US waivers on Iranian oil end

Summary

- A recent official statement from the US confirmed that the current set of waivers on Iranian oil would not be extended beyond May 2nd. The ending of waivers would require the cessation of all oil purchases from Iran, which averaged at least 1.5 million barrels per day (mbpd) in Q1 2019.

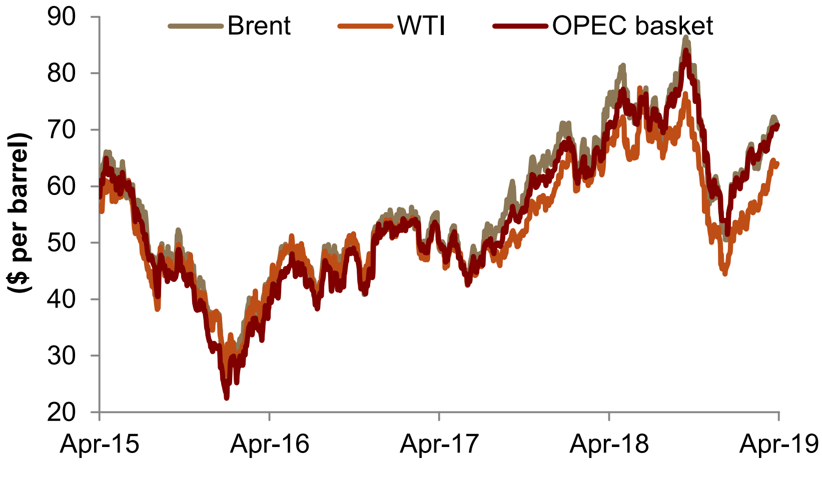
- Total oil output from OPEC averaged 30.5 mbpd in Q1 2019, a sizable 2.5 mbpd (or 7.6 percent) lower than the October 2018 output which is used as a benchmark. Looking ahead, OPEC's oil production for Q2 2019 and indeed for the remainder of 2019 will be determined by the US's decision not to renew waivers.

- We expect to see a new agreement allowing for a higher level of allocated oil production for OPEC and partners (OPEC+) when they next meet in either the Joint Ministerial Monitoring Committee (JMMC) in late May or indeed in the OPEC conference in late June.

- As such, any agreement between OPEC+ that seeks to raise allocated quotas is likely to count on Saudi oil to make up a large portion of the agreed rise in output. As a result, despite Saudi Arabia's crude oil output averaging 10 mbpd in the first quarter of 2019, we have kept our forecast for Saudi oil output at 10.3 mbpd over the course of the year unchanged.

- Currently, Brent oil prices are around $75 per barrel (pb), having gained recently on the back of US's decision (Figure 1). Looking ahead, we still see some upside to oil, especially so in Q2 2019, but a new OPEC+ agreement with higher allocated levels of oil production, together with record US oil output, should ease pressure on prices in the second half of 2019.

Figure 1: Brent oil prices have risen to around $75 pb recently



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Global oil demand growth projections for 2019 were revised down yet again…

Oil demand growth slips again:

In the April edition of OPEC's monthly oil report, global oil demand growth projections for 2019 were revised down yet again. According to the organization, 2019 will see growth of 1.21 million barrels per day (mbpd), the lowest level of growth since 2013. The latest adjustment is the sixth downward revision to OPEC forecasts since the initial forecast was released back in July 2018, and equates to 17 percent (240 tbpd) reduction over the original figure (Figure 2). According to OPEC, lower oil demand was largely driven by revisions in economic growth expectations, especially so for developed Europe and Asia. In fact, in a recent update the International Monetary Fund (IMF) trimmed global economic growth by 30 basis points, to 3.3 percent for the year, citing numerous risks to European Union area growth. As a result, OPEC now expects a higher level of contribution to oil demand growth from US, China and India in Q2 2019 and indeed the rest of the year. The above three countries contribution to demand growth is expected to make up 64 percent in Q2 2019, and 63 percent in 2019 as whole, up from 59 percent previously.

...with the latest adjustment equivalent to a 17 percent reduction over July 2018's forecast.

