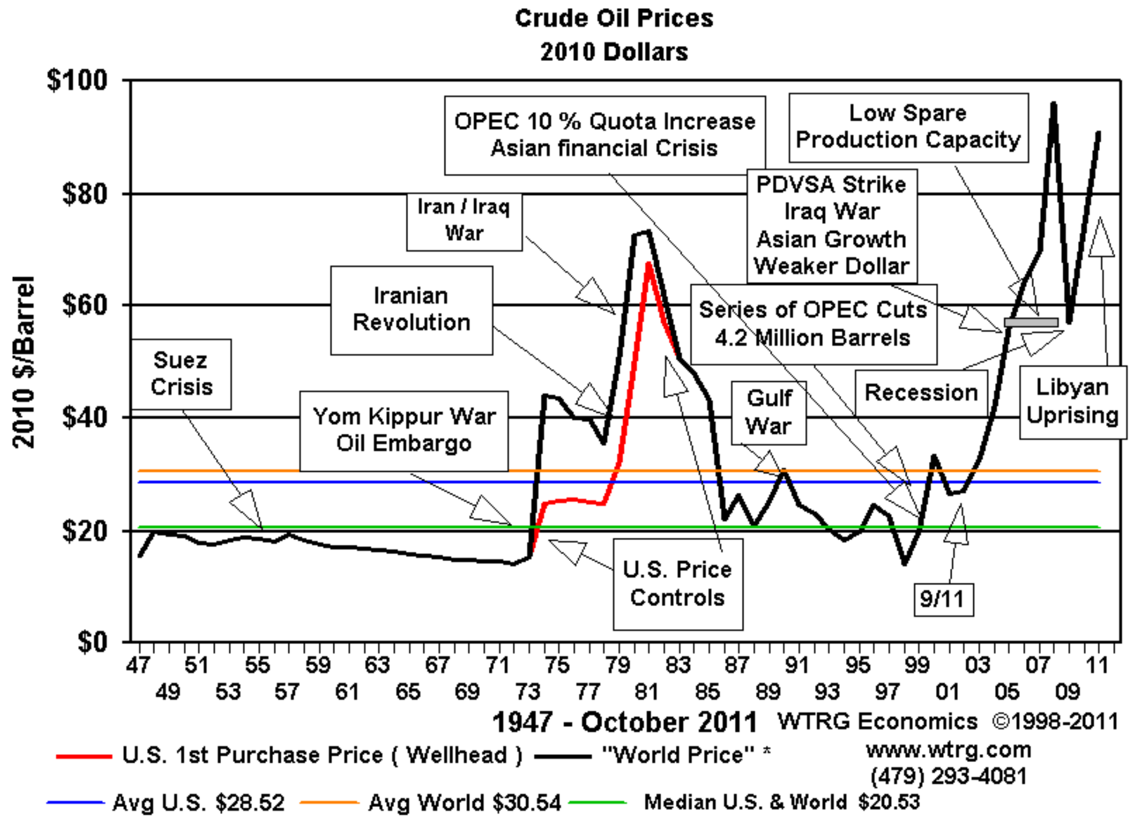
The story of oil supply and demand exercise

Preparation: Enlarge the graph below to A3 size and then paste it onto enough flipchart paper for students to work in small groups/pairs. Alternatively, split each story onto a separate piece of A4.

Task: The students need to match each story to the graph and then use a supply and demand graph to explain in each case what happened to the price of oil. In the flipchart version they can put each graph onto the flipchart with an arrow pointing to the year and you can stick them up on the walls. In the A4 version, they can just do a supply and demand graph between them on each sheet.

The source of all this is: **http://www.wtrg.com/prices.htm**



Yom Kippur War – Arab Oil Embargo

In 1972, the price of crude oil was below $3.50 per barrel. The Yom Kippur War started with an attack on Israel by Syria and Egypt on October 5, 1973. The United States and many countries in the western world showed support for Israel. In reaction to the support of Israel, several Arab exporting nations joined by Iran imposed an embargo on the countries supporting Israel. While these nations curtailed production by five million barrels per day, other countries were able to increase production by a million barrels. The net loss of four million barrels per day extended through March of 1974. It represented 7 percent of the free world production. By the end of 1974, the nominal price of oil had quadrupled to more than $12.00.

Crises in Iran and Iraq

In 1979 and 1980, events in Iran and Iraq led to another round of crude oil price increases. The Iranian revolution resulted in the loss of 2.0–2.5 million barrels per day of oil production between November 1978 and June 1979. At one point production almost halted. …

In September 1980, Iran already weakened by the revolution was invaded by Iraq. By November, the combined production of both countries was only a million barrels per day. It was down 6.5 million barrels per day from a year before. As a consequence, worldwide crude oil production was 10 percent lower than in 1979.

The loss of production from the combined effects of the Iranian revolution and the Iraq-Iran War caused crude oil prices to more than double. The nominal price went from $14 in 1978 to $35 per barrel in 1981.

Opec Fails to Control Crude Oil Prices [1980–1994]

During the 1979–1980 period of rapidly increasing prices, Saudi Arabia's oil minister Ahmed Yamani repeatedly warned other members of OPEC that high prices would lead to a reduction in demand. His warnings fell on deaf ears. Surging prices caused several reactions among consumers: better insulation in new homes, increased insulation in many older homes, more energy efficiency in industrial processes, and automobiles with higher efficiency. These factors along with a global recession caused a reduction in demand which led to lower crude prices. … Higher prices in the late 1970s also resulted in increased exploration and production outside of OPEC. From 1980 to 1986 non-OPEC production increased 6 million barrels per day. Despite lower oil prices during that period new discoveries made in the 1970s continued to come online.

[Late 90s recovery]

The price cycle then turned up. The United States economy was strong and the Asian Pacific region was booming. From 1990 to 1997, world oil consumption increased 6.2 million barrels per day. Asian consumption accounted for all but 300,000 barrels per day of that gain and contributed to a price recovery that extended into 1997. Declining Russian production contributed to the price recovery. Between 1990 and 1996 Russian production declined more than five million barrels per day.

[Price surge in the 00s]

Problems in Venezuela led to a strike at PDVSA causing Venezuelan production to plummet. In the wake of the strike Venezuela was never able to restore capacity to its previous level and is still about 900,000 barrels per day below its peak capacity of 3.5 million barrels per day. OPEC increased quotas by 2.8 million barrels per day in January and February 2003.

On March 19, 2003, just as some Venezuelan production was beginning to return, military action commenced in Iraq. Meanwhile, inventories remained low in the U.S. and other OECD countries. With an improving economy U.S. demand was increasing and Asian demand for crude oil was growing at a rapid pace. …

Other major factors contributing to higher prices included a weak dollar and the rapid growth in Asian economies and their petroleum consumption. The 2005 hurricanes and U.S. refinery problems associated with the conversion from MTBE to ethanol as a gasoline additive also contributed to higher prices.

[The Credit Crunch (2008…)]

[The economic meltdown that affected most of the developed world had a major effect on the oil market, with the price plummeting. This was as a result of higher unemployment reducing car (and therefore petrol) usage and reduced business activity reducing the demand for power.]

[OPEC responds to the credit crunch (2009)]

Following an OPEC cut of 4.2 million b/d in January 2009 prices rose steadily in the supported by rising demand in Asia. In late February 2011, prices jumped as a consequence of the loss of Libyan exports in the face of the Libyan civil war. Concern about additional interruptions from unrest in other Middle East and North African producers continues to support the price…