THE JERUSALEM POST
JPOST.com
Israel's best-selling English daily and most-read English website

Photo by: Courtesy

›Pjmqsjdft xjmqvuVT cbdl jo sfdfttjpo cz zfbsft foefi

By AMIRAM BARKAT/GLOBES
19/02/2011

Economist Yossi Hollander sees apocalyptic consequences from the rise in oil prices, but also a great opportunity for Israel.

Current oil prices will put the United States back into recession by year's end, and a global oil crisis will break out in four to five years, according to Yossi Hollander, chairman of the Israeli Institute for Economic Planning. In an interview with Globes in advance of a session of the Herzliya Conference on rising oil prices, he explained what he believes will happen in the coming years, and why Israel has an opportunity to make large gains.

The session at the Herzliya Conference is against the backdrop of oil crossing the $100-a-barrel threshold and a forecast by the International Energy Agency published three months ago that the price per barrel will reach $200 in 2035.

Globes: National Economic Council chairman Prof. Eugene Kandel recently said that "at a certain price for oil, the world will not want the existence of Israel." Why?

Hollander: "We already know that Europe is ready to sell us oil at $70 a barrel.

There is a price at which even the US will not want our existence.

Everything has its price."

Is it not a bit simplistic to explain such a complex situation using what sounds like a mathematical equation?

"It's a progressive equation.

If you open CNN in the morning, you see that the Gulf states dominate the advertisements. So do you think CNN will continue to be objective?"

That sounds like scare-mongering. In 2008, when the price of oil reached $149 a barrel, experts declared that oil was on the way to $200. It turned out that it was a speculative bubble. Why should we believe you this time?

"There was a large decline in consumption because of the global crisis, and the price of oil fell. Then OPEC cut output by three million barrels, and the price of oil went back up. This year, we have returned to the oil consumption level of in 2008, even though the Western world is still not out of recession. The rise is attributed mainly to China, but also to other developing countries, like India and Brazil. On the other hand, output is not managing to exceed the record set in 2005 of 87 million barrels a day."

But the price is set artificially by a cartel, OPEC, which limits output. If the price were determined in a free market, it would presumably be lower.

"This argument held true until now. All the oil crises to date resulted from reductions in output caused intentionally, as in 1973, or unintentionally, such as in the revolution in Iran in 1979. This time, for the first time in history, the cause of the rise in oil prices is the increase in demand, while it is clear that growth in supply cannot keep pace.

"OPEC still has spare capacity, but no one knows how much exactly. According to the most optimistic estimates, OPEC can increase production by six million barrels per day. China increases its demand every year by two million barrels a day, so the question is not whether the spare capacity of OPEC will be exhausted, but when it will be exhausted – in two years, or in five years."

But as the price of oil goes up, the incentive to discover and develop new fields, such as in the Arctic, grows accordingly.

"There's a great deal of talk about the potential for oil discoveries in the Arctic, but so far nothing has been found there. Two years ago, in Brazil, an oil field was discovered that is considered the largest oil discovery in the past 40 years. Just to put it in proportion, the amount of oil in this field can meet global demand for 100 days in all. But what emerged? That the development costs are so high, that it is worthwhile developing the field only at a price of more than $70 a barrel. Six months ago, someone was found who will finance development of the field, and it will be another seven years before oil starts flowing from it.

"On the other hand, only in the last 18 months, China has increased its oil consumption by three million barrels per day. The Chinese, with their five-year plan, now talk about transferring 250 million people from the country to the city. That means 50 million people who will start using public and private transport, thus increasing China's oil consumption."

But the oil price rise makes oil production from nonconventional sources, such as oil shales, worthwhile. Canada, for example, has reserves of oil from tar sands almost amounting to those of Saudi Arabia.

"Oil-shale production is worthwhile only at over $200. Tar-sands oil production in Canada is worthwhile only above a price of $60 to $65 dollars a barrel, and it causes severe damage to the environment. But the main problem is that, in order for Canada to be able to produce oil in the quantities needed to make up the shortfall, huge investments of money, time and water will be required.

The question is, what will happen in the meanwhile?" And what will happen, in your opinion?

"Oil prices will continue to rise. I'm not prepared to commit to a price, but it will be much higher. In the near term, the global economy will be hit hard. Empirically, the US economy has entered a recession every time US national spending on oil has crossed the line of 4 percent of GDP. Four percent of US GDP is equivalent to about $80 dollars a barrel. That means that if oil prices remain above $80, the US will enter a recession by year's end."

China will take care of itself "In the longer term of the next four to five years, a global oil crisis is expected.

It will begin in less stable places. China will know how to take care of itself; it has $2 trillion. But countries without the economic ability to buy oil, or the military capability to take over oil supplies, will simply remain without oil. African countries like Kenya, which a year ago spent 150% of its trade deficit on petroleum procurement, will drop out of the market completely. In this situation, there is no fuel for transportation, no fertilizers and no pesticides.

People will die of hunger, because the land cannot sustain them all."

In your view, does that also explain what is happening today in Egypt?

"They say that the rise in food prices in Egypt was the straw that broke the camel's back. There is an absolute correlation between the price of food and the price of oil. Not long ago, it was reported that countries like Saudi Arabia were stockpiling food so that it would not happen to them. The Saudis are buying sugar to raise the price of ethanol, which is an alternative to oil. China is building strategic oil stocks, and according to estimates, one third of the increase in oil demand in China was for this purpose. The Chinese understand that the price of oil will go up."

Would you recommend Israel to build a strategic oil reserve?

"Definitely."

Have you taken into consideration the introduction of renewable energy sources for power

generation?

“Oil is used for transportation and not for power generation; this is one of the most common mistakes people make. Only 1% of the power in the US is produced with oil. Even if all the world’s electricity production were from renewable energies, that would barely reduce oil demand 5%. Electricity and transportation are two separate worlds.”

Not when it comes to electric cars.

“I have an electric car.

Today the world produces 70 million cars a year. Suppose all of them will be electric.

This requires raising battery production capacity 4,000 times. That’s a process that will take 20 to 30 years.”

What else would you recommend for Israel?

“We have a very interesting opportunity. We discovered natural gas, and the intention is to use it to generate electricity.

But in my opinion, it makes much more economic sense to use the gas for oil alternatives such as methanol. Today, Israel spends $7 billion a year on oil.

Each price increase of $10 a barrel is another $700 million to $800 million.”

“The government [recently] passed a decision to develop oil substitutes,” Hollander says. “That could be an amazing market for Israel, because the world oil market today is worth $2.5 trillion dollars, and it will be twice that if oil reaches $150 a barrel. Therefore, any Israeli invention or development will bring very high returns.

“Moreover, the fact that there will be research and development infrastructures for oil substitutes puts us in a very good position. The Germans and Americans see the great crisis coming sometime between 2013 and 2017.

When the panic starts, we will be in the right place, and investment will pour in as never before.”

Print Back to original article

About Us | Advertise with Us | Subscribe | RSS

All rights reserved © 1995 - 2011 The Jerusalem Post.