US, China and Indian oil demand a mixed bag:

Latest data from the EIA shows that overall US liquid consumption was up 1 percent year-on-year in Q1 2019.

Latest data from the Energy Information Administration (EIA) shows that overall US liquid consumption was up 1 percent year-on-year in Q1 2019. It seems a reduction in WTI prices by 7 percent quarter-on-quarter and 13 percent year-on-year in Q1 2019, contributed to raising demand.

Looking ahead, according to EIA's 'Summer Fuels Outlook' report…

...US gasoline and distillate fuel consumption is expected to show yearly rises.

Looking ahead, according to EIA's 'Summer Fuels Outlook' report, US gasoline consumption (46 percent of total US liquid demand) is expected to average 9.54 mbpd during the summer driving season (April to September), equivalent to a rise of 29 tbpd, or 0.3 percent, over the same period last year (Figure 3). Meanwhile, distillate fuel demand (20 percent of total US liquid demand) is expected to average 4.1 mbpd over the summer, equivalent to a sizable 5 percent year-on-year rise and the highest consumption since 2007. The main driver of distillate demand is expected to be combination of economic growth, higher industrial output, and increased oil and natural gas drilling activity. Whilst the outlook for the two main components of US liquid demand point to healthy yearly growth, it should be noted that the EIA's forecasts are based on Brent crude oil

Figure 2: 2019 oil demand growth forecast in corresponding OPEC monthly oil reports

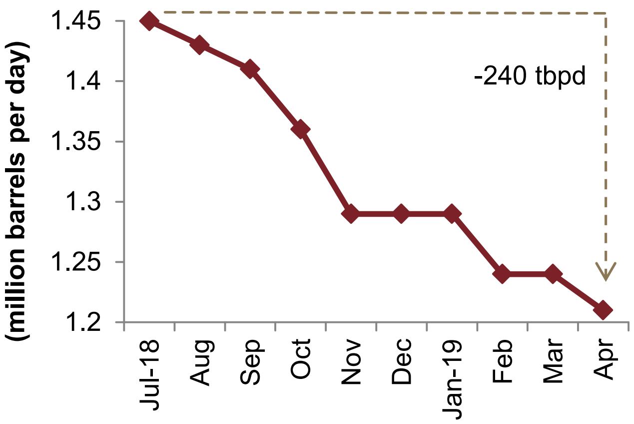
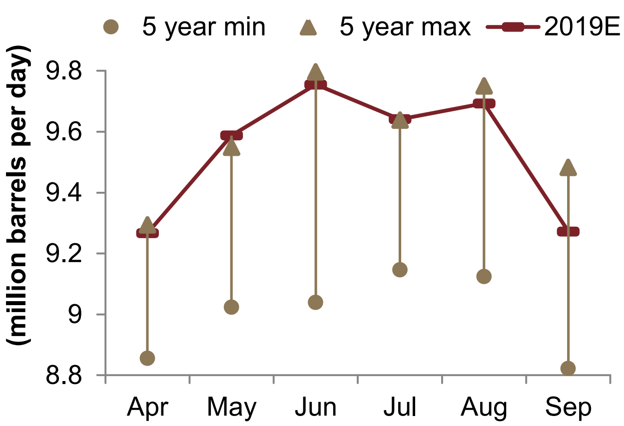


Figure 3: US gasoline demand during summer driving season expected to be close to 5 year highs



China's crude oil imports grew by a sizable 8 percent year-on-year in Q1 2019.

Looking ahead, Chinese oil demand is expected to grow marginally at around 2.6 percent in the Q2 2019…

...slightly lower than growth in 2018 as a whole, at 3.2 percent…

... with one of the risks to demand being various policies that support the reduction of transportation fuel consumption.

Indian crude oil imports were down 2.9 percent year-on-year in Q1 2019.

The slowdown is partly related to a moderation in growth of auto fuels.

prices averaging $67 per barrel (pb) over the summer months.

