



AUGUST 2023

SIPES HOUSTON

ENERGY ENTREPRENEURS

NO AUG LUNCHEON

Great Unconformity Video

Riots To Stop Renewables

US Saudi Relations

Oil Demand Booming

Permian Basin Depleting?

TX Says "No" To Wind Farm



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On the cover:*A gentleman's breakfast.*

LETTER FROM THE EDITOR

There is no luncheon for August. The next luncheon will be on September 21st.

There are a few videos in this newsletter. To watch them, click on the images to be taken to YouTube.

Oil short sellers are bleeding out in the streets. Oil demand is going strong, and to learn more about that, look on Page 14 to learn from Robert Bryce.

For a more Geology focused post, page 4 is a fascinating video about the Great Unconformity in Cody, Wyoming.

I hope some of you were able to leave the Houston heat for some summer vacation time. I know some of you are still selling your prospects, and some are currently drilling their prospects.

The Houston SIPES Board has a new member. Andrew Munoz will be taking over the Website Chair position from Sasha Gumprecht. All of the board members are thankful for the hard work Sasha endured to bring us a new website and streamline many services that make being a member of SIPES much easier. She will be missed.

Stay lean, stay hungry,
Jeff Allen



SEPTEMBER 21ST LUNCHEON

NO AUGUST LUNCHEON

Texas Coastal Processes - Brazos River Delta to Galveston Island

Synopsis:

Sites ~60 miles south of Houston along ~35 miles of the SE Texas coastline provide excellent locations to observe coastal sedimentological processes and their resultant deposits. This section of the Texas coast is characterized by barrier islands separated by tidal inlets and river outlets. The larger, sand-ridge cored, prograding Galveston Island contrasts with the smaller, wash-over dominated, retreating Follets Island and is separated by the stable, long-lived San Luis Pass that exhibits well developed flood and ebb tide delta systems. The Brazos River empties into the Gulf of Mexico to the south of Follets Island and forms a wave-dominated delta system. The Brazos River Delta has undergone significant changes due to human intervention and demonstrates the dynamic nature of sediment movement and deposition along the coast. This section of the coast provides insight into the steady lower energy background processes of sediment movement and the higher energy short term events, and the resultant reservoir characteristics of clastic coastal deposits from these different mechanisms. The understanding gained from these modern systems can be applied as an analog for subsurface exploration and production along the Gulf Coast and elsewhere.

Date & Location:

Thursday, September 21st
Petroleum Club

Time:

Wine Served 11:00am
Lunch Served 11:30am

Purchase Ticket:**Speaker:**

Erik D. Scott, Ph.D.
Vecta Oil & Gas
Rice University
E&P Geoscience, LLC

**REMINDER**

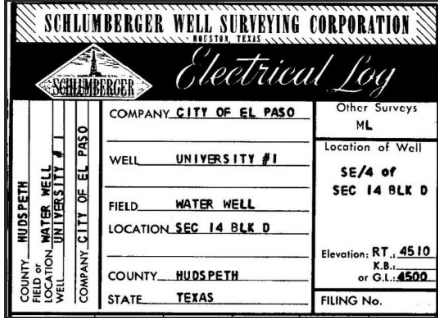
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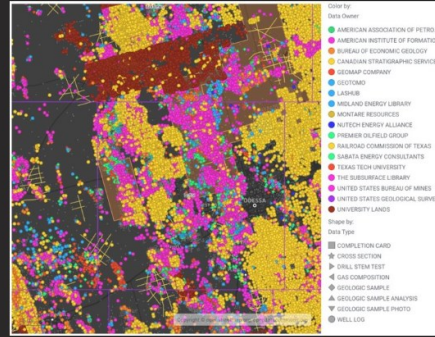


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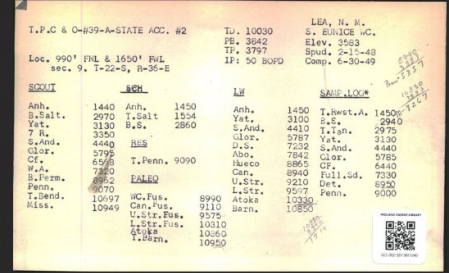
Keep an eye out for the release of our premium version in March 2022!



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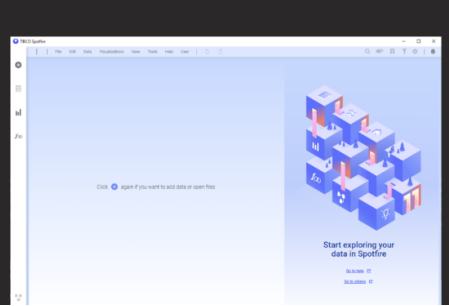
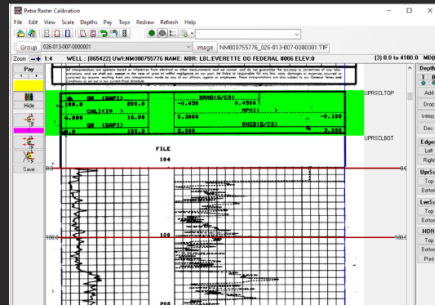
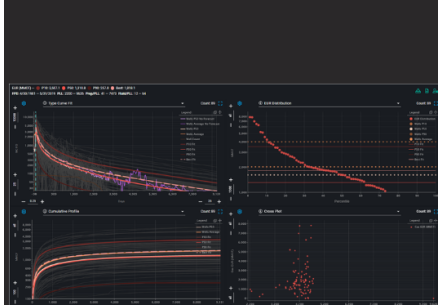
Be sure to check out our proprietary way to catalog well logs and index cards — we can tag & bag data 5x faster and 20% cheaper than our competitors thanks to our strategic partnership with Geolumina!

