

# **The Oil Price Crash: Is this Groundhog Day or Something New and Different?**

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*The Royal Institution*

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## Disclaimer Statement

This set of presentations have been prepared exclusively for discussion purposes during this event. The materials presented should not be understood as GCA forecasts or predictions of oil and gas prices or future industry conditions and they should not be understood as a specific recommendation in respect of any particular decision or course of action.

# Agenda

## **Presentations in The Faraday Theatre – 2.30 p.m.**

- ❑ *Introduction – Is this Groundhog Day or Something New and Different?* - Mike Cline, Executive Director, GCA
- ❑ *Crude Oil Price Overview* – Mike Cline
- ❑ *The Impact of the Oil Price Crash on the E&P Industry* – Ricardo Barreto, Regional Director of Business Consulting, GCA

## **Coffee Break in Ante Room 3.30 p.m.**

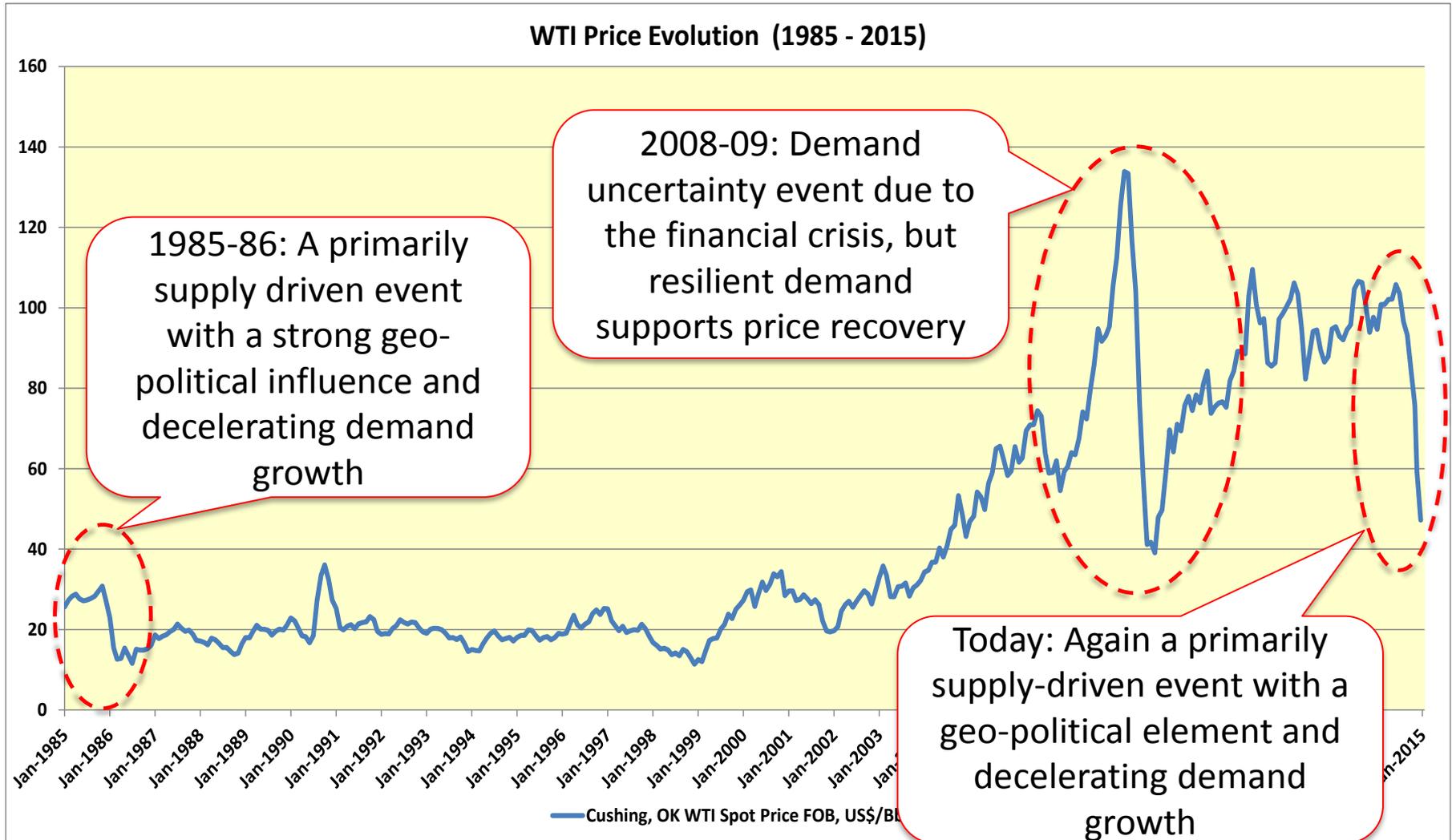
## **Resume Presentations in The Faraday Theatre – 3.50 p.m.**

