



Discussing prices and demand

Posted by [Heading Out](#) on August 11, 2005 - 4:02am

Over on [Econbrowser](#) there is a discussion going on relating to the Hirsch report, which we last discussed [here](#). It is very much an economist's discussion, but contains within it the continued question as to why, if the supply of oil in the world is drying up, haven't we seen higher prices than we currently are. This applies both to current, and, more particularly, futures prices.

Well the times they are a changin'. As was pointed out in the comments section of that post, future prices for oil are now heading steadily up there. And as the season moves on [the price of oil](#) is moving with it. My own belief is that Hirsch was really more interested in proving that if we did not do something to enhance supply, starting fairly soon, we would be in deep trouble. And he anticipated that we had to be working on a solution for 20 years, in order to have enough oil to go around, when supply stopped meeting the demand for oil that would allow us to continue to maintain, worldwide, our current standard of living. The reason that we are here at this site, of course, is that to a large extent we don't think that Hirsch got it right, and in fact we have a darn sight less than 20 years before there is a serious problem. But by putting up the evidence, we do try to let you make up your own minds as to when the problem will arise, but don't expect a long warning. While not deliberate, it does seem that more economists than anyone else are running around telling us that we don't need to worry, and predicting that soon oil prices will be down to \$30, \$35, \$20 - pick a number. (see [here](#)).

After all, as I commented in that earlier post, the public was caught short by the energy crisis of 1977, even though geologists and others in the know had been warning of the problem for some time. The only difference this time around, perhaps, is that the advent of the internet makes it easier to get the word out than it did back then.

The other issue that crops up over there in the discussion that bothers me is this idea that, when demand begins to get destroyed by price increases, that all of a sudden there will be a surplus again, and the price will drop.

Bluntly I think that is hokum! The impact of higher prices will reduce demand at the edges, with prices rising to continually trim demand to what is available. But there will not, initially, be that much difference between supply and the level of demand that is going forward. So that price rises should not, in the immediate short term, go to the heights that Matt Simmons is now predicting.

The problem is that we tend to make judgements more and more based on theory, rather than going out and looking at the reality. There is much talk, in England and over here in the mantra that "technology will solve everything", that "the Stone Age didn't end because we ran out of stones."

Unfortunately to have an alternative we have to have engineers. And in this country that is not a priority as [Robert Samuelson](#) commented in today's Washington Post.

All advanced societies now depend so completely on technology that their economic might is often measured by their number of scientists and engineers. By that indicator, America's economic power is waning. We're producing a shrinking share of the world's technological talent.....Among engineers with bachelor's degrees, the gaps are already huge. In 2001 China graduated 220,000 engineers, against about 60,000 for the United States, the National Science Foundation reports.

Freeman also documents a second worrisome reality: U.S. scientists and engineers aren't well paid, considering their skills and -- especially for PhDs -- the required time for a degree. This means, Freeman says, that "the job market . . . is too weak to attract increasing numbers of U.S. students. . . . From 1990 to 2000, average incomes for engineering PhDs increased from \$65,000 to \$91,000, up 41 percent;...the 891 MBA recipients of the Harvard Business School's class of 2005. At an average age of 27, they command a median starting salary of \$100,000....these new Harvard MBAs also got huge one-time bonuses; the median was \$43,000.

Note that it is an average over-a-life salary for engineers, but a starting salary for MBA's. However he takes comfort in the fact that

In 2002 universities earned \$915 million from (patent)licensing fees, almost four times the 1993 level,

The actual truth being, unfortunately, that most of those fees were for medical items, rather than engineering.

We have got into a world of hurt with depleting expertise in many fields because it has been less economic for Universities to teach the more costly disciplines. This ranges from the [mining](#) and [petroleum](#) schools to such things as [nursing](#) . But then, of course, market forces "must prevail," and we should, perhaps, forget the ancient virtues such as leadership and vision, and planning for the future.

The only problem I have with that is that if it leaves us terribly uncompetitive and unhealthy at a time when the rest of the world is going to be competing for the same resources that we are.

It also means that those who do go into these disciplines (especially the extractive ones) are finding more lucrative starting salaries, and while not yet up to MBA standards, J has mentioned that a couple of new hires (BS Petroleum) he recently talked with, started in the mid \$70's, about \$10k up on the last number I had reported.

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