

Directions:

1. Demonstrate evidence of close reading.
2. Highlight your confusion.
3. Answer the four questions at the bottom of the page.
4. Write a 1+ page reflection in your WN.

As Oil Giants Lose Influence, Supply Drops

Source: New York Times 9/17/08

Note: This week's article is an editorial

Oil production has begun falling at all of the major Western oil companies, and they are finding it harder than ever to find new prospects even though they are awash in profits and eager to expand.

Part of the reason is political. From the Caspian Sea to South America, Western oil companies are being squeezed out of resource-rich provinces. They are being forced to renegotiate contracts on less-favorable terms and are fighting losing battles with assertive state-owned oil companies.

And much of their production is in mature regions that are declining, like the North Sea. The reality, experts say, is that the oil giants that once dominated the global market have lost much of their influence — and with it, their ability to increase supplies.

“This is an industry in crisis,” said Amy Myers Jaffe, the associate director of Rice University’s energy program in Houston. “It’s a crisis of leadership, a crisis of strategy and a crisis of what the future looks like for the supermajors,” a term often applied to the biggest oil companies. “They are like a deer caught in headlights. They know they have to move, but they can’t decide where to go.”

The sharp retreat in all of the commodities’ prices over the last month, about 20 percent, reflects slowing global growth and with it reduced demand for more oil in the short term. But over the next decade, the world will need more oil to satisfy developing Asian economies like China. The oil companies’ difficulties suggest that these much-needed future supplies may be hard to come by.

Oil production has failed to catch up with surging consumption in recent years, a disparity that propelled oil prices to records this year. Despite the recent decline, oil remains above \$100 a barrel, unimaginable a few years ago, causing pain throughout the economy, like higher prices at the gas pump and automakers posting sizable losses.

The scope of the supply problem became more clear in the latest quarter when the five biggest publicly traded oil companies, including Exxon Mobil, said their oil output had declined by a total of 614,000 barrels a day, even as they posted \$44 billion in profits. It was the steepest of five consecutive quarters of declines.

While that drop might not sound like much in a world that consumes 86 million barrels of oil each day, today’s markets are so tight that the slightest shortfalls can push up prices.

Along with mature fields, the companies have contracts with producing countries whose governments allocate fewer barrels to oil companies as prices rise.

“It has become really, really difficult to grow production,” said Paul Horsnell, an analyst at Barclays Capital. “International companies have a portfolio of assets in areas of significant decline and no frontier discoveries to make up for that.”

As a result of the industry’s troubles, energy experts do not expect oil supplies to grow this year in countries outside the Organization of the Petroleum Exporting Countries. Global demand for oil is expected to expand by 800,000 barrels a day, mostly because of rising demand in China and the Middle East, despite lower consumption in developing countries.

This imbalance between supplies and demand will be one thing that OPEC ministers will consider when they meet next month to decide whether or not to increase their production. OPEC has about 2 million barrels a day in untapped capacity that its members control.

The new oil order has been emerging for a few decades. As late as the 1970s, Western corporations controlled well over half of the world’s oil production. These companies — Exxon Mobil, BP, Royal Dutch Shell, Chevron, ConocoPhillips, Total of France and Eni of Italy — now produce just 13 percent. Today’s 10 largest holders of petroleum reserves are state-owned companies, like Russia’s Gazprom and Iran’s national oil company.

Sluggish supplies have prompted a cottage industry of doomsday predictions that the world’s oil production has reached a peak. But many energy experts say these “peak oil” theories are misplaced. They say the world is not running out of oil — rather, the companies that know the most about how to produce oil are running out of places to drill.

“There is still a lot of oil to develop out there, which is why we don’t call this geological peak oil, especially in places like Venezuela, Russia, Iran and Iraq,” said Arjun Murti, an energy analyst at Goldman Sachs. “What we have now is geopolitical peak oil.”

Western companies are far better than most national oil companies at finding and extracting petroleum, experts say. They have developed advanced exploration technologies and can muster significant financing to develop new fields. Many of the world’s exporting states, however, have spurned their expertise.

Oil company executives see a straightforward explanation: a trend known as resource nationalism. They contend that they have been shut out of promising regions by a rising assertiveness in the Middle East, in Russia, in South America and elsewhere by governments determined to keep full control of their oil.

Even in places where they are allowed to operate, the Western oil companies face growing problems. Countries like Russia, Algeria, Nigeria and Angola have recently sought to renegotiate their contracts with foreign investors to capture a bigger share of the profits.

“The problem with the supply side of the equation is a problem of accessing the resources in the ground so they can be explored and developed,” Rex W. Tillerson, the chairman of Exxon, said in a recent interview. “That’s a political question where governments have made choices.”

This sense of being hemmed in helps explain why the Western oil companies want more offshore drilling in the United States. They see it as one of their few options.

These companies have also tried to diversify. They have turned to natural gas as a profitable source of growth. They are tackling hydrocarbon resources, like deep-water reserves, heavy oil or tar sands. And some companies, like Shell and BP, are investing in renewable fuels.

Unquestionably, the oil companies could have done more. They failed to invest heavily in exploration after the oil-price collapse of the mid-1980s, which lasted through the 1990s.

In 1994, the top five oil companies spent 3 percent of their free cash on share buybacks and 15 percent on exploration. By 2007, they were spending 34 percent of their free cash on buybacks — in effect, propping up their share prices — and a mere 6 percent on exploration, according to figures compiled by a team led by Ms. Jaffe and Ronald Soligo of Rice University. As a result, some experts warn that supplies will fall short of the demand over the next decade, perhaps sending prices well above today’s levels.

At a recent conference in Madrid, Christophe de Margerie, the chief executive of the French company Total, said the world would be hard-pressed to raise supplies beyond 95 million barrels a day by 2020. Only a few years ago, forecasters expected 120 million barrels a day by 2030, a level many analysts now view as unrealistic.

The major companies picked up their capital spending around 2005, although much of the increase has been offset by the soaring cost of development. Exxon, for example, expects to spend about \$25 billion annually for the next three years to expand its business, compared with \$15 billion a year from 2002 through 2006.

“It’s amazing the difference from the 1970s, where a lot of money went into exploration, development and production of new resources,” said Paul Stevens, a senior research fellow at Chatham House, a London policy research organization. “It is happening a little bit now, but it is not going to be enough.”

As the power and clout of Western companies erode, the world may become increasingly dependent on government-controlled entities for oil.

While some may be up to the task, like Saudi Aramco, others, like Petróleos de Venezuela, suffer from bureaucratic inefficiencies and political interference.

“We are going to depend on the Venezuelan, the Nigerian or the Iranian oil companies for the future of our oil supplies,” said Bruce Bullock, the director of the energy institute at Southern Methodist University. “This is a troubling trend.”

What is the author’s thesis (main point)? State in one sentence:

List three writing strategies the writer uses to make his argument:

What is the author’s purpose?

Who is the intended audience?