consecutive week and was down 5.6 percent from a year earlier. Gasoline prices continue to fall across the US with the average for regular now at $3.78 – down from $3.93 a month ago.

Much attention is focusing on the effects of the reversal of the Seaway pipeline which will soon be draining away part of the oil glut at Cushing Okla. to Gulf Coast refineries. Initial capacity will be about 150,000 b/d, but plans are underway to increase this to 850,000 b/d by mid-2014. This pipeline should over time reduce the price spread between NY and London oil prices, allowing US and Canadian producers to receive higher, or at least "world", prices for their product.

US natural gas futures spent most of the week trading in the vicinity of $2.30 per million BTU's, up from $1.90 in mid-April. The increase was sparked by a government report showing a small drop in US production in February. Drilling for gas-only now is down by 30 percent from last year. The EIA reported that residential gas use in February hit a 22-year low of 23 billion cu. ft. per day. There has been a considerable shift towards using natural gas in place of coal among power producers—US coal production is down 13 percent from last year. Most analysts, however, believe that US natural gas storage facilities will reach capacity before next winter resulting in another price drop.

For the next few months, oil prices are likely to hinge on the course of the Iranian nuclear negotiations and the oil sanctions which continue to tighten. For now, much of the "crisis premium" seems to be out of oil prices and considering that major speculators are reported to be long oil, we could see further price drops as the markets sort themselves out.

2. The Iranian Confrontation

With only two weeks to go before resumption of the talks over Iran's nuclear program, optimism that some sort of deal can be struck seems to be increasing. Washington and Tehran are saying the chances of war have significantly decreased. In Israel, a backlash seems to be developing against

Prime Minister Netanyahu and Defense Barak's threats and deadlines as a variety of current and former Israeli politicians have been saying that an Israeli strike on Iranian nuclear facilities is a bad idea so long as talks are continuing. The fall in oil prices over the past month partly represents a market consensus that for the time being, the threat that Middle Eastern oil exports could be blocked seems to be subsiding.

As the July 1st deadline for many aspects of the West's sanctions program to come into effect approaches, it is beginning to appear that they will have a significant impact on Tehran's economy. Most major importers of Iranian crude appear to be making some sort of cutback in face of the secondary Western sanctions. Although there has been no public announcement, even Beijing that clearly does not want to see hostilities in the Gulf may be adding to the pressure. With such a wide range of sanctions coming into effect, Tehran, which has a fairly modern economy and relies heavily on foreign investment and imports, would be in considerable trouble if the sanctions were to become a protracted affair.

The recent decline in oil prices, the likely slowing of demand in the US and EU, and increases in OPEC oil production have removed some of the fear that the sanctions will lead to much higher prices and even shortages later this year.

Despite all the optimism, some remained concerned that we are only experiencing a lull between meetings and that there are tough negotiations ahead. For the West, lifting sanctions and supplying medical isotopes to Tehran is not a problem. The Iranians, however, opening their nuclear and suspect military facilities to IAEA inspectors will require a major change in thinking. The Israelis, whose threats of unilateral strikes on Iran is a major driving force in the negotiations, may have to live with well-inspected underground Iranian nuclear facilities and allow Tehran to maintain face in order to gain a settlement.

A key sidelight to the negotiations is the Syrian uprising, where the Russians and Iranians are doing their best to maintain the Assad government in power as the rest of the world becomes more outraged over the indiscriminant killing. Should there be outside military intervention in Syria, the nuclear talks with Iran could be affected. For now things are looking up, but this could be reversed rather quickly.

3. The EU's spreading crisis

It was a rough week in Europe starting with the declaration that Spain was now in a recession on Monday, and finishing with the ouster of French President Sarkozy and the ruling Greek coalition on Sunday. Spain joins Belgium, The Czech Republic, Denmark, Greece, Ireland, Italy, The Netherlands, Portugal, Slovenia, and the UK in recession.

With the emergence of Europe's sovereign debt crisis two years ago, the generally accepted solution has been austerity with major spending cuts, mostly in social services, being implemented in most countries. With the economic situation worsening and no end to budget cuts in sight, Europe's voters are demanding an end to austerity and the development of policies that hopefully will foster growth.

In the case of France, the new socialist President, Hollande, says he will move immediately to implement reforms. Hollande's election calls into question the French-German partnership that has basically determined the Eurozone's response to the debt crisis. The Greek election which seems to have resulted in a situation where the formation of even a coalition government is impossible makes it likely that Greece will reject the bailout terms accepted by the previous government and will have to default on its debts.

A combination of recession, coupled with widespread voter rejection of austerity measures, suggests a period of troubles ahead leading to a deeper recession including the likelihood that there will be defaults on sovereign debt and the failure of some European financial institutions. How far all this

goes is still an open question. It does not take much to predict that the EU's troubles could spread far wider.

The price of oil is clearly involved in all this. First, it is likely that persistent high oil prices over the last two years have taken a toll on the economies of most European countries – and across much of the OECD for that matter. For the immediate future, we have the question of what growing economic problems will do for the demand for oil and its price. Four years ago prices fell by over $100 a barrel in six months cutting high-cost deep-water, tar-sands, and tight oil production significantly. Whether we are in for a repeat of this situation in the next year is something that bears watching.

Quote of the week

- "We must adjust to the fact that our own civilization has reached limits with regard to population, water, soil, raw materials, and energy. In the end, our adaptation will require as much social innovation as technological change, as we learn to live with less, and to live more equitably."

