



# PEAK OIL REVIEW

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### **1. Oil and the Global Economy**

The gradual price increases which took oil up some \$4-5 a barrel in the last two weeks ended on Friday when budget negotiations in Washington broke down. This news sent prices down \$1.20-\$1.40 a barrel to settle at \$88.66 in NY and \$108.97 in London. Despite somewhat better economic news in the US and shrinking diesel and gasoline inventories in the Northeast, fears that major tax increases and federal spending cuts will kick in on January 1<sup>st</sup> have traders nervous. It is widely believed that without agreement in Washington, higher taxes and less spending will trigger off a new recession that will cut demand for oil.

The weekly inventory report showed lower crude and distillate inventories especially along the Gulf coast. Several states in the area levy an inventory tax on oil stock which encourages refiners to keep inventories as low as feasible at year end. US distillate exports to Europe have been running at a million b/d of late further adding to the tight distillate situation.

Natural gas futures rose during the past week on the prospect for colder weather and a larger than expected drop in inventories. After having traded below \$3.30 per million BTU's the week before last, natural gas closed on Friday at \$3.46.

Last week's US drilling rig count came in as something of a surprise. Rigs drilling for oil dropped by 41 during the week to 1340, the lowest level since April. This was the fifth straight weekly decline and the largest one-week drop in the last 20 years. Texas was down 18 rigs to 830 while North Dakota remained the same at 174. The oil-drilling rig count declined in the last quarter for the first time since 2009 due to more efficient drilling operations producing adequate supplies of oil and oil prices which in some cases may be approaching costs of production.

Elsewhere in the world, the European situation remains about the same with the continent slowly slipping into recession, although German business confidence has had a rebound. Italy's Prime Minister has resigned and Greece muddles along with the austerity-wrought hardships growing. In the East, the Japanese election returned the conservative Liberal Democratic Party to power in a landslide on the promise to return economic

growth after 20 years. China's new leaders are promising reforms that will reduce dependence on exports and spend more to get the economy growing at more normal rates.

## **2. The Middle East**

The Syrian situation grows worse as the fighting continues. Some 400,000 refugees are now living in bordering countries and millions more are without adequate food and shelter. The Free Syrian Army continues to make slow progress against government forces and has succeeded in closing the main airports. During the week the rebels attempted to occupy the district of Damascus occupied by the descendants of the Palestinians who emigrated from the new state of Israel in 1948. As this district is only two miles from the center of Damascus, the government reacted strongly by bombing the district, thereby alienating the Palestinians who had remained largely neutral and forcing many to flee the city. The government continues to fire long range scud-type missiles and drop cluster bombs against civilian targets.

Moscow has distanced itself from the Assad government, but refuses to become involved in any effort to pressure Assad to step down. Indeed some now fear that if Assad were to disappear too quickly chaos would reign.

There are some 50,000 Russians or citizens of the former Soviet Union resident in Syria from the decades when Syria was Moscow's best friend in the Middle East. These current or former Soviet/Russian citizens seem to be in increasing danger from rebels who are outraged at the support Moscow has given Assad during the last two years. The Russian Foreign Minister told reporters that Syria was making an effort to concentrate its large stockpile of chemical weapons in one or two locations where they would be safer from falling into the hands of extremist groups. The Israelis have backed this statement saying that for now they are not concerned about the security of Syria's chemical weapons.

Moscow is trying to portray the situation as a stalemate with Assad holding out for an indefinite period, followed by years of chaos as the various insurgent groups battle each other along religious and ethnic lines. However, how much longer Assad can hold out is problematic. Syria's Alawite elite is already decamping for the relative safety of the mountains and the coastal city of Tartus where Moscow for the last 40 years has maintained a small naval maintenance facility. Syria's economy is shrinking fast, power supplies are erratic, and winter has arrived. The rebels seem to be getting an adequate flow of weapons and munitions from the Arab governments opposing Syria, and are capturing much government military equipment.

While Moscow's assessment that Assad will be able to hang on for an indefinite period may be optimistic, the judgment that a long period of instability will follow is probably valid. The specter of an open country where Islamic terrorists could operate freely is of as much concern to Moscow as to the West. The hatreds that have arisen from 40 years of Alawite domination and the atrocities of the last two years will make a post-Assad country difficult to govern; indeed some type of partition may be the only solution. From the perspective of oil exports from Syria and her neighbors, the problems may have only begun.

