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Energy Shock: What Happened to Over-Priced Oil?

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Until recently, Oil giants have been used to record profits – which means that industry experts, nonproductive middle men like Goldman Sachs, and hungry shareholders in the 21st century, now believe their business is 'no longer viable' under $100 per barrel.

The reality: there is an over-supply of oil on the market. For many of the top economies, oil demand has been decreasing. Developed nations have increased energy efficiency and energy sources have diversified. Shale gas has also disrupted the old mix.

With petrol/gasoline prices are down, in the US as low as $2.70 gallon this week – you can see a smile back on the faces of working class Americans, *for now.* On the other hand, for big oil producing countries and their governments, this drop in price not so great – revenues are down and that's causing major strain which will lead to cuts in domestic spending in the short term.

Has the shale gas 'Fracking' revolution is bankrupting the oil industry – or is gas production in the US really a financial bubble, destined to *deflate*?

High on High Priced Oil

Royal Dutch Shell's new chairman Chad Hallyday says that falling oil prices are the top of his agenda and like other "historic majors", oil giants such as ConocoPhillips and ENI, Shell – will reap painful bottom line hits from new lower prices.

Reported by the *Financial Times*, October 31, Hallyday says that each $10 fall in the barrel price means $3 billion less earnings a year and a prolonged period of Brent prices around $85 a barrel would translate to $8 bn-a-year of reduced profits for Shell. Nevertheless Hallyday is not only a former *Bank of America* chief, but also co-chaired the UN's high level group on sustainable energy, which in 2011 pledged a doubling of renewable energy in world energy by 2030.

On its current energy output, this would rather heavily crimp Shell's earnings. But that is only a first-cut analysis.

Shell's "Dash for Gas" strategy dating from around 1998 was originally defended as more sustainable and less harmful to the climate than producing oil and coal.

Corporate investment in gas was ramped up to the mid-decade, but the start of the US shale gas boom from 2009 exposed the company to continuing high investment needs in expanding gas output but unexpected falls in US domestic gas prices. Like several other majors such as BP, its attempted and related "Go for Green" renewable energy investment strategy in the early years of the decade was a low performer, and despite Chad Hallyday's long term relations with the World Wildlife Fund, Shell may take quite some time to renew its attempts to promote and sell "renewable energy".

The bottom line is that bridging to the renewables needs high-cost bridge building based on high prices for fossil fuels and high corporate earnings. With world coal prices almost inevitably set to stay low and with US natural gas prices always struggling to reach and hold $4 per million BTU($23.20 a barrel equivalent), capped by repeated and record-sized world gas finds since 2009 feeding output which is likely to seriously dent current non-US gas prices, this could be a bridge too far. Shell's leading role in 'GTL', or gas to liquids conversion to oil-substitute fuels and chemicals has never been a major revenue earner, and can only break even where gas prices are extreme-low.

Until mid-year 2014, paying for the party was backstopped by the extreme high price of oil. This was the missing link and magic solution, able to bolster corporate earnings and pay for past errors – as well as finance futurist dreams of "totally eliminating fossil fuels" from the energy mix However, as the 2008-2009 oil price crash proved, it is not only Saudi Arabia which decides when oil prices will slump – energy demand in a context of financial markets in free fall is another factor. Combined with ultra low growth rates of oil demand and a Middle Eastern geopolitical context where ISIS does not (presently) threaten oil production, but steals oil and sells it at $33 – $40 a barrel, and increasingly independent Kurdistan sells its oil at $50 a barrel, the life expectancy of overpriced oil is short.

Carbon Capture and the Climate Cult

The UN's efforts to relaunch the bugaboo of runaway global warming and its supposed link with human CO2 emissions, which is curiously always cranked up in wintertime has however this time set up the summertime 1915 Paris climate change summit as the Big One.

We will have to hope for the 'Carbon Correct' cult-community and their slavish media outlets (like the UK's BBC *still* showing us polar bears wading in thin ice) to acknowledge that Paris in July is *always* nice and hot! Agenda items will certainly include moving carbon capture and sequestration to worldwide conventional status, for which British print and TV news media has given outline cost figures of about or around $200 per household (125 pounds) per year as the additional cost of household electricity if all power plant emissions were captured and sequestered.

