

Oil Brief | 2 June 2025

Trade war and rising oil supplies weigh on crude prices

Worries over the health of the global economy amid escalating trade protectionism together with an accelerated unwind of OPEC+ output cuts pushed Brent crude to a four-year low of \$60/bbl in early May – though prices have risen off their lows. Responding to the weaker economic outlook, the IEA downgraded its 2025 oil demand growth projections to a multi-year low of 740 kb/d, which, in the context of faster OPEC+ supply increases and rising non-OPEC flows, risks a supply glut over the medium term. This is the central downside risk to oil prices, signaled by weaker oil futures and a spate of downward price revisions by forecasting agencies. Providing some upside potential is the prospect of supply disruptions from more stringent US sanctions on Iran and Venezuela or a de-escalation in the global trade tariff conflict.

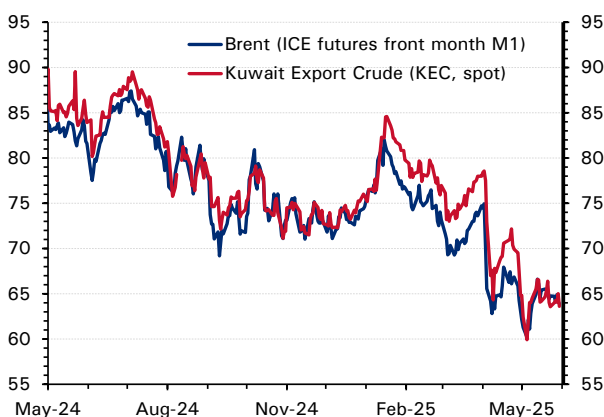
Markets: Trade tariffs and oversupply concerns push prices down to four-year lows from April

Largely unchanged in Q1, benchmark oil prices have dropped precipitously so far in Q2, after President Trump's "Liberation Day" tariff deluge on US trading partners and OPEC+'s decision to accelerate the pace of its supply cut unwinding schedule. Brent fell to four-year lows in April, shedding 15% by the close of the month, the steepest monthly decline since November 2021, and then dropped further to \$60.2 earlier in May. The marker has since struggled to break out of the low-to-mid-60s range, though President Trump's decision to slash tariffs on Chinese goods for 90-days did lift prices marginally.

Prices are now ranging around \$64/bbl, caught between bearish sentiment linked to unexpected crude inventory builds in the US and a third consecutive month of schedule-busting OPEC+ supply hikes on the one hand, and falling US oil rig counts and pessimism surrounding the prospects for a new Iran nuclear deal that would satisfy both the US and Iran on the other. President Trump's "maximum pressure" strategy vis-à-vis Iran and threat to impose even more stringent sanctions on the country's energy exports has been one of the few bullish impulses for oil prices and could puncture the negative sentiment that has befallen

Chart 1: Oil prices

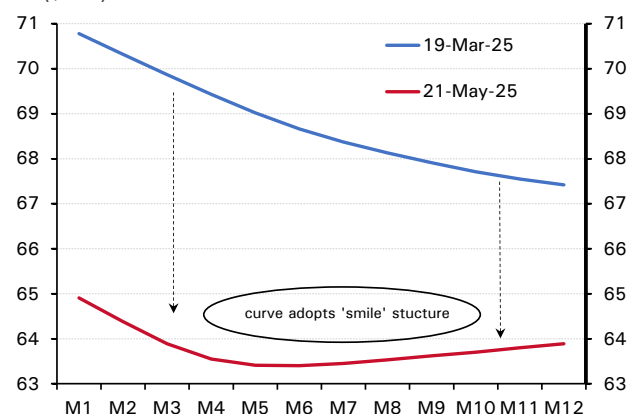
(\$/bbl)



Source: Haver, KPC

Chart 2: Brent 12-month forward curve

(\$/bbl)



Source: Intercontinental Exchange (ICE), Haver

the oil market in 2025. The pessimism has also been evident in the formation of a curious anomaly in Brent's forward curve: while the front end of the curve has been 'backwardated' (near-term prices higher than prices in the future), later month prices have shifted into a contango structure that see prices rising over earlier months. (Chart 2.) This so-called 'smiley' structure is fairly unprecedented and appears to signal that markets believe summer oil demand will be healthy enough to keep prices firm in the short term but insufficient to prevent a surplus and stock builds later on. And this is due to the potent combination of trade-tariff linked macroeconomic weakness and accelerating OPEC+ supply especially.

