

Regional Outlook: United States – Energy Sector

26 May 2007

The first half of 2007 has seen extensive activity in the American energy sector. Innovation and dynamism have entered a market long controlled by large petrochemical and coal conglomerates. Renewable and clean energy technologies are receiving strong, robust growth throughout much of the country with sustained interest from both the domestic and international sectors. Domestically, growth is supported by political legislation, judicial rulings, grassroots public concern, and corporate desire to reduce uncertainty. Foreign interest in the energy sector has increased as US regulation reform alters ownership requirements allowing foreign investment to revitalize US energy assets.

The 2 April 07 ruling by the US Supreme Court that carbon dioxide can be limited under the Clean Air Act has sent many companies into the clean, green camp. Major US utilities and energy conglomerates are interested in containing the cost of future regulation and possible litigation and are therefore actively engaging in the creation of domestic carbon markets, new environmental legislations, and general diversification into cleaner technologies. The capital markets have also responded favorably with several of the large investment banks setting up clean energy funds and the insurance industry is actively looking at the risk posed by climate change.

Recent changes in legislation and regulation have, for the most part, been conducted at the State level with some regional co-operation. There has not been much of a concerted effort from the Federal government to promote growth in the energy sector. The Energy Policy Act of 05 did offer more funding to cleaner technologies it also broadened the definition of clean technology to be much less meaningful. Currently, The House of Representatives have proposed a bill that calls for the repeal of the 2004 tax cuts granted to the petrochemical industry and at the same time negotiating increased royalties on proposed extraction of oil from the Gulf of Mexico. The key players are gearing up for a fight as the harm caused by this bill is very concentrated and the benefits are ambiguous at best and potentially may not materialize at all. The Congressional Budget Office (CBO) estimates “the outlay savings and revenue increases from enacting H.R. 6 would total \$5.5 billion and \$14.0 billion, respectively, over those periods.” [2007 – 2017]. The industry states

strongly that these increases will make domestic oil extraction non-economical. Their argument is that the new taxes will cause the marginal cost of extraction to exceed the market price for oil. Fewer firms will make the decision to invest in new extraction and refining equipment as the return to capital is not sufficient.

There is some validity to this argument; although it is limited by market demand for oil, which is a robust, keeping the world oil price buoyant. The International Energy Agency (IEA) estimated the economic cost of deepwater and super-deep extraction at \$35 and \$40 per barrel, respectively. Therefore, crude oil would need to drop below \$40 per barrel to support industry claims of non-market viability. This is unlikely to happen as long-term oil projections show oil price declining in the near-term and stabilizing in the \$45 to 50 per barrel range through 2030 partially offset by production of previously cost-prohibited extraction (e.g. tar sands, deepwater, enhanced oil recovery, etc.) and reliable substitutes (e.g. bio-diesel, synthetic diesel (Fischer-Tropsch)).

The petrochemical industry has a well established lobby presence and has provided campaign contributions to members of both parties. Passing the resolutions in the Senate may prove difficult politically as support may be withdrawn due to national security concerns regarding self-sufficiency and supply disruptions. Additional concerns will be raised as to how penalizing the petroleum industry will advance development of alternative liquid fuels. H.R.6 states that the funds shall be placed in a “Strategic Energy Efficiency and Renewables Reserve” to “offset the costs of subsequent legislation.”

The benefits of this bill increase government revenue with funds that are earmarked for other legislative initiatives:

- (1) to accelerate the use of clean domestic renewable energy resources and alternative fuels;
- (2) to promote the utilization of energy-efficient products and practices and conservation; and
- (3) to increase research, development, and deployment of clean renewable energy and efficiency technologies.

The benefits are diffuse and ambiguous and so will have less support than will the injured parties.

The resolution passed the House by a roll-call vote of 264 in favor and was sent to the Senate on 18 January 2007.

The economic impact of this bill is not sufficient in and of itself to curtail future investment in oil resources, however, industry opposition may make a concerted effort to suborn or pervert the intended consequences of the bill. Although the bill claims to target “Big Oil”, it adversely affects any C corporation involved in oil extraction. It is unclear if this bill will pass the Senate and if the President would be inclined to sign or veto it. The potential, real or perceived, of damage to the national energy security situation is likely to garner considerable opposition with part of the public.

The public is growing increasingly aware of the environmental risks posed by current energy production and when coupled with increasing oil prices, increasing demand from China, India and the rest of the World, as well as supply disruptions due to conflict and natural disaster, the market is right for expansion of alternative energies and fuels. The capital market and insurance industry are making remarkable strides towards growing the American energy sector as are several of the large utilities. This year alone the wind industry is expected to install 3,000 MW of new generation capacity. The array of technical expertise, tax credits and financing options available make sustained growth in this sector a reality.

Euroasian funds a portion of its loans via an Energy Fund, the details of which are listed under Facility SA1.