THE COMING OIL PRICE COLLAPSE

HOUSTON IAEE
NOVEMBER 2005
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*AS SEEN IN PLAYBOY
THE LAST BEAR

HOW I SEE MYSELF
(an alternate perspective)
BULLS AND BEARS

- $160 CRUDE, $10 GASOLINE
  - NOT VERY CREDIBLE
- $50-60 FOREVER
  - A NEW PARADIGM, SOARING DEMAND
- A $40 PLATEAU? OPEC’S DREAM(?)
- SUB-$20
  - POSSIBLE, BUT SO IS DEMOCRATIC IRAQ
- BACK TO $30: 1986 REVISITED
LAST YEAR
A NEW PARADIGM?

WHAT DO YOU CALL IT WHEN:
- THE CHINESE DEMAND IS GROWING STRONGLY
- OPEC SURPLUS CAPACITY IS MINIMAL
- AND PRICES GO DOWN?

- 1994 AND 1998!!!
2006:
WHICH OF THESE DOESN’T BELONG?

- HIGH OIL PRICES
- SLOWING ECONOMIC GROWTH
- SOARING OIL DEMAND
- BIG BOOMS LEAD TO BIG BUSTS!
WHAT ABOUT PEAK OIL?

- (YOU MUST BE JOKING)
THE CURRENT MARKET
A NEW OIL MARKET?

- RESOURCE FEARS:
  - OIL PRODUCTION HAS/WILL SOON PEAK
  - SAUDI ARABIA LACKING RESOURCES
  - EASY OIL GONE

- CAPACITY
  - REFINING SECTOR STRESSED OUT
  - OPEC HAS NO SURPLUS
  - TEN YEAR LEAD TIME FOR NEW CAPACITY

- DEMAND A ‘RUNAWAY TRAIN’
  - CHINESE, INDIANS BUYING CARS
ANNUAL DEMAND CHANGE: NEW TREND OR OUTLIER?
CHINESE GDP GROWTH

HIGH ECONOMIC GROWTH IN CHINA ALONE DOESN’T MEAN HIGH PRICES
SOME BASIC FACTS

- NO COMMODITY HAS EVER SHOWN A BOOM WITHOUT A BUST
- NO MAJOR CHANGE IN UNDERLYING SUPPLY/DEMAND IS EVIDENT
  - NOW 1.75???
- MARKET IS TIGHTER—AND WILL REMAIN SO (MOSTLY)
- PRIMARY QUESTION IS NON-OPEC SUPPLY TRENDS
LONG-TERM OIL PRICES

[Graph showing the price of oil from 1859 to 1999, with price points ranging from $0 to $50 per barrel.]
OIL PRICE RETURN

CALCULATED AS 10-YEAR AVG ANNUAL CHANGE
OIL COMPARED TO US T-BILL

POSITIVE NUMBER REPRESENTS BETTER RETURN FOR OIL.
HUGE SURPLUS CAPACITY IS NOT THE NORM
   – REFINING SECTOR AN INTERESTING EXCEPTION

CURRENT MARKET IS CLOSE TO DESIRED CAPACITY UTILIZATION
   – HIGHER VOLATILITY FROM 1995

BUT CAPACITY IS RISING:
   – OPEC UP 1 MB/D IN 2006
   – SAUDIS ALONE ADDING 2.5 MB/D MID-TERM

IF DEMAND GROWTH IS WEAK, OPEC SURPLUS CAPACITY COULD GROW BY 1.5 MB/D IN 2006
OPEC PRODUCTION

CAPACITY IS TIGHT, BUT PRODUCTION INCREASING
OPEC SURPLUS CAPACITY

TIGHT CAPACITY ALONE DOESN'T MEAN HIGH PRICES

PRICE COLLAPSES
CALL ON OPEC: IEA

ASSUMES STRONG DEMAND GROWTH IN 2006
OECD INVENTORIES

MILLION BARRELS

Jan-98  Jul-98  Jan-99  Jul-99  Jan-00  Jul-00  Jan-01  Jul-01  Jan-02  Jul-02  Jan-03  Jul-03  Jan-04  Jul-04  Jan-05  Jul-05
LOWER NON-OPEC SUPPLY GROWTH: THEORIES

- GEOLOGY
  - HUBBERT AND PFC

- DIMINISHED ACCESS

- 1998 PRICE COLLAPSE

- M&A DISTRACTION
  - OR LNG, GTO, TAR SANDS, ETC.

- 3 COUNTRIES ACCOUNT FOR 2/3S OF CHANGE IN TREND!
  - ARGENTINA, COLOMBIA, UK
  - ALL ARE TRYING TO RECOVER
DIMINISHED GROWTH
NON-OPEC NON FSU ANNUAL CHANGE

![Graph showing annual change in TB/D from 1970 to 2000. The x-axis represents years from 1970 to 2000, and the y-axis represents TB/D. The graph shows variations in production over the years.]
## NON-OPEC CHANGE (TB/D)

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**BIG SHIFT IS 1998: WHAT A COINCIDENCE!**
WHERE’S THE FLOOR?

WHEN DOES OPEC START TO CUT?
- BELOW $50, $40?
- RATE OF DROP

WILL TRADERS KEEP GOING?
- FUNDS PULLING OUT
- PEOPLE GAMBLE ON FUNDS PULLING OUT
WHAT TO DO...

- EXPECT A WILD RIDE
  - BEHAVIOR SHOULD REFLECT APPROPRIATE RISK TOLERANCE
  - GO LONG IN BUMPER STICKERS
- PRICES OVER $35 MORE LIKELY THAN BELOW, BUT $25 NOT IMPOSSIBLE
- SPECULATIVE SENTIMENT REMAINS A THREAT, DOWN AND UP
- OH, YEAH, HIRE MORE CONSULTANTS