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Like our Spotfire dashboards? Let us put our skills to work on your internal data! We regularly build dashboards for clients as well as provide training for TIBCO Spotfire and Python.

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The Great Unconformity in Cody, WY



The Great Unconformity near Cody, WY: over 2 billion years of geologic time on one surface!

One of the most mind blowing geologic features in western North America, the Great Unconformity represents over two billion years of time between the crystalline basement rocks below and the beach sands above. Team up with geology professor Shawn Willsey as he explores this fantastic unconformity and the rocks on either side near Buffalo Bill Reservoir just west of Cody, Wyoming in Shoshone River canyon.

CLICK ON THE IMAGE ABOVE

WATCH The 11 Min Video



US & Saudi Relations

Today we'll look at the strategic implications of this relationship over the past 40 years and what it looks like moving forward.

Saudi Arabia matters to the US more than many other US allies. Not only are the Saudis massive oil exporters, but they also have strong ties to the world's Muslim population.

Over the past few decades, the US and the Saudis have partnered up to tackle a handful of critical situations; from stalling the Soviets to the war in Afghanistan to spurring economic growth in Europe and Japan, this relationship has proven vital.

The bottom line is with major players like Russia and China already in motion, the US and Saudis won't allow ugly politics to get in the way of geopolitical relations. Saudi Arabia is a power center and doesn't need to be under the American wing, but there's still a mutually beneficial relationship on the table.



CLICK THE IMAGE TO WATCH/LISTEN



SIPES HOUSTON



TX Lawmakers Oppose Wind Farm

Two Texas senators have expressed concerns regarding wind farms proposed by President Joe Biden's administration, citing negative impacts on the economy and the electric grid.

In July 2022, President Biden announced plans for two wind farms off the coast of Texas and Louisiana. The first farm was planned to encompass 546,645 acres in federal waters, approximately 24 nautical miles off the coast of Galveston. The second was slated to cover 188,023 acres about 56 nautical miles off the coast of Lake Charles, LA, according to a Department of the Interior (DOI) press release. If passed, SB 1303 would require a permit signed by Texas Land Commissioner Dawn Buckingham for any "wind power facility on coastal public land."

Middleton has previously been vocal about his thoughts on the wind farm plans. He wrote a letter to the Bureau of Ocean Energy Management (BOEM) to express his concerns in 2022, warning that switching from reliable energy sources would "increase the unreliability of the Texas electrical grid at great taxpayer expense."

"We are also concerned that BOEM is not taking the devastating impact offshore wind has on both recreational and commercial fishing seriously, and that this pattern of disregard will continue in the Gulf of Mexico," he added.

Still, BOEM Director Amanda Lefton said that the project was thoroughly researched.

"BOEM used the most current scientific data to analyze 30 million acres in the Call Area to find the best spaces for wind energy development. We are invested in working in partnership with states and communities to find areas that avoid or minimize conflicts with other ocean uses and marine life in the Gulf of Mexico," she said. "We are committed to a transparent, inclusive and data-driven process that ensures all ocean users flourish in the Gulf." [READ IT ALL HERE](#)

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2023 Deal Buyer Event in Review

