

Exchanging Views at OPEC on International Oil Market and Asian Energy Problems

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On June 24 at the Secretariat of the Organization of the Petroleum Exporting Countries in Vienna, I participated in a meeting for exchange of opinions between OPEC experts and energy researchers from China and South Korea as well as the Economic Research Institute for ASEAN and East Asia, known as ERIA. Topics there included the international oil market and crude oil price trends, Asian energy supply/demand prospects and the emerging energy challenges in the world and Asia. At the meeting, experts gave presentations on specific themes before frank discussions were held in an informal manner. In the following, I would like to summarize the discussions' points that were impressive to me.

First, there were interesting discussions on how to interpret present conditions and prospects for future developments regarding the crude oil price plunge since the second half of 2014. Meeting participants agreed that the plunge was attributable to slowing demand in Europe and China and a sharp increase in U.S. shale oil output that loosened the supply-demand balance. They also discussed the importance of the Saudi Arabia-led OPEC cartel's policy of tolerating oil price declines. Interestingly, however, some participants called for paying attention to money or financial factors including the rising dollar under international monetary easing with regard to the impacts on oil price. Although the benchmark crude oil price has recently risen back to around \$60 per barrel from less than \$45/barrel early this year, most of the participants refrained from viewing the recent development as indicating a full-fledged recovery in oil prices. They still viewed the present oil supply-demand balance as representing an oversupply and remarkably pointed to many price-lowering factors including downside risks for the world economy and Iran's possible oil export expansion that could come on Western countries' elimination of sanctions depending on their negotiations with Iran on its nuclear weapons development.

Second, meeting participants pointed to various uncertainties and challenges regarding the future international oil market, despite the existence of the presently loosening supply-demand balance and falling crude oil price as mentioned above. Remarkably, many pointed out that the present weakness of oil prices would not be sustainable for a medium to long term. As for factors that influence a sustainable equilibrium price level, the participants discussed mainly two concepts, namely those related to the marginal production cost and affordable price levels for consumers and countries. The marginal production cost concept relates to the topic that if oil demand increases by 1 million bpd annually in average, U.S. shale oil and other high-cost oil production as well as low-cost

oil production in the Middle East may play some role over a medium to long term, making the marginal production cost of high-cost oilfields a reference to global oil supply cost structure in the future. The latter concept relates to “affordable price levels” for allowing oil demand to grow mainly in emerging and developing countries where demand is expected to increase in the future. Affordable oil price levels in general are expected to rise as income levels and living standards rise in emerging and developing countries. As indicated by the two different concepts above, the meeting participants broadly agreed that oil prices may rise over a medium to long term.

Therefore, the present weakness of oil prices was dominantly interpreted as a short to mid-term phenomenon. Discussions at the meeting did not indicate that any major change has emerged in future crude oil price assumptions adopted by major forecasting organizations for analyzing energy supply and demand over a long term. The U.S. Energy Information Administration has released a long-term outlook. By around November, the International Energy Agency and OPEC will announce their respective long-term outlooks. We may have to closely watch what crude oil price assumptions would be given in medium to long-term outlooks by these representative forecasters and how and whether the recent crude oil price plunge would affect future oil price assumptions.

Third, I would like to note that discussions at the meeting focused on medium to long-term energy supply and demand forecasts in China, India and Southeast Asia as the gravity center of the international oil or energy market was expected to shift to Asia. Particularly regarding China as the world’s largest energy consuming country where economic growth has decelerated under the “New Normal” economy, meeting participants discussed mainly how China would continue to sustain economic growth after the deceleration and what energy policy the Chinese government would take to influence energy choices.

Given the transport sector’s energy consumption that holds the key to oil demand growth, it is expected that oil demand in the world can continue to increase in parallel to the expansion of automobile/vehicles mainly in the emerging countries. Some participants presented a view that oil supply security would grow even more important in China as its dependence on oil imports increases due to the continuation of substantial oil demand growth over a medium to long term. Interestingly, another participant doubted if China could reduce its dependence on coal for environmental conservation purposes as planned by its government. Based on the IEEJ’s Asia/World Energy Outlook 2014, I explained low-growth scenarios for China and India and their impacts on the Middle East and Russia, attracting robust attention. How to view the probability of the low-growth scenarios and their impacts on Chinese society is one of the most important problems that China or energy experts in the world cannot ignore.

Fourth, meeting participants indicated high interests in energy problems in Japan. Japan’s energy situation and government efforts to overcome problems after the Fukushima nuclear power plant accident are a focus of attention for energy experts in the world even at present. Particularly, questions were made on the issue of nuclear shutdown and its restart in Japan. The other very important topic on Japanese energy issue for the meeting participants was a 2030 energy mix target that has recently been drafted by the government. They indicated great interests in the feasibility of

the energy mix target which includes the targeted share of 20-22% for nuclear, 22-24% for renewable energy, 27% for liquefied natural gas and 26% for coal in total power generation in 2030. The participants understood Japan's policy of trying to achieve the energy mix as "a desirable future for Japan." Citing difficult challenges including an ambitious energy conservation target, difficult efforts to secure public acceptance of nuclear energy, and tough measures to overcome high costs and intermittent supply of renewable energy, however, many predicted fossil energy demand would be greater than indicated in the energy mix target. While understanding Japan's policy target of trying to hold down fossil fuel demand, however, they questioned if such policy would affect Japan's maintenance and enhancement of relations with oil producing countries and its policy of securing stable fossil fuel supply. While Japan is unlikely to see its energy demand grow in the future, it is now the world's third largest oil importer and largest LNG importer. Japan's presence is still great even as the energy market gravity shifts to other Asian countries. Japan will continue to be required to prepare and implement energy strategies and policies, while taking into account the impacts of energy policy of Japan as well as other major countries like China and India on global energy markets.

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