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Running Out of Planet to Exploit

By PAUL KRUGMAN

Nine years ago The Economist ran a big story on oil, which was then selling for $10 a barrel. The magazine warned that this might not last. Instead, it suggested, oil might well fall to $5 a barrel.

In any case, The Economist asserted, the world faced “the prospect of cheap, plentiful oil for the foreseeable future.”

Last week, oil hit $117.

It's not just oil that has defied the complacency of a few years back. Food prices have also soared, as have the prices of basic metals. And the global surge in commodity prices is reviving a question we haven’t heard much since the 1970s: Will limited supplies of natural resources pose an obstacle to future world economic growth?

How you answer this question depends largely on what you believe is driving the rise in resource prices. Broadly speaking, there are three competing views.

The first is that it’s mainly speculation — that investors, looking for high returns at a time of low interest rates, have piled into commodity futures, driving up prices. On this view, someday soon the bubble will burst and high resource prices will go the way of Pets.com.

The second view is that soaring resource prices do, in fact, have a basis in fundamentals — especially rapidly growing demand from newly meat-eating, car-driving Chinese — but that given time we’ll drill more wells, plant more acres, and increased supply will push prices right back down again.

The third view is that the era of cheap resources is over for good — that we’re running out of oil, running out of land to expand food production and generally running out of planet to exploit.

I find myself somewhere between the second and third views.

There are some very smart people — not least, George Soros — who believe that we’re in a commodities bubble (although Mr. Soros says that the bubble is still in its “growth phase”). My problem with this view, however, is this: Where are the inventories?

Normally, speculation drives up commodity prices by promoting hoarding. Yet there’s no sign of resource hoarding in the data: inventories of food and metals are at or near historic lows, while oil inventories are only normal.
The best argument for the second view, that the resource crunch is real but temporary, is the strong resemblance between what we’re seeing now and the resource crisis of the 1970s.

What Americans mostly remember about the 1970s are soaring oil prices and lines at gas stations. But there was also a severe global food crisis, which caused a lot of pain at the supermarket checkout line — I remember 1974 as the year of Hamburger Helper — and, much more important, helped cause devastating famines in poorer countries.

In retrospect, the commodity boom of 1972-75 was probably the result of rapid world economic growth that outpaced supplies, combined with the effects of bad weather and Middle Eastern conflict. Eventually, the bad luck came to an end, new land was placed under cultivation, new sources of oil were found in the Gulf of Mexico and the North Sea, and resources got cheap again.

But this time may be different: concerns about what happens when an ever-growing world economy pushes up against the limits of a finite planet ring truer now than they did in the 1970s.

For one thing, I don’t expect growth in China to slow sharply anytime soon. That’s a big contrast with what happened in the 1970s, when growth in Japan and Europe, the emerging economies of the time, downshifted — and thereby took a lot of pressure off the world’s resources.

Meanwhile, resources are getting harder to find. Big oil discoveries, in particular, have become few and far between, and in the last few years oil production from new sources has been barely enough to offset declining production from established sources.

And the bad weather hitting agricultural production this time is starting to look more fundamental and permanent than El Niño and La Niña, which disrupted crops 35 years ago. Australia, in particular, is now in the 10th year of a drought that looks more and more like a long-term manifestation of climate change.

Suppose that we really are running up against global limits. What does it mean?

Even if it turns out that we’re really at or near peak world oil production, that doesn’t mean that one day we’ll say, “Oh my God! We just ran out of oil!” and watch civilization collapse into “Mad Max” anarchy.

But rich countries will face steady pressure on their economies from rising resource prices, making it harder to raise their standard of living. And some poor countries will find themselves living dangerously close to the edge — or over it.

Don’t look now, but the good times may have just stopped rolling.