Oil price hike can't raise U.S. production

by Steve Parsons

When gasoline prices suddenly shot up in August, irate motorists and oil-dependent industries immediately fingered the oil industry for what everyone suspected was a huge rip-off.

There is no doubt that major oil companies like Royal Dutch Shell, British Petroleum, and Exxon have profited from the oil price windfall. These firms have integrated operations that span oil exploration and drilling, to refining and retail marketing. They also have sophisticated financial subsidiaries speculating on the world spot and futures markets. This insulates the majors from volatile price swings, and enables them, largely, to control petroleum prices for everybody else.

But it is another story for independent U.S. oil producers, the small companies and individual entrepreneurs whose existence is determined solely by the shrinking margin of profit they make in producing the crude oil and natural gas that other companies refine.

The collapse of oil producers

Independent oil producers explore and drill an astounding 85% of the wells in the United States, producing 50% of domestic crude oil and 60% of natural gas. It is a high-risk business. Much of their investment often winds up in "dry holes" that produce little or no oil and gas, and no revenue. For these people, the price of oil and gas must offset not only costs of production, but losses incurred in finding and developing that production.

Without independents, there would be almost no U.S. oil production. With some exceptions, concentrated in larger oilfields, the major oil companies have little interest in investing so much money for so little return, preferring to buy the field or the oil from the independents, and making their profit downstream. Since the 1960s, the majors have increasingly gone abroad to get their oil, at cheaper prices and far less financial risk.

But the U.S. oil-producing industry, and related service and equipment sectors, have collapsed.

Even if the price of oil were to zoom to $100 a barrel, there could be no "oil patch" boom like those from the price surges in the 1970s. That is because the producers and support industries have been crippled over the last five years, in a depression caused by falling oil and gas prices, compounded by insanely punitive federal tax measures.

Since 1984-85, when the industry's production peaked, U.S. crude oil production in the lower 48 states has fallen to its lowest level since the early 1950s. Drilling rig utilization has plunged from an all-time high of more than 4,500 in 1981, to only around 1,000 now—just barely above the all-time low. The number of seismic crews—who explore for new fields—is at a record low, falling from approximately 725 in 1981 to an average of about 500 in 1984, to 125 this year.

Worse, "the industry infrastructure has virtually collapsed," said Conley Smith of the Independent Petroleum Association of America to a congressional committee in July. "The number of oil and gas operators of record has fallen from nearly 13,000 . . . in the early 1980s to less than 5,000 by 1989."

Shortages everywhere

The industry does not have enough trained manpower or equipment to substantially expand drilling, even with the incentive of greater profits from higher oil prices. Charles Mankin, director of the Oklahoma Geological Survey, says that "we have . . . effectively dismantled the exploration industry in this country," and estimates that two-thirds of the crews and skilled manpower have left the oil-producing and equipment industry, creating a labor shortage (see next page).

"The capacity of the U.S. oilfield service and equipment industry to accomplish things—big things like building pipelines or small things like manufacturing drill bits—has withered to about 50% of its peak a decade ago," wrote the *Wall Street Journal* in August.

"Scores of companies have vanished; they've gone bankrupt, merged or simply called it quits. The survivors have slashed budgets, cut loose most of the experienced help, and sold off equipment—or let it rust in back lots and bayous.

"Warehouse shelves are nearly empty of the mundane valves, fittings, and connectors that keep rigs running. In a few months, the industry could actually start running out of the super-strength pipe used to turn drill bits. Even ordinary earth-moving equipment and backhoes are in short supply. Repairs of sophisticated monitoring equipment that once took hours now take days. . . . Shortages are part of the daily routine on most rig sites."

Mankin stressed that "the biggest deterrent in reviving the industry is the difficulty in getting investment capital," regardless of the price of oil. The lack of liquidity in the U.S. economy precludes *any* major increase in capital for productive investment, particularly in oil and gas production, where price volatility can, overnight, turn from profits to disaster.

But even if sufficient capital were magically to become available, there could be no real boom, because most of the major domestic reserves are on public lands—like the Outer Continental Shelf, pristine Alaska, and so-called "wetlands"—which are barred from development by the greenies in our federal government.

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