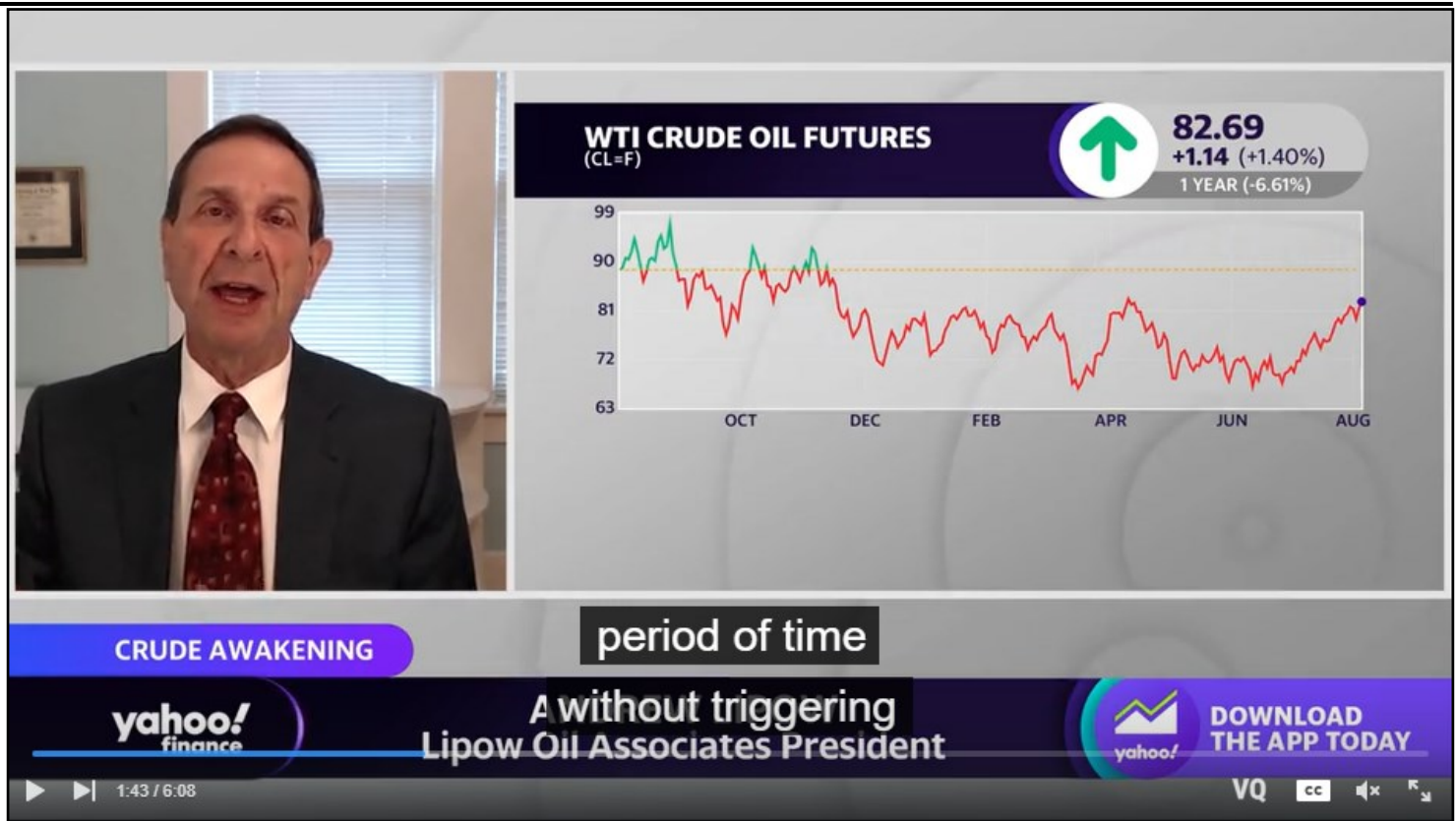


Only real buyers invited resulted in millions of dollars invested directly into conventional prospects. Free food, drinks, cigars, and a raffle of a shotgun and high dollar liquor makes this the most profitable and fun event in our industry.

2023 Deal Buyer Event in Review, continued



Saudi & Russia Continue Cuts



Saudi Arabia has extended its one million barrel-per-day production cuts into September, while Russia announce it will cut oil exports, sending oil prices higher. Lipow Oil Associates President Andrew Lipow tells Yahoo Finance Live the move is "very significant." Lipow say the cuts "really emphasize the point that they are looking for higher prices, because the domestic budgets of these OPEC+ countries simply could not last when oil was under \$70 a barrel."

"I think these cuts are very significant. If we look back to October of last year, OPEC plus has cut over 5 million barrels a day from their production quotas. And these last voluntary cuts by Russia and Saudi Arabia really emphasized the point that they're looking for higher prices because the domestic budgets of these OPEC plus countries simply could not last when oil was under \$70 a barrel." - Andrew Lipow

CLICK ON THE IMAGE TO WATCH THE VIDEO

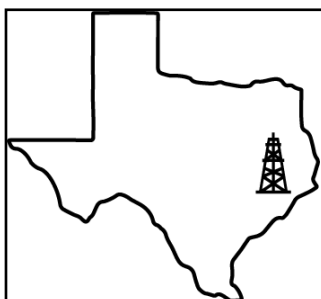


Are We In A Commodity Super Cycle?



In this episode, UBS's Paul Stefansson speaks to Adam Rozencwajg, Managing Partner at Goehring & Rozencwajg Associates, on whether we are in a commodity super-cycle. Together, they discuss the outlook of the commodity market, how the energy transition will impact commodity demand, as well as how far geopolitical tensions today may bifurcate the commodities supply chain.

CLICK THE IMAGE TO WATCH THE 10 MINUTE VIDEO



SIPES HOUSTON

ENERGY ENTREPRENEURS

Massive Riots, Renewable Resentments

The warnings about the landscape-destroying sprawl of wind and solar energy have been coming for nearly two decades. The warnings have come from some of the world's most prominent scientists, government agencies, and energy analysts.

Unfortunately, those warnings were ignored. And now, all over the world, rural people are reacting with fury at the encroachment of large wind and solar projects on their homes and neighborhoods. The backlash has been ongoing for years and can be seen from the Golan Heights to Oahu. Of course, the backlash against the energy sprawl that frequently comes with large-scale renewable projects doesn't fit the narrative being pushed by climate activists, anti-industry NGOs, and their myriad allies at legacy media outlets.

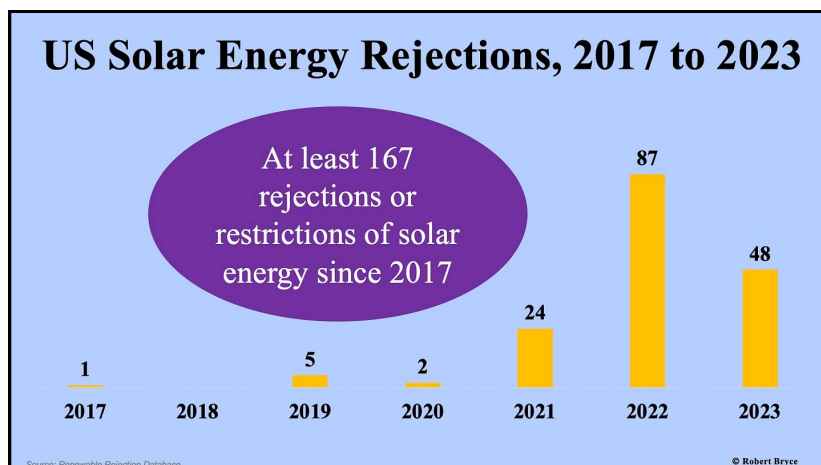
Despite the dearth of honest reporting from outlets like the *New York Times* and National Public Radio, the backlash is irrefutable, it's growing, and it's happening on multiple continents. In June, thousands of Druze residents in the Golan Heights rioted to stop the installation of a large wind project on their traditional lands. Last month, Australia's largest farmers union said it wanted a moratorium on new solar projects. In May, a wind project in Colombia being pushed by the Italian company, Enel, was canceled after it met fierce opposition from the indigenous Wayuu communities.

