Financial Post

Reviving Libyan oil no easy task

A worker's helmet lies on the ground at the Zawiya oil refinery, some 40 kms west of Tripoli. Filippo Monteforte/AFP/Getty Images

Tim Shufelt Aug 22, 2011 – 6:44 PM ET | **Last Updated: Aug 23, 2011 9:51 AM ET**

With Libyan rebels closing in on Muammar Gaddafi, a recognition fell on markets Monday that the task of restoring full oil production will be a monumental one.

It's not a matter of simply turning the taps back on, analysts say. The civil war has brought significant damage to Libyan oil infrastructure. International oil companies are indicating reluctance to return to a region lacking a working government or the basic rule of law. And political stability is far from assured in post-Gaddafi Libya.

"It's going to be slow," said Dominick Chirichella at New York's Energy Management Institute, estimating at least one year before pre-war volumes are realized. "It depends on how quickly the expertise gets back in town and how quickly the workers that have fled the country come back again."

The country's ambiguous future produced a mixed reaction on oil markets on Monday, with Brent crude, which is more susceptible to the Libyan disruption, falling 26¢ to US$108.36 a barrel for October settlement on the London-based ICE Futures Europe exchange. Meanwhile, crude oil for September delivery rose US$1.86 to settle at US$84.12 on the New York Mercantile Exchange.

Prior to the uprising in Libya, the country produced almost 1.6-million barrels of oil per day, about 75% of which was exported.

Although Libyan oil accounts for just 2% of global production, that the oil market is so tight meant a disproportionate market reaction when the country's daily volume fell to 60,000 barrels.

Libya exports a very high quality of light, sweet crude, which has few producers, said Judith Dwarkin, chief economist at Ross Smith Energy Group in Calgary. "It's a bit of a boutique-quality crude."

A return of those barrels to global flows would certainly ease oil market conditions.

For that to occur, however, Gaddafi must officially be ousted and his influence purged from the region. While he looks to be losing his grip on power, lessons from Iraq advise against discounting the strongman, said Chris Preble, vice-president for defense and foreign policy studies at Washington, D.C.-based Cato Institute.

"If we'd written the history of the Iraq War on the day Saddam's statue was torn down in Firdos Square, we'd have a very different story then the one we all know, tragically," he said.

Assuming Libya can avoid a Gaddafi-orchestrated insurgency and prolonged conflict, however, the country has much else to learn from Iraq's slow recovery from war.

Libya, too, needs oil revenues to get back on its feet. "The revenue from oil flows is the main driver of public services, and the ability to build popular support and retain authority, that's how it's done," Mr. Preble said.

At more than 2-million barrels a day, Iraq's oil production has, for more than a year now, exceeded its production before the invasion in 2003.

Most Iraqis now believe, however, that oil revenues are not distributed fairly, a perception that has shaken the country's political outlook.

"The lesson for the post-Gaddafi Libyan government is to avoid that, to make sure there is an equitable distribution," Mr. Preble said.

First, however, the country needs to repair its oil assets. Pipelines have been blown up. And oil facilities were abandoned so hastily with the outbreak of unrest, that they were not shut down properly, Ms. Dwarkin said. "My understanding is that there is significant damage to infrastructure in the producing fields."

Restoring production capacity will require the return of international oil companies. "They may want a lot of comfort that it's a stable situation before they start sending people back in," she said.

Marathon Oil Corp. said Monday it was in preliminary talks with Libyan rebels, but won't return to the country until assured of Libya's stability.

On Monday, SNC-Lavalin Group Inc. said its Libyan engineering projects would remain on hold.

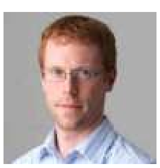
Italian oil company Eni SpA did appear somewhat more confident in Libya's fate, sending staff to examine the prospects of restarting oil facilities in eastern Libya.

"It all depends on how aggressive the independent oil companies get," Mr. Chirichella said.

He expects to see Libya producing up to 300,000 barrels a day within the next few months, and 750,000 barrels by some time early next year. Full production is not likely before the end of 2012, he said.

With files from Reuters

Posted in: Energy **Tags:** Crude Oil, Libya, Libya Oil Production, Oil, Oil Production



TIM SHUFELT
tshufelt@nationalpost.com

BoC will be 'prudent' on stimulus: Carney

U.S. factories slow, stocks plummet

Eurozone fiscal proposal falls flat

Euro fiscal union closer

Roller coaster week ends almost where it began

MORE FROM TIM SHUFELT »