Meanwhile, the bullish speculator positions that had built up in Q1 quickly reversed in Q2 amid the spike in risk and uncertainty that followed April's tariff onslaught and OPEC+'s accelerated resupply timetable. 'Net length', the difference between the number of 'long' (betting on prices rising) and 'short' contracts (positions staked on prices falling) declined by 155,838 lots w/w in the week-ending 4 April, the sharpest drop in the available data. (Chart 3.) Net length has recovered slightly more recently as hedge funds view some upside risk in US-Iran nuclear talks failing to progress.

Oil demand: Growth at slowest since pandemic on tariff-linked trade dislocations

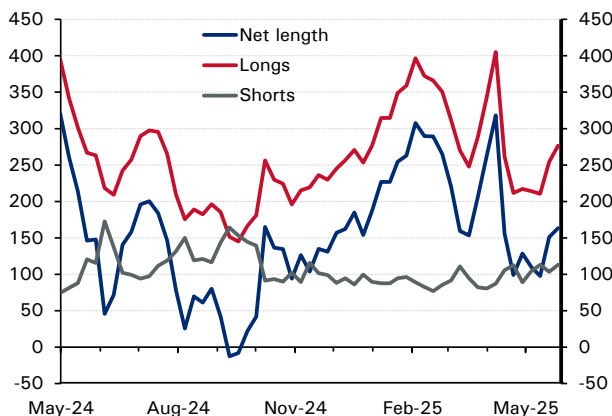
Near-term oil demand growth was revised sharply lower following the escalation of the trade war between the US and China. The International Energy Agency (IEA), taking its cue from the earlier downgrade by the IMF to global GDP growth in 2025 (and beyond), has lowered its forecast for oil demand growth this year to 740 kb/d and 760 kb/d in 2026. (Chart 4.) This is the weakest rate of growth since pandemic-affected 2020. The IEA pegs total oil demand at 105 mb/d in 2025. OPEC lowered its demand growth forecast by a less severe 150 kb/d to 1.3 mb/d for both years. OPEC cites higher petrochemical production, solid road and air mobility as well as robust industrial activity in support of its more bullish oil demand growth projection compared to peers. This would also not be incongruous with its recent policy of fast-tracking the unwinding of members' voluntary supply cuts.

Supply: OPEC+ accelerates output cut unwinding for May, June and July; US peak production on the horizon

Despite broad demand-side worries, OPEC+ surprised the markets by accelerating the pace of unwind of 2.2 mb/d in voluntary output cuts by the 'OPEC-8' (which includes Saudi Arabia, Russia, Iraq, UAE, Kuwait, Kazakhstan, Algeria, and Oman) from 131 kb/d per month from April to 411 kb/d in May and then again for both June and July. The move was ostensibly framed as a bid to 'punish' serial quota violators, such as Kazakhstan and Iraq, for failing to cut production in line with their quota obligations and compensatory cut promises. The Saudis hoped the fiscal discomfort of freefalling oil prices would bring about the discipline

Chart 3: Money manager net length

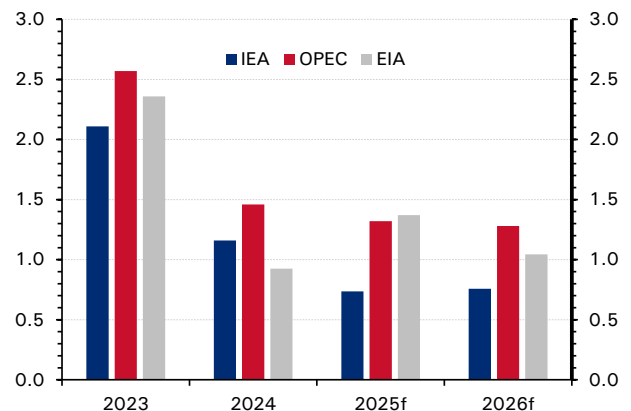
(thousand futures and options contracts)



Source: LSEG Workspace, ICE

Chart 4: World oil demand growth projections

(mb/d)



Source: IEA, OPEC, EIA

that has so far been absent among these overproducing members.