- ❑ *Unlock Value in the UKCS* - Seadhna Wilson, Principal Advisor, GCA
- ❑ *Being Proactive on Reserves Write-downs and Impairments* – John Barker, Technical Director, GCA and Eraj Weerasinghe, Director, Valuations and Business Modelling, Ernst & Young

## **Closing Remarks – 5.00 p.m.**

## **Drinks and Canapes in Georgian Room**

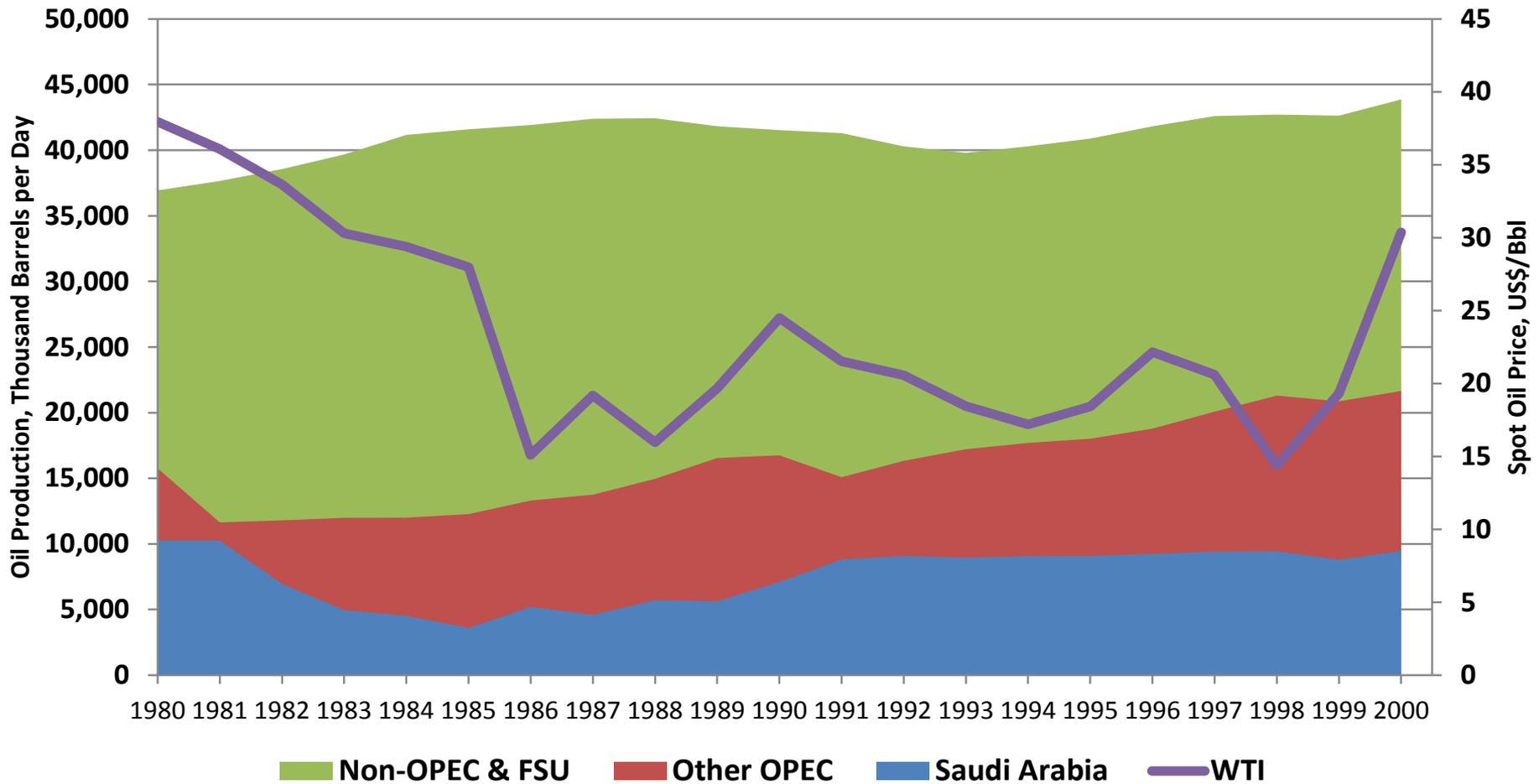
# Historic monthly WTI price suggests we have been here before