Meanwhile, here in the U.S., over the last 10 days, local governments in Illinois, Ohio, and Iowa have rejected or restricted wind and solar projects. Those moves bring the total number of rejections or restrictions in the Renewable Rejection Database to 574.

I'll dive into the details of what's happening in Israel, Australia, Colombia, and places like Erie County, Ohio, in a moment. First, it's essential to put these land-use conflicts into historical context. And that requires a review of the warnings about renewables and land use that have been made over the past two decades. For instance, in 2004, Jesse Ausubel, the director of the Program for the Human Environment at Rockefeller University, declared that "Solar and the so-called renewables are not green when considered on the large scales required." In a piece titled "Big Green Energy Machines," he wrote:

Solar and renewables in every form require masses of machinery to produce many megawatts. They lack efficiencies and economies of scale. Like low-yield farming, to produce more calories, solar and renewables multiply in extent, linearly. Unlike the Internet, solar and renewables cannot become much smaller as they become much larger.

In 2005, Klaus Lippold, a member of the German parliament, told *The Guardian* that "The problem with wind farms is that you have to build them in places where you don't need electricity. The electricity then has to be moved somewhere else...There is growing resistance in Germany to wind farms, not least because of the disastrous effect on our landscape."



MASSIVE RIOTS, RENEWABLE RESENTMENTS, CONTD

Now to Australia. A [July 27 article in RenewEconomy.com](#), was headlined, “Farming lobby wants ban on new solar farms as renewable resentment festers in regions.” Here’s the first part of the article:

Australia’s largest state farming organisation, NSW Farmers, is calling for a temporary ban on the construction of new large-scale solar farms in the state, amid concerns developers are not acting in the long-term interests of regional communities. In a motion passed at the Association’s 2023 annual conference last week, NSW Farmers agreed to call on the state Labor government to place a moratorium on large scale solar developments until “planning deficiencies” around plant decommissioning and remediation are addressed. “Current planning and approval provisions for large scale solar energy facilities do not take into account the long-term interests of agricultural land, rural communities and the rural landscape following the ‘decommissioning’ of the facility,” notes on the motion say. “Agricultural land, rural communities and rural landscapes are at risk in the future and there should be no further development approvals granted until these planning deficiency issues have been fully addressed.”

The article also addressed the urban/rural divide, which is just as real in Australia as it is here in the U.S.:

“If this was happening in...say in Sydney suburbs, there would be yelling and screaming!,” Reg Kidd, the former mayor of Orange and chair of the NSW Farmers energy transition working group told [RenewEconomy](#).”

Also on July 27, Reuters reported that [the Swedish government rejected a 50-turbine offshore wind project](#). Each turbine was to be 290 meters (950 feet) tall. Sweden’s minister for climate and environment said the project “would risk damaging sensitive natural values in an unacceptable way. ”

In late May, Enel announced it was quitting a wind project in the La Guajira region in Colombia due to years of protests. Reuters reported that the 197-megawatt Windpeshi wind project was permanently suspended after “[Blockades organized since 2021 by the local indigenous Wayuu communities...disrupted the project.](#)” The project, which was about one-third completed, was to [cover about 6,145 hectares](#) (about 15,362 acres) of Wayuu lands.

In February, climate activist Greta Thunberg and several hundred other activists blockaded the entrance to Norway’s energy ministry in Oslo to protest a wind project being built on lands used by [indigenous Sami reindeer herders](#). The protest is over a 151-turbine project located about 300 miles north of Oslo. The project, built in 2021, is Europe’s largest onshore wind project. About a week after Thunberg and her accomplices began blocking the ministry, the Norwegian government issued an [apology to the reindeer herders](#). In June, dozens of activists including Sami, again blocked government offices pledging to continue the protests until the government [agrees to take the wind project down](#).

Oh, and one more: On Thursday, August 3, in Canada, the provincial government in Alberta announced it was halting approval of all large renewable energy projects for six months. [According to the Regina Leader-Post](#), the Alberta Utilities Commission “will initiate an inquiry into issues of development on agricultural land, effect on scenery, reclamation security, the role of municipalities and system reliability.”

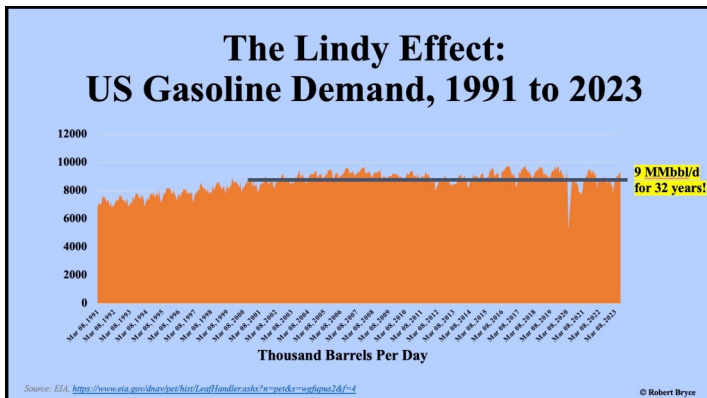
[READ THE FULL ARTICLE BY ROBERT BRYCE HERE](#) ♦

Hydrocarbon Demand is Booming

Last month, in Sevierville, Tennessee, Buc-ee's opened the world's largest gas station. The new retail store has 120 fuel pumps and employs about 350 people. The interior space of the new store covers 74,000 square feet. (A football field covers about 57,600 square feet.) It also has a 250-foot-long car wash that will be one of the longest in the country.

