Gulf of Mexico Rig Count Records Strong Increase

The Gulf of Mexico offshore rig count is currently 20 percent above last year’s level. The strength of the Gulf count can be traced to federal leasing policies, poor prospects in competing offshore areas, and technological changes enhancing the feasibility of drilling and production in deep water.

Rig Activity Boosted by Several Factors

Oil and gas drilling in the Gulf of Mexico is concentrated offshore of Texas and Louisiana. Because much of this area is within the purview of the Federal Government, the nation’s offshore leasing policy has a direct effect on drilling opportunities. In an effort to increase domestic oil and gas reserves, the pace of federal leasing has been accelerated recently (Chart 1). Of all the acreage leased since the program began in 1954, 40 percent has been leased in the past three years. The favorable opportunities provided by the newly available leases have led to an increase in drilling. Activity is also sustained by the Federal Government requirement, for most leases, that a tract be drilled within five years.

Another factor that has buoyed offshore drilling is recent developments allowing placement of platforms in deeper waters. The improvements in technology can be observed from the record for deepwater platforms. In 1976 a new depth record was set when a platform was placed in 860 feet of water. Now, several platforms have been installed in over 1,000 feet of water. New types of platforms have been developed that show promise in extending the depth for oil production to 3,000 feet, far beyond the limits of conventional platforms. This ability to produce oil from deeper water has increased drilling activity in the Gulf of Mexico’s deepwater tracts.

Poor drilling prospects in other areas of the world have also led to an increase in the Gulf of Mexico rig count. Relatively unfavorable government terms for petroleum production and a lack of discoveries have discouraged drilling in some regions, causing rigs to move to the Gulf of Mexico. In July 1983 there were 212 active and inactive rigs in the Gulf. The total number of rigs has increased to 246 recently. Chart 2 illustrates the fall in drilling in 1982 and 1983. Since then, the Gulf count has increased significantly compared with the count in the rest of the offshore areas. Further, the Gulf count has maintained its strength during this summer’s oil price instability, while the Texas onshore count has declined 10 percent.

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Economic Recovery May Have Disappointed OPEC

Despite a world economic recovery, consumption of oil produced by members of the Organization of Petroleum Exporting Countries has not increased. While world oil consumption has grown slowly over the past year, this growth has been matched with increased production from sources outside OPEC. As a result, excess capacity of OPEC producers remains at about 12 million barrels per day, roughly 20 percent of current world oil consumption. This excess capacity and the prospects for slow growth in world oil consumption will continue to test the resolve of OPEC to maintain current official prices.

World Oil Consumption Finally Growing

Following a four-year decline, world oil consumption rose only about 2 percent, or 1 million barrels per day, during the past year. Reductions in the oil consumption per unit of gross national product in major industrial countries (Chart 3), along with slow economic recovery outside the United States, may continue to restrain the growth of world oil consumption for some time. Adjustment to higher oil prices appears largely responsible for falling oil-GNP ratios. The unexpected strength of the dollar has also contributed to falling oil consumption, because the increased value of the dollar against European currencies has made oil, which is priced in dollars, more expensive in some European countries than it was in 1980.

Although weak economic growth outside the United States has restrained the growth in world oil consumption, (Continued on back page)
The recovery in the U.S. energy industry has slowed somewhat in recent months, but firmer oil and gas prices foreshadow further improvement in the sector.

- Lower OPEC crude oil production has reduced some of the downward pressure on crude prices. After recent declines, spot market prices have risen, and non-OPEC producers have exhibited less willingness to discount from official prices. Other factors contributing to firming prices include a 2-percent increase in U.S. gasoline consumption this summer over last and the British coal miners' strike, which has boosted reliance on oil.
- The recent weakness in oil prices has reduced drilling activity. The U.S. rig count fell in July and August, although it was still 7.9 percent above the year-earlier level. The Texas rig count has dropped an average of 3.1 percent per month since June. These monthly declines mask the substantial increase in offshore drilling that has occurred recently.
- Improvement in the leading indicators of drilling activity portends an increase in drilling in the near future. The U.S. seismic crew count continues to outpace its 1983 levels; in August it was 8.2 percent above a year before. The number of well permit applications, another leading indicator, has remained steady.
- The energy recovery in the first half of 1984 led to more jobs in the oil field machinery sector in Texas. Employment in this industry increased again in August, rising 9.9 percent above the level a year earlier. It has now increased in six of the first eight months of this year.
- Excess capacity and foreign competition hinder the refining industry. Refinery employment continued to fall in August, reaching its lowest level since 1982. Several refiners in the region have announced planned layoffs or capacity reductions, and some have closed altogether.
Rig Count (cont.)

Outlook

The short-term outlook for the Gulf of Mexico remains bright. The number of platforms under construction is at its highest level since late 1981. The Federal Government is approving greater numbers of operator-prepared plans for drilling; such plans are an indicator of future drilling activity. The government's program for additional lease sales should provide a plentiful supply of prospective tracts. One factor that may slow the rate of leasing is a continuing controversy between the states and the Federal Government over sharing of revenues from oil fields that straddle both jurisdictions. Legal attempts to settle this dispute could lead to a halt or reduction in leasing. Oil price stability will also play a role in the rig count. If prices were to decline materially, offshore drilling activity would decrease.

—Roger H. Dunstan

Recovery (cont.)

sumption, it may not have held oil prices down by much. Undeveloped oil reserves have very low storage costs, so it is inexpensive for most OPEC countries to hold oil off the market when its demand is temporarily depressed for cyclical reasons. Because general world economic conditions in the late 1970s and early 1980s reduced oil demand, OPEC oil production sharply contracted, restraining the price decline. Conversely, OPEC oil production can be expected to expand when general world economic conditions increase oil demand, restraining any price rise.

Production Pressure

The long-term development of oil resources by non-OPEC producers has continued—largely at the expense of OPEC's market share. From the second half of 1976 to the first half of 1984, non-OPEC oil production climbed from 48 percent of total world oil production to 68 percent (Chart 4). During the same period, OPEC oil production fell 14 million barrels per day. The increase in non-OPEC oil production over the past year just about equaled the increase in world oil consumption.

During 1982 and 1983, much of the pressure on OPEC to increase production was financial. The pressure to earn revenue has been eased, however, because OPEC countries have reduced their investment projects. Nevertheless, the weakness of the recent recovery in oil demand may cause some OPEC countries to reevaluate the long-term desirability of their current production restraint.

—Stephen P. A. Brown