

PREDICTING OIL PRICES: THE SHORTAGE IS IN THE FACTS

Any numbers of energy experts—in Wall Street, in specialist trading outfits and in government bureaus throughout the world—have concluded that, since demand for oil will continue to outstrip supply, crude prices will remain on a firm-to-higher path in the foreseeable future. The problem is that hardly any statistical formulation is based on audited or established facts. Data from countries within the OPEC (Organization of Petroleum Exporting Countries) has proven to be totally unreliable. And oil consumption estimates from countries like India and China are just that, estimates.

Pressed for facts at a recent news conference, an official from the US Energy Information Administration conceded that “we are working on best-available data, not on the type of data we would like to possess.” For example, the Saudi government has been claiming, for well over a decade, that it can increase production by at least 10% at short notice, if and when stability (and sanity) needs to be injected into the energy price spectrum; prior to the start of the March 2003 Iraq war, OPEC’s publicly stated objective was a trading range of US\$22-28 per barrel, and the Saudi concept of price stability has been changing with each passing day.

Moreover, nobody really knows how much oil the Saudis actually sell, and how much excess capacity is waiting to be tapped. For that matter, OPEC’s other members are not too liberal on output data either. Iran, for instance, has never been able to explain the gap between oil revenues recorded in the national budget on one hand and oil sales disclosed in OPEC publications on the other. Iraq’s government claimed yesterday that its monthly oil production had finally exceeded pre-war levels. But, given the quantum of illegal, non-approved oil deals executed by Saddam Hussien, who knows for certain how much oil Iraq was exporting in 2003? And, given the widely fluctuating security situation, is today’s data from Iraq valid for a forecast of tomorrow?

To add to the confusion, a former senior executive of Moscow-based Gazprom revealed in a statement from exile in London that “the story of the vast Russian petrochemical sector is continuously shaped and re-shaped inside the Kremlin. For the Putin administration, oil and gas are highly strategic weapons, and they don’t care a damn for the global demand-supply equation.”

Well, the largest consumer groups don’t care a damn either. Not surprisingly, one has yet to hear anything akin to a mass protest at the steady rise in gasoline prices at American and European pumps.



And, as far as consumption statistics from India and China are concerned, the less said the better. “One bad harvest, which depends largely upon the weather, will halt India’s 10%-plus growth rate in its tracks, simple as that,” a Mumbai-based trader in stock options warned his clients in a blog posting today. At the same time, a Chinese Communist Party executive told foreign journalists in Beijing last week that “higher oil will not impact China, since the biggest component of national GDP growth for the next few years will be non-urban in nature, and incremental consumption of oil will not be too significant. Don’t expect China to lead the charge beyond US\$100 per barrel.”

The fundamental problem in predicting the future of oil prices, of course, lies in the paucity of sufficient facts, either for demand or for supply. When confronted by this fact-shortage, a Citibank analyst cited the terror premium. “The threat of terrorism is contributing at least US\$30 to the price of each barrel of oil sold on the world markets today,” she insisted. “One cannot be too precise here, but the movement of the oil price graph since 2001 is ample evidence that terrorism, or rather the threat of it, has provided the core momentum after oil prices breached the US\$50 per barrel mark.”

Will the absence, hopefully, of a terrorist spectacular over the next 12 months or so cause the terror premium to narrow? And will a major terrorist attack in the West result in the widening of that premium? The more you ask those questions, the more imprecise the opinions become. Because if 30% of today’s crude prices are a consequence of terrorism, then perhaps energy experts should concentrate on studying terrorism rather than pouring over dubious supply and demand statistics!!

In the meanwhile, the entire oil exploration scenario is riddled with inconsistencies. A series of exploration programs, particularly in West Africa and Central Asia, have been placed on slow track, or have been shelved, at least temporarily. At the end of the day, with virtually all price-related projections inherently lacking credibility, it is natural that the focus returns to production, sales and unprecedented profits---whatever the reason for a barrel being priced at US\$90-plus might or might not be.

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