Oil and gas rush speeds-up as prices surge

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By

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With analysts predicting oil and gas prices to continue rising, investors are heading back to the sector.

A promising gas discovery revived interest in Buru Energy (ASX: BRU) earlier this week – delivering a 30% share-price rise in the latest example of investors returning to the politically incorrect oil and gas sector, a move which iron ore billionaire Gina Rinehart successfully made late last year.

Though miles apart in terms of size the common thread connecting Buru (a minnow valued at $97 million) and Rinehart (with her personal $40 billion fortune), is strong demand for gas, a fuel which is seen as a halfway house on the road to a renewable energy future.

A growing gas shortage in eastern Australia, accompanied by rising prices, is what drew Rinehart into a partnership with Korea's steel giant Posco in a joint $900 million takeover of Senex Energy.

That deal was settled at a time oil was selling for US$73 a barrel and showing signs of firming as global demand recovered from a two-year COVID-caused slowdown.

Since then, war in the Ukraine and sanctions on Russia have super-charged oil, which is now selling for around US$114/bbl, down from an early-March peak of US$127/bbl, which was a 14-year high.

There could be even higher prices to come as a global shortage of oil and gas worsens with one leading investment bank, Goldman Sachs, forecasting an oil price of US$175/bbl towards the end of the year and other analysts tipping a peak price of US$200/bbl.

What will happen if the oil price continues surging?

If those prediction of stunningly higher future prices are correct a number of developments can be expected, including:

- a revival in oil and gas exploration and project development as mothballed projects are dusted off;
- demand destruction as industry and households struggle to pay fuel bills;
- a sharp increase in sales of electric cars even as makers struggle to keep pace with demand; and
- higher prices for the family of battery metals such as lithium, nickel, copper and cobalt.

In time, as Bruce Apted from State Street Global Advisers pointed out earlier this week, the rally in oil and gas will fade as has always happened in the past with demand destruction butting head-first into increased production.

The challenge for investors is working out how long the current upward price move can last and while impossible to prove it is likely that government discouragement of oil and gas exploration and production could result in higher prices as some producers play catch up, while others direct capital into the long-term potential of renewables such as wind and solar.

Buru's share-price rise followed the latest testing of its Rafael gas discovery in the desert country south of Derby in Western Australia, a region which the small company has had almost to itself after an exit of oil majors because of poor exploration results.

High quality gas discovery

The latest report from Buru said the gas encountered was high quality (low carbon dioxide), with indications of the gas column being larger than originally mapped.

Whether it is the discovery, which puts Buru on the radar screen of bigger oil and gas companies remains to be seen but it is the sort of find in a highly-regarded onshore location which will be attracting attention despite decades of past failure.

Renewed interest

Other small oil and gas companies are also starting to attract renewed interest, including Vintage Energy (ASX: VEN) which has risen from $0.08 to $0.11 (up 37.5%) over the past month as it prepares to spud the onshore Cervantes-1 well in the North Perth Basin on-trend from the producing Cliff Head, Jingemia and Hovea oilfields.

Otto Energy (ASX: OEL), which is exploring in the southern US state of Louisiana, Cue Energy (ASX: CUE), Norwest Energy (ASX: NWE), Carnarvon Energy (ASX: CVN) and Central Petroleum (ASX: CTP) are also attracting increased interest as the oil price continues to rise.

Environmentalist's nightmare

What's happening in oil and gas is an environmentalist's nightmare because it had been hoped that the world could be weaned off its fossil fuel habit in order to try and limit global warming.

War in Ukraine, accompanied by threats to stop buying Russian oil and gas, has upended a plan hatched at last year's COP26 climate change conference in Glasgow to limit future oil and gas exploration. Even US President Joe Biden has changed his tune – calling for increased oil production.

Oil market

Small oil and gas companies have reacted modestly to changes in the oil market with the biggest winners at the top of the sector, led by Woodside Petroleum (ASX: WPL), which is up 41% to $32.15 since the start of the year, Santos (ASX: STO), which has risen 18% to $7.81, and Beach Energy (ASX: BPT), which is up 23% to $1.61.

The rest of the year could see prices continue to rise strongly, especially if an alarming forecast from the International Energy Agency is correct.

According to the IEA, the Paris-based energy think tank of western countries, the world is heading into the biggest oil and gas supply crisis in decades.

Global supply shock

The agency says what's happened so far in energy markets is just a warm up for what's to come, because sanctions on Russia are not yet fully in force, but will bite from next month when Russian supply could drop by as much as 3 million barrels a day – 3% of global production.

“A global oil supply shock is now plausible,” the IEA said, triggering lasting changes to energy markets, including a faster transition away from oil.

The IEA's proposed plan to mitigate the damage of sky-high oil and gas prices includes a number of radical suggestions, some of which last surfaced in the 1970s oil shocks when Middle East oil producers embargoed exports.

Top of the IEA's list is a worldwide 10 kilometre an hour reduction in highway speed limits, a three-day work from home regime, car free Sundays in cities, greater use of trains and limits on plane travel by business people.