



A different view of the gas situation

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Topic: [Supply/Production](#)

When we write about the developing problems in supply of oil and natural gas, the response, whenever there is a drop in price, is that we are totally wrong, rather than recognizing that there are still fluctuations between levels of supply and demand.

In this regard there is a potential in the near term for a drop in natural gas prices, as noted by [Harry Chernoff](#) due to a significant reduction in demand. His "back of the envelope" calculation is that the drop in demand from the shut down of industrial operations such as ammonia manufacture, now exceeds the amount of gas still shut-in in the GOMEX. There is thus a current build up in supply that may, depending on how demand changes with the cold in the short term, lead to significant changes in the price of gas.

The point is that unless the weather loads are substantial enough to maintain the market perception of potential end-of-season shortages, gas prices are vulnerable to a 20-30% drop even with no change in oil prices.

Unfortunately this is only going to be a short-lived phenomenon.

In the bigger picture, nothing that took place this summer in gas production and demand and nothing relating to the storage or pipeline situation changes the bleak long-term outlook for North American gas supply against the relentless increases in demand. The Energy Information Administration recently reported that the industry's reserve additions in 2004 were 118% of consumption versus 111% in 2003 and 118% in 2002 but that additions from new fields (as opposed to field extensions and new reservoirs in old fields) were by far the smallest they've been for at least the past 10 years. Despite all the drilling (and rapidly rising finding costs) roughly 90% of the reserve replacement is now coming from field extensions and barely 4% from new fields. The oil ratios are similar. From a short-term economic perspective, this increased intensity of operations at existing fields is a positive factor, indicating economic efficiency. From a long-term resource perspective, however, the implications are extremely adverse. The truly new resources simply do not exist at the quantities and the costs to which the country has become accustomed.

Sadly, however, the short term events may cause the longer term concerns to be discounted once more, and needed solutions will be pushed to the back burner for a while longer.



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