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Socialist Oil Death Spiral

By Richard W. Rahn
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Socialism always plants the seeds of its own destruction, and state-owned oil is no exception. Most people do not realize that about 90 percent of the world's liquid oil reserves are controlled by governments or state-owned companies. Exxon Mobil, the world's largest privately owned oil company, owns only 1.08 percent of the world's oil reserves, and the five largest private global oil companies together own only about 4 percent of the world's oil reserves.

There is enough liquid oil in the ground to last generations; and when oil sands and oil shale are included, there is enough oil to last centuries. If there were a truly free market in oil, with both the reserves and production owned and controlled by many competitive companies, the price of oil would be a fraction of today's price.

The high price of oil is a direct consequence of artificial supply constraints imposed by the Organization of Petroleum Exporting Countries and other countries, including the United States, and the incompetence and mismanagement found in most state-owned oil companies. OPEC is an international government cartel made up of Iraq, Iran, Kuwait, Libya, Angola, Algeria, Nigeria, Qatar, Saudi Arabia, the United Arab Emirates and Venezuela. These nations control about 77 percent of the world's known liquid crude oil reserves.

Most of these countries and other major oil producers that rely on mainly state-owned companies, such as Russia, have underinvested in exploration and development of new production facilities and mismanaged the ones they have. (If politicians understood the facts and were truthful, they would rant against "greedy" socialists rather than private oil companies.)

Venezuela, despite having perhaps the sixth-largest oil reserves in the world, has falling production because of the mismanagement by the Chavez government. Mexico also is suffering from falling oil production because the government refuses to allow private oil exploration and production companies, and the state-owned oil company, Pemex, is corrupt and incompetent. By contrast, the U.S. only has about 2 percent of the world's oil reserves, but produces little more than 8 percent of global production, largely because they are privately owned and managed.

A decade or two from now, the socialist states will have severe regrets for their current misbehavior, and this is why. When prices rise, people seek alternative sources and substitutes for the high-priced commodity. When oil prices are above $30 or $40 a barrel, suddenly the Canadian oil sands and Colorado oil-bearing shale become economic, and those reserves are larger than known liquid oil reserves.

The short-run problem is that development of oil sands and oil shale requires enormous up-front investment and many years. Canadian oil sand production is now ramping up rapidly, but it will be a few years before it can replace most of North America's needs for oil from outside the continent.

Recently, there has been additional good news. Shell Oil has announced its new in-situ (i.e., in-ground) extraction technology in Colorado could be competitive at prices of more than $30 per barrel. However, it will take quite a few years to get into major production.

Despite the current infatuation with biofuels, they are unlikely to ever produce more than a small share of the market because they are not price competitive with liquid, sand and shale oil when all attendant costs are taken into account, such as higher food prices. Petroleum accounts for about 40 percent of U.S. energy supply and about two-thirds of it is imported. Most petroleum is used for transportation, which accounts for about 28 percent of U.S. energy use.

Now, for the really good news. The new car you purchase a decade from now is almost certainly to be totally electrically powered. Huge strides are being made in battery technology, and even existing batteries have just about reached the point where they are sensible for automobiles. Mitsubishi has just come out with an all-electric car, the sport MIEV. And Nissan and Renault have announced they will be in full-scale production of electric cars by 2012.

As people move to electric cars, the need for gasoline and imported oil will quickly disappear. Nuclear and clean coal plants must expand to produce the additional electricity, but they produce energy at a fraction of the cost of petroleum. The new battery technology will also help solar and wind power become more economically feasible because they will be able to store it. Even so, solar and wind will only be a small part of our energy future because of their inherent production limits.

In sum, a decade from now, the world will no longer be held hostage by the socialist OPEC cartel. Liquid fuels (oil) are mainly needed for transportation; but when electricity takes over much of that market, America, Europe, China and Japan will find they can produce all of the electricity they need from nuclear, coal, hydro, biomass, geothermal, solar and wind resources.

North America will also be independent from foreign oil because of the oil sands and oil shale developments, which are likely to be protected from drastic reduction in world oil prices. OPEC and its fellow travelers will be left with a far less valuable commodity, because their present, shortsighted, high oil price strategy is causing their customers to develop economically and environmentally sound alternatives more quickly than if there had been a truly global free market in oil.

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