Navigating Dynamic Shifts: A Transformative Period in the Oil and Gas Industry

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Global demand for oil is surging to unprecedented heights, driven by a robust summer air travel season, increased utilization in power generation, and a thriving petrochemical sector in China. Forecasts indicate that global oil demand will experience a significant growth of 2.2 million barrels per day (mb/d), reaching a peak of 102.2 mb/d in 2023, with China being the primary driver, accounting for over 70% of this expansion. However, as the momentum of the post-pandemic recovery slows down and factors like lackluster economic conditions, stricter efficiency standards, and the proliferation of electric vehicles start to influence consumption patterns, the growth rate is predicted to decelerate to 1 mb/d in 2024.

In contrast, the global oil supply faced a setback, plummeting by 910 thousand barrels per day (kb/d) to stand at 100.9 mb/d in July. A significant reduction in Saudi Arabian production was responsible for a dip of 1.2 mb/d in output from the OPEC+ alliance, landing at 50.7 mb/d. Conversely, non-OPEC+ production managed to climb by 310 kb/d, reaching 50.2 mb/d. Projections indicate that global oil production is poised to witness an expansion of 1.5 mb/d, reaching an all-time high of 101.5 mb/d in 2023, primarily fueled by non-OPEC+ gains of 1.9 mb/d driven by the United States. The upcoming year is anticipated to be dominated by non-OPEC+ supply growth, with an increase of 1.3 mb/d, while OPEC+ might only contribute 160 kb/d.

Refineries are grappling with the challenge of meeting the escalating demand, as the transition to new feedstocks, operational interruptions, and soaring temperatures have led to operational constraints for many facilities. This situation has contributed to a squeeze in gasoline and diesel markets, propelling margins to a six-month high. Despite the prevailing pressure on naphtha due to competition from inexpensive LPG and subdued petrochemical activity outside China, there has been a tightening in the market for high-sulfur fuel oil, as refineries turn to lighter and sweeter grades to replace lost OPEC+ crude. In an unusual turn of events, high-sulfur fuel oil prices in Rotterdam have surpassed North Sea Dated prices for the first time in nearly three decades.

Consequently, the inventories of both crude oil and refined products have experienced a notable contraction. In July, observed oil stocks recorded a decline for the third consecutive month, with OECD industry stocks plummeting by more than 100 million barrels below the five-year average. Looking ahead, market dynamics are expected to tighten further during the autumn, as Saudi Arabia and Russia extend their supply cuts until at least September. The OPEC+ coalition's substantial spare capacity of 5.7 mb/d provides the potential for the alliance to raise output later in the year. This could offer respite to refiners, enabling them to escalate production and alleviate pressures in the product market. However, if the current OPEC+ production targets remain intact, there is a possibility that oil inventories could shrink by 2.2 mb/d in the third quarter of 2023 and by 1.2 mb/d in the final quarter, potentially driving prices even higher.

In the realm of prices, ICE Brent futures have undertaken a robust upward journey, leaping by $11 per barrel to attain $86/bbl in July. This surge can be attributed to an improved macroeconomic sentiment and a tightening market. Reduced Saudi output and lower Russian loadings further fueled the resurgence in prices, causing crude forward curves to deepen into backwardation. As of the latest update, Brent prices are hovering around $87/bbl, nearing the zenith of the 2023 spectrum.

Key indicators underscore the steady march of global oil prices during July and early August, reflecting the long-anticipated phenomenon of a tightening market. The convergence of more pronounced OPEC+ supply reductions, an optimistic macroeconomic outlook, and a historic pinnacle in global oil demand has propelled this price escalation. Dated North Sea crude marked a $10/bbl upswing over the month, arriving at approximately $85/bbl, the highest level observed since April. The landscape of heavy sour crude markets, impacted by production cuts, has led to a rare phenomenon where Dubai crude trades at a premium to Brent. Additionally, Urals crude has breached the price cap established by G7 nations, rendering Russian oil exports ineligible for G7 and EU maritime services.

July saw a dip of 1.2 mb/d in oil supply from the OPEC+ alliance, culminating in a near two-year low. This reduction was primarily due to voluntary cutbacks from Saudi Arabia. Consequently, the alliance's production dwindled to 50.7 mb/d, marking a decrease of over 2 mb/d since the start of the year. In contrast, non-OPEC+ producers witnessed a surge in output by 1.6 mb/d to reach 50.2 mb/d over the same period. Nonetheless, expectations for growth from non-OPEC+ sources for the remainder of the year remain restrained. The United States, Brazil, and Guyana emerged as frontrunners in the expansion, collectively witnessing a year-on-year rise of around 15%, culminating in exports exceeding 9 mb/d in July. This surge bolstered the availability of light sweet grades in the Atlantic Basin. While the US accounts for a significant 80% share of the global supply growth in 2023, equivalent to 1.2 mb/d out of the total 1.5 mb/d, this dominance is projected to wane in the coming year as activity within the shale industry slows down.

The landscape of global oil demand painted a record-breaking picture, with June witnessing consumption reaching an unprecedented 103 mb/d. This momentum may carry forward into August, potentially setting yet another peak. Following a period of subdued readings, OECD demand underwent upward revisions for both May and June. As a result, overall consumption rebounded in the second quarter of 2023 after witnessing contraction over two successive quarters. Chinese demand also outpaced projections, surging to new heights despite persistent apprehensions about the economy's vitality. The annual outlook suggests that global oil demand is en route to an expansion of 2.2 mb/d, culminating in a historic high of 102.2 mb/d. However, as the post-pandemic recovery matures and the energy transition picks up pace, growth is poised to decelerate to 1 mb/d in 2024.

IEA (2023), Oil Market Report - August 2023, IEA, Paris https://www.iea.org/reports/oil-market-report-august-2023