Economic Update

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Oil

Oil rally stalls on reemergence of global growth concerns amid rising oil stocks

> Omar Al-Nakib
Senior Economist
+965 2259 5360
omarnakib@nbk.com

Highlights

- **Brent crude back trading around $62.5/bbl on global economy and oil oversupply concerns.**
- **Bearish sentiment stoked by US-China trade deal delays and continued increases in US crude stockpiles.**
- **Global oil demand growth in 2019 revised down again, by 0.065 mb/d to 1.0 mb/d—the weakest in three years; growth in 2020 was also trimmed, to 1.2 mb/d, following downgrades to global macro growth by the IMF.**
- **OPEC+ compliance in September skyrockets to 230%, almost entirely due to Saudi outages stemming from the drone strikes.**

Oil back on defensive after early November rally

Oil prices were back in familiar territory as the first week in November drew to a close: buffeted by a combination of overarching global macro concerns, specifically the off/on progress in US-China trade talks, and oil oversupply worries. International crude oil benchmark Brent crude was last trading at around $62.5/bbl (+16.2% ytd), down from its more than 4-week high of almost $63/bbl on 5 November. The US crude benchmark, West Texas Intermediate (WTI), was trading at $57.2/bbl (+26.1% ytd). (Charts 1-3.)

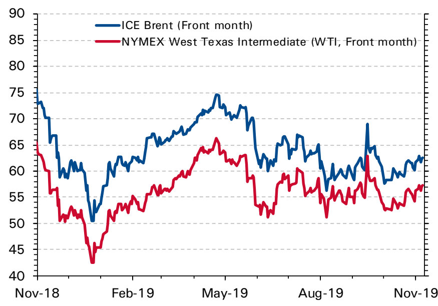
Both markers had been enjoying three days of gains on the back of signs of progress in US-China trade negotiations—a 'Phase One' trade deal had been talked about—as well as positive US jobs numbers and manufacturing data. But following reports that US President Trump and his Chinese counterpart Xi Jinping may not be able to sign the long-coveted partial trade deal until December, and the publication by the US Energy Information Administration (EIA) of data showing that US crude stockpiles had increased by much more than expected (+7.9 million barrels to 446.8 mb by the week ending 1 November), prices were once more on the back foot.

Also imparting a bearish spin on proceedings were reports that the OPEC+ group is unlikely to push for further production cuts at their next scheduled ministerial meeting in December. This came after OPEC, in its World Oil Outlook 2040, predicted that world oil demand would grow by a modest 1.0 mb/d over the medium term while US shale production would increase by a robust 40% by 2025. The producers' group anticipated a decline in its own market share from the current 35% to 32% by 2025.

Prices traded sideways in October in the absence of specific triggers

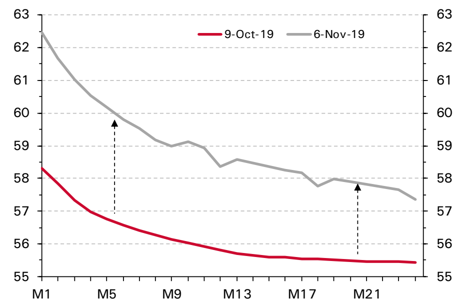
With Saudi crude production restored to 'normal' levels relatively quickly in October after the drone strike on the Abqaiq/Khurais oil processing infrastructure the previous month, oil prices had traded sideways for most of October. Any lingering geopolitical risk premia disappeared with the full restoration of Saudi production. And with supply-

Chart 1: Benchmark crude oil prices
($/bbl)



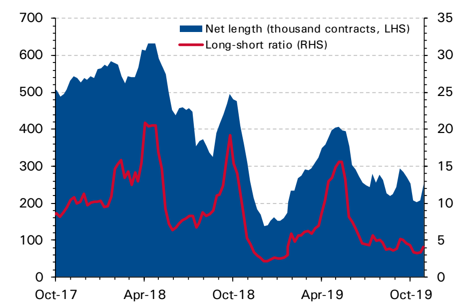
Source: Refinitiv

Chart 2: Brent forward curve to 24 months
($/bbl)



Source: Bloomberg; note: x-axis denotes forward months

Chart 3: Money manager net length
(Brent combined futures and option contracts)



Source: Bloomberg

side triggers largely absent, anxieties about the trajectory of global economic growth were once again in the ascendancy.

