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Emerging Market Oil Use Exceeds U.S. as Prices Rise (Update2)

By Mark Shenk


Enlarge/Details

April 21 (Bloomberg) -- Traffic jams in Beijing and humming air conditioners in Dubai are replacing U.S. highways and suburbs as the driver of global oil prices.

China, India, Russia and the Middle East for the first time will consume more crude oil than the U.S., burning 20.67 million barrels a day this year, an increase of 4.4 percent, according to the International Energy Agency in Paris. U.S. demand will contract 2 percent to 20.38 million barrels daily, the IEA says.

Economic growth of more than 8 percent in China and India, coupled with increasing car ownership among the countries' combined populations of 2.45 billion people, will more than compensate for falling U.S. demand. Oil use worldwide will increase 2 percent this year because of growth in emerging markets, the Paris-based IEA says.

``Does the U.S. matter anymore?'' said **Mike Wittner**, head of oil research at Societe Generale SA in London. ``Has the U.S. mattered for the last few years? It is debatable. As far as the oil market is concerned, demand growth is going to be continued to be driven by China and the Middle East.''

The rising oil price will benefit Exxon Mobil Corp., BP Plc and Royal Dutch Shell Plc, while punishing a U.S. airline industry that recorded four bankruptcies in a month. Higher energy costs will push up food costs at a time when corn and rice are close to new highs.

Crude oil futures rose 79 cents to settle at a record $117.48 a barrel on the New York Mercantile Exchange today, more than twice the level of three years ago.

Emerging Markets

CIBC World Markets, Societe Generale and Barclays Plc say oil prices are heading higher because of increasing fuel consumption in emerging markets, regardless of a U.S. downturn.

``The U.S. recession will be a footnote as far as the oil market is concerned,'' says **Jeffrey Rubin**, chief economist at CIBC World Markets Inc. in Toronto, who has correctly forecast higher oil prices since 2000. ``Supply isn't growing and demand is growing robustly in the developing world.''

Oil will average $120 a barrel for all of 2008, compared with almost $98 in the first quarter of the year, and reach $150 ``by the end of the decade,'' Rubin said.

Historically, a recession in the U.S. would lead to lower prices. Oil fell 26 percent to $19.84 a barrel in New York in 2001 when the economy contracted. The U.S. consumes 24 percent of the world's oil, down from 26 percent seven years ago.

Oil demand in both China and India will rise by 4.7 percent, according to the IEA. China, the world's second-biggest energy user, will consume 7.89 million barrels of oil a day this year. India will use 2.92 million barrels of oil a day in 2008, more than is pumped by OPEC member Venezuela.

Energy Use

Emerging markets burn a fraction of the energy of the U.S., leaving room for growth. The 2.45 billion people in China and India used only half as much crude as 301 million Americans last year. The average person in China consumed less than 20 percent as much energy as the average American in 2005, according to U.S. Energy Department. In India, energy use is less than 10 percent of America on a per-capita basis.

China's passenger car sales jumped 22 percent to 6.298 million last year and may rise 16 percent to about 7.3 million this year. China may boost vehicle output by a million units a year for the next decade to reach 20 million a year by 2017, according to the China Association of Automobile Manufacturers.

Russia and the Middle East are benefiting from rising oil prices. Russia's economy expanded at an annual 8 percent rate in the first quarter, the Economy Ministry said on April 17. Russia, the world's second-biggest oil exporter, will probably grow 7.1 percent this year, Russian Finance Minister **Alexei Kudrin** said on April 11.

Russian Growth

The Russian government plans to spend some of its new wealth on updating Soviet era transport links. Russia may invest as much as 21 trillion rubles ($895 billion) to improve transportation infrastructure during the next seven years, Transport Minister **Igor Levitin** said on Feb. 1.

Middle Eastern economic growth will probably accelerate to 6.1 percent this year from 5.8 percent in 2007, the International Monetary Fund said April 9. Oil demand in the region will surge 5.8 percent to 6.97 million barrels a day this year, according to the IEA.

``Many emerging economies are relatively isolated from the impact of the U.S. recession,'' said **Edward Morse**, chief energy economist at Lehman Brothers Holdings Inc. in New York. ``In the Middle East demand is expected to grow 350,000 barrels a day this year. These are a large number of very small countries having rampant demand growth.''

Hot Summer

Prices may rise as much as $20 a barrel this summer because of Middle East power needs, Morse said. A hot summer would likely result in more burning of crude oil for power generation and a diversion of natural gas from enhanced recovery of oil deposits.

``The predominant market view is that the emerging economies will overcompensate for any possible demand slump in OECD countries,'' said **Eugen Weinberg**, an analyst at Commerzbank AG in Frankfurt. ``I couldn't rule out that oil may go to $150.''

The Paris-based Organization for Economic Cooperation and Development represents 30 industrialized nations, including the U.S., Japan and Germany.

Government price caps and subsidies in India, China and the Middle East protect the public from higher gasoline and diesel prices, measures designed to limit inflation. In Iran, OPEC's second-biggest oil producer, subsidized gasoline pump prices are 1,000 rials a liter, about 11 U.S. cents.

Price Subsidies

``Subsidies of commodity prices buffer populations in oil emerging economies from price increases,'' Morse said. ``This has the effect of increasing fuel demand.''

U.S. pump prices have followed crude oil higher. Regular gasoline, averaged nationwide, rose 2.7 cents to a record $3.445 on April 18, according to AAA, the nation's largest motorist organization. In the U.K. a gallon of gasoline cost $7.99 on average on March 31, according the Automotive Association.

``Even if the fundamentals in general, particularly this quarter, were to weaken, we would think investment flow could be pushing prices to records anyway,'' Wittner said.

Investors have transferred money into commodities, especially energy, during the past year because their returns have outpaced stocks and bonds. Oil gained 22 percent, while the S&P 500 slid 5.6 percent and government bonds returned 12 percent, according to Merrill Lynch & Co. indexes.

Investments tied to commodity indexes rose as much as $4 billion in the first quarter, a third more than in the final three months of last year, Standard & Poor's said April 18.

``It makes sense for investors and hedge funds to invest in these commodities with the weakness of other markets,'' said **Eric Wittenauer**, an energy analyst at Wachovia Securities in St. Louis.

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