Part of the deal was that overproducing members would in good faith compensate for their non-compliance by cutting production according to a mutually agreed timetable thereby offsetting some of the supply that was about to be released. According to OPEC secondary sources, the average aggregate volume of OPEC-8 compensatory cuts required as 'payback' for members' overproduction from January 2024 to March 2025 is 305 kb/d, which would have easily offset the 131 kb/d of monthly incremental production OPEC-8 had originally planned. This would have resulted in a de-facto output cut. That said, in April, the first month in the schedule that called for higher OPEC-8 supply, monthly supply gains from the group, at 23 kb/d, fell far short of the 131 kb/d that had been planned. Only four of the eight producers – Saudi, the UAE, Oman and Russia – increased production. Despite lowering output in April, Kazakhstan and Iraq were once again producing well above their respective quotas never mind honoring compensatory cut pledges. Declaration of Cooperation (DOC) production (excluding quota-exempt Iran, Libya, Venezuela and Mexico) fell slightly in April to 30.0 mb/d (-17 kb/d). (Chart 5.)

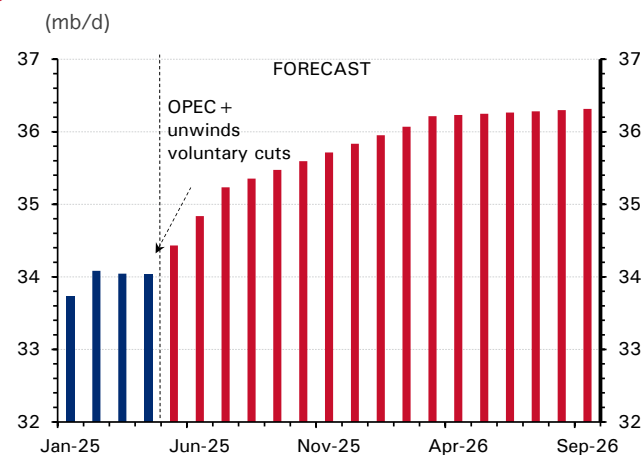
In the US, crude production hovered near record levels of 13.4 mb/d by mid-May, as per Energy Information Administration (EIA) data. (Chart 6). Following the plunge in oil prices and the downturn in global macroeconomic prospects, the EIA lowered its forecast for US crude oil output growth this year by nearly half to 208 kb/d, the slowest rate of expansion since 2021. For 2026, growth is expected to decelerate even further to just 82 kb/d as producers pull back on activity amid lower oil prices. According to a Dallas Fed energy survey, the average breakeven price in the shale patch to drill a new oil well is around \$65/bbl, several dollars above the current price of West Texas Intermediate.

US shale firms have also been grappling with the challenges of rising gas-to-oil and water-to-oil ratios, which are straining infrastructure and raising operational costs. The EIA is projecting US crude oil production to peak in 2027 at 14 mb/d, with shale oil production topping out at 10 mb/d before declining through to 2050. The recent decline in oil prices is also weighing on broader non-DoC production, prompting downgrades to the outlook, though at an estimated 1.3 mb/d this year according to the IEA, supply growth is still well outpacing demand growth. This is being driven by higher production in Brazil, Guyana, and Canada as well as in the US. For 2026, however, the IEA sees non-DoC supply growth lagging demand growth, at 820 kb/d.

