

[CFR: China Poised to Shock the Oil Market And Its Possible Consequences for Hyperinflation](#)

I found this paper published by the Council on Foreign Relations to be a plausible argument in favor of the exhaustion of cheap oil, also known as *Peak Oil*. This growth in Chinese oil consumption into the 'knee of the curve' given its growing per capita income could very well cause an oil shock as the title of the paper suggests. As you may recall it was an oil shock that triggered the stagflation of the 1970's, a *black swan* event if there ever was one.

The weakness in its logic is assuming that things which happen in one country will necessarily happen in others, based on relatively simple vectors like per capita income. Examples of possible differences are the national infrastructure in roads, deployment of population relative to travel needs and the availability and pricing of public relative to private transportation. Since these are often significantly affected by policy decisions it is sometimes difficult to forecast them accurately.

Notice that China is under running the trends of the comparison countries at current levels. Why would we assume they would start tracking more closely to model once a certain threshold is surpassed? And then there are the growth assumptions for China, which could be optimistic. Extending aggressive trends is sometimes a dangerous forecasting method. It would also have been interesting to see where India fits on this chart.

Most of these factors modulate the timing of the outcome, but not necessarily the outcome itself. So the trend to cheap oil exhaustion remains persuasive; but as we all know, anything can happen, and sometimes it does.

As competition for oil increases it could have interesting effects on currency valuations, inter currency rates, and international relationships.

It was a bit of a coincidence that I had just reread [How Hyperinflation Will Happen](#) by Gonzalo Lira. It is a compelling read.

He had asked me to provide some feedback and any possible weakness in his argument, which I did in a comment at his site and in a few email responses.

Here is my edited comment from his site:

Although the scenario of a 'run on Treasuries' is possible as a path to hyperinflation, I do not think it is probable unless there is a significant 'trigger event' to precipitate it. The magnitude of the 'trigger event' required could lessen with time if the US financial situation continues to deteriorate.

Why do I say this? Because the TBTF banks have no incentive to join in the selling if the Fed stands to defend a price in the market. For JPM and Citi it is likely to be suicide to do so. Even the mighty Goldman is unlikely to *buck* the system, as it were. The NY Fed not only knows

where the bodies are buried, it has helped to bury quite a few of them itself.

It took a 'Soros' for example to call the Bank of England out in their support for the pound in that famous incident. I see no such party of sufficient size and inclination now to take on the US Treasury and NY Fed in the debt markets.

I do think a trigger event or incident is possible. I believe it would involve an exogenous party of size, for example China, and an announcement regarding Treasury reserves.

I also think the Treasury run could be triggered by a precipitous decline in the value of the dollar. Note this implies the Treasury run would start on the shortest end of the curve, Fed notes of zero duration. Then the longer end would follow.

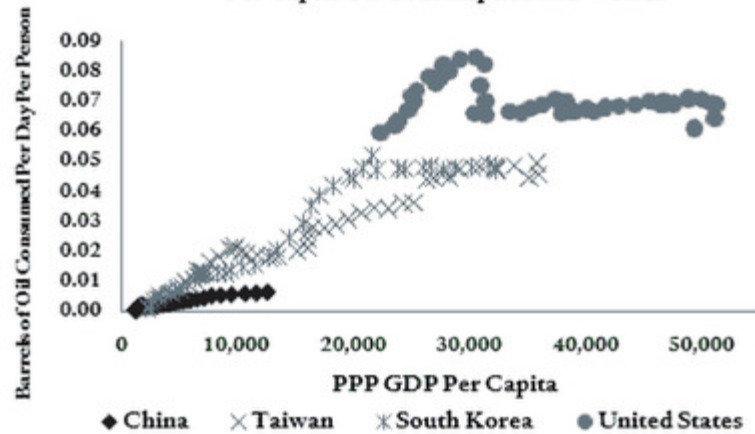
Very nice description of such an event, and chilling to say the least. But I think we are some distance from this without a substantial 'trigger event.'

And then I picked up this CFR essay which describes something which might fit the criterion of a 'trigger event.' After all, it was the oil embargo which precipitated the stagflation of 1970's. An oil shock could shake an already weakened US dollar as the trade deficit opened into a yawning chasm.

But I do remain convinced that hyperinflation is unlikely simply because the TBTF banks 'have the Fed's back' which is why they were allowed to continue to remain in business, with substantial subsidies, and grow even larger. All it takes to create a *money machine* is the Federal Reserve of New York and one or two captive Primary Dealer banks. The dodgy backroom deals are probably more abundant than we realize or suspect even now. And I do not even wish to think of the loathsome creatures that would enjoy taking advantage of a crisis of this magnitude to further promote their oligarchy and a New World Order.

As a reminder, black swan events like market crashes and runs on banks tend to be on the edges of probability. But they can happen, and are more likely to happen at certain times. Therefore it is potentially fatal to assume that things will always remain the same, and that the big trend changes will never occur.

China Poised to Shock World Oil Markets Per Capita Oil Consumption and Wealth



Data Source: OECD, BP,
IMF, US Census, BLS.

blogs.cfr.org/geographics

Figure: Paul Swartz Council on Foreign Relations

China Will Force the World Off Oil

By Paul Swartz

August 23, 2010

As a country's per capita income increases, its per capita oil consumption increases. Consumption growth tends to be modest up until \$15,000 income per head, but then accelerates rapidly. China is quickly approaching this point. South Korea, which consumes 3% of world oil output, is too small to disrupt oil markets.

China is too big not to disrupt them. Were China's per capita oil consumption to be brought up to South Korea's, its share of global consumption would increase from today's 10% to over 70%. In order to cap China's share at 22%, which is the U.S. share today, global oil output would have to increase by a massive 13% per annum over ten years – well beyond the 1% growth averaged since 1975.

This rate of growth is inconceivable, even if vastly more expensive sources of supply, such as the Canadian oil sands, were developed at breakneck speed. If China's recent economic growth pace continues, it will surpass South Korea's current per capita GDP shortly after 2020 – meaning that the world may be forced onto alternative energy sources much sooner than it realizes.