This $5 bn-a-year hike of electricity prices would be a "reasonable price to pay" according to UK academic 'Carbon Capture and Storage' (CCS) experts like professor Stuart Haszeldine.

However this expert, like others is forced to admit that currently operational CCS installations not also providing gas for EOR-enhanced oil recovery through reinjection into depleting oil wells are very few and far between. Imagining they could be "ramped up" to handle all power plant emissions, even in small densely-populated countries like England, by 2030, is stretching the imagination.

The IPCC – which the media claims is the "UN's climate protection agency" despite having no formal UN status – has been stretching its imagination and our ability to believe in this technology pipe dream for years, and on the basis of learn nothing-forget nothing is still whining about it today – despite the scientifically controversial status, as well as extreme high cost of any national large scale CCS strategy. The US

National Academy of Sciences in two separate 2012 studies by different researchers concluded that CCS is viable "despite its very high cost" and also published data on the earthquake-provoking risks of widespread CCS.

In its March 2013 report 'Decommissioning in the North Sea' the UK Royal Academy of Engineering gave considerable attention to CCS as an alternative for decommissioning and removal of North Sea oil and gas installations, forecast by the Academy to cost around $50 bn (£35 pounds) to 2030 unless alternate uses for non-performing and obsolete oil-gas equipment can be found. The Academy's workshop report was, however, forced to admit that the current experimental, small scale and high cost examples of "pure CCS" not used for EOR concern, were at most, only a few million tons of CO2 per year.

World total human CO2 emissions, including emissions from mining, transport, industry and agriculture are about 30 billion tons per year. Also reported by the Academy, the abandonment costs of CCS when injected aquifers or basalt formations, or other storage media become saturated, will be similar or possibly higher than for abandoned oil-gas installations.

Saudi: ‘We’re not bothered’

According to professor Jim Krane, from Rice University, Saudi Arabia may have a big hand in the current oil price parlor game.

“If you’re somebody who looks at geopolitics and energy, you could come up with any number of ways or any number of reasons why the Saudis are not doing what they would usually do”.

“There [are] lots of good reasons for them to keep on producing, but exactly why they’re doing it, probably only a few dozen people in Saudi Arabia know that,” he adds. NPR also explains here:

“One popular conspiracy theory is that Saudi Arabia is trying to deprive Russia of valuable oil revenues because of its support of Bashar Assad’s regime in Syria. Saudi Arabia is opposed to Assad. Another target is its arch-rival in the region, Iran. Bronson says the low oil prices are hurting Russia and Iran, both of which depend heavily on oil exports and require higher prices than Saudi Arabia does to meet all their domestic needs.”

‘Paying for the Party‘

Falling oil prices not only threaten the national budgets of almost any major (and several minor) oil producer and exporters, from Russia and Venezuela – to Malaysia and Argentina, but also oil producing regions and states within federal republics. Note that almost half of Russia’s state*revenues* are from oil and gas – and they are feeling that pain.

Back in in 1987, with WTI-West Texas Intermediate oil trading at less than $20 a barrel, after reaching nearly $40 a barrel before in 1986, Texan lawmakers faced one of the worst budget shortfalls in the state’s history. They ultimately slashed spending and approved more than $5 billion-a-year in *new taxes*. At that time, oil and gas production taxes made up close to a quarter of all Texas tax revenue, making the state’s budget especially vulnerable to oil price volatility.

The “hidden consensus” since at latest the 2005-2007 period is that high oil prices are normal as long as world and regional GDP growth is positive. Rationales for this extend far and wide from budget balancing for free-spending governments, even of oil importer countries where fuel and energy taxation is a major contributor to state spending. Paying for the pipedream of CCS, and decommissioning obsolete oil-gas installations, as well as paying for a forced march transition to renewable energy can be added to the list. In the case of Shell and other “historic majors” their own transition away from the upstream, and their uncertain dabbling in renewable energy are other high-cost ventures needing the solid basis of extreme high oil prices to pay for the party.

As we are finding in recent months – there is no rational energy-economic basis for triple-digit oil prices, and the major problem is forecasting how far oil prices can fall, to a now high cost break-even threshold for an increasing number of producers, in the $75 a barrel region.

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