

# The Eternal Oil Curse

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Despite continuing street protests, Prime Minister Vladimir Putin remains very likely to return for a third term as president, probably after the first round of the election on March 4. Although he will begin an extended, six-year term under a cloud, he can at least comfort himself that crude oil prices remain sky-high and, even better, are forecast to further increase. The consensus among oil market analysts is that the world has entered an era of costly oil, which could even trigger international conflicts over sources of supply. Russia, which has both oil and the world's second-largest nuclear arsenal, is sitting pretty.

High oil prices, which underpin Russia's wealth and are largely responsible for Putin's political success, should help him keep his promise of economic stability and a gradual spread of prosperity from his cronies to the masses. But in reality, far from providing a solid petrodollar cushion for his regime, oil may end up being its greatest vulnerability.

Oil prices are notoriously difficult to predict. Moreover, whenever analysts start saying that the world is running out of oil, as they did in the late 1970s, oil prices tend to go into a decline. On the other hand, predictions of plentiful, cheap oil, such as ones issued in the early 1970s

and the late 1990s, are promptly refuted by periods of expensive oil and oil shortages.

In the first decade of the 21st century, oil prices were clearly driven by increased global demand. China was the most obvious culprit, as it industrialized and became the world's largest car market, while other emerging economies such as India, Brazil, Indonesia and Turkey also put a strain on supplies. Since 2000, demand for oil from "new economies" increased from around 34 million barrels per day to over 50 million bpd this year.

But overall oil demand has now stabilized and may even go in reverse. Since the mid-2000s, oil consumption in the United States, Europe and Japan has fallen by around 3 million bpd. This could get worse, as Europe is probably facing a nasty recession. Economic growth in China and elsewhere is slowing. Meanwhile, high prices have led increased production and development of new technologies, which help producers pump more oil out of the ground. Oil is now produced from shale and offshore wells, while natural gas as well as wind and solar energy are supplying a growing share of global energy needs. Equally important, high prices have led to a greater emphasis on energy efficiency and conservation. In fact, a serious long-term glut may now be developing in the oil market.

Yet, oil prices remain high. Since early 2011, when North Africa and the Arab Middle East were unsettled by revolutions, crude has been reflecting political concerns. In early 2012, tensions with Iran have triggered fears that a regional conflict could shut down the Strait of Hormuz through which some 20 percent of the world's oil deliveries pass daily.

Russian protests also contributed to higher oil prices. Production disruptions in Russia are a remote possibility, but rating agency Fitch cut its outlook on Russia's debt from positive to stable, citing political concerns. Prices on the Moscow bourse are still soft. But a larger longer-term danger is a stagnating world economy. While oil demand is weakening, politically driven oil price increases could create a dangerous bubble in the oil market. When it bursts, pressures on the Putin administration will increase. As the 2008 crisis showed, Russia can live with oil at \$80 per barrel, but not at \$50.

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*The views expressed in opinion pieces do not necessarily reflect the position of The Moscow Times.*

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