

Oil Signing Its Own Death Warrant, Says UK Report

So far, high oil prices have not caused recession in the economically developed world. Indeed, continuing high oil prices are contributing to more efficient use of current technology and in the long-term they are energising moves toward sustainable energy technology.

However, oil is signing its own death warrant by pricing itself out of the market and making previously expensive alternatives highly attractive to energy consumers. These are the findings of *A New Era for Oil Prices*, a new report published by Chatham House.

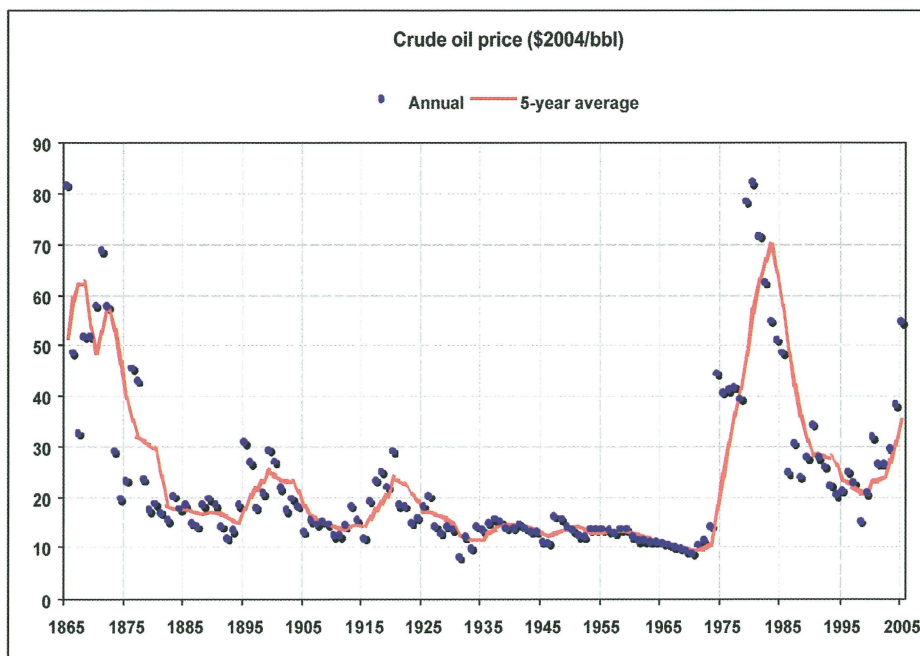
In the report, author John Mitchell says the continuing high price of oil at well over \$US50 a barrel, more than double the previous 20-year \$US25 average, does not look like going through any real readjustment in the near future.

But far from being a wholly negative occurrence, the paper argues that the high oil prices are forcing oil consumers into using current technology more efficiently. While the current debate is centred on the creation of new technology to increase energy efficiency, Mitchell highlights the fact that a better use of current technology could save a huge amount of the world's energy supply.

As theoretical examples the report highlights the US vehicle market. If it switched to vehicles with the same efficiency as current Japanese or European models, then US oil imports could drop by one third. Conversely, outside of the transport sector, if Europe followed the US's lead and began substituting other fuels for oil to the same extent that the US has done, then world oil demand could fall by a further 20%.

In the longer term the report also argues that if, as expected, oil prices stay high, then new alternative energy supplies, which are currently deemed too expensive, would become increasingly attractive to energy investors.

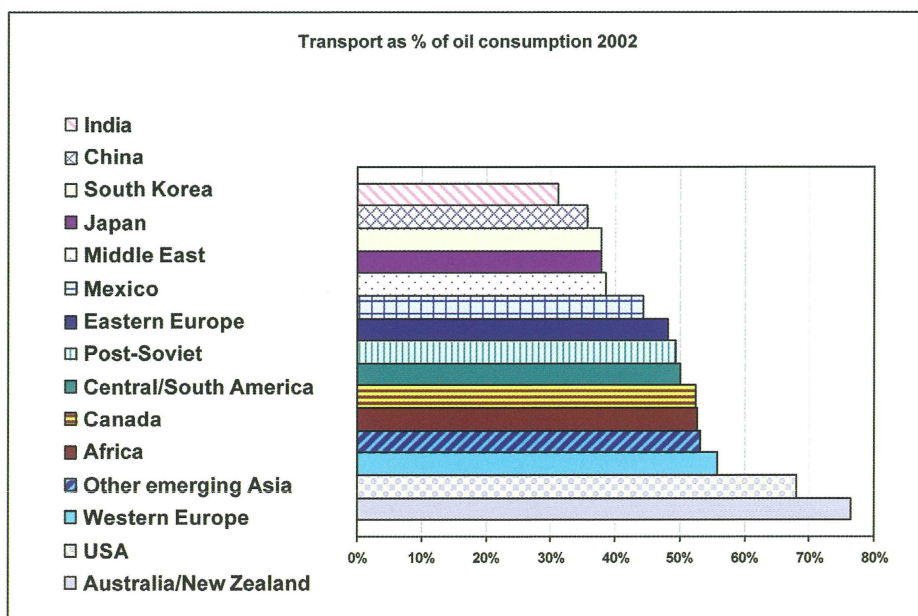
Commenting on peaks and plateaus, the report says the 'peak oil' image supposes that most economically recoverable oil reserves are already known, and that they will be produced up to a technically maximum rate of depletion – around 10% per year, so that after the peak, decline will be rapid. In fact, it says the major holders of the reserves – OPEC governments – follow a more conservative policy of depletion of 3-5% per year, guaranteeing 20-30 years of supplies so that oil will not 'run out' suddenly. 'Plateau' rather than 'peak' is the appropriate image. How much oil can be economically recovered also depends on future prices and costs. Reserves at \$US10 are not the same as reserves at \$US50.



The history of crude oil prices shows the annual price of Brent crude oil in 2004 dollars from 1865 to 2005, compared to a five-year moving average. Usually, the price has returned close to a five-year moving average within 2-3 years. From 1886 to 2003 the annual average price appeared to fluctuate around \$US 25 (2004 dollars). Since July 2005 the daily spot price of Brent crude has averaged over \$US 60 per barrel, reflecting a combination of developments over 2004-5.

The report concludes that oil is therefore not necessarily the main driver when it comes to global energy prices. As consumers become more accustomed to high prices they will increasingly find ways of mitigating their

reliance on oil, which ultimately will weaken the oil industry's global standing and expose it to ever widening competition from energy efficient products and services. ■



Source: US EIA, *International Energy Outlook 2005*.

This oil for transport chart compares the proportion of oil used in transport in major countries. Most countries used more oil outside the transport sector than the US, where competing fuels have been available for a long period of time for non-transport uses, energy markets have been liberalised for roughly twenty years, and there is a diverse, flexible economy.