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A Personal view on the World Oil Market Based on Dialogue with OPEC

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On October 24, I visited the Secretariat of the Organization of the Petroleum Exporting Countries (OPEC) in Vienna for a dialogue on prospects for the international energy and oil market. The annual dialogue took place between numerous OPEC Secretariat executives, and I and other experts from major Asian research institutes, and energy industry officials. These participants had vigorous discussions under the Chatham House rule. Based on the dialogue, I here would like to share my personal view on the present situation and prospects for the international oil market.

First, the dialogue led me to feel anew that great uncertainties exist concerning the short-term outlook for the international oil market and crude oil prices. Attracting attention at the dialogue were signs of changes in oil supply and demand fundamentals supporting crude oil price hikes from the beginning of 2018. A joint oil production cut by OPEC and some non-OPEC oil producing countries including Russia started in 2017 and successfully worked to eliminate oversupply and reduce oil inventories. This is a fundamental factor supporting the crude oil price rebound and hike. In the current international market, however, supply is expanding globally while downside risks for demand are feared. As a result, data at the International Energy Agency indicate that commercial oil inventories in the Organization for Economic Cooperation and Development turned up in June and continued increasing in July and August.

While oil demand in 2019 is expected to increase by 1.3 million barrels per day with global economic growth at 3.6-3.7%, supply growth is predicted by some analysts to exceed the demand increase to push up inventories from the beginning of the year. In the United States that is leading the supply expansion, production is predicted by many analysts to increase by 1.2 million bpd in 2019 from 2018 after posting a record rise of 1.8 million bpd in the previous year. Canada and Brazil are also expected to expand production. Russia, which has participated in OPEC and non-OPEC oil producing countries’ joint oil production cut, is also expected to raise production by more than 200,000 bpd in 2019.

OPEC production is also increasing. Total OPEC production, excluding output by Equatorial Guinea and Congo that joined OPEC in and after 2017, continued to decrease until hitting a low of 31.56 million bpd in May 2018, according to the International Energy Agency. After OPEC decided on its effective production expansion at its meeting in June, however, OPEC production rose gradually, reaching 32.34 million bpd in September, up about 800,000 bpd from May. As a result, OPEC production clearly surpassed call on OPEC, or OPEC production required to achieve a supply-demand equilibrium, in the second and third quarters of this year, leading to an increase in inventories.

In such situation, global economic risks have shaken markets. A global stock market crash triggered by a New York market plunge on October 10 seemingly came to a pause. On October 24 when we were meeting with OPEC Secretariat officials, however, the Dow Jones industrial average on the New York Stock Exchange suffered a heavy fall of more than 600 points, triggering a global stock market crash again. Financial market participants now have no choice but to remain sensitive to signs of the future course of the global economy. In the dialogue with OPEC, participants had interesting discussions on the impact of the escalating trade war on the global economy and oil demand, leading me to feel that the meeting was highly interested in the matter.

As for oil oversupply that could be caused by the deceleration of oil demand growth on the realization of global economic risks amid general production expansion, oil market analysts still remember the “Ghost of Jakarta” as noted in “A Japanese Perspective on the International Energy Landscape (390).” In the future, OPEC will be required to do a very difficult job of steering oil production policy.

Meanwhile, Iran’s oil exports and production have been decreasing due to U.S. economic sanctions. Middle Eastern tensions regarding Iran are steadily growing. As hopes are growing on Saudi Arabia’s surplus production capacity to cover a decline in Iranian oil exports, global attention is focusing on the oil kingdom’s importance for oil market stability. At such time, the so-called Khashoggi scandal is shaking Saudi Arabia, leading developments in the kingdom to attract global attention. As mainly Western countries grow critical of Saudi Arabia, the kingdom’s politics, economy and policies are becoming a great matter of concern to the world. Various uncertainties about the future course of the Middle Eastern situation and the difficulties in predicting future developments have played a role in increasing oil market uncertainties. The oil market is likely to remain unstable and nervous in the immediate future, sandwiched between the “Ghost of Jakarta” and growing geopolitical risks in the Middle East.

The dialogue at the OPEC Secretariat led me to feel anew that there are various uncertainties about the long-term oil market outlook. On the demand side, the issue of peak oil demand cannot be ignored. As noted by the World Oil Outlook 2018, a long-term outlook released by OPEC in September, a main scenario for most long-term outlooks in the world indicates that global oil demand will continue increasing until 2040 to 2050, supported by growth in demand for oil for petrochemical production and transportation (covering automobiles, ships and aircraft). However, future energy transitions may include not only continuous, sustainable and evolutionary ones but also revolutionary ones that would bring about disruptive or dramatic changes. Particularly, it may be difficult for anyone to project the impact of any revolutionary transition. OECD countries’ strong oil phase-out policy countering the 1970s oil crises was coupled with a recession to reduce global oil demand in the first half of the 1980s. Whether or not anything would happen to dramatically change growing non-OECD oil demand will be very important for the future.

Numerous important uncertainties also exist about oil supply. One of them is about future U.S. shale oil production. Given that U.S. shale oil production has been a central factor behind the international oil market’s dramatic changes over the past five years, it is natural for the future course of U.S. shale oil to be important. While the WOO 2018 projects U.S. oil production to turn downward in 2027 with shale oil output peaking out, the U.S. Energy Information Administration predicts U.S. oil production to continue moderate growth through 2050. Whether or not U.S. oil production would peak would have great influence on the global oil supply-demand balance. Various long-term outlooks are divided over future Russian oil production as well. Various uncertainties about future oil production in the United States and Russia competing for the position of the world's largest oil producer indicates that the significance of supply and demand adjustments by the other most important oil producing country of Saudi Arabia would increase further.

The world is full of uncertainties. Those responsible for energy policy and business decisions are always required to consider how to address uncertainties.

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