Buc-ee's, which is based in Texas and has about four dozen locations, doesn't allow 18-wheel trucks at its locations. As a company spokesman explained: "We are set up for the family traveler...we don't have the space or the capacity to hold 18-wheelers in the lot." All those family travelers who will be stopping at Buc-ee's to get a refill on brisket, beef jerky, and 20 gallons of dino-juice show why gasoline will stay around for years to come.

Indeed, wagering on gasoline's staying power looks like a safe bet. As can be seen in the graphic above, U.S. gasoline demand has been at 9 million barrels per day for more than 30 years. Demand will stay strong because America has a vast fleet of cars and trucks that burn gasoline and they aren't going away anytime soon. Yes, EV sales are growing. But new cars (EVs included) are expensive. It's usually cheaper to maintain an older car than to buy a new one. And the longer motorists keep their cars, the longer they are likely to keep them because brands like Toyota, Honda, and Nissan, were designed to last.



In May, S&P Global Mobility reported: "With more than 284 million vehicles in operation on US roads, the average age of cars and light trucks in the US has risen again this year to a new record of 12.5 years," adding this was "the sixth straight year of increase in the average vehicle age of the US fleet." S&P continued, noting "the volumes of vehicles ages 6-14 will grow by another 10 million units by

2028, adding to an already favorable volume of vehicles in the aftermarket target range." (My driveway provides proof of the aging fleet. Our youngest vehicle is a 2012 Acura. The oldest: a 2005 4Runner. We'll be keeping that vehicle for another decade. Why? We just put a new engine in it.)

The continued demand for gasoline reflects the Lindy Effect, which says that the older something is, the more likely it is to stick around. Author Nassim Nicholas Taleb explained the Lindy Effect in his 2012 book, *Antifragile: Things That Gain From Disorder*. He wrote, "If a book has been in print for 40 years, I can expect it to be in print for another 40 years." Put another way, the older something is, the more likely it is to be around in the future. Given the growing age of the U.S. auto fleet, as well as the 32-year history of gasoline demand, it's logical to assume the Lindy Effect will apply to gasoline.

Jet fuel demand is also booming. A report published this month by India-based Fortune Business Insights projected the global aviation fuel market will grow from \$352 million in 2022 to about \$656 million by 2029. Like jet fuel, diesel fuel remains an irreplaceable transportation fuel. That's particularly true in developing countries. In May, diesel fuel demand in India hit a new record of 2 million barrels per day.

A few days ago, the International Energy Agency projected that global oil demand will climb by about 2% this year, and reach a new record of 102.1 million barrels per day. The Paris-based agency expects demand to grow by another 1.1 million barrels per day in 2024.

What about natural gas? Demand for that fuel continues to be robust, both here in the U.S. and around the world, and according to McKinsey, it will continue to grow for at least another decade. As I reported here on July 1, in *The Energy Transition Isn't*, domestic use of natural gas is booming:

Domestic gas use in 2022 jumped by a whopping 5.4% and hit a record 85.3 billion cubic feet per day. In March, the Energy Information Administration reported that gas consumption set monthly records in 9 of 12 months in 2022. Not only did annual use hit a new record, but the U.S. also set a new record for daily high demand. On December 23, U.S. gas use hit 141 billion cubic feet. The previous record was 137 billion cubic feet per day.

Given all of these facts, why don't investors like the companies that produce oil and natural gas? And why am I writing about the stock market?

Before going further, let me be clear: I don't own any of the stocks that are mentioned here. I am not a financial analyst and I am not of-

Hydrocarbon Demand is Booming, contd

offering investment advice. The vast majority of my investments are in ETFs. As I have mentioned many times on the Power Hungry Podcast, my biggest holding is the Schwab Dividend ETF.

I'm writing about the stock market because the discounts on oil and gas stocks reflect a belief that oil and gas are going away. But there's scant evidence to support that claim. As I have said many times, if oil didn't exist, we'd have to invent it. It's a miracle substance. Commerce requires transportation. Transportation requires oil. If there's no oil, there's no commerce. Put short, as Art Berman has said, oil is the economy.

Given these facts, why are oil and gas stocks selling at such a discount to the broader market? I've been discussing this with my brother, Wally Bryce, for months. Wally is an above-average brother. He's also a CPA, a savvy number cruncher, a longtime insurance executive, and an avid stock market observer. His analysis: "Mr. Market is saying this stuff is going away." (Mr. Market is an allegory invented by Benjamin Graham to describe the workings of the stock market and as Wikipedia explains, "the danger of following groupthink.")

The discounts are also occurring because some institutional investors are divesting from hydrocarbons. To cite just one example, in 2021, Harvard University announced it would quit investing in fossil fuels. As Wally explained it, "A lot of investors are saying 'I won't buy these stocks at any price.' They are refusing to buy them. A lot of the big endowments, pensions, and foundations are saying 'we won't touch it.' There are fewer buyers in the market. And the buyers aren't buying even though by most financial metrics, these stocks are incredible bargains."

