

# Monthly Oil Market Update

## Key Highlights

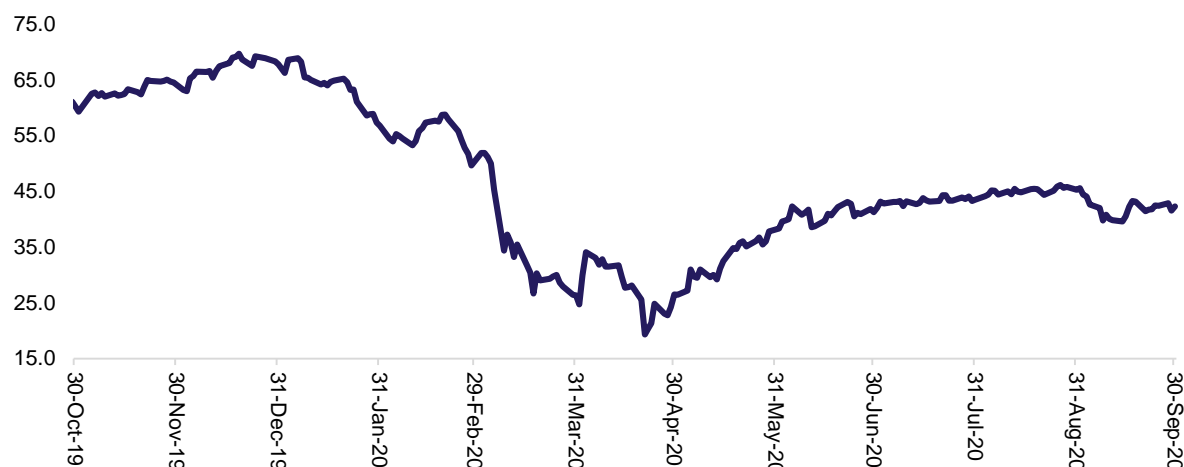
- Nigeria production reached a low of 1.47mbpd in September (excluding condensates), the lowest since December 2016 when Niger Delta militants attacked oil infrastructures.
- Nigeria grade Bonny light declined by \$4.07/barrel to average \$40.8/barrel in September from average of \$44.90/barrel in August. The Bonny Light-Brent discount widened to \$1.20/barrel from \$0.05/barrel in August.
- Global crude oil market to remain in deficit over the rest of the year, with average of 2.96mbpd in Q4 (lower than 3.08mbpd in Q3).
- Irrespective, prices will remain range bound due to slower inventory draws at a rate of 3.0mbpd in Q4 (compared to drawdown of 3.1mbpd in Q3) relative to inventory buildup at a rate of 7.2mbpd in Q2.
- Brent crude oil price will average \$42/barrel in Q4 (from Q3 average of \$42.98/barrel) with 2020 average of \$41.19/barrel.

## Bearish Market Sentiment Takes a Toll on Prices

Notwithstanding widened market deficit in the month of September to 3.56mbpd (from 2.48mbpd in August) following a faster increase in demand relative to supply, bearish market sentiment due to the prospects of fresh lockdown restrictions in Europe following resurgence of the coronavirus pandemic kept oil prices subdued in September. Also, trade tensions between the U.S and China further exacerbated in September following the new licensing restrictions issued by the Trump administration on US firms exporting certain products to China's biggest semiconductor manufacturer. Overall, Brent crude oil spot prices declined by \$3.1/barrel from August to average \$42.02/barrel in September. The moderation in oil prices in September largely reflects the slower rate of inventory drawdown amidst rising production in the US and faltering compliance among OPEC+ members. Also, the front-month futures price for Brent crude oil settled at \$40.95/barrel on September 30, a decline of \$4.33/barrel from August 31, 2020 while the front-month futures price for West Texas Intermediate (WTI) dropped by \$2.39/b during the same period, settling at \$40.22/barrel.

With the elevated inventory levels keeping prices range bound, Saudi Arabia official oil pricing template for November, offered Arab light delivery to Asia at a discount of \$0.40/ barrel (compared to discount of \$0.50/barrel in October) to the Oman/Dubai average, U.S delivery premium is maintained at \$1.05/barrel (compared to \$1.65/barrel in September) versus ASCI and discount of \$2.00/barrel is maintained (discount of \$1.80/barrel in September) to ICE Brent for delivery to Northwestern Europe.

Figure 1: Brent oil price in 2020 (\$/bbl.)