China's crude oil imports grew by a sizable 8 percent year-on-year in Q1 2019, but declined by 5 percent quarter-on-quarter. Part of the quarterly drop can be explained by seasonal factors related to new year festivities, which usually results in lower demand. Additionally, it seems China raised the level of imports as crude oil prices declined at the end of 2018 and early 2019, but lowered imports as prices recovered in February and March (Figure 4). In particular, Chinese purchases of Venezuelan crude oil hit recent highs of 512 (thousand barrels per day) in February, which would have likely been loaded onto ships in December and January.

Looking ahead, Chinese oil demand is expected to grow marginally at around 2.6 percent in the Q2 2019, slightly lower than growth in 2018 as a whole, at 3.2 percent. The outlook for the rest of 2019 is the same, with OPEC forecasting oil demand growth at 2.7 percent, due to demand from the industrial sector and rising passenger car sales. That said, despite recent economic stimulus measures which have lifted various indices, such as the Chinese manufacturing PMI, downside risks to oil demand still remains. According to OPEC, the main risks relate to a slowing of the economy as well as various policies that support the reduction of transportation fuel consumption. In fact, China's drive to reduce pollution in major cities has led to a ramp up in investment in electric transport, including a roll-out of electric buses. Such measures are expected to contribute to lowering demand growth for oil products with a recent report by BloombergNEF stating that a cumulative 270 tbpd of diesel demand could be displaced by electric buses by the end of 2019.

Indian crude oil imports were down 2.9 percent year-on-year in Q1 2019. The slowdown is partly related to a moderation in growth of auto fuels, which, in turn, reflects a moderation in domestic passenger vehicle sales. According to the Society of Indian Automobile Manufacturers (SIAM), last fiscal year (year to March 2019) domestic passenger vehicle sales rose by 2.7 percent, the slowest rate of growth in five years. A rise in the number of people car sharing, lack of financing options and uncertainty linked to the upcoming Indian general election were some of the reasons cited for weaker sales growth.

Figure 4: Chinese oil imports rose to record highs during a recent fall in oil prices

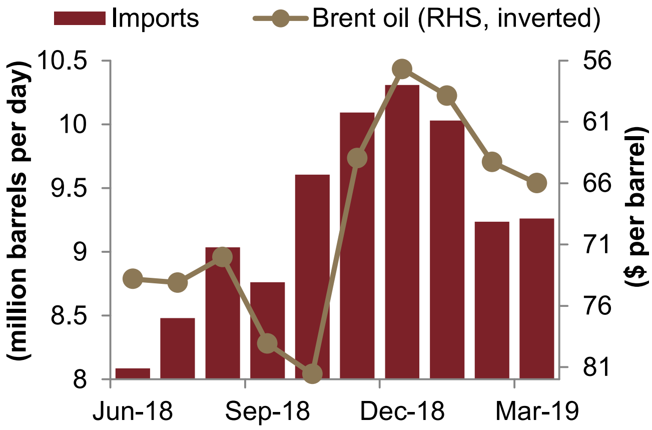
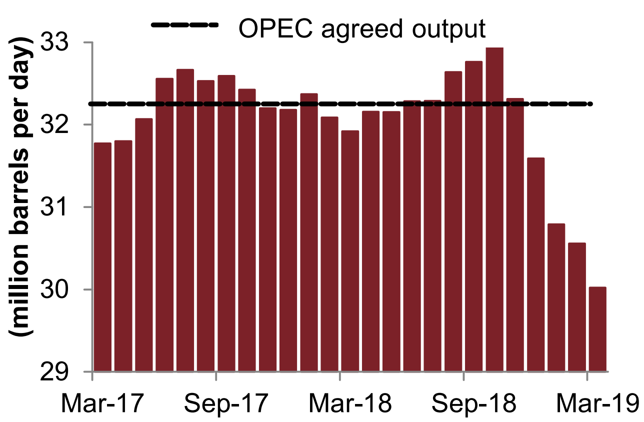


Figure 5: OPEC oil output reduction steeper than agreed levels



Looking ahead into Q2 2019, vehicle sales are expected to pick up once the final round of elections are completed in mid-May.

