Energy Insider by William Engdahl

Volcker ends the drilling boom

Some basic industrial economics suggest a shift in strategy is urgent for U.S. independent companies.

From the end of the last year through the middle of March, domestic U.S. oil and gas exploration underwent the sharpest decline in history. In this three-month span, the number of active drilling rigs fell to about 3,900. The all-time peak in activity was almost 4,600 last summer when the advantage of high potential profits in the face of collapse in the overall economy made oil exploration "almost the only game in town," as one independent called it. But as rapidly as certain political decisions fed the domestic "oil boom," it seems to have collapsed.

The irony of the sharp swings in domestic oil exploration is thus that the underlying reasons are entirely lawful. It is not the case that the oil sector was "overheated." The remainder of the economy—steel, auto, agriculture, highway construction, transportation, and other oil and natural gas consumers—is in the early stages of deliberate Fed-induced depression.

I have been talking with independent oil and gas producers as well as financial houses which specialize in such investment. While very few appreciate with sufficient urgency what is at stake in the monetary Russian roulette of Mr. Volcker, all of them know something serious is wrong.

One Dallas-based industry analyst who himself heads an independent oil company, Philip Crouse, estimates that as much as $6 to $8 billion of what he calls "funny money" has disappeared in the last three months from the speculative rush into oil drilling. By "funny money," Crouse explains, he means funds which chased into U.S. domestic oil drilling because of the unique conjuncture of events of the last three years.

In 1980, the Carter administration introduced a phased decontrol of domestic crude-oil prices. John Sawhill was running Department of Energy policy as Deputy DOE Secretary. Sawhill, who drafted strategic energy policy for David Rockefeller's Trilateral Commission, is a long-standing strategist for Arco Chairman Robert O. Anderson's zero-growth think tank, the Aspen Institute. This point is relevant because Sawhill's oil decontrol strategy had nothing to do with a solution to tight energy supplies in the wake of the Iran cutoff of 1979. He instead coupled the higher price (which predictably increased incentive for more domestic drilling) with the largest domestic tax in the nation's history: a $227.3 billion dollar excise tax at the wellhead. Sawhill and Carter at the time emphasized that this tax, termed the "Windfall Profits Tax," would ensure continued "conservation." What it specifically ensured was a windfall for Robert O. Anderson. Arco's oil is primarily in the rich North Slope of Alaska; Sawhill wrote the Windfall Profits Tax Act of 1980 to *exempt* Alaska oil.

The effects of domestic decontrol, combined with Reagan's February 1981 decision to impose immediate decontrol of domestic oil to world-price levels, created a special incentive for "funny money" from Canada, Europe, and the Bahamas as well as legitimate small investors searching for some haven amidst the general economic collapse.

The problem with all this is the fundamental lack of sound economic-growth strategy for the nation. During the 1980 election campaign, Reagan was backed by some of the most financially influential political action committees, those linked with various groups in Texas, Louisiana, and other locations of independent producers. Rightly angry with Carter-Sawhill policies such as the windfall tax, they backed Reagan to the hilt.

Numbers of groups such as the national Independent Petroleum Association of America, TIPRO in Texas, and IPAMS in the Rocky Mountains, poured millions into the Reagan and other Republican campaigns. This was well and good in the face of Jimmy Carter. But the outlook was tragically "single-issue." As a result, groups with influence such as the IPAA abstained from the fight against Volcker and Stockman while they focused on legal efforts to repeal the windfall tax and push for immediate natural-gas decontrol.

As a symbol of their own narrow-interest stupidity, the same IPAA which mobilized to defeat the windfall tax gave Anderson their highest honor last November. And Arco is one of the few oil stocks being pushed by Wall Street today—because Arco's Alaska oil is exempt from the windfall tax.