



And so it begins . .

Posted by [Heading Out](#) on May 23, 2005 - 6:36am

Yawn, a new day, and what with doing homework and all, we need some coffee and a sandwich to get our day started. And so we go back to our local sandwich shop, but there is a line at the door. And the proprietor is standing there, so you ask him if he is going to have enough coffee and sandwiches for everyone. "No problem," he says " I have a whole room of bread and fillings and coffee, just go on in and enjoy." And you look through the window and, sure enough, there are new ovens, the shelves are full of different breads, and so you go in.

But the problem is that there are only two people behind the counter, and although they are very nice, they can only serve so fast, and so the line grows longer, and you wait and wait. It sounds familiar, right, the number of times you have been in a restaurant and they have not had enough help. Well, in some ways it is the same way with the current oil problem. There is plentiful oil under the sands and seas of the Middle East, but it has to be served up first.

And the first thing that has to happen is that the oil has to be brought out of the ground, through a well. Kuwait has [just announced](#) that last year their 14 drilling rigs drilled 73 new wells over the course of the year, and their production costs remained at about \$1 a barrel.

As we have commented before Saudi Arabia has only a few more than twice as many rigs as Kuwait, and thus the number of new wells it can drill in a year is also limited. It is the same story as with our sandwich shop owner, there is a plentiful supply, but there is not enough service between the kitchen and the counter to meet the growing need. And because it takes time to hire and train helpers (or to build drilling rigs) a lot of customers are going to start getting as angry as you do when service is bad at a restaurant. And in the case of Saudi Arabia the serving of the oil includes separating the water and gas from the oil, and again one starts to bump into current constraints on delivered production.

The other problem, of course, is that while our sandwich shop owner is showing off the bread coming from the new ovens he has just installed, he is not mentioning the loss of bread from ovens that he has had to take out because they are worn out. And the same is true of the world oil community. There is a lot of talk about the new production coming on line, but not nearly as much about the depleted reserves that are having to be replaced.

Consider, for example the North Sea, where UK production has dropped 14% since last year and where Norwegian production is also falling, to a net world loss of perhaps 500,000 bd this year. Where will they get the supplies to make this up, since they had customers for that oil? It appears that part of the, at least short term, answer is through the United States. As was pointed out in a Dow Jones newswire article on Friday (courtesy of [Alaron](#)) the US is now shipping diesel fuel from the Eastern seaboard in every increasing amounts to Europe.

According to the most recent EIA export figures, U.S. exports were running at a normal

rate of about 100,000 barrels a day in January and February. But in March and April, as European supplies remained tight, traders reported an unusually large number of cargoes of diesel and other distillate fuels to Latin America and Europe from the U.S. Gulf Coast and New York harbor.

Sunoco Inc. (SUN) said May 5 that it exported diesel in April for the first time ever.

Diesel demand is growing much faster than ordinary gas, and is the major fuel for truck transport and rail, so the fact that demand is already starting to match supply means that prices will likely not come down.

And since the shortage of diesel is related to a growing shortage of world supply, then what we might be seeing is the first precursor in our arrival at Peak Oil. And because we live in a global economy, the shortages that will develop in other countries will also have an impact here, as the higher prices now begin to impact our domestic commerce, diesel being the fuel of choice for trucks (which bring us the coffee and the ingredients for the sandwiches).

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