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QUESTION:
WHAT IS WORSE THAN CRUDE OIL AT $US100 PER BARREL ?
ANSWER:
A SUDDEN AND MATERIAL DROP IN THE CRUDE-OIL PRICE

Regardless as to how badly and/or how long a US economic downturn/slowdown/recession affects the world stage, it will make only limited difference to the world's seemingly unquenchable thirst for oil.

The pace of progress of the emerging markets of the world, especially those of the People's Republic of China (PRC) and India, will, most likely, continue and the increasing requirement from energy is unlikely, in the next 5 years or so, to dissipate.

A pronounced increase in the energy requirements of the emerging markets of the world, in addition to those of the PRC and India, guarantees that the price of crude oil will easily break through the $US100 per-barrel level – and stay at those high levels.

The world has been slow off the mark, thus far, to create sufficient renewable energy sources so as to take the edge off the fast rise in the price of crude oil.

Even the oil refineries of the world have been caught, flat-footed for the most part.

Renewable energy, created from the sun, the wind, waves, photovoltaic cells, etc, basically remain in their infancy as far as being commercially viable at this juncture although in territories, such as The Cook Islands, solar energy is powering small houses, during the daylight hours.

The price of crude oil has risen by about 400 percent between 2002 – when the cost of a barrel of crude oil was about $US20 – and today.

Due to the weakness of the US dollar vis-à-vis most other *'hard'* currencies of the world, not every country has suffered to the same extent due to the vagaries brought about by the rapid, oil-price increase, which has been exacerbated by the weak translation value of the once, almighty greenback.

The euro, as an example, has appreciated against the US dollar to the record high of $US1.4730, while the British pound stands at a 26-year high to the US dollar at about $US2.107.

On adjustment, therefore, taking into consideration the de facto appreciation of the euro vis-à-vis the US dollar, the international oil-price increase, in euro terms, is reduced to about 300 percent instead of 400 percent.

Similar adjustments could, also, be made for the British pound.

It is likely that the euro will continue to appreciate against the US dollar and one should not be surprised to see the euro hit $US1.50-plus before the year is out.

So, while the phenomenon of the de facto appreciation of the euro against the US dollar may *'soften'* the impact of rising crude-oil prices for Europeans, at the same time, it cuts a swath through the competitiveness of this part of the world for its goods and services.

Better, one may like to conjecture, would be for the price of crude oil to be quoted in euros or sterling than in US dollars?

The US dollar, for donkey's years, has been the preferred, international currency of commerce, but questions must be raised as to whether or not the time is approaching for the world to change, or modify, somewhat, its thinking about the US dollar as being the preferred international currency of commerce.

It was only a year or so ago that the translation value of the Canadian dollar was at a 17-percent discount to the US dollar: Today, the Canadian dollar, on foreign-exchange markets, is being quoted at about a 7-percent premium to the US dollar.

However, one must bear in mind that the US economy is, still, the largest and most-important single economy of the world.

This situation is unlikely to change in a hurry.

At the same time, however, the US has lost a great deal of its standing, internationally, especially in the industrial sector of its economy: Its motor-vehicle industry has been almost completely usurped by Asian producers for fuel-efficient vehicles while Europe has taken the lead for quality produced vehicles, from buses to multi-purpose vans to luxury motor cars.

The US economy, at the same time, leads the world in respect of high-technology goods and services; and, it is likely to continue to hold this position for the foreseeable future.

Enterprising US companies are exporting know-how to other parts of the world and this is paying large dividends because, on their home turf, it is difficult for US industry to compete with low-cost countries in Eastern Europe and Asia.

Joint ventures and/or taking minority equity stakes, for many a US corporate enterprise, has been proven to be a good and continuing source of material income, allowing the US enterprises *'to ride'* on the back of its foreign partners.

Where the US has been dragging its feet is in investments in oil refineries, the search for more commercial oil fields, and renewable energy sources to supplant fossil-fuels.

Much of that which ails the world, today, is a direct result of these historic oversights.

In 2002 when the price of crude oil appeared to be breaking through the $US20 per-barrel level, it was strongly assumed that the price of crude oil would settle down in due course and return to *'reasonable'* levels.

As such, it appeared to make little financial sense, in 2002, to invest heavily in new refineries or increase, where possible, output at existing refineries.

That was the consensus at board level of most US and European energy companies in 2002.

Today, those same *'thinkers'* rue the day that they took that line of reasoning.

While it was very evident, as far back as 2 decades ago, that the PRC was about to blossom with the adoption of a modified, market-driven economy, many people in the West failed to realise the significance of the rapid rise of the economy of this Asian Communist country.

Too late did US industrialists learn how they could not compete successfully against the low cost of labour and land in the Middle Kingdom.