Is this the time to buy energy stocks? Maybe. Oil and gas companies are returning big chunks of their profits to shareholders and many analysts see them as value stocks. The companies are aggressively buying back their stock and boosting dividends. But they are also being challenged by fears of an economic slowdown. Furthermore, the industry faces significant political risk from the Biden Administration. I don't say that as a partisan. I'm not a Republican or a Democrat. I am disgusted.

But this fact is simply true: the Biden Administration is the most anti-hydrocarbon administration in American history. I could cite numerous examples to prove that point. I'll give you just two: On his first day in office, Biden canceled the Keystone XL Pipeline. In May, his EPA issued a proposed rule that could hamstring nearly all of the coal-fired, and gas-fired power plants in the country. As I noted in my piece, EPA v. The Grid, the agency:

announced a proposed rule that could force the closure of every coal-fired power plant in America as well as most of the natural gas plants if they cannot cut their emissions by 90%. Here's how Politico reported on it: The new rule will require, "most fossil fuel power plants to slash their greenhouse gas pollution 90% between 2035 and 2040 — or shut down."

While the political risk from Biden and the ESG crowd is real, the bigger problem may be the industry's remarkable ability to find and produce hydrocarbons. The oil and gas sector has a century-long history of boom and bust in which it has repeatedly been victimized by its success. While it's true that the global supply of hydrocarbons is finite, it's also a truism that the more oil and gas we find, the more oil and gas we find. And the more oil and gas that gets produced, the more efficient drillers get at pulling it out of the ground. The decades-long problem for the oil industry hasn't been too little oil, it's been too much. That fact gave us prorationing under the Texas Railroad Commission for 40 years, until 1973, when that job was seized by OPEC. (Which, by the way, copied the TRC's prorationing model.)

Ten years ago, the average oil production from a new oil well in the Permian Basin was about 200 barrels per day. Today, according to the Energy Information Administration, the average new well in the Permian is producing about 1,000 barrels per day. That increase in efficiency means the industry needs fewer drilling rigs and fewer roughnecks, which means lower costs. That's great for consumers, but it can be hell on investors. In short, there are many wildcards at play including the global economy (and therefore energy demand), the future of the ESG movement, and maybe most important, the sector's ability to cut costs and boost output.

A final note: Buc-ee's recently broke ground on a new location outside of Luling, Texas. When it opens later this year, it will seize the crown of the world's largest gas station from the Sevierville location. The Luling store will have 75,000 square feet of shopping space.

[READ THE FULL ARTICLE HERE](#)

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Can anyone see in this picture where Oil and Gas extraction took place? Of course not because it is one of the least destructive forms of energy extraction on earth. Now do battery metals. Happy Friday Friends 🍷



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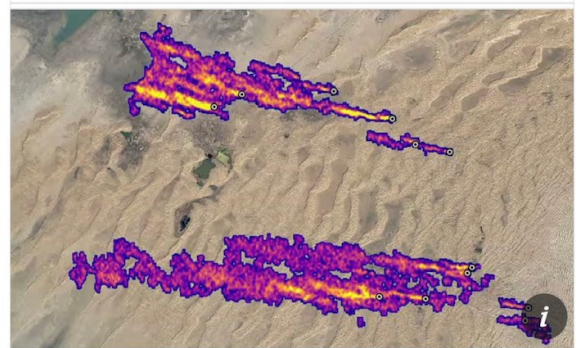


Collin McLelland 🇺🇸 @FracSlap · 1h

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Turkmenistan

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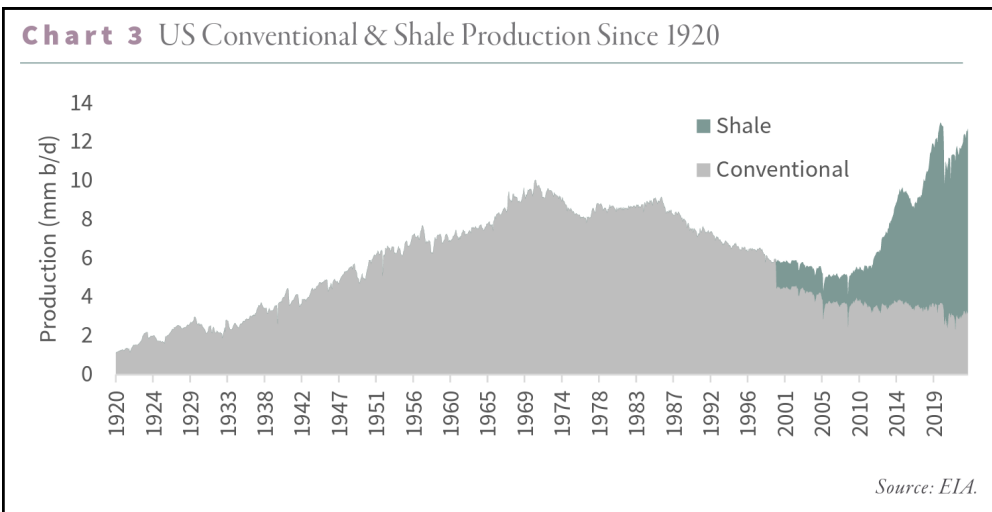
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PERMIAN DECLINE?

The most crucial development in global oil markets is depletion in the Permian basin. We first warned about this in 2018, predicting the Permian would peak in 2025. In retrospect, our analysis was too conservative. We now believe the basin could peak within the next twelve months. The implications will be as profound as when United States oil production peaked in 1970, starting a chain of events ultimately sending prices up five-fold over ten years. If we are correct, this could not come at a worse time for oil markets: inventories are tight, production in the rest of the world is declining, and investors are incredibly complacent.

