Mind the energy investment gap

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In my opinion, a global energy crisis and an investment crisis are likely to affect Australia well before any climate crisis. I have six reasons for saying this.

First of all, energy demand growth, mainly in the developing countries, is outstripping supply. The “peak oil” theory (the theory that oil fields are depleting at a rate in excess of global consumption) does not explain the global energy security problem. The fundamental cause is energy demand growth, which is itself driven by population growth, economic growth, industrialisation and urbanisation.

Second, national oil companies continue to exercise significant control over global oil production levels. Although they have an incentive to maintain supply and protect their oil revenues, they show no signs of wanting to run down their reserves prematurely.

At the same time, many of the oil-exporting countries are experiencing political unrest.

Third, most undeveloped oil fields are in offshore areas with high development costs and many carry the risk of maritime border conflict.

Fourth volume and price risks in energy supply are systematically passed through to importing economies and consumers, who have less and less control over what happens. Today, Japan, Germany, France, Spain, the Netherlands, South Korea, Taiwan and Singapore are 100 per cent dependent on foreign oil. India is 75 per cent dependent, the United States is 60 per cent dependent, China is over 50 per cent dependent and Australia is 40 per cent dependent. They are all vulnerable to a global oil supply crisis.

Fifth, efforts by governments to devise effective regulatory responses to the threat of global climate change have stalled, adding to investment uncertainty. A recently-released study by Mercer indicates the need for institutional investors to better hedge their climate change risk by investing 40 per cent of their portfolios in “climate-sensitive assets”, with an emphasis on those that can adapt to a low-carbon environment.

Sixth, in the aftermath of the global financial crisis, the availability of investment capital is less assured.

These unprecedented circumstances are combining to open up a serious energy investment gap. The transportation sector, including the shipping, aviation and motor vehicle industries, is particularly vulnerable. Could this eventually expose the economic foundations of the global economy to intolerable strain?

Policymakers in all countries have been too slow to respond. Since 2008, the International Energy Agency has been reminding us that “current trends in energy supply and consumption are unsustainable, environmentally, economically and socially”.

All of these factors point to the most important priority for governments being to provide investors with more attractive, durable policy settings, with the aim of reducing the investment gap.

However, this begs the question: investment in what? If there is little prospect of finding oil in Australia, investment must be made in sustainable substitutes. What might they be? And how and when will the required investments be made?

These are not simple questions and the answers depend on a myriad of variables.

These questions will be explored further at the upcoming Energy State of the Nation event to be held by the Energy Alliance in Sydney on March 31. See www.energyalliance.com.au for further details.

Robert Pritchard is executive director of the Energy Alliance of Australia.

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