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Submission to the Finance and Expenditure Committee on the Budget Policy
Statement 2005 (BPS 2005) and associated December Economic and Fiscal Update
2004 (DEFU 2004)

Introduction

This submission is from The Sustainable Energy Forum Inc (SEF).

SEF requests the opportunity to appear before the Committee to speak to our submission. Our contact details are above. The contact person is Tim Jones, Management Committee member.

The objective of The Sustainable Energy Forum Inc. is to facilitate the transition to sustainable energy. The Forum has about 130 individual and corporate members, including business people, academics and interested individuals.

In accordance with SEF's submission policy, we declare that this submission has been prepared and reviewed by members of the SEF Management Committee. Due to time constraints, it has not been circulated to all SEF members for approval.

Comments

Between the Budget Economic and Fiscal Update 2004 (BEFU 2004), released in May 2004, and DEFU 2004, Treasury's estimate of the oil price at the end of the forecast period rose from US \$19.50 per barrel to US \$35 per barrel — an increase of 80% in just over six months. Furthermore, both the BEFU 2004 and DEFU 2004 predictions assume a decline in price from current levels during the forecast period. In the case of the BEFU 2004 prediction, this proved to be incorrect.

SEF submits that there is a high likelihood the DEFU 2004 estimate is at the low end of a wide range of possible future oil prices. Oil prices have entered a period of unprecedented uncertainty, due to swiftly rising demand (particularly in China and India), geopolitical concerns, the threat of terrorist attacks on the production and distribution of oil, and concern over an impending peak in world oil production. In such an environment, sharp and sudden oil price rises are likely, with negative effects on the New Zealand and world economies. Therefore, SEF **recommends** that the Treasury's oil price forecasting methods be reviewed, and that, rather than deciding on

one forecast price, Treasury model the economic effects of a range of oil price outcomes by the end of each forecasting period.

At some point, world oil production will peak, and then decline — a phenomenon commonly known as "Peak Oil". This will lead to a sharp, sustained rise in world oil prices, and physical shortages of oil. A possible upper bound on the oil price in a Peak Oil situation may be the cost of producing oil from a non-petroleum source such as coal, which capped the oil price in the 1970s. We note that the climate change consequences of such oil production are likely to be most adverse.

Until recently, most estimates were that Peak Oil would not occur for many decades. In recent years, a number of reputable bodies have predicted that Peak Oil may occur much earlier than previously expected. The Association for the Study of Peak Oil, comprised of experienced petroleum geologists, is currently predicting that the peak will occur in 2007. Other bodies, using different methodologies, predict the peak by 2020. US official estimates tend to be more optimistic.

The most pessimistic projections may be wrong, although recent events — such as the sharp increase in world oil demand, and the large downwards revisions of oil reserve estimates by Shell Oil and others — have lent weight to them. If the peak does occur soon — which can only be confirmed after the fact — the effects on an unprepared economy will be severe. Therefore, SEF **recommends** that the Government set up an interdepartmental working party on Peak Oil, to work in consultation with relevant civil society organisations, with the aims of evaluating the various Peak Oil scenarios, modelling their effects on New Zealand, and making recommendations on policies to mitigate their impact. We further **recommend** that the scope of policy investigations should include consideration of the full range of renewable energy sources and strategies to reduce the demand for transport fuels, so that New Zealand becomes more resilient with regard to imported energy.

Recommendations

1. That the Treasury's oil price forecasting methods be reviewed, and that, rather than deciding on one forecast price, Treasury model the economic effects of a range of oil price outcomes by the end of each forecasting period.
2. That the Government set up a interdepartmental working party on Peak Oil, to work in consultation with relevant civil society organisations, with the aims of evaluating the various Peak Oil scenarios, modelling their effects on New Zealand, and making recommendations on policies to mitigate their impact.
3. That the scope of policy investigations should include consideration of the full range of renewable energy sources and strategies to reduce the demand for transport fuels, so that New Zealand becomes more resilient with regard to imported energy.