Looking ahead into Q2 2019, SIAM expects vehicle sales to pick up once the final round of elections are completed in mid-May. Beyond Q2 and into the rest of 2019, oil imports may rise due to a lack of development in India's upstream activity. The current Indian administration had targeted to reduce both oil and gas imports by 2022, but the reverse has happened in the last five years. Currently, more than 84 percent of oil consumption came from imports, compared to circa 80 percent in 2014, whilst gas imports made up 43 percent of total consumption, up from 31 percent over the same period.

OPEC +; will they, won't they?:

OPEC crude oil production was down 5 percent year-on-year and 6 percent quarter-on-quarter in Q1 2019.

OPEC crude oil production was down 5 percent year-on-year and 6 percent quarter-on-quarter in Q1 2019 as a moderation in output was maintained as per an agreement outlined late last year. Total oil output from the organization averaged 30.5 mbpd in Q1 2019, a sizable 2.5 mbpd (7.6 percent) lower than the October 2018 output which is used as a benchmark (Figure 5). Most notably, 70 percent of the reduction in output since October last year came from only five countries. That said, only two of the five, Saudi Arabia and UAE, were able to voluntarily reduce production, whilst the other three, Iran, Venezuela and Libya, involuntarily reduced output over the same period (Figure 6).

Most notably, 70 percent of the reduction in output since October last year came from only five countries.

In fact, Iran, Venezuela and Libya have, for various reasons, seen a combined 1.9 mbpd reduction in output since the start of 2018. For Iran, despite the postponement in implementation of US sanctions by six months, to May 2019, customers began to reduce oil purchases from mid-2018 onwards. Meanwhile, in Venezuela, a socio-economic and political crisis coupled with sanctions from the US has resulted in oil output plummeting. Lastly, whilst Libya's oil output has not been as badly affected as Iran or Venezuela, the resurfacing of civil strife in recent months has led to fluctuating output (Figure 7).

OPEC's oil production for the remainder of 2019 will be determined by the US's decision not to renew waivers on Iranian oil…

Looking ahead, OPEC's oil production for Q2 2019 and indeed for the remainder of 2019 will be determined by the US's decision not to renew waivers that had allowed nine countries to buy Iranian oil without facing US sanctions. A recent official statement from the US confirmed that the current set of waivers would not be extended beyond May 2nd. The ending of waivers would require the cessation

Figure 6: Saudi Arabia and the UAE's reduction in oil output since Oct. 2018 has been voluntary

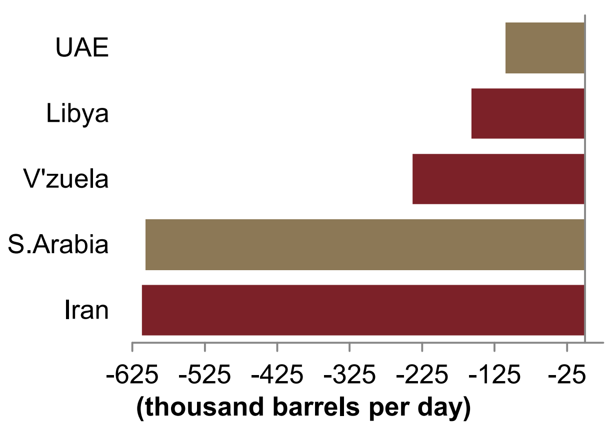
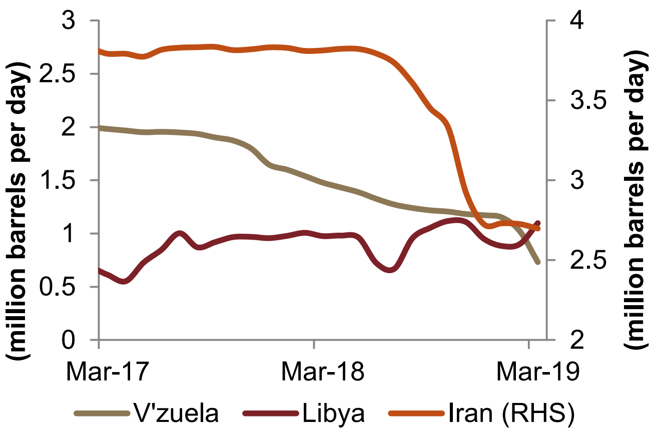