## We saw an “Efficient Producer’s” strategy in the 1980s

- ❑ In the early 1980s, oil prices were buffeted by softening U.S. / European demand and rising production from the North Sea
- ❑ Saudi Arabia sought to defend prices by reducing production
- ❑ By late 1985, Saudi Arabia changed strategy to increase production and defend its market share – an “efficient producer’s strategy”
- ❑ OPEC production reached record highs
- ❑ A very successful strategy:
  - U.S. production reversed course and started to decline; domestic drilling plummeted with high cost wells suddenly uneconomic
  - Low oil prices stimulated demand and contributed to economic growth
  - OPEC market share increased in the US market
- ❑ But the harsh reality was the oil market faced years of oversupply, languishing for the next 15+ years

# The Efficient Producer's strategy was effective

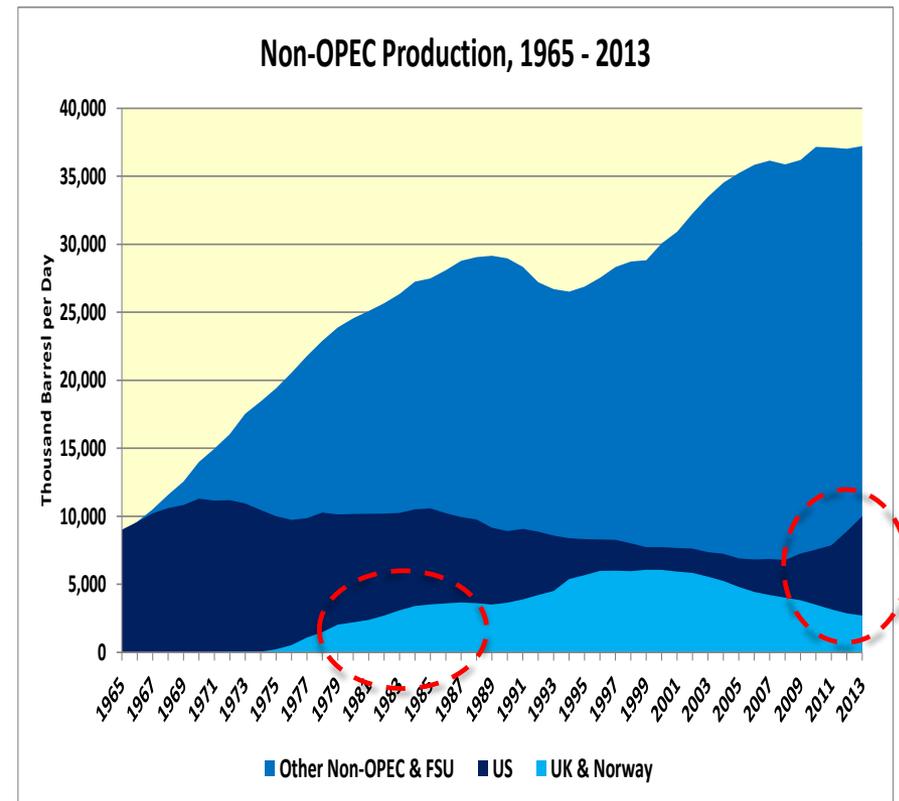
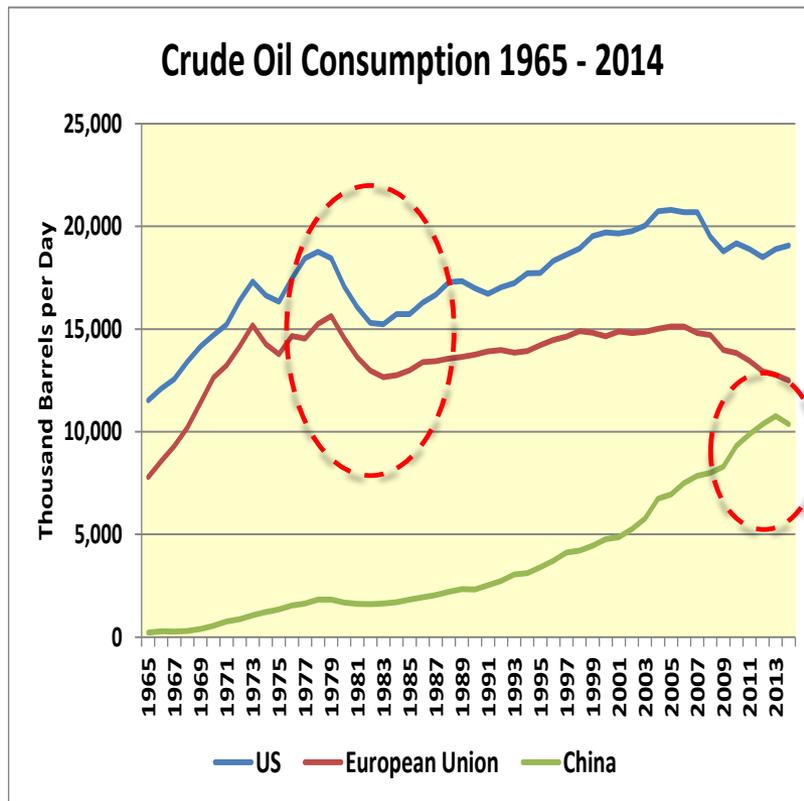


