Oil: A Less Favourable Outlook

The Oil Market Report for August, released last Friday by the International Energy Agency (IEA), contained bad news for those betting on a sharp rise in oil prices. While the growth outlook for global supply and demand held steady, the level of demand for oil since 2015 was revised significantly downward. New estimates show weaker demand in many emerging countries, including China. While past IEA forecasts combined with stable production from Organization of Petroleum Exporting countries (OPEC) suggested a notable oil market deficit in the future, the revised outlook now suggests a near-equilibrium market in 2018. In this context, global crude inventories could remain high, limiting upside pressure on prices.

Note, however, that the IEA’s outlook assumes that U.S. crude oil production will continue its rapid rise in the coming quarters. As shown in graph 2, the number of active oil rigs has stabilized after the WTI (West Texas Intermediate) plunged under US$45 per barrel at the end of spring. This moderation of investment could be a sign of a coming slowdown in U.S. crude production, especially if prices were to again fall significantly below US$50 per barrel.

IMPLICATIONS

The downward revision of global demand suggests that WTI prices could remain fairly close to the US$50 per barrel mark in the coming quarters. The U.S. dollar’s expected appreciation could also limit crude oil gains. Our year-end targets have therefore been lowered slightly, to US$52 and US$55 per barrel for 2017 and 2018, respectively. However, U.S. production will need to be watched closely.

Mathieu D’Anjou, CFA, Senior Economist