Figure 7: Iran, Venezuela and Libya oil output has declined by a combined 1.9 mbpd since start 2018



...but we expect to see a new agreement allowing for an higher allocated level of oil production for OPEC+ in May or June.

of all oil purchases from Iran. This means that at least 1.5 mbpd of oil (equivalent to purchases from Iran's five largest customers in Q1 2019) will have to be supplied from other sources (Figure 8). In this context, we expect to see a new agreement allowing for a higher allocated level of oil production for OPEC and partners (OPEC+) when they next meet in either the Joint Ministerial Monitoring Committee (JMMC) in late May or indeed in the OPEC conference in late June. That said, there is still the possibility that the OPEC+ agreement is disbanded altogether (Box 1).

Box 1: Russian concerns

That said, there is still the possibility that that the OPEC+ agreement is disbanded altogether, primarily because of Russian reluctance.

Russian officials have increasingly become lukewarm, or in some cases outright cold, to the idea of extending an OPEC+ agreement beyond when the current one expires in June. One area of contention relates to privately owned Russian oil companies' and their belief that the OPEC+ agreement does not fit in with their own respective growth plans. The hesitancy on behalf of such oil companies could explain why Russian oil production did not reach committed levels by end of Q1 2019. Under the OPEC+ agreement, Russia was expected to reduce oil output by 228 tbpd over October 2018's level, but at the end of March, only around half of this amount had been achieved (Figure 9).

Looking ahead, Russia may be less inclined to join any further agreements in the future, although at this moment in time, the official position remains a 'wait and see' approach. One other factor that is likely to influence Russia's final decision is the extent of growth in US oil supply.

US oil output and exports rising:

In Q1 2019 total US crude oil production averaged just shy of 12 mbpd, up 16 percent year-on-year…

The latest EIA monthly drilling activity report shows that US oil supply from three of the major shale oil plays (Bakken, Eagle Ford and Permian) hit a record 7 mbpd in April 2019 (Figure 10). The acceleration of shale oil output has helped propel total US crude oil production to record levels. In Q1 2019 total US crude oil production averaged just shy of 12 mbpd, up 16 percent year-on-year whilst the EIA expects sequential rises in each and every quarter until its forecast period to 2020, when production is expected to hit 13.3 mbpd. Meanwhile, the rise in oil production has allowed the US to

Figure 8:Iranian crude oil purchases totaled 1.5 mbpd from five main countries

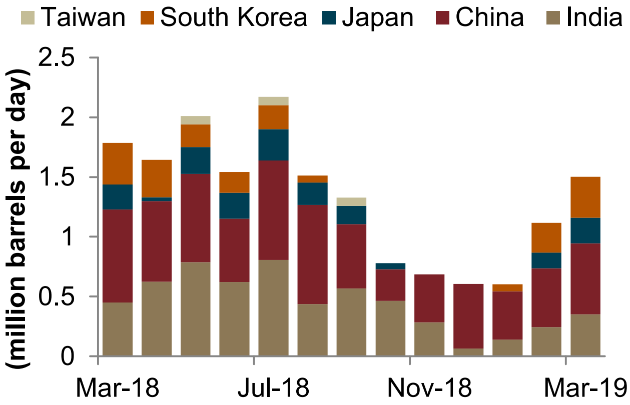
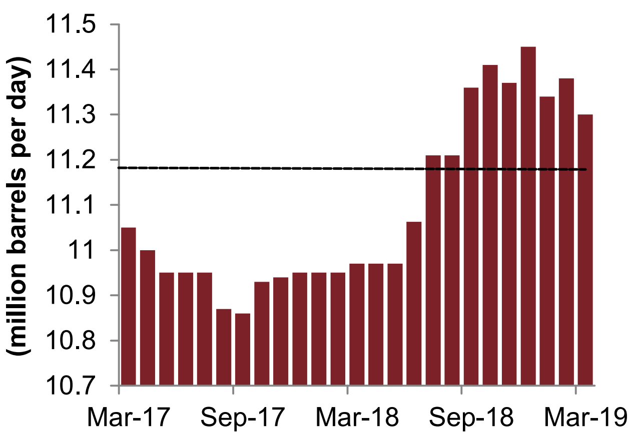


Figure 9: Russian crude oil production still higher than committed levels



…. whilst the EIA expects sequential rises in each and every quarter until its forecast period to 2020, when production is expected to hit 13.3 mbpd.

substantially raise the level of oil exports. In 2018, the US exported 2 mbpd of oil, compared to 1.2 mbpd in 2017, and up from virtually zero in 2010. According to the EIA, the three largest importers of US crude oil were Canada, South Korea and China.