  - Richard Heinberg

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

- **Libya's** Arabian Gulf Oil Company has cut oil production by another 10,000 b/d due to protests that have closed off its headquarters for nearly two weeks. (5/5, #8)
- **Shell** said it had declared force majeure on Nigerian Bonny Light crude oil production due to oil theft and that 60,000 barrels per day of oil had been shut down. (5/5, #10)
- **Spain's** Repsol may halt the delivery of nine ships carrying LNG to Argentina in retaliation for the South American government's pending nationalization of its YPF unit. (5/4, #13) (5/5, #11)
- Amid concerns that a new Middle East war is looming, Israeli Prime Minister Binyamin Netanyahu has approved a special budget to fortify and protect **Israel'**s rich natural gas fields in the eastern Mediterranean. (5/5, #6)
- Japanese and Russian officials are exploring the possibility of building a **natural gas pipeline** to ensure Japan's energy security. They also discussed shipping liquefied natural gas from the Sakhalin plant on the east coast of Russia.. (5/5, #14)
- **Japan** is switching off its last working nuclear reactor. The third reactor at the Tomari plant, in Hokkaido prefecture, is shutting down for routine maintenance. It leaves Japan without energy from atomic power for the first time for more than 40 years. (5/4, #16) (5/5, #15)
- The Fukushima crisis is eroding years of Japanese efforts to reduce **greenhouse gas** emissions blamed for global warming, as power plants running on oil and natural gas fill the electricity gap left by now-shuttered nuclear reactors. (5/4, #18)
- Vermont's legislature moved to ban hydraulic **fracturing**, passing on a 103-36 vote the latest iteration of a bill that now goes to Governor Peter Shumlin, a Democrat, who is expected to sign it. (5/5, #20)
- **Nigeria** plans to increase crude oil production to 4 million barrels per day by 2020. In addition, the East African country also plans to boost liquified gas production by an additional 20 million metric tons a year from the present 26 million tons. (4/30, #17) (5/1, #13)
- The 3 Battalion of Nigerian Army destroyed over **600 illegal refineries** in a Nigerian village and neighboring waterways. The commander of operations, described those behind the illicit trade as economic saboteurs. (5/4, #11)

- The Obama administration will soon issue sweeping new **environmental-safety rules** for hydraulic fracturing on federal land, setting a new standard that natural-gas wells on all lands eventually could follow. (5/4, #19)
- **US coal production** in the week ended Saturday totaled about 17.9 million st, 12.9% below that of the comparable week of 2011 and 0.5% lower than that in the week ended April 21. (5/4, #21)
- Eight global automakers will demonstrate a harmonized **single-port DC-fast charging technology** at the upcoming EVS26 event in Los Angeles. The system is intended to accelerate more affordable deployment of electrified vehicles and fast charging infrastructure. (5/4, ##26)
- **World energy demand** should grow 25% by 2030, mostly supported by the needs of emerging markets, French oil major Total'sChief Executive Christophe de Margerie said. (5/3, #4)
- The tight oil boom is fuelling a rise in the **burning of waste gas** after years of decline, a World Bank source told Reuters ahead of the release of new data. Global gas flaring crept up by 4.5 percent in 2011, the first rise since 2008 and equivalent to the annual gas use of Denmark. (5/3, #6)
- **Low natural gas prices** in the US mean the fuel is likely to gain significant market share in transport, said Mark Williams, the Downstream Director of Shell. (5/3, #18)
- Energy-producing states are bracing for lower tax revenue from the plummeting price of **natural gas**, which is just above half of what some states forecast when they put together budgets for 2013 and beyond. (5/3, #19)
- President Evo Morales has announced that his government is completing the nationalization of **Bolivia's** electricity sector by seizing control of its main power grid from a Spanish-owned company. (5/2, #7)
- A **10-year research plan** outlined by the White House will focus on how human economic activity influences climate change, the administration said. The White House said it formalized a 10-year strategic plan for the U.S. Global Change Research Program. (5/2, #11)
- **Chesapeake Energy Corp.** will name an independent chairman to replace Aubrey McClendon and halt an incentive program that allowed the chief executive officer to amass personal stakes in thousands of company-operated wells. (5/2, #12)
- **Phillips 66**, the refining company spun out from ConocoPhillips, plans to double its fuel exports from the US in the next two years as oil production surges but gasoline demand declines. (5/2, #16)
- **OPEC output** in April has hit its highest since 2008 as extra crude from Iraq, Saudi Arabia and Libya more than compensates for the lowest Iranian supply in two decades ahead of an EU embargo. (5/1, #5)
- **ConocoPhillips** agreed to pay around $297 million to compensate for an oil spill in Bohai Bay China last year. ConocoPhillips's China subsidiary spilled around 700 barrels of oil in their Penglai oilfield, the country's biggest offshore oilfield which it operates in a concession with government owned CNOOC. (5/1, #17)
- Pipeline operators in the US are capable of handling the rush of **tar sands oil** expected from Canada, a trade group leader said. The Sierra Club said the US will import more than 1.5 million barrels of tar sands oil from Canada by 2020, a 10 percent increase over current levels. (5/1, #24)

- US electric utilities are renegotiating **coal contracts** and finding other ways to reduce coal deliveries as a mild winter and competition from less-expensive natural gas combine to weaken demand for power plants' longtime staple fuel. (5/1, #25)
- **Venezuela** will construct three oil refineries in China, the state-run Venezuelan oil company PDVSA said. (4/30, #18)
- **China** invested a total of $222 million in the domestic shale gas sector last year. (4/30, #19)
- US imports of what environmentalists are calling **"dirty oil"** are set to triple over the next decade, raising concerns over the environmental impact of extracting it and whether pipelines can safely transport this Canadian oil. (4/30, #22)
- **TransCanada Corp.** is "actively" pursuing a way to ship oil rather than natural gas along a key west-east pipeline network, as prices for the Alberta oil fetch low profits in the US. (4/30, #23)