Short-Term Oil Market Outlook: Prospects, Risks and Uncertainty

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Volatility is the name of the game

- Volatility, uncertainty (and confusion!)
- Market torn between a bullish micro-oil story and a bearish macro story
- Exacerbated by potential government intervention that could have big impact on oil market dynamics (price caps, embargoes, restrictions of products exports, additional release of stocks from SPR) and macro policy (aggressive tightening of monetary policy)
- Volatility also reflects tightness in some market segments (refining constraints; low diesel stocks)
Volatility not limited to price levels but also to spreads

OIL MARKET OVERVIEW

Brent and WTI, M1-M2

Source: Argus

Dubai, M1-M3

Source: Argus
Volatility in products cracks

2020 was a particular tough year for US shale producers.

Gasoline margins NWE

 source: Argus

Gasoil/Diesel and jet margins SING

 source: Argus

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Key elements of the micro-oil story

- Expectations of larger Russian crude and products disruptions as EU embargoes come into force
- End of crude stock releases from SPR
- OPEC+ will balance the market
- Moderate non-OPEC supply growth
- Geopolitical risks outside Russia (e.g., Libya, Iran, Nigeria)
- Low buffers in the system: Limited spare capacity; stocks well below the 5-year average (particularly products)
- Gas-to-oil substitution supporting demand

Decomposition of upside risks

Notes: Brent price.
Source: OIES
Key elements of the macro story

- Global economic recession with big negative impact on oil demand
- Depth and duration of the recession
- No signs that China will alter its zero COVID-policy anytime soon
- Micro-oil factors (limited Russian supply disruption; continued release of stocks from SPR; high US shale response; until recently potential full return of Iran oil supplies)

Decomposition of downside risks

Notes: Brent price. Source: OIES
Key Factors Shaping Market Expectations I: Russian Disruption
Prospects of Russian supply disruption a key factor shaping expectations

Disruption limited so far and well below initial expectations at the start of the Russia-Ukraine war (around 400,000 b/d)

Ability to redirect crude exports away from Europe to other parts of the world (e.g., Asia, Med)

Through offering discounts and easier payment conditions

Services and logistics not acting as constraint so far (shipping, insurance)
Crude exports are above pre-war levels

Russia crude exports by destination

Russia crude oil export shifts

Source: Argus, Kpler, OIES

Source: OIES

2020 was a particularly tough year for US shale producers.

OIL MARKET OVERVIEW
Alternative sources to cover loss of Russian supplies

2020 was a particularly tough year for US shale producers.

EU-27 crude oil imports excl. Russia

Source: Kpler, OIES

EU-27 crude oil import shifts excl. Russia

Source: Kpler, OIES

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Filling the Russian crude gap

US crude exports to Europe and Asia

WAF crude exports to Europe and Asia

Source: Kpler, OIES

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Reflected in sharp movements in differentials

WAF grades v North Sea Dated

Forties v North Sea Dated

Source: Argus
Quality of EU crude imports changing

- European imports of medium/light sweet increased shifting the mix away from medium sour
  - Diesel cracks higher
  - Cost of desulfurization increased as gas prices increased
  - Imports of Russian Urals fallen

**EU-27 crude oil import shifts excl. Russia**

Source: Kpler, OIES
Russian product exports have declined

Russia product exports by destination

Russia product export shifts

Source: Argus, Kpler, OIES

Source: OIES
EU products market remains tight

OECD Europe product stocks v 5-year average

- Gasoline
- Middle distillates

Source: IEA, OIES

EU-27 product imports from Russia

Source: Kpler
EU refinery constraints persist

2020 was a particularly tough year for US shale producers.

Notes: EU-16 refers to EU-15 plus Norway. Source: Argus
Diesel situation worsened

- Strikes have paralyzed French refining sector
- Strikes have taken more than 800,000 b/d almost 5% of EU refining capacity (also seasonal wave of maintenance)
- Suppliers had to draw heavily from inventories
- This is contributing to high and volatile margins

Source: Kpler, OIES

Gasoil/Diesel and jet margins NWE

Source: Kpler, OIES
US products exports elevated

**US product stocks v 5-year average**

- Gasoline
- Middle distillates

Source: IEA, OIES

**US oil product exports**

- Diesel
- Gasoline
- Jet
- Gasoil
- FO
- Other

Notes: FO group includes cracked FO, SRFO, VGO, slurry, CBFS and cutter stock.
Source: Kpler

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US refinery utilization at high rate

2020 was a particular tough year for US shale producers.

Source: US EIA

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China’s refineries come to the rescue?

China refinery runs

China oil product exports

Source: Argus

Source: Kpler
Export quotas raised but will China export more diesel?

