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Forget about ’peak oil’ and focus instead on ’peak power’

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Financial Times ’Insight’ column (April 2, ’Companies & Markets’ section) which may be too quick to dismiss the role of the free-falling dollar in dollar-denominated oil prices, but makes an interesting case for the necessity of the current ’speculative’ $100+ a barrel rate based on total stocks, once producer countries’ excess capacity levels are considered *in relation to their own domestic energy needs*. The author unwittingly comes close a ’Midnight Notes’-type argument: the Opec states are forced to provide for electricity demand from growing and increasingly urbanized (read: proletarianized) populations, to the point of actually having to *import* oil to run power plants. Consequently ’excess’ (i.e. world market-ready) capacity is falling, pushing market prices up, even as inventories and capacity increase in absolute terms.

Also casually dropped in is the interesting claim that some of the Opec countries’ oil revenue has ’found its way into’ funds speculating in oil futures, thus pushing prices up further. Chavez-loving leftists should pray that this abstract perpetual-motion machine has a long time left to run.

Forget about ’peak oil’ and instead focus on ’peak energy’

Opec’s disappearing excess capacity is the root cause of oil above $100 a barrel.

The decrease in excess capacity started last summer after power shortages in the Gulf region. After the summer heat receded and some excess capacity again became available, it quickly vanished again. [...]

Opec blamed the runaway price on speculators and the US policies that have fuelled speculation, including lower interest rates and the weak dollar.

But the blame also rests on some Opec members. [...] Some of [these counties’ oil] revenues found their way into funds that speculate in oil futures. Ironically, ’petrodollars’ have helped drive oil prices to new records.

In addition, the way that some organizations and analysts have interpreted market fundamentals is flawed, because they exclude the role of excess capacity. [...] The historical relationship between total oil stocks and oil prices has an embedded assumption in it which analysts are now ignoring: excess capacity should not decline below a certain level.

[...]

In spite of rising inventories, vanishing capacity makes current total stocks so small that the increase in oil prices is the necessary result of market fundamentals.

Therefore oil prices will remain high and might continue to break records this summer, regardless of capacity expansion by Opec members and regardless of talk about ’peak oil’. Our focus this year should be on exports from the oil producing countries, especially in the Gulf region, not on production or capacity increases. Capacity might increase, but exports could well decline. Why?

Economic growth, population growth and urbanization in the Gulf have increased demand for electricity to the extent that power shortages will be the norm in the next few years. Power shortages and inadequate generation capacity have delayed several development projects, industrial plants and other contruction projects in several Gulf cities. A large number of housing towers stand empty in some Gulf cities for lack of elctricity.

It is not ’peak oil’ that is fuelling the current increase in oil prices, it is ’peak power’. Sadly, the whole world will pay for these power shortages in the form of higher oil and gas prices. A heat wave this summer would force countries in the Gulf region to divert natural gas from use in the oil fields to power plants during peak demand. This, in turn, will reduce oil production and crimp exports. Counties that use water injection will divert crude oil from exports and burn it directly in power plants.

The result is a decrease in exports – and an environmental disaster. Let us remeber that there is no additional natural gas in the region. All natural gas, including gas from unfinished projects, has been allocated. Let us also note that these countries have started importing fuel oil for power plants. Such imports have become expensive and put strain on the world refining markets. In short, even building more power plants will not solve the problem. There is no gas for these plants.

One final complication: diverting crude from exports will lower government revenues, which are used in part to finance these plants!

One fact is clear: if Opec had excess capacity, it could flush out speculators, lower oil prices and help the ailing dollar, thereby helping itself by increasing production.

To conclude: let us forget about ’peak oil’ for now and focus on the more immediate crisis: ’peak power’.