

## Crude oil: The IEA View

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### Overview

According to the IEA the overhang in global oil stocks has diminished considerably and prices have recovered. This in turn has rewarded those taking part in output cuts and has also unleashed a new wave of growth in output in USA. Coupled with gains from Brazil, Canada, and Norway, oil markets now look adequately supplied through till 2020.

### What will be the driver?

A strong world economy is expected drive oil demand. IEA expects demand to grow at an average annual rate of 1.2 mb/d for the period till 2023. By 2023, oil demand will reach 104.7 mb/d, up 6.9 mb/d from 2018. China and India will contribute nearly 50% of the increase in global oil demand.

### But, there are some interesting countervailing developments

There are signs of substitution of oil by other energy sources in various countries. China for example has some of the world's most-stringent fuel efficiency and emissions regulations. Sales of electric vehicles are rising and there is strong growth in the deployment of natural gas vehicles including trucks and buses. This will significantly slow gasoil demand growth.

### Where will demand emanate from?

The fastest-growing source of demand is petrochemicals especially in USA and China. About 1.7 mb/d, or 25%, of our total demand growth to 2023 will be accounted for by ethane and naphtha. Global economic growth is lifting more people into the middle class in developing countries. Higher incomes mean sharply rising demand for consumer goods and services. A large group of chemicals derived from oil and natural gas are crucial to the manufacture of many products that satisfy this rising demand. Examples include personal care items, food preservatives, fertilizers, furnishings, paints and lubricants for automotive and industrial purposes.

### Is investment taking place?

Each year the world needs to replace 3 mb/d of supply lost from mature fields while also meeting robust demand growth. Investment is hence required for maintaining current production and meeting future demand growth.

IEA estimates that discoveries of new oil resources fell to a low in 2017, with less than 4 billion barrels of crude, condensate and NGLs found. In particular oil production from China, Mexico and Venezuela fell by a combined 1.7 mb/d in the last few years due to lower investment.

An added concern is that investment is overwhelmingly focused on the light tight oil (LTO) in USA. Therefore upstream investment may be inadequate to avoid a significant squeezing of the global spare capacity cushion by 2023, even as costs have fallen and project efficiency has improved.

### **The OPEC-non-OPEC dynamics**

With OPEC capacity growing only modestly the focus has shifted to non-OPEC countries led by USA.

- US output is expected to grow by 3.7 mb/d. Total liquids production in USA will reach nearly 17 mb/d making it the top global producer which will also match the level of its domestic products demand.
- Brazil, Canada and Norway will also contribute to supply growth.

### **How about refinery products?**

Excess global refining capacity is set to increase due to the slowdown in refined product demand growth. Global refining capacity additions to 2023 are forecast to amount 7.7 mb/d while growth of refined product demand will slow to 5 mb/d. The growing excess refining capacity will eventually put pressure on margins.

With growing refining throughput, Asian import requirements will grow by over 3.5 mb/d. The Middle East countries will remain the largest suppliers, but their exports will only grow by 1 mb/d, given their focus on domestic refining. Other sources such as Angola and Nigeria will have lower availabilities and this will provide opportunities for new suppliers mainly the US.

### **The market in 2023**

- Oil market likely to tighten by 2023 with increased risk of price volatility.
- The market could go through two phases during the next six years.
  - o Through 2020, record supply from non-OPEC countries more than covers expected demand growth.
  - o By 2023, if investments remain insufficient, the effective global spare capacity cushion falls to only 2.2% of demand and raises the possibility of oil prices becoming more volatile until new supplies come on line.
- The US shale sector responded quickly to rising prices both in 2010 and in 2017 and will continue to adjust to price signals in the future.
- There will still be a continued reliance on OPEC countries for a major share of global supply. Within OPEC more than 2 mb/d of spare capacity is held in Saudi Arabia. In turn, this emphasizes the crucial role OPEC's largest producer continues to play in providing stability to global oil markets.

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