Shifts in the Geopolitical Landscape and Their Impact on Petroleum Sector Capex Strategies

Golden, CO
April 14, 2016

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Chaos Prevails

“Venezuela Data Shows World’s Top Inflation”

“Putin’s Targeted Strike – The Meaning of Russia’s weapons sales to Iran”

“Russia Wins Policy Points. Now What?”

“China Defends Efforts to Create Official Islands in Disputed Seas”

“Obama Courts Chaos with His Taliban Fantasy”

“Europe’s Energy Escape Valve: U.S. Gas”

“Rise Of The Regional Hegemons - Russia, Iran and China are Advancing as The U.S. Retreats”

“Moscow Acts to Unblock China Financing”

“Uncle Xi’s Bear Market”

“Al Qaeda helps Pro-Saudi Forces in Yemen”

“What’s Lost in Iranian Nuke Deal – Middle East Nations are Arming to Kill with Conventional Weapons”

“Saudi Arabia Won’t Come to Oil’s Rescue”
Figure 2

Expect the Unexpected

- China chills German economy (et al)
- Venezuela assembly head pulls no punches (nor does Maduro opposition)
- Russia disrupts (Baltics, Ukraine, Syria, IPO’s, etc.)
- Saudi Aramco actually launches its IPO (upstream? downstream? petrochemicals?)
- Rapprochement between Iran and Saudi Arabia in 2016 (subject to five very unlikely conditions)
- WSJ Oil poker: “Why Saudi Arabia won’t fold” (yet?)
- Iran’s influence over Iraq escalates significantly

The possible positives could translate into another self-defeating “V-Shape” recovery
“Arab Spring” Has Morphed Into “Winter”

A virtual Cold War condition now exists between Saudi Arabia and Iran
Figure 4
Overlapping Energy Power Triangles

Historical view: To US and West
Toward a New Realignment of Interests

Figure 5

U.S. Oil Production by Type in New Policies Scenario

Note: The World Energy Model supply model starts producing yet-to-find oil after it has put all yet-to-develop fields into production. In reality, some yet-to-find fields would start production earlier than shown in the figure.

Toward a New Realignment of Interests

Top Three World Oil Producers

Source: EIA. Russia production includes crude oil and other liquids.
Figure 7

World Events and Oil Volatility – Nominal Pricing (1971 – 2016 YTD)

- 1973 Arab Oil Embargo
- 1978 Iranian Revolution
- 1979 Shah deposed
- 1980 Saudis abandon "swing producer" role; oil prices collapse
- 1990 Iraqi invasion of Kuwait
- 1991 Gulf War ends
- 1999 Iranian oil in production precipitates the decline
- 2001 Prices rise sharply on OPEC cutbacks, increased demand
- 2011 Back from the abyss
- 2014 Fiscal Cliff fallout concerns
- 2015 Syrian civil war escalates
- 2016 ISIS on rise
- 2017 Russia challenges Ukraine
- 2018 Saudis considering partial sale of Saudi Aramco?

Source: EIA.
Figure 8

Toward a New Realignment of Interests

Oil Supply Overhang in Perspective

Global Oil Demand / Supply (MMBopd)

Historical
Projected

Global Supply
Global Demand

Demand is Greater than Supply
Supply is Greater than Demand

Source: EIA.
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Elimination of the ban on U.S. oil exports is ultimately a development with price containing potential.
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“Following Oil” – Key Lessons Learned

- Markets continuously endeavor to work, but in their own time and at their own pace
- Flawed economic and policy incentives ultimately cause or exacerbate supply shortfalls (or sometimes even create undesirable surpluses)
- Black swan events entail especially noteworthy risks
- It is often darkest just before the dawn
- Powerful regenerative economic forces result from the application of well-incentivized capital focused on high-priority societal problems or needs
- Periodic consolidation and reorganization (via mergers and sales) are integral to the evolving natural order of the petroleum-sector economy
- Shifting global macro-economic drivers can overwhelm even a well-executed plan and thus necessitate midcourse adjustments in strategy for both corporate players and national entities
- Old geopolitical grudges tend to reemerge, often at inopportune times and with adverse consequences (Ukraine, Syria, South China Sea, China/Japan)