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Oil Mercantilism:

World is not about to run out of oil: Steve Hanke

Apr, 08, 2011 (LBO) - A top US monetary economist has poured cold water on fears about the world running out of oil, an idea which gains special prominence when the US Fed loosens monetary policy, debases the dollar and sends commodities bubbling up.

Oil prices are now hitting highs not seen since the 2008 and the US has not shown any signs of tightening monetary policy. Meanwhile talk of the world running out oil, 'energy security', 'food crisis' and 'food security' are again doing the rounds.

Easy Targets

"Every president since Richard Nixon has asserted that we are sitting ducks for those who brandish the oil weapon," Steve Hanke, professor of applied economics at The Johns Hopkins University in Baltimore, wrote in an online post at Cato@Liberty.com

"To keep the evildoers at bay, the government must adopt policies that ensure our energy independence. Like his predecessors, President Obama is worshiping at this altar.

"And why not? How many elections have been lost by blaming foreigners for an impending crisis?"

Loose monetary and fiscal policy during President Nixon's time forced the dollar off the gold standard firing a massive commodity bubble including the so-called oil shock.
Nixon at the time even halted exports of food commodities, instead of tightening policy.

Commodity prices were only tamed after 1981, after then Fed chairman Paul Volcker tightened monetary policy, bringing commodity prices including gold, back down to earth.

Hanke, now senior fellow at the Cato Institute was in 1981 an economist at the President Reagan's Council of Economic Advisors.

The 1980's (now called the period of Great Moderation) had Europe in particular rushing in with price support schemes for farmers as prices went tumbling down. Headlines of the time had words like 'butter mountains' and 'milk lakes' instead of 'food crisis.'

Commodity prices are heavily influenced by reserve currencies, especially if a reserve currency is a widely used denominator currency.

Hanke says most people do believe that mineral resources, including oil, are doomed to disappear.

Ob(l)ivious

"It's obvious: Start with a given stock of provisions in the cupboard, subtract consumption and eventually the cupboard will be bare," says Hanke.

"But what is obvious is often wrong. We never run out of minerals. At some point it just costs too much to produce them profitably."

In the 19th century he say the big energy scare was in Europe, with the continent expected to run out of coal.

"That doomsday scenario never materialized," says Hanke. "Thanks to a plethora of substitutes, the prices that European coal could fetch today are far below its development and extraction costs.

"Consequently, Europe sits on top of billions of tons of worthless coal."

He says the concept of fixed reserves is meaningless.

Proven oil reserves, he says represent a "warehouse inventory of the expected cumulative profitable output, not a fixed stock of oil thought to be in the ground."

He says oil is sold in a market where every barrel regardless of its sources, competes with every other barrel.

"Think globally, not locally. When we do, the dwindling reserves dogma becomes nonsense," Hanke says.

"In 1971, the world's proven oil reserves were 612 billion barrels. Since then the world has produced approximately 990 billion barrels.

"We should have run out of reserves fourteen years ago, but we didn't. In fact, today's proven reserves are 1,354 billion barrels, or 742 billion barrels more than in 1971."

"How could this be? Thanks to improved exploration and development techniques, costs have declined, investments have been made and reserves have been created. The sky is not falling."

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