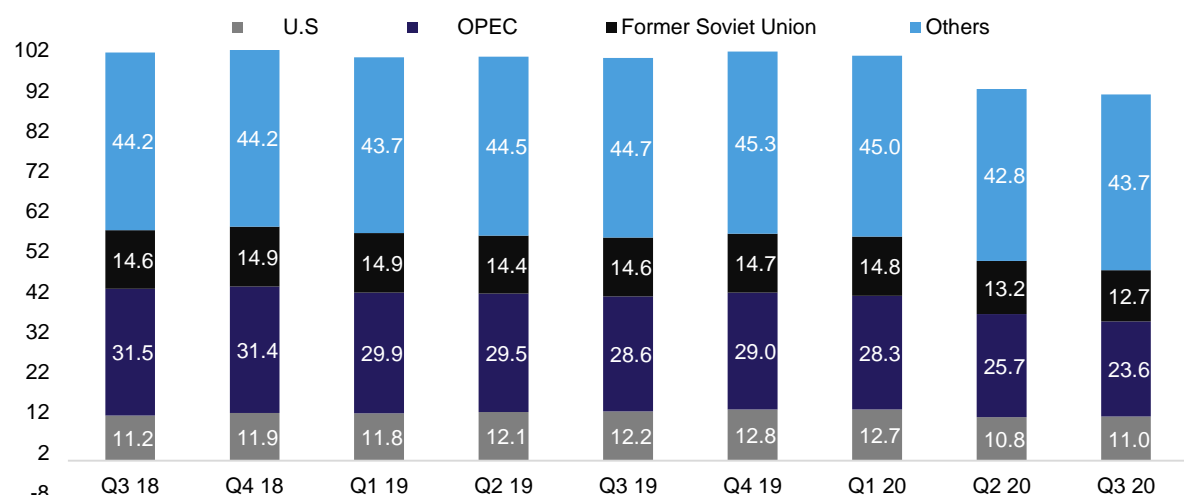


Source: Bloomberg, NOVA Research

## OPEC+ Agreement Continues to Keep Output in Shape

In Q3 20, global crude oil supply declined by 1.36mbpd to average 91.1mbpd relative to 92.5mbpd in Q2 20. The decline in supply over the period stemmed from both cuts from OPEC producers by 2.01mbpd (to average 23.6mbpd compared to average of 25.7mbpd in Q2 20) and Russia of 467kbpd, both of which more than offset increase in shale production (200kbpd to 11.0mbpd from 10.8mbpd in Q2 20). Reflecting the failure by members of the OPEC+ to meet up with the agreed production including compensatory cuts, global oil production over September increased by 247kbpd to 91.70mbpd with U.S (+363kbpd) accounting for a large proportion of the increase.

Figure 2: World Petroleum and Other Liquids Production (mbpd)



Source: EIA, NOVA Research

Similar to the month of August, compliance to the expected catch-up cuts by countries who overproduced during the first phase of the deal and in August continues to falter. In the month of September, OPEC 10 production declined by 0.015mbpd in September to 21.645mbpd (0.170mbpd above the stipulated Aug. to December quota) compared to 21.660mbpd in August. With the timeframe for the catch-up cuts extended until December 2020 (at the last Joint Ministerial Monitoring Committee meeting) and May-August overproduction of 1.64mbpd, expected additional monthly cuts

starting September to compensate for the over-production should be in excess of 0.380mbpd. However, based on official OPEC document, out of the 7 members who exceeded production quota, only 4 (Congo, Equatorial Guinea, Iraq and UAE) have submitted a plan to catchup with the excess production. On the September production relative to expected cut based on the Phase 2 agreement, the group achieved compliance rate of 100% (from 106% in August), adjusting for the expected compensatory cuts neutered the September compliance rate to just 79%. The lower adjusted compliance was further magnified due to overproduction by Saudi Arabia, who exceeded its quota for the first time since the accord with September production rising 0.118mbpd to 9.01mbpd. To make up for overproduction during the Phase 1, Nigeria production reached a low of 1.47mbpd, the lowest since December 2016 when Niger Delta militants attacked oil infrastructures. Irrespective, Nigeria is still yet to fully compensate for the over production during the Phase 1 of the deal, with remaining compensation cut of 294kbpd. Excluding the OPEC 10, production in Libya picked up in September to 0.130mbpd as the blockade of export terminals are relaxed, while Venezuela and Iran remain constrained by US sanctions.