Over the weekend, the new Egyptian constitution was approved by the electorate. While this would be a significant milestone on Egypt's path to democracy, the political stability of Egypt is still in question. New parliamentary elections will take place in two months. Egypt faces many problems, including a growing population, the threat of having the Nile's flow curtailed by a dam in Ethiopia, and global warming which is endangering food supplies for 83 million people.

Egypt produces about 700,000 barrels of crude a day and consumes slightly less resulting in a small net export. The government spends about \$16 billion a year subsidizing retail oil prices in the country. Cairo realizes that these subsidies cannot continue, but, as yet, has not mustered the political courage to phase them out in the face of what is sure to be widespread opposition.

On Friday, the US and EU announced another round of strengthened sanctions against Iran which has admitted that its oil revenues are down by about 50 percent due to the sanctions. Although Tehran has long experience in avoiding foreign economic sanctions, this time is different and the effort is starting to hurt. How long this will take to cause policy changes or political instability remains to be seen. India, which must import 80 percent of the 3.5 million barrels it consumes each day is expected to keep trimming its imports from Iran to avoid the penalties that would come from violating the Western sanctions. For now we can only expect the vise to continue closing slowly around Tehran for the immediate future

Xinhua reports that some progress was made in discussions between the IAEA and Tehran last week on inspection protocols for Iran's nuclear industry.

### **3. Troubles in Iraq**

The only good news out of Iraq last week was that crude production is expected to exceed 3.2 million b/d in December. Iraq is now OPEC's second largest oil producer and its Oil Minister hopes to increase production to 3.7 million b/d next year and 4 million in 2014.

Tensions in Baghdad, which have been increasing since the US troops pulled out a year ago, reached new highs this week with the arrest, under orders from Shiite Prime Minister al-Malaki, of 10 bodyguards protecting the Sunni Finance Minister on charges of treason. This follows the conviction earlier this year of Vice President al-Hashemi, now a fugitive in Turkey, on charges of running a death squad. The situation was further complicated by the incapacitation with a stroke and evacuation to Germany of 79 year old Iraqi President Talabani who has been widely praised as the only man in Baghdad who could mediate among the warring factions.

The arrest of the bodyguards has brought thousands of Sunnis into the streets where they briefly blocked the main highway from Baghdad to Syria and Jordan. In the meantime bombs targeting security forces, officials and army patrols continue to go off nearly every day. Although Baghdad is widely perceived as tilting towards Iran, the past year has brought better relations with other Arab states.

In addition to the unstable political situation in Baghdad, the country faces whatever falls out from the Syrian uprising and the continuing confrontation with its Kurdish province over oil policy. Relations between Baghdad and Erbil worsened last week as Baghdad refused to make a second payment to the Kurds for the oil they were exporting through the northern pipeline, and Erbil retaliated by cutting the flow of oil to a trickle amidst recriminations.

The issue of western oil companies drilling in Kurdistan came to the fore again last week when Baghdad warned Exxon that it would be a grave mistake to start drilling in extensive border regions that are contested as to whether they are or are not part of Iraqi Kurdistan. Baghdad went so far as to warn Exxon that it would "face the Iraqi army" should it start drilling.

All this turmoil is not good for a country that has a large share of the Middle East's untapped oil reserves and is counted on to be a major factor in global oil exports in coming decades. It is nearly ten years since the US invasion overthrew the Hussein regime and it is clear that the country in its current form has a long way to go before it achieves the political stability necessary to produce continuing larger quantities of oil each year.

By modern standards, Iraqi oil is still rather cheap and easy to produce, but given the increasing geopolitical problems on the horizon, it is difficult to see production growing at the rate the government hopes.

### **Quotes of the week**

- "... oil and gas production in the United States is surging and is expected to continue to rise. This trend has led a parade of analysts and even the government's National Intelligence Council to predict that, after four decades of failed attempts, America might soon become energy independent. This view, if taken too far, is not only wrong, it is dangerous. The United States would remain entangled with the

global oil market indefinitely even if it were to import no oil. Political leaders lulled into a false sense of security by rising domestic oil and gas output run the risk of making big mistakes.”

