جدوى للإستثمار
Jadwa Investment

July 2021

Quarterly Oil Market Update

OPEC+: a temporary divergence

Summary

- According to OPEC data, Q2 2021 oil demand rose by 3 percent quarter-on-quarter and a sizable 14 percent year-on-year. The outlook for the remainder of the year is consistent with previous estimates, with oil demand expected to keep growing quarter-on-quarter in Q3 and Q4 2021 (Figure1). Overall, only transportation fuels (jet fuel and gasoline) are showing sizable differences in demand when compared to pre-pandemic levels.

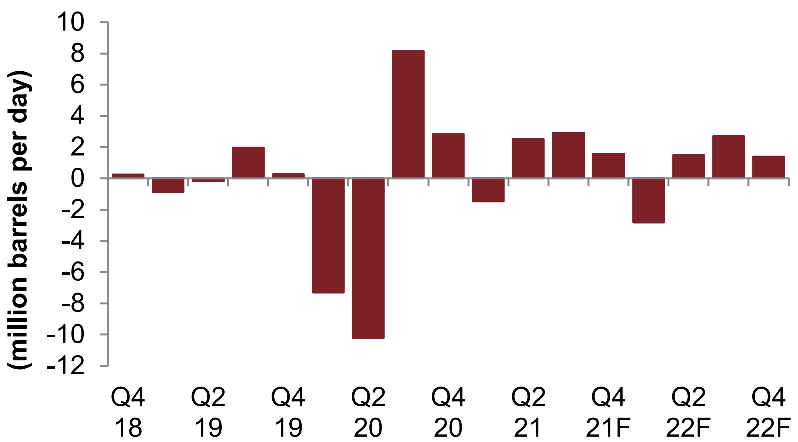
- Looking further ahead, OPEC expects oil demand to climb by 3 percent on a year-on-year basis in full year 2022, to a total of 99.9 million barrels per day (mbpd), similar to levels seen back in 2019.

- On the supply side, OPEC and partners (OPEC+) continued exhibiting strong levels of compliance during Q2 2021, with (over) compliance averaging 113 percent. More recently though, OPEC+'s ability to maintain similar levels of discipline have come into question, with the alliance unable to agree on how to proceed over the remainder of the year in recent meeting.

- That said, at the time of writing, OPEC+ was reportedly getting closer to an agreement, although a formal announcement has yet to be made. Overall, we remain confident that an agreement will be made in the near term, which, in turn, should result in a further unwinding of OPEC+ supply over H2 2021.

- Meanwhile, even with WTI oil averaging $64 per barrel (pb) during H1 2021, no major rises in US oil production have ensued, and neither are they expected to. Latest Energy Information Administration (EIA) data shows that US oil output is virtually unchanged at 11 mbpd since the turn of the year, and only 2 percent higher year-on-year in Q2 2021. Moreover, the EIA expects US oil output to be 6 percent lower at the end of 2022 when compared to peak 2019 output.

Figure 1: Quarterly change in global oil demand



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..the outlook for the remainder of the year is consistent with previous estimates…

...with oil demand expected to keep growing quarter-on-quarter in Q3 and Q4 2021.

Looking further ahead, OPEC expects oil demand to climb by 3 percent on a year-on-year basis in full year 2022.

On the supply side, OPEC+ continued exhibiting strong levels of compliance during Q2 2021…

...with (over) compliance averaging 113 percent.

Transportation fuel demand still lagging:

According to OPEC's data, Q2 2021 oil demand rose by 3 percent (or 2.5 mbpd) quarter-on-quarter and a sizable 14 percent (or 12 mbpd) on a year-on-year basis. The outlook for the remainder of the year is consistent with previous estimates, with oil demand expected to keep growing quarter-on-quarter in Q3 and Q4 2021. Overall, only transportation fuels (jet fuel and gasoline) are showing sizable differences in demand when compared to pre-pandemic levels.

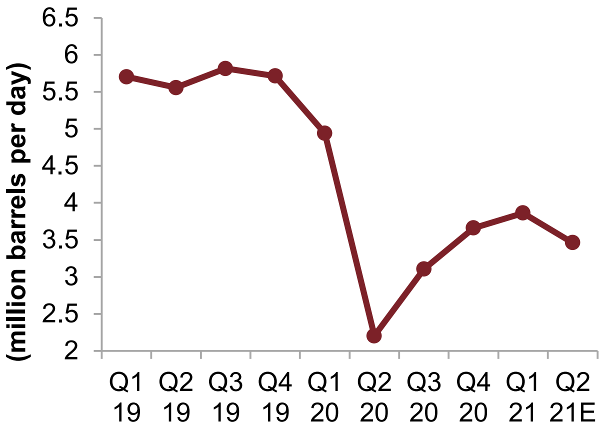
Looking ahead, gasoline demand is expected recover further in the near term, especially as regional/country-wide travel (which can be covered by motor vehicles) in major demand centers is opening up. For example, data from the US's Energy Information Administration (EIA) shows that US gasoline demand in Q3 2021 is expected to be only 4 percent lower than the same period in 2019, whereas jet fuel will likely remain 18 percent lower than the same period two years ago. Moreover, according to a recent report by the International Energy Forum (IEF), global jet fuel demand remained circa 30 percent below 2019 levels during Q2 2021 (Figure 2) and is unlikely to return to pre-covid-19 levels until at least 2023, largely as a result of the slow return of long-haul flights (which accounts for 30 percent of total aviation fuel demand).