Market balance and price outlook: Risks tilted to the downside amid a scarcity of upside catalysts

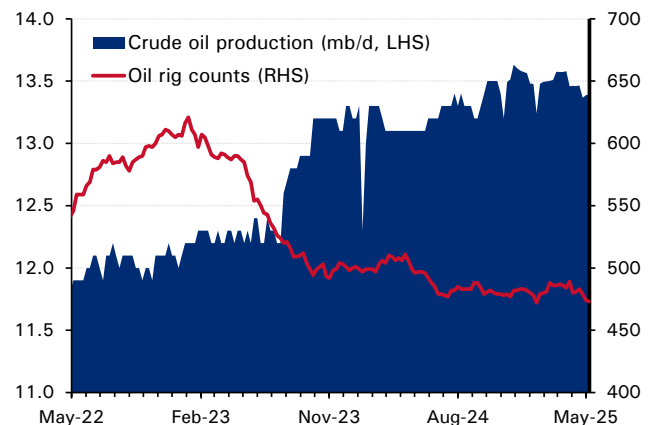
Weaker oil demand prospects due to trade tariff-linked global macroeconomic headwinds and rising supply both from OPEC+ and non-OPEC+ producers, are weighing heavily on market sentiment and by extension oil

Chart 5: DoC crude oil production*



Source: OPEC; *quota members, excl. compensatory cuts

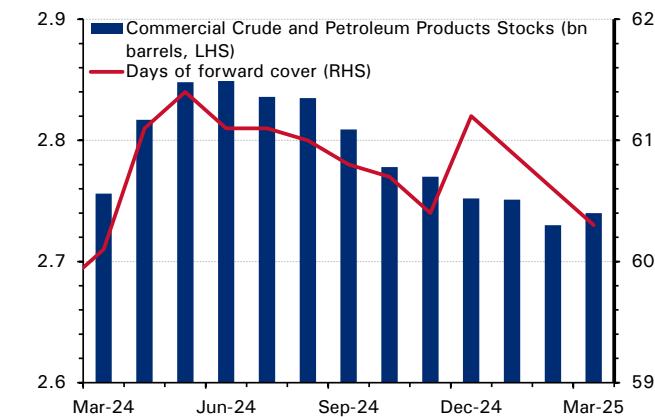
Chart 6: US crude production and rig counts



Source: EIA, Baker Hughes

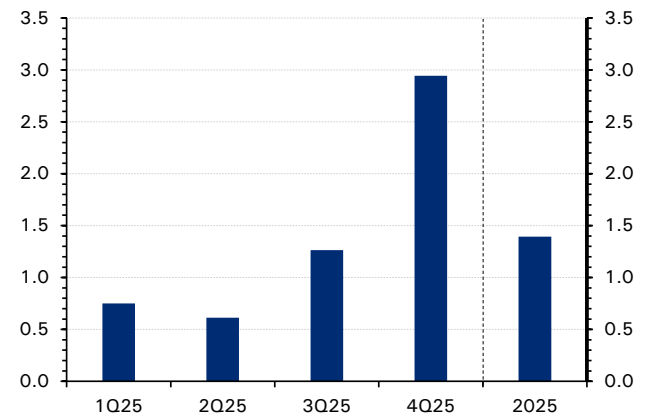
prices. The fundamentals are signaling a loosening oil market that will shift from a slight supply deficit last year to a pronounced surplus in 2025. The IEA estimates the “call” on OPEC+ (the volume of OPEC+ crude needed to balance the market after accounting for demand and non-OPEC supply) to be in the region of 41.2 mb/d on average in 2025. OPEC+ was already pumping significantly above the IEA’s estimate for the call in Q1 2025 (+800 kb/d) before the group decided to ramp up output in April. And the increase in OECD commercial crude stocks in March was beginning to reflect that. (Chart 7.) With OPEC-8 seemingly pressing ahead with a more rapid resupply pace, that buffer will quickly erode. Assuming no change to current OPEC-8 policy and no offsetting compensatory cuts, the entirety of 2023-2024’s 2.2 mb/d of supply cuts would have been unwound by October 2025 (rather than the original late 2026), pushing the market into firm surplus territory, averaging 1.4 mb/d, according to our calculations. (Chart 8.) Risks to our standing oil price forecast of \$70/bbl (2025 and 2026) are increasingly concentrated to the downside, barring significant supply-side geopolitical disruptions such as tighter Iran sanctions or, on the demand side, an upturn in global economic prospects, perhaps by a rolling back of trade tariffs.

Chart 7: OECD inventories



Source: OPEC, Haver

Chart 8: Implied global stock change (mb/d)



Source: IEA, NBK estimates

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