Overarching macroeconomic concerns

Both the International Monetary Fund (IMF) and the International Energy Agency (IEA), lowered their forecasts for the global macroeconomic and oil demand growth pictures, respectively, in October. The IMF cited rising trade barriers and increased geopolitical and trade uncertainty among the factors driving a 'synchronized' global slowdown, that left growth in 2019 at 3.0%—the slowest since the financial crisis more than ten years ago. Projected economic growth in 2020 was reduced by 0.2% points to 3.4%. The IEA, for its part, trimmed its oil demand growth forecast again for 2019 by 0.065 mb/d to 1.0 mb/d and for 2020 by 0.11 mb/d to 1.2 mb/d, respectively, although the agency did acknowledge that some of this year's adjustment was due to 2018 crude demand figures in the US being revised upwards. (Chart 4.) As things stand, oil demand growth in 2019 will likely be the weakest in three years, reflecting softness in Europe, India, Japan, Korea and the US. Chinese oil consumption, however, continues to be robust.

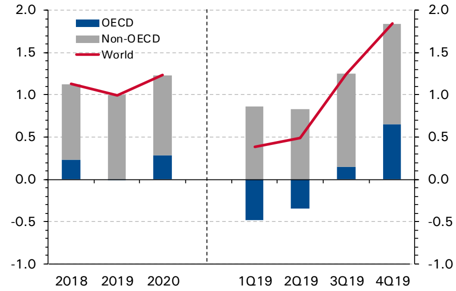
Non-OPEC supply gains despite record OPEC+ production cut compliance

Markets appear to have largely shrugged off the drone attacks on Saudi oil facilities and the negative implications for global oil supplies. The Abqaiq/Khurais outage were the largest contributors (1-1.2 mb/d) to the steepest monthly fall in oil supplies (1.5 mb/d) in more than a decade; declines in Norway and Canada as well as further falls in Venezuelan production accounted for the rest. Nevertheless, non-OPEC supply growth, led by robust US shale growth, dominates the supply outlook, helping to offset the cutbacks in production that OPEC+ has orchestrated this year. US crude production reached a historic high of 12.6 mb/d in October. (Chart 5.) The IEA sees US crude oil production alone increasing by 1.2 mb/d in 2019 and 0.9 mb/d in 2020, which accounts for at least 75% of the crude that OPEC+ has removed from the market.

Due to Saudi Arabia's involuntary production cut in September, OPEC+ compliance skyrocketed to 230% from 120% in August. (Chart 6.) OPEC and its partners were characteristically tight-lipped about further OPEC+ production cuts, preferring to wait until December's biannual ministerial meeting before making any announcements. So long as some OPEC producers, such as Iraq and Nigeria, continue to produce above their quotas, it does not seem likely that further cuts will be on the cards.

Chart 4: world oil demand growth

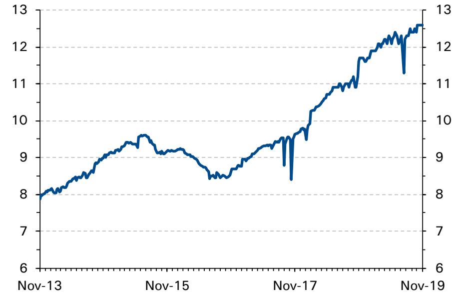
(million barrels per day, mb/d)



Source: International Energy Agency (IEA)

