The Oil Drum: Europe
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BP CEO: Oil markets will save us

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The CEO of BP, Tony Hayward, has published, on the occasion of the publication of BP's statistical yearbook, an Op-Ed in the Financial Times with a pretty self-explicit title: Let the markets solve the energy crisis. But it's also very devious, as his ode to markets allows him to mix reasonable arguments with highly toxic ones, and it's going to be very hard to make the distinction that he is correct on some respects but not in others...

Basically his arguments boil down to 3 points: there is no speculation (prices are justified by fundamentals, markets work fine), renewable energy is not serious (too small, mostly), and there is no peak oil (plenty of reserves around). and of course, his solution is simple: oil majors are ready to invest and let market forces solve the supply problem, but political obstacles prevent them, and governments must therefore help by removing these.

What is true is that speculation is not to blame, and that there are political obstacles to investment today. The rest is not quite so true. And that mix, which I expect is deliberate, has one main subtext: "don't worry" (and don't try to move off oil).

OK, here's the text in full.

> When I became BP chief executive just over a year ago, I warned that the supply and demand balance for energy was very tight. But, in common with most people, I never expected to see the oil price go quite as high, quite as rapidly, as it has in the past few months.

Ah, "most people." This could be seen as yet another indictment of the common wisdom of the "serious" people (I don't think he includes anybody else amongst "people") that pontificate day in and day out in newspapers, think tanks and industry fora and, somehow, still have more credibility than those that have forecast current events with a lot more success.

Of course, short term movements cannot be predicted easily, but long term trends, especially such momentous ones as the irresistible increase in oil prices over the past 5 years, can and have been announced by many commentators, which have been too easily dismissed.

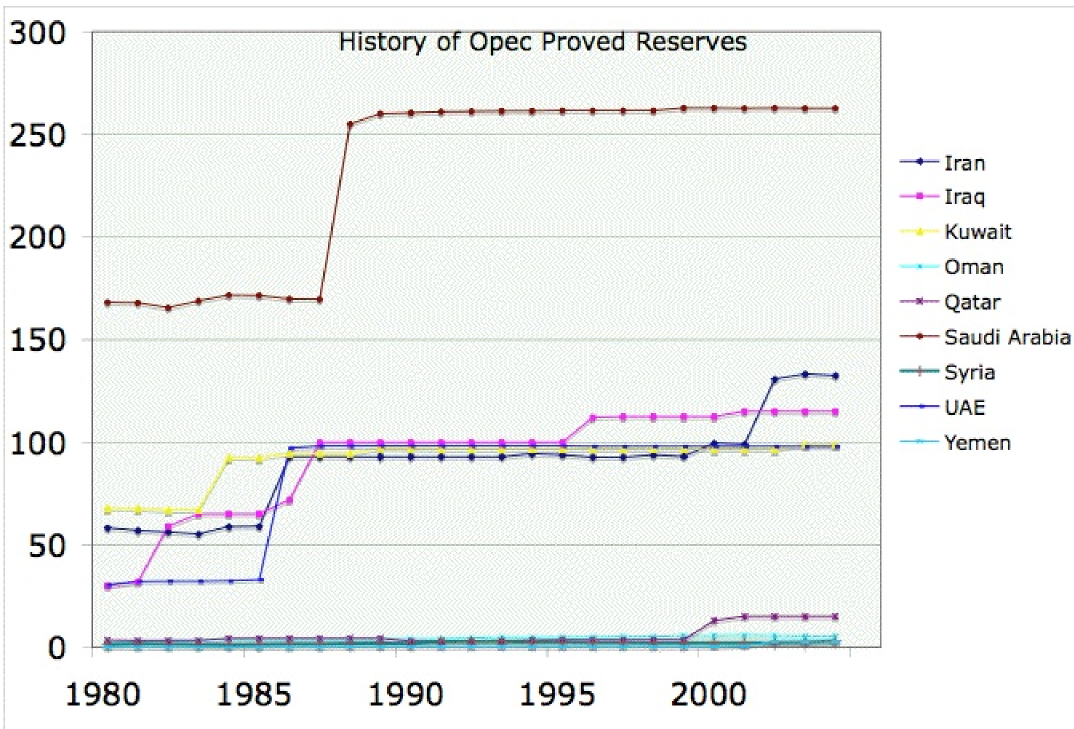
While it's easy to crow now, a call for accountability of the pundits would still seem to be appropriate.

> Unsurprisingly, with consumers and businesses everywhere facing much higher fuel costs, emotions are running high. I understand those feelings. Governments and the energy industry are urgently looking for solutions. But if we are to act sensibly, we must start with the facts. We must accept the world as it is, not as we hope for it to be.