Looking further ahead, OPEC expects oil demand to climb by 3.3 mbpd (or 3 percent) on a year-on-year basis in full year 2022, to a total of 99.9 mbpd (Figure 3), similar to demand back in 2019.

OPEC+: a temporary divergence?

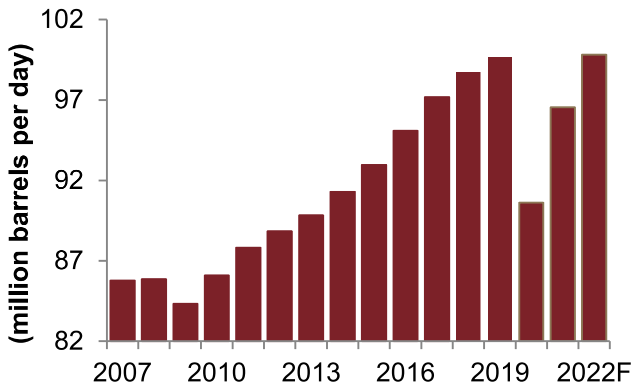
OPEC and partners (OPEC+) continued exhibiting strong levels of compliance during Q2 2021, with (over) compliance averaging 113 percent. As has been the case since the start of the current agreement, Saudi Arabia led the way (at circa 139 percent over compliance) despite partially reversing its voluntary 1 mbpd reduction during the quarter. Other strong contributions in compliance came from Angola & Nigeria, albeit due to technical difficulties in the latter's case. As was the case in Q1, (see our previous Oil Update), these strong levels of compliance were achieved as Brent oil prices trended higher (which averaged $69 pb in Q2, the highest in two years). More recently though, the alliances' ability to maintain similar levels of discipline have come into question, with a recent OPEC+ meeting concluding without an agreement on how to proceed in the second half of this year. The

Figure 2: Jet fuel still affected*



*data from 20 largest consuming countries

Figure 3: Global oil demand in full year 2022 hitting pre-pandemic levels



More recently though, the alliances' ability to maintain similar levels of discipline have come into question…

main sticking point seems to be related to UAE's grievance over the benchmark to which its output is measured against (with the Gulf state wanting a higher benchmark, which, in turn, would allow for higher oil output), it also includes issues over how long the current OPEC+ agreement should last.

...with the alliance unable to get an agreement on how to proceed in the second half of this year.

Looking ahead, it was reported that OPEC+ was getting closer to an agreement, although, at the time of writing, no formal announcement had been made. Whilst an agreement would be welcome, it is worth noting that any renegotiation of a benchmark for one OPEC+ member raises the possibility of other countries also asking for similar reviews, which could add another layer of complications to future OPEC+ supply (Figure 4).

US oil maintaining discipline:

Meanwhile, even with WTI oil averaging $64 per barrel (pb) during H1 2021…

…no major rises in US oil production have ensued, and neither are they expected to.

Latest EIA data shows that US oil output is virtually unchanged at 11 mpbd since the turn of the year.

A recent Federal Reserve Bank of Dallas Energy Survey of 155 US companies showed that an average WTI oil price of $31 per barrel (pb) was needed to cover operational costs at existing oil wells, and an average price of $52 pb was needed to profitably drill new oil wells (Figure 5). Despite this, with WTI oil averaging $64 pb during H1 2021, no major rise in US oil production has ensued, and neither is it expected to do so. Latest EIA data shows that US oil output is virtually unchanged at 11 mpbd since the turn of the year, and only 2 percent higher year-on-year in Q2 2021. Moreover, the EIA still expects US oil output to be 6 percent lower at the end of 2022 when compared to peak 2019 output. The muted outlook in US oil production stands in contrast to the US oil sector of the past, where higher oil prices were swiftly accompanied by higher oil output. It now seems to be the case that US oil operators are more keen on using any windfall from higher oil prices to pay down debt and/or pass these gains onto investors via dividends. This focus on value is evidenced by better performance in the stock market, with the S&P oil & gas index rising by 60 percent year-to-date, versus 18 percent for the main S&P index.

Oil price outlook:

Although variants of covid-19 are still rampant around the world, oil demand related risk is, on the whole, receding.

Brent oil prices averaged $69 pb during Q2, rising 13 percent quarter-on-quarter. The continued global roll-out of vaccinations (and related pick-up in economic activity) helped push oil demand higher, which, in turn, kept global oil balances in deficit by 1.6 mbpd despite some unwinding of OPEC+'s oil output during the quarter (*please see May's edition of our Chartbook for more details*) .

