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Oil's "Lower for Longer" theory begins to crack.

Oil: One Year

That's the global price of crude oil, this past year. During most of it, oil has seemed to be firmly trapped in the $40 - $60 range which the oil market bears (and there've been lots of them) called the "Lower for Longer" scenario. But these past 3 months have acted a little differently, haven't they, as oil rocketed up 35%.

The "Lower for Longer" theory was thunk up during oil's awful bear market from 2014 to 2016, and beyond—as oil wallowed in this $40 - $60 swamp, after its bounce up from the Bear Market bottom. As Outlook has noted more than once, there are a great many clever people in the investment world—and they have no trouble coming up with sophisticated explanations of just about anything going on in any market. The real "trouble," however, is that for all their cleverness, they are also mere human beings, subject to all the weaknesses of us non-clever people, maybe more. And one of the worst of those weaknesses, when it comes to investing, is our powerful mental and emotional tendency to conclude that whatever a market is doing right now, it'll probably keep doing that for quite a while. It is just hard for us to imagine dramatic changes in the status quo—so even when we think we're being mighty analytical, we usually find our analyses gravitating toward the conclusion that dramatic changes just aren't in the cards.

Outlook has felt, this past couple of years, that "dramatic change" was the one sure thing in the oil market's future. It's been a real pleasure, as we waited for it, to find a very small number of analysts who agreed, and who backed up their opinions with deep research into the oil market's "facts," and with common sense observations about the eternal workings of supply and demand. So it was with even more pleasure that we read yesterday's piece in the Wall Street Journal, titled "U.S. Shale Juggernaut Shows Signs of Fatigue." The reporters gathered a good many colorful quotes from shale executives, and it was really remarkable how those remarks exactly echoed what those hardy few analysts have been saying for up to two years now, without getting much agreement until now.

- **“There are no new shale plays that have come forward,” said Mark Papa, chief executive of Centennial Resource Development Inc. and former CEO of EOG Resources Inc. “Their ability to spew forth infinite streams of oil is really just a myth.”**

- **Though the EIA has revised its forecast for oil production, which has averaged roughly 9.16 million barrels a day so far this year, its estimate is still too high, according to Harold Hamm, CEO of Continental Resources Inc. “The EIA’s phantom forecast needs huge growth to catch up to projections,” said Mr. Hamm, one of the pioneers of North Dakota’s Bakken Shale formation.**

- ***Pioneer Natural Resources PXD -0.46%* Co. CEO Tim Dove said at a conference in Oklahoma City that a “thundering herd” of investors has asked the company to focus on returns, not growth. The firm stunned shareholders in August when Mr. Dove said some recently drilled wells in the Permian basin—a region in Texas and New Mexico that has *become the hottest drilling spot in the world*—were a “train wreck.” Underground pressure problems stymied output and delayed drilling for months, he said. Pioneer says the problem has been solved, but the solution added about $400,000 to the cost of each well. Now, Pioneer is having to chipping away elsewhere to make up the difference.**

- **Delays for fracking and related services are also becoming problematic. Permian producers *Parsley Energy , PE -1.78% Callon Petroleum Co. CPE -2.67%* and *QEP Resources Inc. QEP -5.58%* recently reduced production estimates, citing delayed fracking services and other challenges.**

- **Based on barrels pumped per foot of well length, new wells in key regions of the Permian basin haven’t been significantly more productive since 2014, according to Tudor Pickering Holt & Co. “All these factors are pointing to slower, more methodical development,” said David Pursell, managing director at Tudor Pickering Holt, an energy investment bank. “That needs to happen.”**

- **Critics have long complained that a tie between company leaders’ pay and production growth (rather than profits) has led to a “drill at any cost” mentality. “They need to drill at a regulated pace, generate returns and give that cash back to shareholders,” said Mr. Holt (of Invesco, a major investor in shale companies.)**

Every one of these observations—and more—were made by our “hardy few” oil-market bulls, among the analysts, over the past 12 to 24 months. Most of them were also made by Mr. Paal Kibsgaard, CEO of Schlumberger (Oil Equipment King, and new Outlook core company.) To say that they were disbelieved and dismissed would be understating it. But they were right and, as always with the market, the tide of opinion only began to shift their way after the price of oil began to move up, sharp and fast enough, to shake the tide-swimmers into wondering if, just possibly, “dramatic change” might be in the cards after all.

At Outlook we aren’t wondering . . . we’re pretty sure of it. We’re holding some outstanding companies, which have coped with the oil Bear Market very well: Conoco, Schlumberger, Royal Dutch Shell, Transocean. We suspect it will be a long ride.

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