Oil price outlook:

Brent oil prices averaged $63 pb in Q1 2019, down 6 percent on a quarterly basis as concerns over demand put pressure on prices. That said, the quarterly average disguises the fact that Brent oil prices recovered to around $68 pb towards the end of the first quarter as OPEC data confirmed compliance to the output agreement and OECD commercial oil stocks began to fall below their five year average (Figure 11).

Currently, Brent oil prices are around $75 pb, having gained recently on the back of US's refusal to grant waivers on Iranian oil.

Currently, Brent oil prices are around $75 pb, having gained recently on the back of US's refusal to grant waivers on Iranian oil. Looking out into the remainder of Q2, we still see some upside to oil with year-to-date Brent averaging $65 pb, whilst our forecast for the whole of 2019 is at $66 pb. That said, we also expect to see a new agreement allowing for a higher allocated level of oil production from OPEC+, and this together with rising US oil output should ease pressure on prices in the second half of 2019 (Box 2).

Looking ahead, we expect to see a new agreement allowing for a higher allocated level of oil production for OPEC+…

….as well as rising US oil output…

...which will ease pressure on prices in the second half of 2019

Box 2: Saudi crude oil production

Based on OPEC's March secondary sources data, and total Saudi Aramco capacity of 12 mbpd, Saudi Arabia currently has around 2.2 mbpd in excess capacity. As such, any agreement between OPEC+ that seeks to raise allocated quotas is likely to count on Saudi oil to make up a large portion of the agreed rise in output. As a result, despite Saudi Arabia's crude oil output averaging 10 mbpd in the first quarter of 2019, we have kept our forecast for Saudi oil output at 10.3 mbpd over the course of the year unchanged.

Figure 10: US shale oil from Bakken, Eagle Ford and Permian hitting record levels

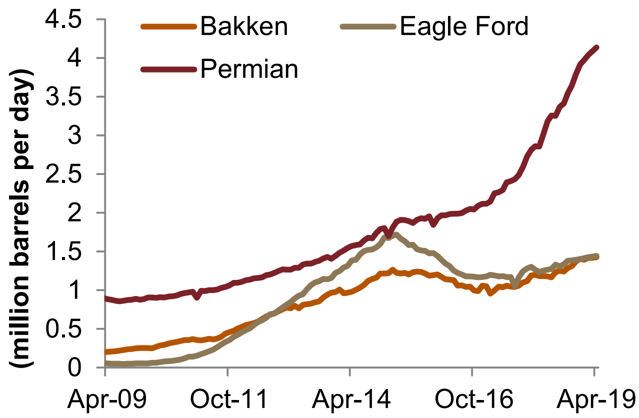
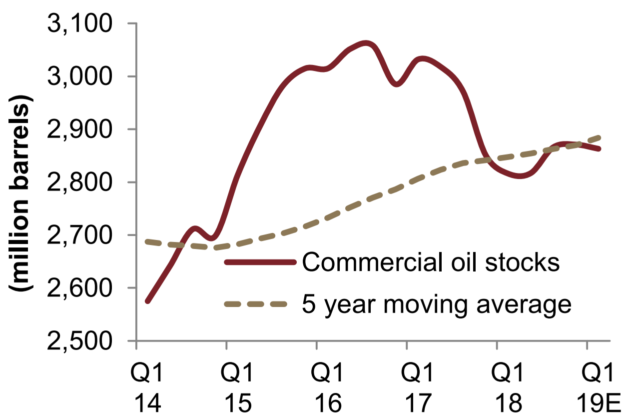


Figure 11: OECD commercial oil stocks now below moving five year average



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