Let’s Sweat It Out, Again

By BILL WADE, *Wade & Partners*

(12/29/11) The high stakes standoff between Iran and the U.S. over the Strait of Hormuz, the passageway for one-fifth of the world's oil, was inflamed Thursday when Iran's navy claimed to have recorded video of a U.S. aircraft carrier entering the Port of Oman. "If they (the West) impose sanctions on Iran's oil exports, then even one drop of oil cannot flow from the Strait of Hormuz," Salami said on state TV. On Wednesday, the U.S. Fifth Fleet said it would not tolerate any disruption of the strait. If push comes to shove, what would a military confrontation in the strait look like… and how would it affect oil prices worldwide?

Our ongoing oil shortage is a prime example of bureaucrats trying to steer the economy at a macro level while being willfully blind to the complexities of the micro level. Government intervention (by definition) results in non-economic decisions.

Well of course it does, with the special interest buzzards continuing to rip the flesh off two more promising domestic oil projects while the Iranians threaten military action in the Straights of Hormuz.

Does Anyone Care about Real Oil Independence?

The Keystone Pipeline System will transport synthetic crude oil and diluted bitumen ("dilbit") from the Athabasca Oil Sands in northeastern Alberta, Canada to multiple destinations in the United States. These include refineries in Illinois, Cushing oil distribution hub in Oklahoma and proposed connections to refineries along the Gulf Coast of Texas.

The Keystone XL has faced lawsuits and criticism from environmentalists and some members of the United States Congress. The U.S. Department of State in 2010 extended the deadline for federal agencies to decide if the pipeline is in the national interest, and in November, 2011, President Obama postponed the decision until 2013.

The Bakken formation occupies about 200,000 square miles of the subsurface of the Williston Basin, underlying parts of Montana, North Dakota and Saskatchewan. Various estimates place the total reserves at up to 24 billion barrels … bigger than Alaska’s.

New rock fracturing technology available starting in 2008 has caused a recent boom in Bakken production. By the end of 2011 oil production rates will reach nearly 600,000 barrels per day, outstripping the capacity to ship oil out of the Bakken.

Both Projects Are Political Footballs

Like earlier prophets of doom, today’s Washington establishment — both parties — fail to appreciate capitalism’s ability to adjust and innovate. They concentrate on negatives, real or imagined.

As I follow the Sunday morning political gabfests, it is clear that the coming election has focused the electorate on three issues:

1. Jobs and Unemployment
2. Middle East Involvement
3. Building an Economy that Lasts

Development in just the Bakken could lead to an estimated two million jobs — quickly. Output from the XL pipeline could drop our oil dependence to less than 40 percent of total needs, while we become a net exporter of energy with the tremendous amount of natural gas freed up … with no ANWR drilling!

Although we are the third largest crude oil producer, about half of the petroleum we use is imported. Some are surprised to learn that 49 percent of U.S. crude oil and petroleum products imports already come from the Western Hemisphere (North, South, and Central America, and the Caribbean).

About 18 percent of our imports of crude oil and petroleum products come from the Persian Gulf countries of Bahrain, Iraq, Kuwait, Qatar, Saudi Arabia and United Arab Emirates … as unstable a crew as exists anywhere.

It Was neither Iron nor Law.

In 1798, British economist Thomas Malthus predicted that the imbalance between population growth and food production would cause the world to starve to death. Doomsayers called it Malthus’ “Iron Law”.

Malthus fell into the old trap of underestimating everyone’s intelligence but his own. He was incapable of imagining reapers, combines, tractors, insecticides and fertilizers (or foolish governments that would pay farmers not to farm).

Today, the Luddites of both parties in Washington are proposing regulations that cling to the belief that they have defined absolutes in a world of rapidly changing technologies. It’s not the first time.

Some Examples:

1. A Presidential commission appointed by Hoover in 1929 later reported to Franklin D. Roosevelt on how to plot our course through 1952. The 1,600-page report was 13 volumes prepared by 500 “researchers.” There

was not a word about atomic energy, jet propulsion, mass communication, antibiotics, transistors or computers.
2. The World’s Fair of 1939, dedicated to the *World of Tomorrow*, not only failed to suggest any of these advances, but did not even entertain the idea of space exploration.
3. Futurist Herman Kahn’s world renowned opus on the year 2000 never mentioned pollution, water conflicts ... nor was there any real emphasis on the energy shortage.

Those who came closest to anticipating the future were science fiction writers, unencumbered by elaborate research or prestigious committees, armed only with the courage to dream. Gene Roddenberry, H.G.Wells, Arthur Clarke and Jules Verne proved more prophetic than all the government ‘futurists’ put together.

Substitute for Ox Entrails

Ronald Reagan’s key economic advisor, Walter Wriston, said it well: “Our latter-day Malthusians, whose forecasts are often dignified with computer print-outs (which substitute for ox entrails) appear oblivious to the fact that man, given the proper incentive and freedom to act, has repeatedly found substitutes for dwindling materials.”

More examples:

1. The United States was denied 90 percent of its sources of natural rubber during World War II, but technological ingenuity created synthetic rubber which is now more widely used than the natural product.
2. One of the most common substances in the world is bauxite, but it was not regarded as much of an asset until the way to make aluminum was perfected.
3. Coal was not even considered a resource before the Steam Age. Uranium was considered worthless prior to the Atomic Age.

OPEC, Take Note

From the Pilgrims until the Civil War, whale oil was a major source of artificial lighting.

The Civil War disrupted whaling … no *Rainbow Warrior* needed. Alcohol (its substitute) was taxed heavily and its price nearly doubled to $2.55 a gallon.

Naturally there were cries of profiteering and demands for Congress to “do something.” The government, however, made no move to ration whale oil or to freeze its price or to tax the “excess profits” of the whalers.

Prices were permitted to rise. Consumers began to use less whale oil and the

whalers invested in new ways to increase productivity. Meanwhile men with vision and capital began to develop kerosene and other petroleum products. By 1896, the price of whale oil had dropped to 40 cents a gallon.

The Present Is the Sine Qua Non of the Future

Shortages, then and now, can be eliminated when prices are allowed to exercise their age-old functions of ‘market clearance’.

Shortages, then and now, become a crisis when government intervenes. A free market is not chaos but a continuous economic referendum.

We must permit the innovative talents of the American people to function. Our current energy problem will be solved, probably in ways that no one here can now foresee. Fossil … synthetics … battery hybrid … or something entirely new. Who knows?

It is clear, however, that starving today’s economy is in no way a shortcut to eventual energy innovation and independence.

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