

Lacalle, Daniel & Parrilla, Diego – The Energy World Is Flat

John Wiley & Sons, 2015, [Business] Grade ★★★

Two portfolio managers offer their view of the energy markets in a forceful manner. Their opinions would have few supporters a year ago but after the recent declines in oil prices the followers have probably increased in numbers. Madrid born Daniel Lacalle entered the financial markets after working a decade in the energy sector at Repsol. At PIMCO Lacalle was voted number one among European buy-side managers. Diego Parrilla is a commodity hedge fund manager. Their thesis is that energy prices will drift downwards over the longer term. *“The last barrel of oil will not be worth millions. It will be worth zero.”*

As the authors see it a number of factors conspire to drive energy prices down. Future energy demand is often overestimated. Increasing efficiencies has meant that the amount of oil needed to generate a percent of GDP-growth has been going down for decades. Despite okay economic growth post the financial crisis US has actually had flat energy consumption since 2005.

Short-term substitution between energy sources is tricky as power plants, ships, vehicles are constructed for one energy source and the life of this equipment is long. Over time however, differences in prices between energy sources spur human ingenuity and substituting technologies are created. Oil has had a near monopoly on powering means of transportation – until now. Electric cars and other emerging technologies are starting to make their way into the vehicle fleets lowering the demand for oil.

At the same time technological advances have created a supply glut in energy markets. This applies to fracking and horizontal drilling in the natural gas market as well as for state subsidized and overbuilt renewable energy sources. What

really drives the “flattening” of the energy market, meaning the equalization of access and price levels, is a combination of build of pipelines, an expansion of LNG capacity, better connected energy grids and a more geographically diverse access of alternative energies like shale gas in China, tar sand in Canada, deep-sea oil in Brazil and so on. The result of all the above factors is lower and more uniform energy prices for the long run.

I like the thesis; I’m more mixed when it comes to the book. The author – and I write in singular as it is unclear what Parrilla has contributed – is smart, knowledgeable, experienced and funny in a cynical kind of way. He’s also unfocused, comes about as superior and lecturing and as lazy as he hasn’t taken the time to structure the book better. Although I agree that most of what’s being said sounds reasonable it doesn’t have to be said so many times in so many places in a book and some of the topics are fairly remote from the subject of energy markets – Lacalle’s opinions on investing, politics and economics all get air time. It’s hard to figure out whom the book has been written for. The book should have been shorter and more distinct.

That said the public discourse on energy markets too often centers on the views of Wall Street analysts and oil executives who have a vested interest in rising energy prices or on environmentalists and peak-oilers who substitute flaming opinions and good intentions for broad understanding of a very complex sector. This book brings forward a voice that is in short supply, which is excellent.

In the end it’s a balance between an interesting point of view and a less than perfect workmanship as an author and editor – I’m glad to have read the book.

Mats Larsson, September 2, 2015