The sleeping giant

Demand for oil in China may affect entire world. **Interviewed by Steve Trusty**

U.S. oil prices fluctuate, it's true, but the trend is unequivocally upward. U.S. consumers may be surprised to know that a leading push on that rising trend is the sprawling, densely populated nation of China — where latent capitalism is energizing a very old country's commercial rebirth. In 2006, according to the Energy Information Administration (EIA), China's oil consumption will increase to 38 percent of the total growth in worldwide oil demand. Its consumption for 2006 will exceed its 2005 levels by nearly 500,000 barrels of oil per day.

"In the 1990s, China was exporting excess oil," says John Barnes, chairman and CEO of B&R Energy LLC. "In the past two years, however, it has passed Japan in imports, generally, and as an oil importer is second only to the U.S."

Smart Business asked Barnes about China's increasing appetite for oil, the current global outlook, and what U.S. consumers should be thinking about.

John Barnes
Chairman and CEO
B&R Energy LLC

What does China have to do with the price of oil?

The most obvious answer is that economic growth takes energy, and China's economy is growing. According to EIA records, China's real gross domestic product (GDP) is estimated to have grown at 9.9 percent in 2005, down slightly from the 2004 rate of 10.1 percent. Economic forecasts remain strong for China, with real GDP expected to increase 9.9 percent in 2006.

Since most of that growth is low tech, the Chinese need more energy to manufacture more and, in turn, to run an economy that is picking up speed. Look at its size and population. In particular, consider that China's rising middle class is buying and using more personal vehicles.

Ten years ago, China used less fuel than it produced and was exporting the excess. Now it can't meet its own demand. As the world's oil demand catches up with worldwide oil availability, price rationing is inevitable. When prices climb too high, marginal users cut back and, in effect, rebalance supply and demand.

In the end, however, it is a seller's market and the speculators will continue to drive prices upward as demand exceeds new discovery and production.

Do you believe China's energy needs will continue to rise or level off?

Let's look at that conservatively. Say the current need is 2 million barrels of oil a day and annual growth continues at 10 percent. Next year, China will require 2.2 million barrels a day. A year later, demand exceeds 2.4 million. In five years, China's needs will be in excess of 3 million barrels of oil a year, 50 percent more than the current intake.

Now think vehicles. North America has 932 cars for every 1,000 people. China has four cars for every 1,000 people. But for every vehicle added per 1,000, China needs 500,000 more barrels of oil per day.

Finally, factor in the economic growth in India, the U.S., and other reaches of the globe. Clearly, for the foreseeable future, the globe has no excess oil.

But isn't there more to all this than the price of oil?

Yes, there is — a lot more. Steel prices, cement prices, copper prices —almost every commodity's trend is aimed at the heavens. What's more, the cost of fuel hides myriad other costs; hydrocarbons for plastics become more expensive, and everything that requires shipment by a hydrocarbon-fueled vehicle will simply cost more. Differentials will continue to grow. The price of some consumable goods may drop from time to time, but it won't be because there is a dip in demand or price of energy.

What can or should U.S. consumers be doing?

First, we must support policies to increase and improve U.S oil production. We must tap known oil fields, where it already takes four to five years from the time we break dirt to when production begins. And we need to have started that yesterday.

Meantime, we need alternative sources to maximize our supply — alternatives that make money sense. We also need to look at alternative ways to produce energy. While we explore for oil with what we know today, let's exploit available technology to research and develop entirely new ways to find more oil.

China is building 30 nuclear generators to expand growth, not to mitigate it, while the U.S. has not brought a new nuclear plant online since May 1996. Only three valid construction permits remain, and construction has been halted on all of them.

All that said, at every turn, we must look for ways to conserve — both to save on the cost of fuel and to decrease our need for it. And again, we need to start yesterday.

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