In other words: "we know you're suffering, and are unhappy about it, but please be certain it's not our fault" [**ED** - sentence reworded to eliminate profanity]

> On Wednesday, BP is launching the latest edition of the BP Statistical Review of World Energy. This is the 57th year of its existence and during that time the review has established a reputation as one of the most reliable sources for objective energy data worldwide. At times such as these it is a useful analytical tool for those both inside and outside the industry.

Yes, let's not mention that OPEC (and a few other) country reserves have not been independently verified for more than 20 years, and that BP uses official national data from these countries without questioning them. Let others quote them as authoritative, and let the lies be repeated and disseminated unquestioned.



(*From an earlier Oil Drum story, using BP numbers from 2 years ago*)

> It also exposes some myths that need to be put to rest if we are to find the right solutions to big global problems such as energy security and climate change.

While it is welcome to see climate change mentioned, it is more interesting to note that the energy side of the equation is framed in terms of *security* and not in terms of **scarcity**. Hawyard will remain within that "safe" frame for the rest of the article.

> The first myth is that high prices are caused by technical factors, such as speculation. While these factors may have an impact on the margins, the data clearly show that high prices are really caused by economic fundamentals.
>
> Global energy demand growth in 2007 was above average for the fifth year in a row,

> driven by the fastest period of economic growth since the early 1970s. Demand growth is concentrated in those emerging nations that also subsidise fuel prices, such as China, India and - increasingly - the oil-producing nations themselves.

It is only natural that speculation would come near the top of issues touched upon by Hayward, given the cries we hear around the world, and while oil majors are not the main culprits (financiers enjoy that "honor"), they are not far behind. And of course, given that this is an issue where he is on strong ground (speculation is at best a distraction, at worse a scapegoat) he can score some easy points.

But he actually makes a convincing case, in line with what the IEA has stated yesterday (even if it seems to have been spinned very differently in most media outlets):

> Yet energy supply has struggled to respond. Production by the Organisation of the Petroleum Exporting Countries fell by 350,000 barrels of oil a day last year. The production situation is even more challenging in the market-oriented nations of the Organisation for Economic Co-operation and Development, where many existing basins are maturing fast. In Britain, for instance, North Sea gas production recorded the world's lar-gest decline for the second year in a row, falling by 10 per cent in 2007. UK oil output rose very slightly, but this is a one-off, based on a single big new field. Production remains on a downward trend.
>
> The last time oil prices surged to this kind of level, 30 years ago, new production from the North Sea helped bring prices down. This time, new OECD production will have to come from frontier provinces such as the Canadian oil sands, the Arctic and the deep waters of the Gulf of Mexico.
>
> Another big impact on supply is Russia, where production has begun to decline. It is a little-known fact that, until now, the growing demand for oil from China and India in recent years has been met almost barrel for barrel by rising supply from Russia.

His diagnosis here is spot on, and it is very important that it be made by him (and the IEA) rather than only by pesky bloggers, and that it include a number of points that have yet to make it into the "common wisdom":

- demand growth is still very strong, and it is not just coming from China, it is also increasingly coming from oil-producing countries themselves;
- production is stagnating overall, and declining in a number of regions: OPEC (despite its apparently plentiful reserves, Russia and, more significantly, in regions that "we" control, like the North Sea and the US (no explanation given);
- incremental production can only come from "frontier" areas, ie expensive and low EROEI (although Hayward does not touch that concept, of course). There is no sivler bullet or quick fix like Alaska and North Sea were 30 years ago.

But given the tone used, one can guess what the stage is for: the first two bits are in the "not our fault" category (nasty countries closed to us), and the last one is in the "hey look at what we can do" (we're hre to help). And that does not fail:

> Access to resources for international oil companies such as BP remains very restricted. Resource nationalism is on the rise. That is important because it is the oil majors that have some of the best technology for bringing difficult resources on-stream.

which sets the stage for the bigger point:

> Myth number two is that the world is running out of hydrocarbons. Not so. The world has ample resources, with more than 40 years of proven oil reserves, 60 years of natural gas and 130 years of coal. The problems in bringing on new production are not so much below ground as above it, and not geological but political.

The standard "we're not running out of oil, it's just those pesky governments blocking us" argument, ie the claim that this is just a temporary problem that has an easy fix if a few selfish bureaucrats/nationalists could only get out of the way. This is dangerous on two levels:

- one is to think that political obstacles are minor, ie that it will be easy to force Russia or Saudi Arabia (or Venezuela or Iran or even US politicians) to open their door or the spigot. This perpetuates the narrative that other countries in the planet are here to provide us with the necessary goods or services, independently of their own priorities or needs; it conveys that their sovereignty is a fiction that we tolerate with just a bit too much patience, but that we could push out of the way if it really became necessary; more generally, it dismisses completely the notion that our economies are acutely vulnerable to political events in these places and that, even if oil were plentiful in the long term, such events can create a lot of pain and disrtutpion in the short term that we are not planning for;

- it is of course more dangerous in that it hides the fact that there IS a long term problem; by focusing (in an artifically theatrical way) on short term issues, it prevents us from doing anything about the long term crisis - which is quite scary when you think that this is an industry where investment decisions commit us to infrastructure and patterns of activity for many decades.