**Figure 3: OPEC crude oil production based on secondary sources, tb/d**

	Sep-19	May-20	Jun-20	Jul-20	Aug-20	Sep-20	New Quota
Algeria	1,020	819	807	808	860	850	864
Angola	1,399	1,275	1,224	1,173	1,210	1,180	1,249
Congo	335	285	302	284	286	280	266
Equatorial Guinea	122	90	114	110	118	105	104
Gabon	197	194	204	189	214	150	153
Iran, I.R.	2,164	1,954	1,947	1,936	1,950	1,900	Exempt
Iraq	4,732	4,160	3,714	3,752	3,460	3,710	3,804
Kuwait	2,658	2,198	2,085	2,158	2,291	2,290	2,297
Libya	1,160	80	92	100	120	130	Exempt
<b>Nigeria</b>	<b>1,848</b>	<b>1,584</b>	<b>1,497</b>	<b>1,488</b>	<b>1,390</b>	<b>1,470</b>	<b>1,495</b>
Saudi Arabia	8,796	8,479	7,540	8,406	8,990	9,010	8,993
UAE	3,083	2,478	2,332	2,430	2,693	2,600	2,590
Venezuela	644	558	336	339	340	340	Exempt
<b>Total OPEC</b>	<b>24,190</b>	<b>21,562</b>	<b>19,819</b>	<b>20,798</b>	<b>21,512</b>	<b>21,645</b>	<b>21,815</b>
<b>OPEC 10</b>	<b>28,158</b>	<b>24,154</b>	<b>22,194</b>	<b>23,173</b>	<b>23,922</b>	<b>24,015</b>	<b>N/A</b>

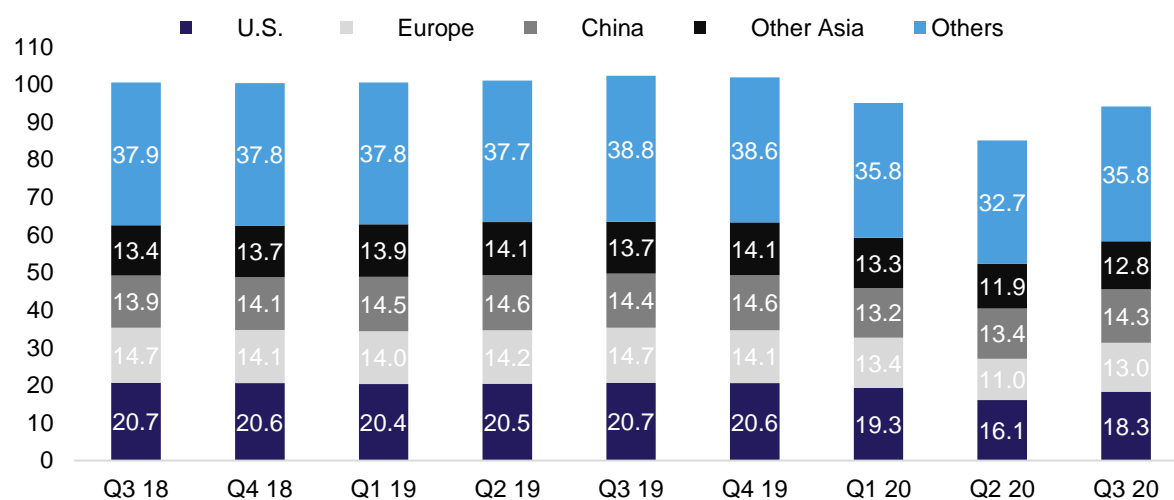
Source: OPEC Monthly Oil Market Report, EIA, NOVA Research

### Gradual Improvement in Demand, But Still Far From Normal

Global oil demand increased by 9.17mbpd over Q3 20 to average 94.2mbpd relative to 85.08mbpd in Q2 20. In September standalone, consumption increased by 1.33mbpd (higher than the growth in August of 0.616mbpd) to 95.3mbpd compared to August level of 93.9mbpd. The uptick in September stemmed from further relaxation of COVID-19 travel restrictions. Particularly, consumption among OECD and non-OECD countries increased by 5.2mbpd and 3.9mbpd to average 42.6mbpd and 51.6mbpd respectively over Q3 20. For OECD, most of the increase stemmed from USA (2.2mbpd)

and Europe (2.0mbpd), which combined accounted for 81% of the total increase in OECD during the period. Also, resumptions of manufacturing activities necessitated increase in demand in Japan (158kbpd) and Other OECD (442kbpd). For the non-OECDs, the increased emanated from Other Non-OECD (1.3mbpd), China (889kbpd), Other Asia (858kbpd) and Eurasia (802kbpd). China alone accounted for 23% of the total increase in oil consumption over Q3. In September standalone, consumption increased by 1.33mbpd (higher than August increase of 616kbpd) to 95.3mbpd, following higher consumption in China (+778kbpd), OECD Europe (629kbpd), Other Asia (464kbpd) and Other Non-OECD (464KBPD), all of which more than offset the declines in USA (-635bpd) and most other regions.