China oil products export quotas

Source: Argus
India refining have been a bright spot

India refinery runs

Source: PPAC

India oil imports from Russia

Source: Kpler

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Key Factors Shaping Market Expectations II: The Macro Environment
Recession and global oil demand

- Global growth prospects have been downgraded
- China’s comeback will be delayed and more gradual than previously expected, due to COVID flare-ups, its strict zero-COVID policy and domestic economic challenges; A large stimulus remains unlikely, further weighing on the outlook
- Pent-up demand/gas-to-oil substitution could offset some of the near-term demand pressures, but it is very challenging to quantify
China’s demand contracts

2020 was a particularly tough year for US shale producers.

Source: Argus, Blavatnik School of Government (University of Oxford), OIES
Market moves from deficit to surplus

Global supply/demand balance (consensus)

Global supply/demand (with and without SPR)

Notes: Consensus averages estimates from IEA, US EIA and OPEC.
Source: OIES

Source: IEA
The OPEC+ Response

- Real cut less than 2 million b/d announced (close to 1 million b/d)
- Decision not totally unexpected and consistent with previous cycles (in response to GFC)
- Consistent with most recent behavior during the COVID cycle (proactive and pre-emptive in face of deteriorating market balances)
- Cohesion of group (many members producing well below quota; no renegotiation of quotas)
- Context matters

Source: OIES
Short-term oil outlook
**Key assumptions: Russian supply**

- Russian oil production declines gradually towards year-end to reach close to 900,000 b/d below pre-war levels, before disruptions peak in February 2023 when EU sanctions are in full effect to average 1.25 mb/d in 2023.

- Re-routing Russian crude from West to East can put strain on logistics (shipping; access to Aframax tankers).

- Finding insurance coverage outside EU/ G7 challenging.
Key assumptions: Russian exports

Under the full effect of the EU ban, Russian total oil exports (crude and products) to Europe decline by another 1.9 mb/d, 1.2 mb/d of which are diverted to Asia and the rest of world.

Russia oil exports curtailment assumptions

Notes: Compared to Jan/Feb-22 levels.
Source: OIES
Key assumptions: Economic prospects

Monetary policy tightening and sticky inflation push several advanced economies into recession over the coming quarters.

Global GDP growth forecasts

Notes: Global GDP is forecast to 2.8% in 2022 and 1.7% in 2023.
Source: Oxford Economics

G7 economies recession indicators

Notes: Shows simultaneous contractions in output, imports, exports, investments and industrial production in each member country.
Source: Oxford Economics, OIES
2020 was a particularly tough year for US shale producers. Global demand growth is forecast to 1.8 mb/d in 2022 and 1.7 mb/d in 2023, as y/y demand is expected to contract in the coming two quarters for the first time post-2020.

Global oil demand

Source: OIES
2020 was a particularly tough year for US shale producers. OECD demand growth in 2023 is expected to fall to 400,000 b/d from 1.1 mb/d in 2022 and China’s demand to contract y/y by 460,000 b/d in 2022 and rebound by 610,000 b/d in 2023.
Gas to Oil substitution

Oil substitution results to 460,000 b/d incremental demand over October 2022 and March 2023, with 50% of the gains concentrated in Europe.

Oil substitution assumptions

Source: OIES
Global balance risks

A global recession remains the largest downside risk in 2023 having the potential to induce a substantial negative impact on demand growth that could slow sharply to 0.5 mb/d versus the Reference 1.7 mb/d.

Global oil demand growth: Reference v Recession scenario

Notes: Modelled projections.
Source: OIES
Oil supply outlook (1/2)

Global oil supply is forecast to grow by 4.6 mb/d in 2022 and 1 mb/d in 2023, with non-OPEC crude adding 1 mb/d of growth this year.

Global oil supply

Source: OIES

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US crude supply is seen leading growth by 700,000 b/d in 2023, followed by 300,000 b/d from Brazil and 200,000 b/d each from Canada and Norway, while further gains from elsewhere remain marginal.

Global oil supply growth by producer/liquids

Source: OIES
US shale supply outlook

US crude supply in 2022 is expected to grow by 600,000 b/d, a rise by nearly 700,000 b/d exit-to-exit by December, and 720,000 b/d in 2023 albeit exit-to-exit growth falls to 460,000 b/d.
2020 was a particularly tough year for US shale producers. Reference forecast for Brent stands at $100 in 2022 and $94/b in 2023, while the Brent Prospect that considers the uncertainty underlying the outlook edges slightly lower at $93/b in 2023.
Global balance

The oil market is expected to shift into surplus in 2022 by 430,000 b/d and return to a small deficit of -270,000 b/d in 2023, with deficits on a quarterly basis reappearing no sooner than H2 2023.

Global balance

Source: OIES

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Stocks remain below the 5-year average

OECD commercial stocks v 5-year average

Source: OIES
OIES Oil Monthly

Short-term oil market outlook

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