Whenever we make long-term thematic predictions, we construct a road map of things we should expect to see. Since price is rarely a good proxy for fundamentals, we need hard data that confirms we are going down the right path, even during the inevitable periods when the oil price is moving against us. Based upon our original work back in 2018, we concluded the Permian would roll over once operators drilled most of their best Tier 1 locations. Before peaking, per-well productivity would fall as operators drilled lower-quality inventory. This is what has happened. For the first time, productivity per lateral foot registered a 6% year-on-year decline in the Permian. According to our models, this proves the industry has drilled its best wells; basin-wide production decline is likely not far behind. With the Eagle Ford and Bakken unable to grow over the last eighteen months, once the Permian rolls over, the shale revolution will shift from growth to decline, and Hubbert's Peak will reemerge with a vengeance.

The past decade has indeed been remarkable for global oil markets. Operators first succeeded in developing natural gas shales before adapting the techniques to the oil shales starting with the Bakken in North Dakota. The Eagle Ford was developed next, and then finally, the largest of all, the Permian, with its stacked pay potential, started its development in 2012. The results were without precedent. After



having declined by 50% over forty years, the US abruptly reversed course to become the largest oil producer in the world. Shale oil production went from zero to 10 m b/d, more significant than Saudi Arabia.

The shales could not have come at a better time. In 2003, China joined the World Trade Organization, and its crude demand growth markedly accelerated. In 2005, non-OPEC production growth began to falter, forcing crude markets into a structural deficit. As inventories fell, prices rose, prompting Malthusian warnings almost daily on CNBC and Bloomberg that we were

“running out of oil”.

The shale revolution changed everything. By 2014, non-OPEC production growth reached 2.2 mm b/d, the most robust growth since at least 1966 — driven entirely by the shales.

As the shales ramped up between 2010 and 2018, they seemed limitless. However, even in the early stages of field development, there were warning signs that shale basins adhered to the same depletion principles as conventional fields. Enormous is not the same as infinite, we argued and warned that depletion would eventually take hold.

The shales seemed particularly invincible between 2014 and 2017. In the autumn of 2014, Saudi Arabia stunned the oil markets when it abandoned its role as a swing producer. Crude balances shifted into surplus in the middle of 2014, and instead of cutting production to balance the market, Saudi Arabia announced it would grow output by nearly 1 mm b/d. Immediately, crude prices fell by 15% from \$75 to \$60 per barrel and would drop by 65% over the next eighteen months to bottom at \$26 by spring 2016. With much lower prices and capital-intensive drilling, shale developers reduced their drilling activity by 80%. In the summer of 2014, the industry turned 1,600 rigs; less than two years later, the rig count stood at only 325. Saudi Arabia relented in late 2015, with prices stabilizing a few months later, in February 2016. The shale rig count bottomed in June.

Somehow shale production stabilized and started to grow shortly after that. Even though the rig count was still down 60%, US production

PERMIAN DECLINE?, CONTD

was again registering yearly growth as soon as April 2017. By 2018, the shales were growing by 1.8 mm year-on-year — a record, despite a rig count that remained 50% lower than in 2014.

The shales seemed to defy the laws of physics: they could grow materially despite much lower drilling activity. The industry appeared to have entered a world where it no longer needed increased drilling to boost production.

How was this possible? The answer was drilling productivity. Between 2013 and 2017, the average shale well went from averaging 70,000 barrels of oil over the first twelve months to 140,000. On the Midland side of the Permian basin, the primary source of supply growth, twelve-month productivity nearly tripled from 50,000 to 140,000 barrels.

Since each well brought on so much more oil than before, the industry could now achieve with 400 rigs, what it took 1,600 rigs to produce a few years earlier.

Conventional wisdom believed the industry had improved its drilling and completion of shale wells. The ability to stay in the zone, the choice, and the volume of proppant and fluid were all said to have resulted in sharply higher drilling productivity. Wall Street and the energy industry both promoted a consistent narrative. We felt there were several unanswered questions and undertook a study to consider what was driving surging well productivity. If the industry had radically improved drilling techniques, it would ultimately be bearish for the sector. A previous low-quality Tier 2 location could now be transformed, through enhanced drilling and completion techniques, into a top-quality Tier 1 well. As a result, the inventory of best wells would explode, and the shale basins would continue to thrive for years to come.

Modeling well performance is hugely complex. Shale basins are highly nonlinear with high degrees of variable inter-dependence. As a result, traditional statistical techniques, such as the linear regressions used by most analysts, fall short. We turned to advanced methods, including machine learning and neural networks, and achieved surprising results. Instead of improved drilling techniques, we concluded that two-thirds of the improved productivity between 2013-2018 came from favoring the best drilling locations. In 2013, 22% of Midland wells were Tier 1. By 2018, Tier 1 represented 50% of all wells. Since a Tier 1 well is nearly twice as productive as a Tier 2 well, the migration from lower to higher quality areas drove a massive amount of the improved well productivity.

The industry was not turning Tier 2 into Tier 1 but, instead, was aggressively depleting its inventory of top-quality wells.