- [Michael Levi](#), The New York Times

- “Peak oil is dead.”  
- [Ed Morse](#), Citigroup

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

- **OPEC** will cut crude exports by 2.6 percent as demand during the northern hemisphere winter begins to slacken, according to tanker tracker Oil Movements. (12/21, #5)
- The Nigerian National Petroleum Corporation (NNPC) said it recorded **774 line breaks** on its pipeline from Lagos to Ilorin depots, this year. The Group’s Managing Director decried the unending incidents of pipeline hacking and product theft. (12/21, #12)
- **China's diesel exports** rose to the highest level in more than two years in November and pipeline natural gas imports increased to a record, while purchases of liquefied natural gas declined. (12/21, #13)
- The first oil tanker carrying **Bakken crude** to Irving Oil Corp.'s refinery in Canada from Albany, New York, ran aground in the Hudson River, delaying the first of what is expected to be many voyages on the route. (12/21, #17)
- **Wind-turbine installations** are poised to exceed natural gas-fueled power plants in the U.S. for the first time this year as developers race to complete projects before a renewable energy tax credit expires. (12/18, #28; 12/20, #28; 12/22, #16)
- The **Mississippi River** has receded to critically low levels after months of drought, severely affecting US commerce. Already, barges are being filled only to 50 or 60 percent capacity so they won't sit as low in the water. (12/18, #21; 12/22, #18)
- In one of the costliest rules in its history, the US **EPA** established the first nationwide caps on mercury and other pollutants from industrial boilers while bowing to industry demands to give companies more time to comply. (12/22, #23)
- The British government said it wants to set up the right tax regime to support an emerging **shale** natural gas industry in the country. (12/21, #20)
- Recent announcements by the **UK government** encouraging development of shale gas are not enough to ensure its commercial viability. The key determinant will be the quality of the subsurface and well performance, Wood Mackenzie said. (12/21, #21)
- The world will burn 1.2 billion more tons of **coal** annually by 2017 than in 2012, putting coal close to oil as a leading energy source, the IEA said. (12/18, #5; 12/20, #14)
- Norwegian energy company **Statoil** announced it was spending \$590 million to acquire acreage in the Marcellus shale in the United States. (12/20, #18)
- A report led by **US Geological Survey** -- "Impacts of Climate Change on Biodiversity, Ecosystems, and Ecosystem Services" -- says animal and plant species are flowering, laying eggs or migrating in different ways and at different times than in previous years. This pattern, the USGS said, is accelerating. (12/20, #19)

- The **UK's oil production** fell to 684,000 b/d in October, down 32% on the same month of 2011, as planned maintenance on the large Buzzard oil field and at a processing terminal hampered output. (12/20, #24)
- Mexico's state-owned oil company **Pemex**, is having one of its best months this year for crude-oil production, and it comes after an even better November. However, it looks like the oil monopoly will fall short of its internal goal of ending the year-on-year slide in oil output since 2004. (12/19, #11)
- **President Chávez** has come down with a respiratory infection as he seeks to recover from a complicated procedure for cancer, a government official in Caracas said. (12/19, #12)
- Rep. Ed Markey, D-Mass., said he was "disappointed" there were flaws in a study on the potential benefits of natural **gas exports** from the US. Markey, ranking member of the House Natural Resources Committee, said a report submitted to the Department of Energy on gas exports was outdated and contained "key missteps." (12/18, #20; 12/19, #15)
- A **Saudi** online newspaper says more than 3,000 nationals of the kingdom, including prominent writers and academics, have endorsed a study that recommends lifting a ban on women driving. (12/18, #8)
- **Kuwait's** provisional budget surplus surged 43 percent to \$52.2 billion in the first seven months of the fiscal year, boosted by oil income. (12/18, #9)
- A **Yemeni natural gas company** said it was the victim of sabotage when attackers struck a 38-inch pipeline connected to the country's coast. Last summer, the Yemeni government said it was losing around \$15 million per day because of attacks on national energy infrastructure. (12/18, #13)
- Exxon Mobil said it signed agreements to start exploration work in the deep waters off **South Africa**. (12/18, #14)
- The Liberal Democratic Party's victory in **Japan's elections** is seen as a boost for nuclear energy. Shigeki Matsumoto, an analyst at Nomura said the LDP's victory would have more implications for Japan's long-term energy policy rather than on the immediate possibility for restarting idled nuclear reactors. (12/17, #14; 12/18, #16)
- An analysis of the output from 18 different global climate models indicates that **India's** average annual surface air temperature could go up by between four and seven degrees Celsius by the end of this century. (12/18, #17)
- A new report looking at **public transport** use over the first three quarters of 2012 has found that ridership has increased by 2.6%, amounting to 201 million more trips taken in the first nine months of the year than were taken in the same time period in 2011. (12/18, #22)
- Russian energy company **Gazprom** announced that engineering surveys are under way for development of LNG facilities at the Shtokman field in northern Russia. (12/18, #26)

