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The 2012 Oil Crunch vs. Cash for Clunkers

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World oil production is beset by declining fields and stagnant investment, and Saudi Arabia is predicting a new price spike even higher than the one in 2008. In the midst of this looming crisis, HR2751 is set to saddle the USA with a brand-new crop of gas-guzzling vehicles.

Via the UAE comes a warning from Saudi Arabia: crude oil prices are likely to spike above last year's record high. "If others do not begin to invest similarly in new capacity expansion projects, we could see within two to three years another price spike similar to, or worse than, what we witnessed in 2008."

This is no surprise to anyone who's been following the peak oil news, and it seems very unlikely that anything can be done on the supply side. If oil production is to keep pace with the historically rising consumption curve, we'll need 20-30 million barrels per day of new production by 2030 just to keep pace with depletion elsewhere. That's several new Saudi Arabias.

Where would this capacity come from? Not Mexico; its fields are sliding fast (Cantarell at 30%/year) and Pemex has neither the capability to develop difficult new resources nor the legal ability to partner with private oil companies. Not Venezuela; Chavez steals anything that comes into his country. Not Canada; the tar sands are terribly expensive to develop and are unlikely to hit 3 million bbl/day. Not Russia, which is past peak and following the same route as the USA's lower 48. Not Brazil; even if the 8 billion barrels in Tupi can be pumped at an initial 10%/year, that is only about 2 million bbl/day. And certainly not ANWR or the Bakken shale, which are good for perhaps 2 mmbbl/day total.

Non-solutions = we're screwed

There is NO solution to this problem on the supply side. The supply needed to continue BAU does not exist; oil prices high enough to expand supply will instead collapse the economy before that supply can be brought to market. The only way this challenge will be met is on the demand side, by shifting to other energy sources where it is feasible and aggressive economizing where it is not.

What's depressing is the utter inadequacy of our government response. Let's take this "Cash for Clunkers" bill (HR2751). It would give a $3500 rebate for the purchase of a vehicle achieving as little as ***two miles per gallon more than the one traded in***. A five MPG increase nets $4500.

This will help clear dealer lots, but it won't do squat for our real problems:

- It will not significantly reduce our fuel consumption; we will still be burning far too much to

accomplish too little.
- It will not fix the bad production mix of the auto companies; it adds demand for guzzlers only slightly less thirsty than the ones they'd replace. But worst of all,
- It will leave us with a brand-new fleet of guzzlers which will not be paid off for years at the exact time when we are facing radical increases in the cost of oil.

It's almost as if this bill was *intended* to screw the country.

A back-of-the-envelope calculation

Let's try an example here. Suppose that Joe Sixpack has a 10-year-old pickup that's EPA rated at 17 MPG combined, which he drives 20 miles one-way to work 250 days a year plus 50 miles each weekend. His fuel consumption is 741 gallons per year. He has a choice of trading it for a Model X achieving 19 MPG plus $3500, a Model Y achieving 22 MPG plus $4500, or a Prius netting 50 MPG plus $4500.

At historical gasoline prices of perhaps $1.50/gallon, his fuel expenses were around $1100/year or under $100/month; this is quite bearable. But at today's local price of about $2.80/gallon, this jumps to $2075/year or $173/month; the extra $80/month has to come from somewhere, which is either his non-existent savings or the consumer economy. This is a substantial hit; if Joe makes $40,000/year, the increase is roughly 2% of his income. Things aren't much better with the trade-ins. The Model X's thirst costs $1857 ($155/month) to slake today, and the Model Y costs $1604/year ($134/month). Only the Prius gets costs down into the realm of reason, at a mere $59/month. Joe could pay off some debt and take his lady out for a night on the town now and then.

It will get worse. Much, much worse.

But we're not done yet. If crude prices head toward $200/bbl in 2012, gasoline will be above $5/gallon. At $5/gallon, feeding the 17 MPG monster costs $3706/year ($309/mo), which is over 9% of Joe's gross income. The Model X takes $3316/$276 (over 8%) and the Model Y $2864/$239 (over 7%). Only the cost of the Prius remains in sane territory, at $1260/year or $105/month—roughly 3% of Joe's income, or about what the old pickup cost at $1.50/gallon. The Prius, or something like it, is the only vehicle that Joe can afford to keep driving at that point.

You may have noticed that I ignored the rebates in the cost calculations. They barely matter. If Joe banks $3500 on the Model X and gas goes to $5, his fuel costs will eat those savings in about 16 months; if he buys the Model Y, the $4500 in the bank will pay his increased fuel bills for about two and a half years. Joe will be out of savings while he's still upside-down on his new car loan. Again, only a Prius-class car can save his budget.

Of course, this is in addition to the credit crunch. The USA needs to be paying its debts off, not adding to them. Are we going to be able to finance a whole new fleet of guzzlers, and then the crude to run them? Or will we face a surge of business failures, credit-card defaults and mortgage foreclosures which make the last two years look like a corner lemonade stand on a rainy weekend? My money (what's left of it) is on the latter, and building another fleet 3 years from now when this year's becomes unaffordable to run is out of the question.

The yawning gap between the crisis and the response

If our government was attuned to the looming problem, we would be seeing some real action on these problems. Nothing like HR2751 would receive a committee hearing, let alone House passage. We would be closing truck production lines and converting them to non-automotive products, while pushing to get Fiat's and other manufacturers' high-economy products into the remaining plants as rapidly as possible. US auto suppliers would be paid to re-tool for the new models, and Toyota's US Prius production line would be opened ahead of schedule. We'd be settting a high and steadily increasing floor on fuel prices, to keep that money inside the country instead of flowing out to oil producers.

Congress won't even ***think*** about anything like that.

Can we stop the Guzzler Subsidy Bill of 2009? Perhaps not. But if I was going to try, I'd call my congresscritters and Senators and tell them something like this:

- By 2012 *at the latest*, we will be facing fuel prices even higher than 2008.
- Paying people to buy inefficient vehicles is insane, no matter what they drive now.
- If we are going to survive the next oil-price surge, we need a fleet which gets closer to 50 MPG than 20. Anything less puts the economy at great risk.
- Achieving that fleet means Detroit has to build it, and the public has to buy it... and that means Congress cannot waste our money promoting anything less.

At this point it's up to you. Can you stop this runaway train before it runs off the collapsed bridge? I'm not sanguine, but I can hope.