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Key Points of Medium-term Oil Market Outlook

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Many uncertainties are still lingering in the international oil market exposed to downside risks including the European economic crisis and the Chinese economy's slowdown, as well as upside riskd such as geopolitical risks to the supply side. It is difficult to anticipate the future course of the market on the assumption of great uncertainties. Under such situation, however, a benchmark or reference with regard to market outlook is very valuable.

On October 12, the International Energy Agency released its "Medium-Term Oil Market Report 2012" that could become one of such outlooks. The report analyzes oil supply and demand, biofuels, crude oil trade, oil refining, oil pricing and other matters related to the international oil market over the next five years up to 2017. The IEA has other famous oil market outlooks including the Monthly Oil Market Report as a short-term outlook for the coming one to two years and the World Energy Outlook as a long-term forecast for the next two decades. The medium-term outlook covers the next five years for which oil supply projects and relevant investment trends can be estimated with certain accuracy, providing unique points in relation to a market direction analysis. Here, I would like to indicate key points for anticipating the future international oil market based on the IEA medium-term outlook.

First, the IEA report revised downward global oil demand estimates in view of recent global economic conditions, while still predicting oil demand to continue increasing under economic growth of 3-4%. The report projects global oil demand to increase at an annual average rate of 1.3% (or 1.2 million barrels per day annually) from 89.79 million bpd in 2012 to 95.68 million bpd in 2017. From the previous IEA medium-term outlook released last December, the demand estimate for each year is lowered by between 500,000 and 900,000 bpd. Particularly, the largest downward revision is given for China. For 2016 for which projections in the latest and previous reports are comparable, the latest estimate for China is given at 10.91 million bpd, more than 1 million bpd lower than the previous estimate, though with an upward trend for oil demand expected to continue. Behind the downward revision may be slowing demand growth under the recent economic conditions as well as global progress in energy conservation through fuel efficiency improvements.

Even after the downward revision, however, the estimated annual oil demand growth of 1.3% can be viewed as firm. Given that annual global oil demand growth since 2010 has been less than 1% (or an average 800,000 bpd), future demand could change, depending on global economic conditions.

Second, the supply side features impressive growth projected in oil supply from Non-OPEC countries. The latest report estimates that non-OPEC oil supply may increase at an annual average rate of 1.7% from 53.22 million bpd in 2012 to 57.53 million bpd in 2017. For 2016, non-OPEC oil supply is revised upward by 760,000 bpd from the previous outlook. The upward revision reflects a substantial increase in U.S. shale (tight) oil production (from 1.31 million bpd in 2012 to 3.33 million bpd in 2017). U.S. oil output is projected to expand by about 2.5 million bpd in five years from 8.95 billion bpd to 11.41 million bpd in 2017. This indicates that global oil supply and demand will greatly change on U.S. shale oil production, following the big changes in gas supply-demand in US caused by “shale gas revolution”. In this respect, US oil import dependence (share of net oil import against total oil demand) is predicted to fall from 52% in 2012 to 39% in 2017. Even the medium-term outlook indicates that the United States is going in the direction of self-sufficiency in oil.

Third, the downward revision of demand and the upward revision of non-OPEC production as noted above in connection with the supply-demand balance resulted in a cut in projected demand for OPEC crude oil (or “Call on OPEC”), indicating stagnation in call on OPEC. Demand for OPEC crude is projected to almost level off from 30.35 million bpd in 2012 until 2016 before rising to 31.21 million bpd in 2017. Given that some OPEC countries including Iraq are expected to moderately increase production capacity, the cartel’s surplus production capacity is estimated to continue an uptrend. While demand for OPEC crude is expected to stagnate, Iraq’s output is projected to increase along with its production capacity, which is estimated to expand from 3.14 million bpd in 2012 to 4.77 million bpd in 2017. Therefore, OPEC is likely to face a new challenge regarding production adjustment.

Given the above analysis, the IEA report seems to suggest that the supply-demand balance in the international oil market will basically ease over the medium term. But a great number of variables remain uncertain, indicating that various developments are conceivable. For example, the IEA report, while predicting firm non-OPEC oil production, points out that unexpected oil output falls which actually happened in Syria, Yemen, Sudan, the North Sea and Brazil over the past few years indicate downside risks to the supply side. On the other hand, geopolitical risks are difficult to take into account for this kind of outlook. A major geopolitical risk factor that could have great impacts on the international oil market may be the possible destabilization of the Middle East including the situation surrounding Iran from late this year to next year.

A presumption for the latest IEA oil outlook is that the average crude oil import price for the IEA countries will decline from $107 per barrel in 2012 to $89/barrel in 2017. In this respect, we may have to pay attention to such key factors as the European and Chinese economies, U.S. oil output, Iraq's oil output expansion and OPEC’s responses, and various geopolitical risks, which could affect future crude oil prices.

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