

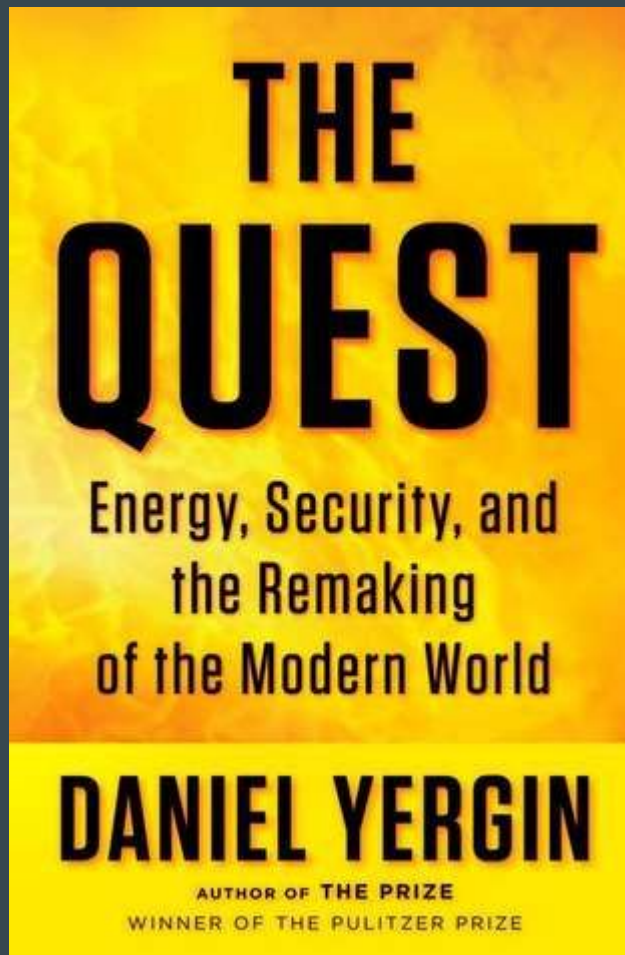
# The Quest: Part 1



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# Part One Outline

1. Russia Returns
2. The Caspian Derby
3. Across the Caspian
4. “Supermajors”
5. The Petro-State
6. Aggregate Disruption
7. War in Iraq
8. The Demand Shock
9. China’s Rise
10. China in the Fast Lane



# 1. Russia Returns

- Throughout its lifespan, the Soviet Union was heavily reliant on oil and gas for its economic success. Naturally, after it's dissolution, the most pressing issues were:

1.) How will the nation run?

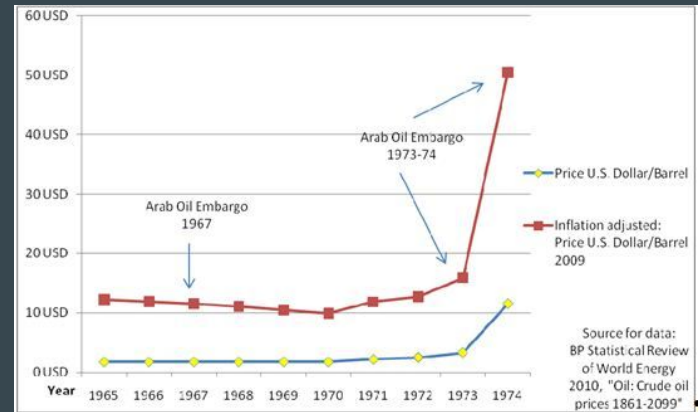
2.) Who will be in control of the oil and gas markets?

- Privatization was the solution to which the nation turned



# 1. Russia Returns

- The 1973 Arab Oil Embargo affected almost every economy of the world
- For the USSR, this led to a great influx in money, which may seem like an inherently good thing, but only in the short run as it turned out
- This influx in cash actually delayed the Soviet Union's economy from reformation away from dependence on gas and oil
- In 1986, a massive surplus of oil dropped prices drastically, severely hurting the USSR's oil driven economy



# 1. Russia Returns



- As the Soviet Union came to an end, the government was shifting to a much less centralized form
- This then forced a restructure of government owned oil to be privatized
- Oil companies such as Lukoil, Surgut, and Yukos took the reins
- Vagit Alekperov, the leader of Lukoil, the most notable of these three companies, bought out and merged numerous smaller oil companies to make Lukoil possible



# 1. Russia Returns

- At the same time, a new politician in Russia quickly grew to power, Vladimir Putin. As a mining student, Putin believed oil and gas were the key to economic recovery and the “entry of Russia into the world economy”.
- Mikhail Khodorkovsky, the leader of Yukos, and Putin disagreed on many political issues. Thus, Khodorkovsky bypassed Putin on many important political issues. Putin had him arrested and Yukos dismantled.
- With the help of these newfound oil companies, Russia again became the largest producer of oil. The country’s oil industry adapted very well, becoming an ample source of wealth for the nation.
- This being said, Russia still needs to decrease its dependence on oil to avoid another economic failure