Likewise, too late did Detroit, Michigan, realise that the second-largest economy of the world, namely Japan, would usurp the hallowed position, held by the US in the development and manufacture of motor vehicles.

With the rapid rise of the economies of Asia, the thirst for oil exacerbated to historic levels.

And that is the situation as it stands, today.

And that is one of the chief reasons that the price of oil is more than likely to crack the $US100 per-barrel level in short order.

That is not the end of the story, however.

Political tensions over the past 5 years, especially, has caused an imbalance in crude-oil production.

Today, questions are being posed about the Government of Iran and whether or not this fundamentalistic Muslim country will determine to try *'to punish'* the West for the economic sanctions that have been imposed on the country due to the Iranian Government's refusal to halt its *'irreversible'* production of nuclear technology, which is seen by the West to be a precursor to the manufacture of weapons of mass destruction.

Iran's principal oilfields are located at the head of The Persian Gulf in the south-western region and are considered among the richest in the world.

Reserves are estimated at 92.80 billion barrels, sufficient to maintain present production levels for more than the next 70 years.

Iran, also, has one of the largest reserves of natural gas of any country, amounting to 12.60 percent of the world's total reserves.

The country is the second-largest oil producer in the world.

The US and many other western countries fear Iran should the country manage to become a nuclear power, such as India and Pakistan.

Unlike North Korea, which, only one year ago, was on the threshold of becoming another nuclear power in Asia, hung out the *'for sale'* sign and agreed to dismantle its nuclear facilities in exchange for oil and food, Iran is a different situation – because it is not for sale at any price.

If push comes to shove, the Government of Iran could well make life difficult for the Western World by simply cutting off its oil exports to the West and blockading the vital sea links.

If the US and its allies determine to threaten war with Iran, it would only make worse an already difficult situation.

The psychological effect of such a threat, however, would drive up the price of crude oil by another 10 percent, overnight.

Stand by for crude oil at $US110 per barrel!

On the other hand, as things stand today, there is a concerted effort by the West to guarantee that Iran never has the ability to perfect nuclear technology to the stage of being able to manufacture weapons of mass destruction.

The Government of Iran stands pat, stating that the country must have nuclear power, regardless of the threats from the West.

One has to pray that diplomacy will succeed without the requirement of another war.

The Other Side Of The Picture

The only thing worse than crude oil, at $US100-plus per barrel, is a sudden and material collapse in the price of the black ooze.

If the price of crude oil were to fall by, let us say, 20 percent within a very short period of time, there would be utter chaos on the financial markets and equity markets, around the world.

Venezuela, Saudi Arabia, Norway, Russia, the United Arab Emirates and a number of other Middle Eastern countries have accumulated, over the past few years, huge and, hitherto, unbelievable fortunes.

Using their oil wealth, these countries have imported machinery and equipment to the benefit of the producing countries – the US, members of the European Union, the United Kingdom, etc.

Also, these oil-rich countries – excluding Venezuela – have invested in US-dollar denominated bonds and other negotiable instruments.

Thus emerged what are commonly referred to today as sovereign funds.

These are massive amounts of money, much of which is injected into corporate entities, owned by sovereign governments, a large percentage of that money, looking for a home where there is a satisfactory return.

The Singapore Government, as an example, makes use of a number of corporate entities in order to make investments abroad.

One such entity is Prowell Ventures Pte Ltd, a Singapore-domiciled corporate entity, owned by this authoritarian government, which takes minority positions in various companies, some of which companies, seek a public listing.

One of the companies in which Prowell Ventures Pte Ltd took a minority position was in DaChan Food (Asia) Ltd (□) (Code: 3999, Main Board, The Stock Exchange of Hongkong Ltd).

Prowell Ventures Pte Ltd, today, has a 5.88-percent stake in this Taiwan-controlled company which, last September, pitched its Initial Public Offering in the Hongkong Special Administrative Region (HKSAR) of the PRC.

Due to the strength of the US economy, the rise in the price of crude oil, from about $US20 per barrel in 2002 to nearly $US100 per barrel, today, has made only little ripples in the largest single economy of the world.

But the situation, today, is that the economy of The Land of The Free and The Home of The Brave faces forced retrenchment.

When the US economy was firing on all cylinders, foreign investors cultivated a taste for US-dollar denominated assets.

That appetite for such investments has since waned.

That is one of the main reasons for the US dollar’s translation value to have fallen, dramatically, against other *‘hard’* currencies, of late.

If the price of crude oil comes off too much too quickly, it is highly probably that large-scale investments will be withdrawn from the US in order to put a financial finger in leaking, sovereign-fund dykes.

This would, most likely, create havoc on international money markets and equity markets, the likes of which the world has never witnessed in the past.

Chaos would ensue, to be sure.

And World War III – an oil war to end all oil wars – could well be the result of this chaos as Armageddon becomes, once more, the watchword from one country’s capital city to the next.

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