New American

Written by Bob Adelmann on October 11, 2016

Saudi Energy Minister: Crude Oil at $60 Not "Unthinkable"

Saudi Arabia's energy minister, Khalid al-Falih, asserted at the World Petroleum Congress in Istanbul on Monday that he is optimistic that members of the OPEC cartel will agree on production cuts at its meeting in late November, and that it isn't "unthinkable" that as a result, crude oil prices could hit $60 a barrel by the end of the year.

Following late September's informal meeting when the cartel agreed to appoint a committee to come up with options in time for the Istanbul meeting, energy traders drove the price of crude above $50 a barrel. On Monday it nearly touched its highest level for the year, reacting to Russian President Vladimir Putin's support for OPEC's possible cut in crude oil production to "stabilize" the market.

Such a production cut, if it takes place (OPEC members are notoriously fickle about keeping solemnly-pledged agreements), would be designed to push crude oil prices higher, but still low enough to keep "rivals from raising their output," according to OPEC's secretary-general following the September meeting in Algeria.

That's going to be a trick, according to a conversation *The New American* had with a top official at Sanchez Oil and Gas Corporation located in Houston. According to that official, new technology keeps driving break-even points ever lower — so low that even his conservative company is looking at restarting some rigs. He said that OPEC tried to play a game with American producers by flooding the market and driving prices down so low that many of them would leave the field. "They hurt us," he added, "but they also hurt themselves, perhaps more than they anticipated."

{modulepos inner_text_ad}

Even though Saudi Arabia's lifting costs for its state-owned Aramco oil producer is around $5 a barrel, the drop in crude from $100 a barrel to $50 "has cost them dearly. They have lots of bills," said the official.

Indeed they do. Saudi Arabia's young people are suffering under painfully high unemployment, despite the massive welfare state that the country has installed when oil prices were high and profits were massive. Today the country is deep in the red and has seen its gigantic foreign currency reserves melt away by a third. Cutting those welfare benefits is the last thing the rulers want to do, but they have been forced to as their plan to drive oil prices down hurt their own interests at least as much as it did the Americans.

Working against the nascent plan by OPEC is the reality that at current levels, those American companies can produce at a profit. For instance, Anadarko's CEO Al Walker said in July, when oil was in the 40s, that "a sustained $50/b oil price is likely to emerge as we move into 2017 [which] will provide the necessary cash margins and cash … improvements [that will] encourage us to accelerate activity."

For Hess Oil, that moment wasn't far off, either. It has been driving down operational costs so far that "when oil prices approach $60/b, we'll begin to ramp up activity, starting with the Bakken Shale [Formation lying beneath Montana and North Dakota]."

Two weeks earlier, ExxonMobil confirmed "a world-class discovery well [about 120 miles offshore of Guyana] with a recoverable resource of between 800 million and 1.4 billion oil-equivalent barrels. "

Natural resources consulting firm Mackenzie Wood said that more production is coming online even with oil prices well under $60. A total of 13 million barrels per day of new supply could hit the markets in less than 10 years, said the firm, adding: "This is more than at any point since 2009 and 1.5 million barrels per day more than a year ago. The place where the action is taking place is in the U.S. in … tight oil plays [shale formations where producers] have made tremendous productivity gains."

That's what caused the Saudis to miscalculate, according to the Sanchez oil executive: "They underestimated our ability not only to produce, but to produce profitably even at these lower levels. That caught them by surprise."

He added that he wouldn't be surprised to see oil back above $100 a barrel, but not in the immediate future. There's just too much incentive for U.S. producers to put rigs back into operation at present levels. The problem then would be finding and hiring enough capable roughnecks to bring them back online.

A graduate of an Ivy League school and a former investment advisor, Bob is a regular contributor to The New American *magazine and blogs frequently at LightFromTheRight.com, primarily on economics and politics. He can be reached at badelmann@thenewamerican.com.*

Related article:

Reality Sets In: OPEC Ready to Cut Production to Raise Oil Prices