## A few comments on why 2008 was different

- ❑ If the 1985/6 event were supply-driven, then 2008 can be said to be fear-driven
- ❑ The financial crisis heralded by the collapse of Lehman Bros. created fear and uncertainty as to the length and depth of the impact on major economies
- ❑ Oil prices reacted sharply to this fear and uncertainty
- ❑ Major economies were more resilient than might have been expected and demand was not fundamentally undermined
- ❑ The recovery was relatively rapid

# The 2014/15 price crash looks like déjà vu all over again...or does it?

- The similarities between the 1980s price crash and today are striking in some respects
- Both can be characterized as supply-driven events



## 2014/15 events have similarities with the 1980s...

- ❑ Also a supply-driven event with different players
- ❑ Exacerbated by softening demand in key markets
- ❑ Similar geo-politics with a discordant OPEC, plus non-OPEC producers pursuing their own particular interests
- ❑ Saudi Arabia and the Gulf States pursuing an “efficient producers” strategy
- ❑ If the 1980s events presaged an extended period of low / flat oil prices but ultimately recovery to high oil prices - is there reason to believe the 2014 event will be different?
- ❑ If Saudi Arabia’s strategy was successful in the 1980s, will it be successful again?

# Should we expect quick recovery (e.g. 2008), a longer-term recovery (e.g. 1980s), or are we facing a New World?

## Restoration

- 'Efficient Producers' strategy drives down prices
- Retrenchment in investment by inefficient IOCs restores the supply / demand balance
- Many high-cost producers are eliminated, particularly in the U.S. unconventional space
- Prices rise and "normal service resumed"

## Revolution

- Most producer nations must produce "all out" to meet budget requirements
- Constant adaptation by high cost producers confounds predictions of their demise
- Constrained sources of supply re-emerge, such as Iran, Libya etc.
- Major economies reduce energy intensity and continue the shift to gas, renewables, and nuclear
- Low or moderate oil prices become the norm

**Are we facing an Old World or a New World?**

## Only the brave (or reckless) can say they know how this latest event will work out...

- ❑ Experience suggests that when prices are driven down by over-supply in a fractured, complex geo-political environment, a sustained recovery may take years, not months to materialize
  
- ❑ What the ultimate recovery will look like is also interesting
  - Issues of adaptation in technologically-driven sources of supply are interesting and cannot be dismissed easily
  - Driving out unconventional producers may be harder than it seems
  - The potential contribution of Libya, Iran etc. may be significant (or not)
  - The rate of growth of gas and renewables in the total energy mix may outpace expectations
  - Cost structures may adapt to the new environment more quickly and dramatically than expected
  
- ❑ There are reasons to be optimistic – understanding and adapting to uncertainty is what many people in this industry do very well

# How do we find a way to be strong and prosper in the new environment?

- For most companies and resource holders, surviving and prospering in this kind of environment means change and adaptation
  - Today's agenda is all about examining how to not only avoid the pitfalls, but to also take advantage of the opportunities presented

