Wall Street Journal [1]

APRIL 16, 2011

Oil Without Apologies

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It's the day after President Obama delivered his most recent vision of America's energy future, and I'm sitting in the sunny corporate offices of Chevron, the country's second-largest oil company. Let's just say John Watson has a different view.

The Chevron CEO is a rare breed these days: an unapologetic oil man. For decades—going back to Jimmy Carter—politicians have been peddling an America free of fossil fuels. Mr. Obama has taken that to an unprecedented level, closing off more acreage to drilling, pouring money into green energy, pushing new oil company taxes, instituting anticarbon regulations. America is going backward on affordable energy, even as oil hits $110 a barrel.

Enter the tall, bespectacled Mr. Watson, who a little more than a year ago stepped into the shoes of longtime CEO David O'Reilly. An economist by training, soft-spoken by nature, the 53-year-old Mr. Watson is hardly some swaggering wildcatter. Yet in a year of speeches, he has emerged as one of the industry's foremost energy realists. No "Beyond Petroleum" (BP) for him. On energy, he says, America "has a lot to learn."

Starting with the argument—so popular among greens and Democrats—that we are running out of oil. "Peak oil"—the theory that global oil production will soon hit maximum levels and begin to decline—is a favorite among this crowd, and it is one basis for their call for more biofuels and solar power. Mr. Watson doesn't dismiss the idea but explains why it remains largely irrelevant.

In theory, he says, "we've been running out of oil and gas for a long time," yet technology creates new opportunities. Mr. Watson cites a Chevron field long in decline down the road in Bakersfield—to the point that for every 100 barrels of oil "in place," the company was extracting only 10 or 20. But thanks to a new technology called steam flooding, Chevron is now getting 70 to 80 barrels. "Price creates incentive, and energy will be developed if there's demand for it at the price you can develop it," Mr. Watson says. In that sense, "oil and gas are plentiful."

Don't believe it? Over the past 30 years, even as "peak oil" was a trendy theme, the world's proven reserves of oil and natural gas increased 130%, to 2.5 trillion barrels.

Or consider America's latest energy innovation: hydrofracking for abundant and cheap natural gas. This advance, says Mr. Watson, took even the industry "by surprise"—as evidenced by the many U.S. ports to import liquid natural gas that are now "sitting idle." Chevron last year paid $3.2 billion to buy natural-gas producer Atlas Energy as its foray into this new market.

Mr. Watson has little time for the Beltway fiction that America will soon be able to do without, or nearly without, fossil fuels. Yes, "we need all forms of energy." But the world consumes 250 million barrels of energy equivalent today, only a "tiny fraction of which" is wind and solar—and even those "are not affordable at scale," he says.

As for biofuels, "we would need to consume land the size of states" to hit the country's current ethanol targets. Chevron is investigating biofuels, but Mr. Watson says the "economics aren't there" yet. Unlike many CEOs, Mr. Watson insists on products that can prosper without federal subsidies, which he believes are costly and lacking in transparency when "consumer pockets are tight, government pockets are tight."

Bottom line: "We're going to need oil and gas and coal for a long time if America wants to keep the lights on."

He seems to mean it, too: Chevron recently announced the largest capital and exploratory budget in its history, $26 billion to drill in Australia, Western Africa and the Gulf of Thailand, among other places. Some of that cash will go to the Gulf of Mexico, though Mr. Watson wishes there were more U.S. opportunities.

"Most of the well-developed world—Australia, Western Europe—they develop their resources base, they inventory it, they develop it, and they view it as a good source of jobs and revenue," he says. The U.S.? "We are a country" that for too long has taken "affordable energy for granted."

The Chevron exec was "pleased" to see Mr. Obama acknowledge that "oil and gas were fuels of the future—because I hadn't heard that before. That's a significant step." Looking to reassure Americans about rising gas prices, the president nonetheless resorted to the old standby of calling for a one-third reduction in U.S. oil imports by 2025. Mr. Watson thinks that's a fine goal, but he points to the enormous disconnect between what the president is proposing and existing policies.

The only conceivable way to meet that goal is by dramatically increasing U.S. oil production—immediately. The White House recently bragged that last year American oil production hit its highest levels since 2003. What it failed to mention is that it takes years for leases to start producing, so credit for last year's surge goes to the Bush administration.