**Figure 4: World Petroleum and Other Liquids Consumption (mbpd)**



Source: EIA, NOVA Research

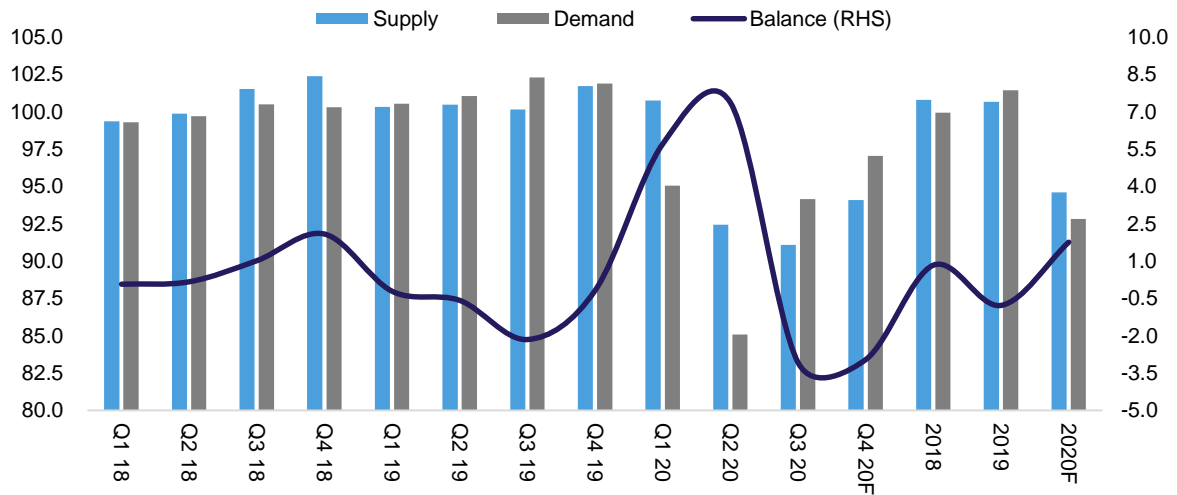
### Further Downward Review of Crude Oil Demand

In its October Short-Term Energy Outlook, the EIA lowered its forecast for crude oil consumption in Q4 by 0.448mbpd to 97.05mbpd, with full year 2020 consumption now revised lower by 0.230mbpd to 92.84mbpd (below 2019 average of 101.5mbpd). While the relaxation of lockdown restrictions across industrial economies and the construction of a new petrochemical crackers in China during the second half of 2020 are expected to support demand, EIA lowered Q4 demand projection in OECD and Non-OECD by 0.344mbpd and 0.100mbpd to 44.33mbpd and 52.73mbpd respectively. The downward adjustment in OECD was dominated by now lower expected consumption in USA (-351kbpd) and in the Non-OECD by Other Asia (-137kbpd). In October standalone, consumption is forecast to increase by 624kbpd to 95.88mbpd dominated by higher demand in China and Eurasia, which are expected to offset decline of across other regions and 1.13mbpd in USA alone for October.

As mentioned above, while OPEC produced 0.170mbpd below its Phase 2 planned cut, September production is still 1.35mbpd above the level expected to meet up with overproduction between May and August. With the extended timeframe to meet up with the catchup to December, OPEC production is estimated to decline by 1.52mbpd over Q4 from September level if all members fully comply with the Phase 2 deal and the associated compensatory cuts. EIA estimates, global production to increase by 3.01mbpd in Q4 to 94.1mbpd, dominated by increased production among OPEC members (+2.11mbpd) and non-OPEC members (+0.893mbpd). In October standalone,

supply is forecast to increase by 1.0mbpd to 92.70mbpd dominated by higher supply by OPEC (+701kbpd). Overall, total world supply is expected to average 94.58mbpd in 2020 (compared to 100.6mbpd in 2019).

**Figure 5: Historical and Forecast Oil demand, supply and balance (mbpd)**



Source: EIA, NOVA Research

### Still Elevated Inventory Will Keep Prices Range Bound

Notwithstanding the expectation of the market remaining in a deficit over the rest of the year, with average of 2.96mbpd in Q4 (lower than 3.08mbpd in Q3), crude oil prices are expected to be range bound due to the still elevated inventory levels occasioned by the cumulative market surplus of 39.2mbpd over H1 2020. Despite the gradual drawdown, U.S. commercial inventory are still 13% above the five-year average. EIA expects inventory draws at a rate of 3.0mbpd (3.1mbpd in Q3) in Q4 compared to inventory build-up at a rate of 7.2mbpd in Q2. As a result, EIA forecasts Brent crude oil will average \$42/barrel in Q4 (lower than September estimate of \$44.17/barrel) with 2020 average of \$41.19/barrel which is lower than average of \$64.34/barrel in 2019. For us, we believe the gradual opening of key economies and minimal infection rate could result in a rebound in oil demand, which coupled with full compliance by OPEC+ will provide further upside potential for prices. However, a renewed lockdown due to second wave of the Cvid-19 and faster pace of export resumption in Libya could see prices slide further to the bottom.