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I see this developing based on three main themes that are well entrenched.

Exporters to Consume More

The major exporters of crude oil in the Middle East have experienced a boom during the latest energy boom. Demographically, their populations are growing and GDP per capita has been improving of late. This results in more internal consumption and national oil companies must divert more revenue to social programs. My belief (which is supported by IEA data), is that within a generation many of the current exporting countries will be exporting less than they are today. I will focus on this issue in future articles and provide some data and projections based on the IEA statistics.

Lack of Economic Investment Opportunities

Most oil producers evaluate future energy projects based on a rate of return hurdle. To make these complex calculations you must assume a number of unknowable variables including expected future oil prices. The current environment of declining economic activity, unavailable credit and falling energy demand has forced energy companies to drastically reduce energy price forecasts. As you can imagine, this means that few projects can achieve the required minimum hurdle rate of return. The end result is that future projects are cancelled or delayed meanwhile the relentless mathematics of depletion wittle away at current oil production.

Taxes and Government Regulations

We are increasing regulations and complexity in the energy sector (carbon capture, cap and trade, environmental regulations are examples) while taxes are being increased (latest US budget proposals eliminates all subsidies and royalty breaks on US energy producers). I am not trying to make a political point here, just highlighting the unintended consequences of recent government actions. This will further dissuade the development of new energy projects and potentially reduce existing energy production.

Next month I will be making a powerful argument why we need to continue developing the oil sands so that we will benefit from the coming energy boom.

Derek Gates, CFA

Founder of the Oil Sands Sector Index TM

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(403) 454-0881 www.SWMindeX.com