But what about the BP Gulf spill? Mr. Watson blames the "cultural aspects and behavioral aspects" of the particular drilling rig that exploded. He roundly disagrees with the finding of Mr. Obama's spill commission that the "root causes" of the spill were "systemic" to the industry.

"There is no evidence to support that. I don't know how that conclusion was reached. I know the industry has drilled 14,000 deep water wells without having this sort of problem." As for the moratorium, "I can understand taking a pause. I can't understand shutting down a whole industry for a better part of a year."

Chevron has three deep water rigs in the Gulf, so the ban cost it millions of dollars in idle rigs and lost jobs. For the country, says Mr. Watson, it means "less oil." Offshore drilling takes years of lead time. Mr. Watson cites Chevron's Gulf "Tahiti" project, which started producing about 18 months ago. It has taken "the better part of a decade to do the seismic work, drill the exploratory wells, evaluate those wells, drill other development wells, to delineate it, to build the facilities and to place the oil wells online," he explains.

The endless moratorium has already meant that "if you go out to the middle of the decade, there are already 200,000 to 300,000 barrels a day of oil that aren't going to be produced that year. . . . That won't be retrieved." And the lost production number is getting larger, since the new Bureau of Ocean and Energy Management is still dallying on permits—and those primarily for backlogged projects, not new leases.

Democrats are now arguing, as Mr. Obama did in his speech, that the oil industry already "holds tens of millions of acres of leases where it's not producing a drop." Some are advocating "use it or lose it," calling for the government to strip oil companies of their leases if they don't immediately start producing.

Mr. Watson explains why this is bogus. Only one-third of Chevron's offshore leases are classified as "producing" oil and gas today. The other two-thirds either are "unsuccessful" (they don't hold viable oil or gas) or "are in varying stages of development—seismic work, drilling wells, constructing facilities." Mr. Watson says companies would be crazy to sit on productive lands, since leases require costly bonus payments and annual rental payments to the government.

If Washington institutes Mr. Obama's "use it or lose it" policy, Mr. Watson says, it will mean less U.S. oil production. And how does this help Mr. Obama with his goal of reducing imported oil?

As for soaring oil prices, Mr. Watson blames growing demand, tighter supply, Mideast uncertainty and inflation. He doesn't predict future price trends, though during a recent analyst call he warned that the drilling moratorium would only make them higher. Lost production in the Gulf is "going to represent a sizable chunk of the spare capacity that the industry expects to see. And that will impact prices, and that will retard economic growth."

The economy is also why Mr. Watson won't pay the usual energy CEO lip service to new carbon regulations. The cap-and-trade bill the House passed in 2009 was "poorly conceived and it collapsed under its own weight for good reason," he notes.

The EPA move to regulate carbon is no better: "It's not why the Clean Air Act was put in place, and it doesn't seem to be the right way to attack concerns about greenhouse gas emissions," he says. The EPA

is “placing huge new regulatory burdens on industries that are import sensitive.” The regulations will place burdens on refineries, putting “their competitiveness at risk, and ultimately we’ll produce less gasoline here and end up importing it from refineries that are less energy efficient overseas."

Mr. Watson says Americans can accomplish a great deal with “affordable conservation.” And “a wealthy economy,” he adds, “is better able to deal with the costs of greenhouse gas abatement than a poor economy.” Since “large numbers” of countries are “unlikely to take aggressive action on greenhouse gas emissions,” the “U.S. is going to have to decide, just as California is going to have to decide, if they want to go it alone. . . . Are they willing to place the burden on our economy and our consumers, at the expense of jobs?"

That pretty much sums up the broader choice America faces on energy policy. It can listen to the Washington siren song on alternative energy, pouring scarce dollars into green subsidies, driving up the cost of energy, and driving out U.S. manufacturing and jobs. Or it can embrace our own fossil fuel resources, which are cheap and plentiful.

“What I see are people who want affordable energy,” says Mr. Watson. “They want strong environmental standards—they want a lot of things—but first and foremost they want affordable energy. And if you want affordable energy, you want oil, gas and coal."

Ms. Strassel writes the Journal’s Potomac Watch column.

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[1] http://online.wsj.com/article/SB10001424052748704013604576248881417246502.html