> Myth number three is that we can switch quickly to a low-carbon economy. While biofuels, wind and solar energy are growing rapidly, they comprise a tiny share - less than 2 per cent - of global energy production. Humankind remains dependent on fossil fuels and coal is the fastest-growing of all the main fuel types. Carbon emissions continue to rise. We clearly all need to work harder if we are to tackle the threat of climate change.

The usual silly argument that renewables are still small and therefore will remain so. We have not tried yet to make them big. To a large extent, renewables are still being developed against the common wisdom of the serious people and against ferocious lobbying by traditional sectors (both the coal and nuclear industry spend a lot of effort lobbying against wind) and prominent NIMBYs, and they have never been a priority of policy (there are policies in place, and they work, but they are still seen in Washington, Brussels and other capitals like London or Paris as something that you do to look green rather than because it makes sense). As I've argued many times, wind is cheap, understood, and able to provide a lot more of our energy than generally admitted, but that idea has yet to sink in, and Hayward's argument is typical of that.

Sure, coal is growing fast, but that's because policies push that way, and because policies that would make things different are dismissed and/or fought tooth and nail by industry.

> So how are we to secure the energy needs of the world in the 21st century? The evidence is that where markets are allowed to operate, they do work. That is what the data in the review show. And that is the real source of hope for the future. Consumers in Europe and north America are already responding to high prices by moderating demand. They are also beginning to embrace energy efficiency. Where investment is allowed to take place, energy production responds positively. Last year, US oil and natural gas production increased - in the case of oil, for the first time since 1991.

Using the small drops in demand in the US and Europe ignores the fact noted earlier in the article, ie that demand growth is coming mostly from other countries. And it conveniently ignores the fact that the West is the only part of the world where demand could shrink (given that in many parts of the world, especially the big new consumers in Asia and oil-rich countries, energy is subsidized and consumers have yet to feel the prices hikes in full) - and it took a five-fold increase in oil prices to cut demand by a couple percent!

Pointing to a small increase in US production (why not repeat here the note and the similar hike in UK production last year?) suggests that oil production could be increased by significant amounts at home, with investment. but there are effectively no restraints on investment in the areas already opened to production, and as he noted above "the trend is downwards." Opening up new areas like ANWR or offshore for drilling would certainly create a lot of profits for the oil industry in the short term, but would be highly unlikely to reverse the production decline. and the volumes at stake are insignificant on the global scale (total US reserves, including those in all the closed off areas, are currently equal to about one year of world consumption, or 5 years of US consumption).

But pointing that things are moving (or could move) in the right direction on both the demand and supply fronts suggests that, again, the oil crisis is temporary and easily fixable.

> The conclusion is therefore simple. Producers and consumers should be encouraged to respond to the market's signals. High prices are saying that we need more investment - in energy efficiency, new production, new technology and new energy sources such as wind, solar and nuclear.

Huh? High prices are the signal. What more encouragement people need? Either they respond to the signal, or they don't. That's what markets are about, isn't it?

Of course, he wants *more*. The solution is always more, not **less**. Never. and somehow wind and solar deserve a line here, despite having been dismissed as irrelevant just a paragraph above. But it's so politically correct to mention them, alongside the things we really care about: more drilling (and more nuclear too).

> In order for that to happen, businesses and governments must act together. Companies know that they need to invest more, which is why BP and its peers have been raising capital expenditure substantially. But governments must do their bit too, by removing the barriers to that investment, improving access to resources and modernising the tax structures we work in.

No mention, of course, that BP's investments have been going up because its costs have been goign up, rather than because it is exploring or developing more fields. No mention of the fact that, other than the bump from adding TNK production to its own production, BP's output has been declining over the past 5 years. No mention that majors barely control a few per cent of world oil reserves and have becoming increasingly irrelevant, despite the headlines and hate they generate with their huge profits.

And a conclusion that encapsulates the spirit of our times: there is no problem, however momentous, that cannot be resolved with lower taxes (I presume that's what he means by "modernising" tax structures, right?).

After 30 years of voodoo economics, we get this sad "all is well, we'll save you if you lower our taxes" gambit and it will be seen as the height of seriousness.

But maybe this is a good thing, because this is certainly not going to slow the relentless rise of oil prices, and its very real consequences on our economies. and maybe, maybe, at that point, our politicians, keen to save their sorry asses, will stop listening to "serious" people and their unctuous, don't-rock-the-boat talk, and will actually go for policies that work.