## 2. The Caspian Derby

- The oil field under the Caspian Sea, the third largest producing oil field in the world, has been the subject of debate and territorial turmoil for many years



## 2. The Caspian Derby

- The obvious concern with oil obtained from the Caspian was where it should go
- Once deciding that a pipeline would be the most efficient form of transportation, many factors were at play in order to decide where the pipeline should be laid
- After much debate, the BTC pipeline (pictured below) was finally decided on and finished construction in 2005





# 3. Across the Caspian

- In 1985, the Kazakhstan controlled oil field Tengiz caught fire for nearly 400 days after a massive oil and gas blowout
- This fire threatened the future of the field until foreign investors, specifically Chevron from the United States, were brought in to update the infrastructure of the area to include pipelines to more easily work the fields



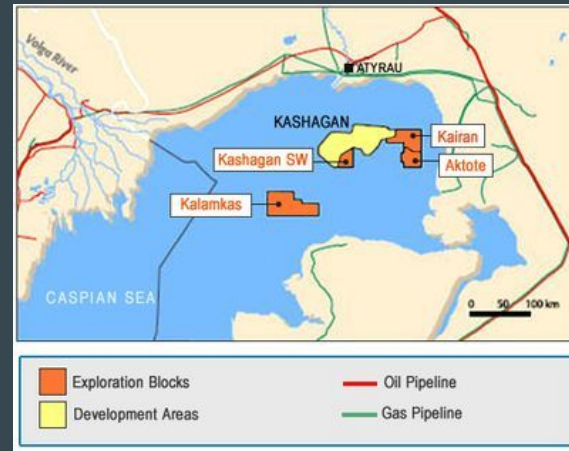
### 3. Across the Caspian

- A contract of a 50/50 split of ownership between Chevron and Kazakhstan of the pipeline was drawn up with 80% of economics given to Kazakhstan
- The pipeline was proposed to run through Russia, which proved to be an issue as they resented US involvement and considered Tengiz as their oil
- Eventually, after negotiation with Russian oil giant Lukoil, a deal was finally agreed upon and the pipeline was finished in 2001



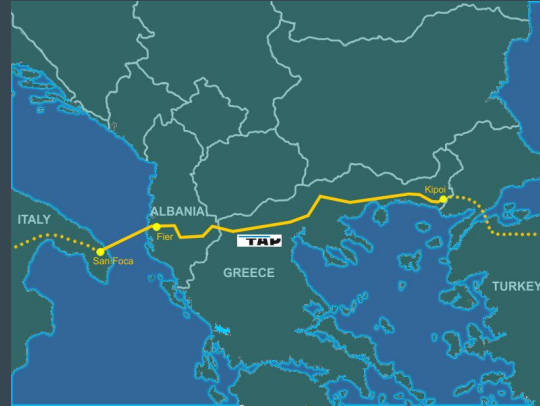
# 3. Across the Caspian

- Another important oil field across the Caspian was Kashagan, the largest field discovered since 1968
- ‘Across the Caspian’ might be a bit misleading here, as this field is actually an offshore field in the far North East corner of the Caspian Sea
- Many technical difficulties came along with the discovery of this field, and not too many countries could jump on the opportunity, China was the first



### 3. Across the Caspian

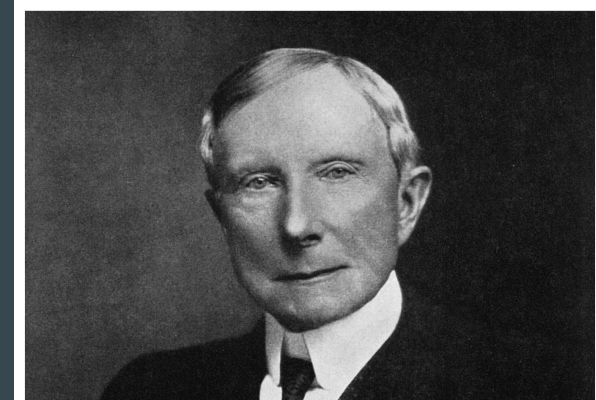
- With a vast wealth of oil resources, Turkmenistan is another important player across the Caspian Sea



- The TAP (above, right) and COAP pipelines met much resistance, most notably that from the Taliban who had control over Afghanistan and Pakistan at the time

## 4. “Supermajors”

- In the mid-1800’s John D. Rockefeller realized the potential of creating a well organized company from the new volatile American oil industry
- As a result, one large company was formed, the Standard Oil Trust Company
- Rockefeller became the first billionaire and is still regarded as the world’s richest man to have lived