Figure 4: OPEC+ output could rise if an agreement is reached soon

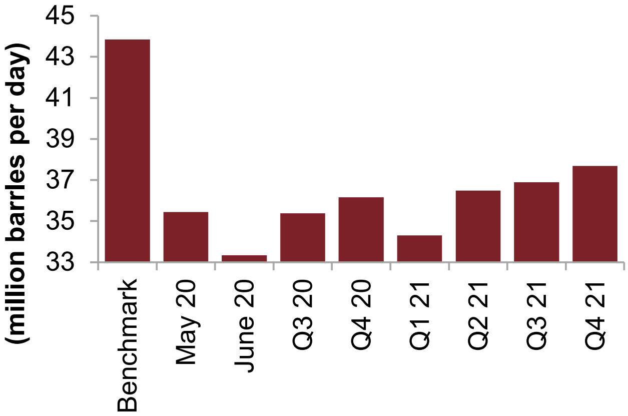
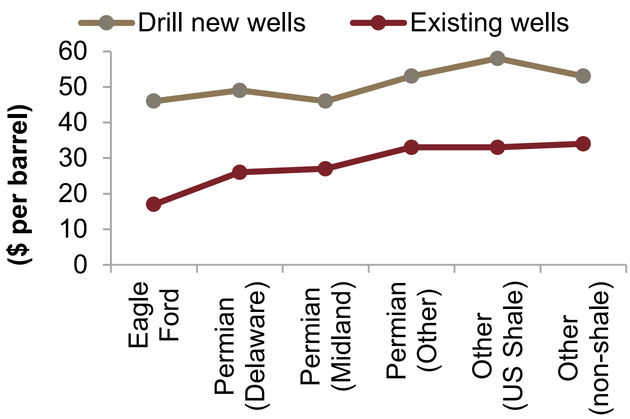


Figure 5: WTI oil prices to cover operational costs in existing wells and to profitably drill new wells



At the same time, hitherto muted supply side risks are now higher due to the lack of progress in a recent OPEC+ meeting.

That said, we remain confident that an agreement will be made in the near term, which, in turn, should result in a further unwinding of OPEC+ supply.

Although variants of covid-19 are still rampant around the world, oil demand related risk is, on the whole, receding. Looking ahead, further roll-out of vaccines (and boosters) should allow for more relaxation in covid-19 measures in more parts of the world, thereby aiding quarterly rises in oil demand. At the same time, as noted above, hitherto muted supply side risks are now higher due to the lack of progress in a recent OPEC+ meeting. That said, we remain confident that an agreement will be made in the near term, which, in turn should result in further unwinding of OPEC+ supply (which was originally reported to be around 400 tbpd per month from August to December 2021). Accordingly, we see daily oil balances remaining in deficit during the rest of the year (Figure 6), thereby allowing commercial oil inventories to trend closer to their long term average (Figure 7).

Figure 6: Daily oil balances to remain in deficit in H2 2021...

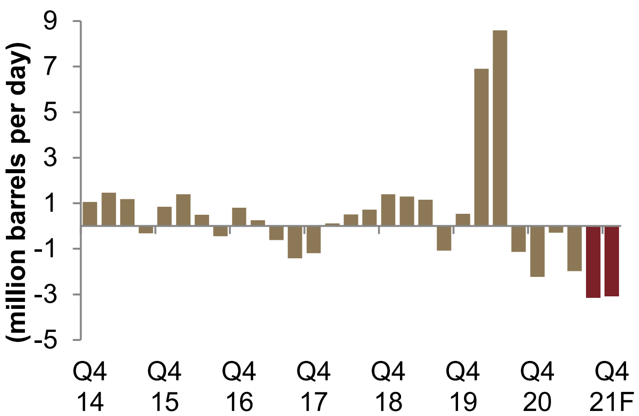
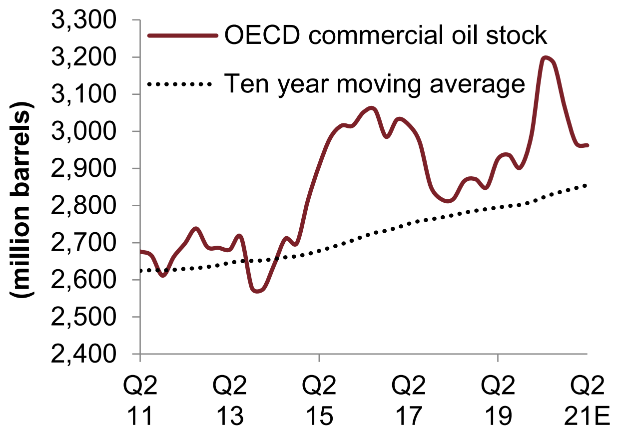


Figure 7: ...which should help push OECD commercial oil stocks towards long term average



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