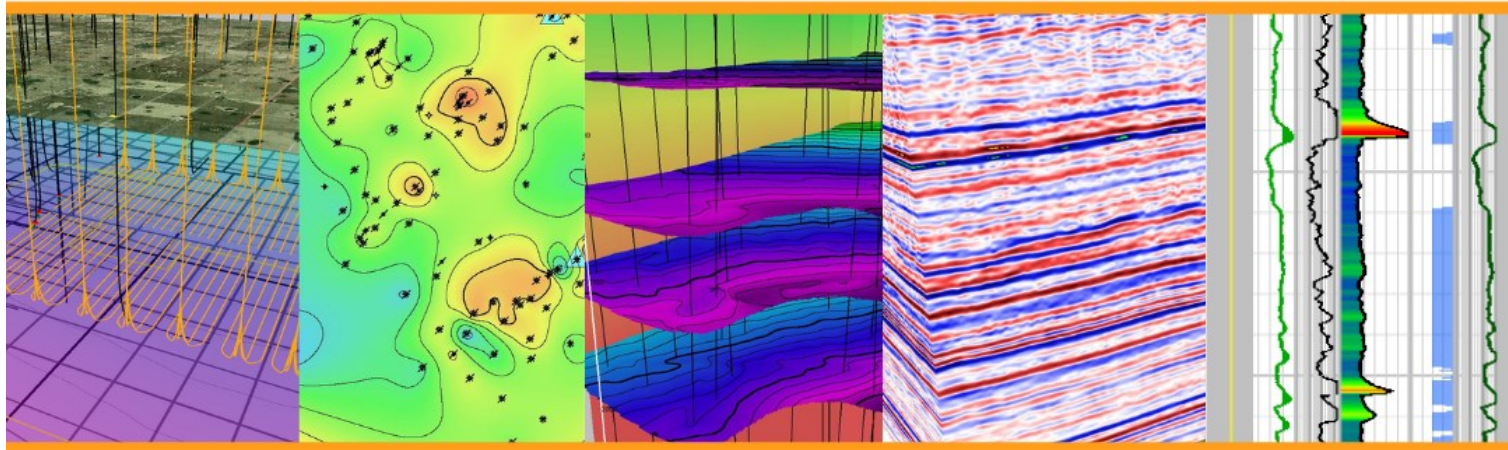
We determined that the pace of high-grading could not continue, particularly in the Eagle Ford and Bakken. Our models suggested that by 2018, 60% of the best acreage in those two earliest developed basins had already been developed. The Permian was developed last, so it still had over 60% of its Tier 1 areas left to drill, but we were concerned that given its pace, it too could soon become depleted. In our 2Q2019 letter, we predicted the Eagle Ford and Bakken would quickly peak while the Permian plateau in the late 2020s at 6.5 m b/d. While the Permian would still manage to grow another 2.5 m b/d from 2018 levels, its annual growth rate would slow materially from 500,000 m b/d per year between 2013-2018 to only 200,000 b/d between 2019 and 2029.

Finding attractive investment opportunities in shale E&P companies will become very difficult. Here too, we believe our machine-learning models can help. Based on current drilling activity, the average publicly traded Permian company will run out of Tier 1 drilling locations within 3.7 years. Our core positions, on the other hand, likely have between five and ten years of high-quality drilling ahead of them. As productivity becomes harder to achieve, these companies should present good opportunities. Already, we have seen rumors of Exxon - Mobil seeking to acquire Pioneer Natural Resources. We own Pioneer and do not know whether these rumors are true. However, we firmly believe that as the market realizes how little Tier 1 acreage remains, those with the best inventory will be treated as valuable assets.

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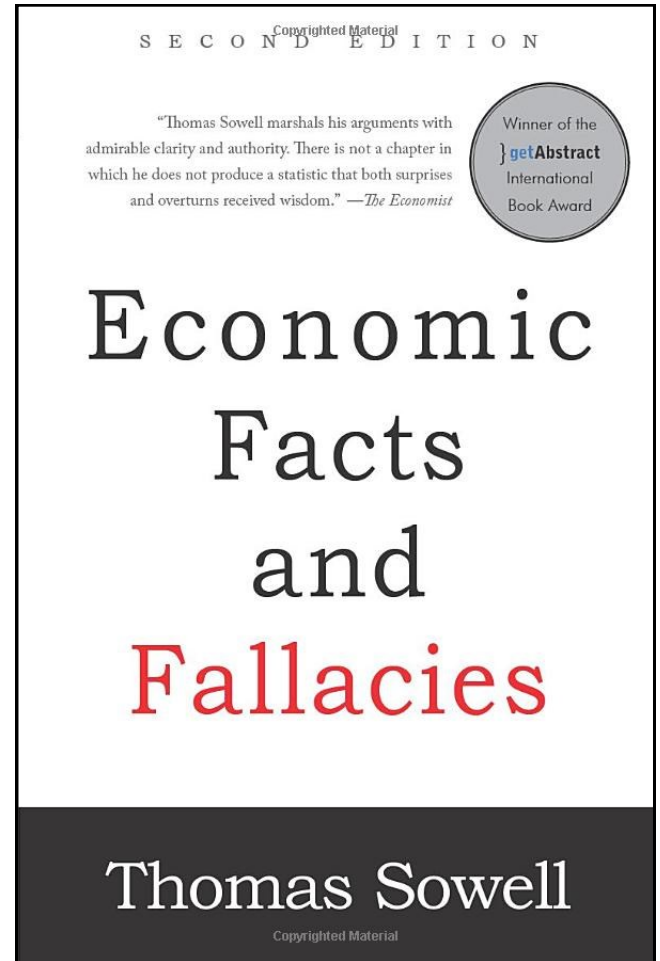
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