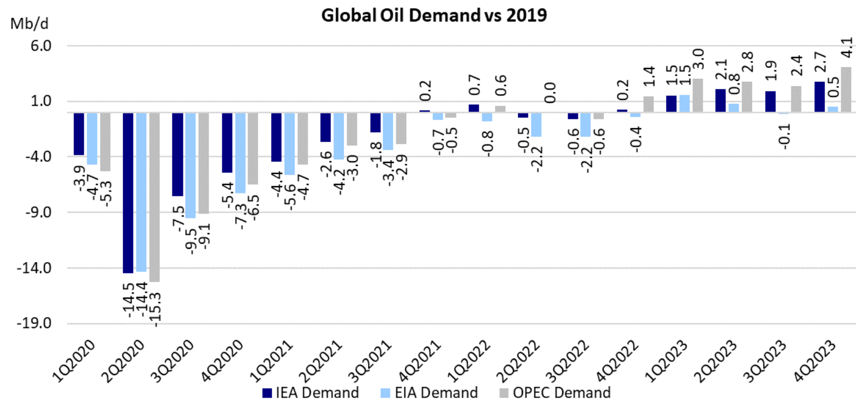
Diverging Views

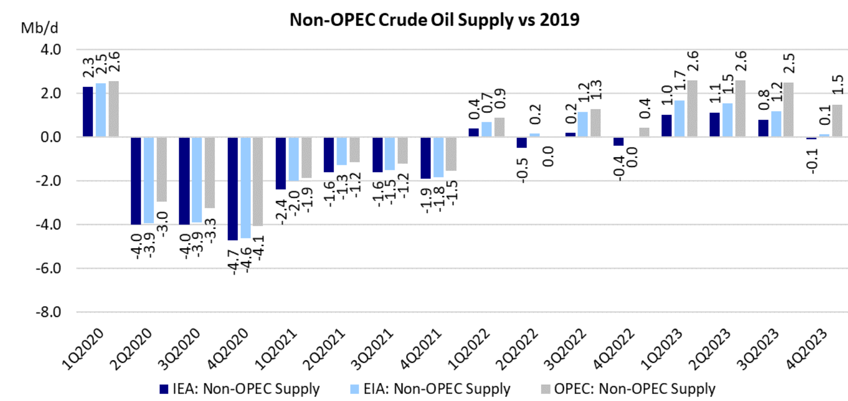
The IEA and OPEC have a different oil market outlook

Every month, three widely followed oil prognosticators give their opinion on the current and future oil balances. The U.S. Energy Information Administration (EIA) usually publishes its Short-Term Energy Outlook (STEO) first, followed by the Oil Market Report from the IEA and the OPEC Monthly Oil Market Report. Comparing the absolute numbers for oil demand and supply of these publications is not always possible (or useful), because they use slightly different definitions. However, comparing them with previous forecasts and their own historical timeseries alleviates that problem. The Covid-19 significantly disrupted the oil markets in 2020 and 2021 making year-over-year comparisons between agencies even more difficult. Therefore, to put the current and future oil market developments in perspective, we compare the various supply and demand projections with a pre-pandemic baseline of 2019. The most recent reports from the agencies demonstrate a few things. The future is highly uncertain and there is difference of opinion about oil supply and demand balances for the near-term as well as the medium-term.

Figure 1 clearly shows the significant decline in global oil demand in the first half of 2020. The second half of that year and throughout most of 2021, the oil markets staged a recovery as demand gradually returned while the economic impact of the pandemic receded. By Q4 of 2021, demand was back at 2019 levels. While 2022 was expected to be a year of growth, this has not panned out so far. Higher commodity prices and supply chain issues have fueled inflation, triggering central banks to implement interest rate hikes. This has created significant economic uncertainty. The Russian invasion of Ukraine exacerbated these trends and added a layer of geopolitical risk. Western sanctions against Russia have also created uncertainty about Russian oil exports. As a result, global oil demand growth stagnated so far in 2022.

The outlook for 2023 is for growth to resume. The EIA and the IEA both expect 2.1 million barrels per day (Mb/d) oil demand growth next year, while OPEC forecasts 2.7 Mb/d more demand. Where is all this new oil going to come from. The OPEC+ countries have indicated that they don't have much spare capacity (only Saudi Arabia and the United Arab Emirates can boost production) and many producers are struggling to even meet their current quota. Currently, OPEC+ produces 2.7 Mb/d below its official target. Therefore, it is Non-OPEC production that needs to pick up the slack. The IEA expects more output from the U.S., Canada, Brazil and Guyana to make up for most of the additional oil that is needed. OPEC+ output is expected to remain flat or slightly down as increases in core OPEC are not expected to compensate for the declines in Russian production.





Source: IEA, EIA, OPEC

This could become a problem. Both the IEA and OPEC forecasts suggest a potential shortfall in supply next year. Obviously, a tightening oil market would drive up prices and could lead to demand destruction. Alternatively, pressure could mount to relax the sanctions on Russia or try to implement a price cap instead that will keep more oil flowing.

While the IEA and OPEC both expect demand growth in 2023, they have different views on the second half of 2022 and in their reports they cite several drivers underlying their forecast. Compared to last month, the IEA lowered demand growth expectations for 2H 2022 for the Americas, as sharply higher prices are having an impact on gasoline demand in the U.S. At the same time, they increased European oil demand growth by 200-300,000 b/d as the IEA expects that extremely high prices and potential shortages of natural gas will lead to significant gas-to-oil switching in the EU. OPEC takes a different view. They worry about the economic impact of the Russian invasion of Ukraine, high global inflation and corona virus lockdowns in China. OPEC reduced their forecast for global oil demand this quarter by 720,000 b/d. Against this backdrop, the largely symbolic 100,000 b/d OPEC+ production hike may be less of an issue. However, the key is where Russia's output will go in the second half of the year. OPEC only expects a 400,000 b/d reduction in Russian output over the next 6 months. In contrast, the IEA expects Russian production to decline by 1.2 Mb/d as the EU implements its ban on seaborne oil purchases.

The tanker industry will need to keep an eye out on the developments in the oil markets. The outlook is very uncertain, but at the moment that does not seem to have a negative impact on freight rates.