## **Commentary: ASPO-USA Meets with DOE Officials -- Some Things We Learned**

By **Jan Lars Mueller**,

On Monday, December 17, representatives of the Association for the Study of Peak Oil & Gas USA (ASPO-USA) met with senior officials of the Energy Information Administration (EIA), including Administrator Adam Sieminski, and staff from other offices within the U.S. Department of Energy (DOE). The meeting was arranged following a letter that ASPO-USA sent to Energy Secretary Steven Chu and Sieminski after his appointment as EIA administrator earlier this year. The letter outlined key questions and concerns regarding oil and gas information that EIA provides.

The meeting was intended to help ASPO-USA and DOE-EIA better understand each other's perspectives and explore ways that ASPO-USA might collaborate with DOE and EIA's to enhance their information products. EIA officials discussed their priorities and the challenges they face, while ASPO-USA representatives discussed the goals of our work and our specific concerns.

ASPO-USA's concerns generally followed two themes: 1) projections for future oil and gas supply should properly consider technical and economic factors that may constrain U.S. domestic production; and 2) DOE and EIA need to recognize broader trends that may be increasing the risk of a world oil crisis. While it was an important opportunity to present analyses by ASPO-USA-affiliated experts, the greatest benefit of the meeting was gaining a clearer understanding of the factors that are shaping EIA's work and the opportunities for ASPO-USA to provide constructive ongoing input.

Of relevance to our concerns, we learned that EIA information on drilling costs and other costs of oil and gas production may not be very robust. Their projection models, therefore, may grossly underestimate the significance of increasing production costs as a constraint on oil or gas supply. EIA's projection models seem to be more demand-driven than supply-driven in general (we will be reviewing the assumptions and inputs of their models to confirm how supply constraints are or are not factored into their projections). In addition to offering assistance in gathering and evaluating such cost data, we suggested tracking different types of oil and gas separately, so that their varying technical and cost constraints can be more properly and clearly assessed.

Moreover, in pressing issues regarding world oil production and rising global consumption, we became more cognizant that EIA, despite being the nation's central source of energy information, does not have a clearly defined mandate to track global trends nor collect and report international energy data. ASPO-USA representatives conveyed that this was an issue where we and other outside experts could be helpful in providing both assistance and an impetus to address such issues more thoroughly. We discussed and mutually recognized that there are major problems with inconsistent and unreliable data from different countries. However, we also noted that there are analyses and interpretations of global trends that can be made based on existing data from reliable sources.

Perhaps most importantly, we learned that EIA's interaction with and input from experienced experts in technical oil and gas issues may not be as regular and rigorous as it should be. EIA receives advisory support from the American Statistical Association's Committee on Energy Statistics, but this input is primarily focused on statistical methods. EIA conducts and participates in various meetings and conferences where special technical issues are discussed, but these meetings seem to be relatively ad hoc and lack continuity. As a way of building a closer working relationship between EIA and ASPO-USA, as well as promoting input from a broad diversity of outside experts, we offered to help organize a series of meetings or workshops to address in-depth the questions and issues that ASPO-USA has raised. We also posited the need and potential benefits of a broader standing advisory body of outside experts, though establishing such a body is a somewhat longer-term prospect.

In sum, we opened direct channels of communication and created a solid foundation for future cooperation. At the same time, we are developing a more concrete understanding of their work, so that our questions, input, and criticisms of their work can be more specific and constructive.

**Jan Lars Mueller** is the Executive Director of the Association for the Study of Peak Oil & Gas USA