## 4. “Supermajors”

- Two factors in the late 90’s lead to one the largest restructures of the petroleum industry that we have seen to date
  - 1.) The 1997 Asian financial crisis, due to massive lending and accruing of debt, that impacted economies around the globe
  - 2.) The signing of OPEC’s ‘Jakarta Agreement’ with a goal to raise their production “by two million barrels per day” which ended the fight over quotas and overproduction
- This combination lead to OPEC increasing production when demand was low
- Massive layoffs took place across the globe in the industry

## 4. “Supermajors”

- As oil companies in the US grew, and competition rose, many of these companies sought mergers
- CEO of BP, John Browne, offered a merger with Mobile, but in the end, neither party could meet and agreement they felt sufficient
- BP then merged with Amoco in the largest industrial merger
- In response, Lee Raymond, CEO of Exxon, contacted the CEO of Mobil. The two companies merged to form what was called the “New Oil Behemoth”



# 5. The Petro-State

- The story of Venezuela, the 'Petro-State' is one that many nations have often known too well throughout history
- Sole dependence of an economy on oil and gas is a recipe for disaster when oil prices fluctuate, and Venezuela is no exception





# 5. The Petro-State

- If this story of Venezuela has taught us anything, we hope the lesson is for future economies not to “put all of their eggs into one basket”
- Only time will tell if another sudden drop in oil price will spell disaster for yet another economy



# 6. Aggregate Disruption

- The “Internet” made it easy for people to communicate with each other
- “Distance” was disappearing



# 6. Aggregate Disruption

## THE DAY THAT CHANGED EVERYTHING

- On September 11, 2001, the US was attacked by Al Qaeda
- Security was the central preoccupation
- World's biggest oil region, the Middle East, was also the region from which Al Qaeda had emerged
- Oil consumption and oil imports were a security risk

# 6. Aggregate Disruption

## “ALO PRESIDENTE” - VENEZUELA

- Hugo Chavez - re-elected president of Venezuela in 2000
- Took control of Petroleos de Venezuela - PDVSA - the state oil company
- Used his television show to fire 7 board members of PDVSA
- April 12, 2002, Chavez was asked to resign and was taken into custody
- 3 days later, he was in control of the country again

# 6. Aggregate Disruption

## NATURAL DISASTER

- August 25, 200, Hurricane Katrina hits Gulf of Mexico



# 7. War in Iraq

- Iraq's economy runs on their large production of oil
- Connections to 9/11 and links to Al Qaeda
- Believed to have weapons of mass destruction



# 8. The Demand Shock

- West Texas Intermediate (WTI) was ground zero for the world oil price
- The demand for oil increased by almost 4 times globally between 2003 to 2006
- Countries were taking oil supplies off the shelves because of the demand surge



# 8. The Demand Shock

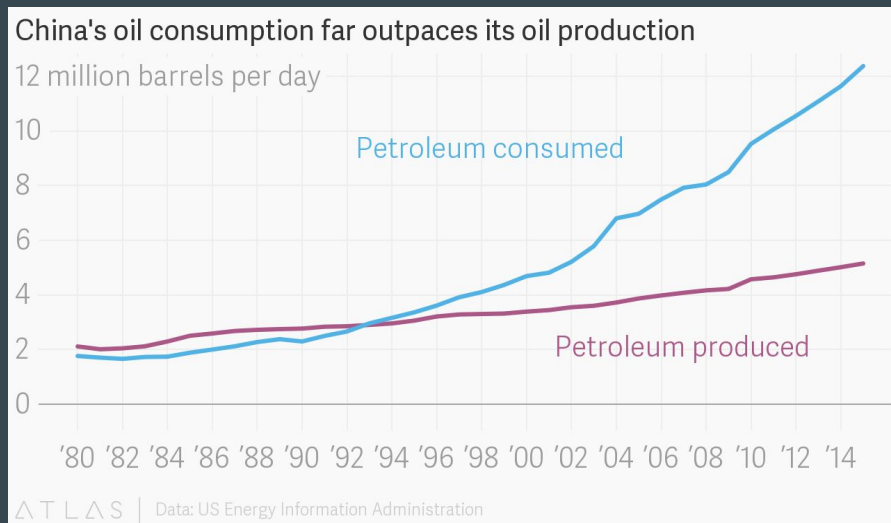
- Airline industry was hit the hardest
- Car sales impacted directly





# 9. China's Rise

- China became a global oil giant towards the turn of the century
- By 2010, China was the second largest economy in the world
- China became an importer than an exporter
- China's partnered with Russia but faced competition from Chevron in 2005



# 10. China in the Fast Lane

- Politics v.s. Oil Market
- US v.s. China
- Coexistence
- Success trade-offs



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