Chart 5: US crude production

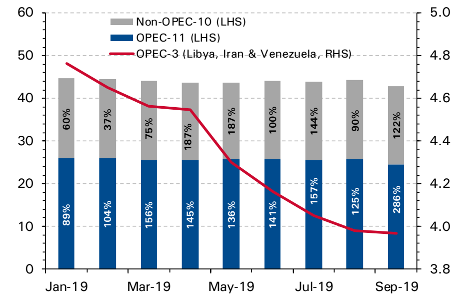
(mb/d)



Source: US Energy Information Administration (EIA)

Chart 6: OPEC+ production & compliance

(mb/d; % figures denote compliance)



Source: OPEC (secondary sources)

Head Office

Kuwait
National Bank of Kuwait SAKP
Abdullah Al-Ahmed Street
P.O. Box 95, Safat 13001
Kuwait City, Kuwait
Tel: +965 2242 2011
Fax: +965 2259 5804
Telex: 22043-22451 NATBANK
www.nbk.com

International Network

Bahrain
National Bank of Kuwait SAKP
Zain Branch
Zain Tower, Building 401, Road 2806
Seef Area 428, P. O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

National Bank of Kuwait SAKP
Bahrain Head Office
GB Corp Tower
Block 346, Road 4626
Building 1411
P.O. Box 5290, Manama
Kingdom of Bahrain
Tel: +973 17 155 555
Fax: +973 17 104 860

United Arab Emirates
National Bank of Kuwait SAKP
Dubai Branch
Latifa Tower, Sheikh Zayed Road
Next to Crown Plaza
P.O.Box 9293, Dubai, U.A.E
Tel: +971 4 3161600
Fax: +971 4 3888588

National Bank of Kuwait SAKP
Abu Dhabi Branch
Sheikh Rashed Bin Saeed
Al Maktoom, (Old Airport Road)
P.O.Box 113567,Abu Dhabi, U.A.E
Tel: +971 2 4199 555
Fax: +971 2 2222 477

Saudi Arabia
National Bank of Kuwait SAKP
Jeddah Branch
Al Khalidiah District,
Al Mukmal Tower, Jeddah
P.O Box: 15385 Jeddah 21444
Kingdom of Saudi Arabia
Tel: +966 2 603 6300
Fax: +966 2 603 6318

Jordan
National Bank of Kuwait SAKP
Amman Branch
Shareef Abdul Hamid Sharaf St
P.O. Box 941297, Shmeisani,
Amman 11194, Jordan
Tel: +962 6 580 0400
Fax: +962 6 580 0441

Lebanon
National Bank of Kuwait
(Lebanon) SAL
BAC Building, Justinien Street, Sanayeh
P.O. Box 11-5727, Riad El-Solh
Beirut 1107 2200, Lebanon
Tel: +961 1 759700
Fax: +961 1 747866

Iraq
Credit Bank of Iraq
Street 9, Building 187
Sadoon Street, District 102
P.O. Box 3420, Baghdad, Iraq
Tel: +964 1 7182198/7191944
+964 1 7188406/7171673
Fax: +964 1 7170156

Egypt
National Bank of Kuwait - Egypt
Plot 155, City Center, First Sector
5th Settlement, New Cairo
Egypt
Tel: +20 2 26149300
Fax: +20 2 26133978

United States of America
National Bank of Kuwait SAKP
New York Branch
299 Park Avenue
New York, NY 10171
USA
Tel: +1 212 303 9800
Fax: +1 212 319 8269

United Kingdom
National Bank of Kuwait
(International) Plc
Head Office
13 George Street
London W1U 3QJ
UK
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

National Bank of Kuwait
(International) Plc
Portman Square Branch
7 Portman Square
London W1H 6NA, UK
Tel: +44 20 7224 2277
Fax: +44 20 7486 3877

France
National Bank of Kuwait
(International) Plc
Paris Branch
90 Avenue des Champs-Elysees
75008 Paris
France
Tel: +33 1 5659 8600
Fax: +33 1 5659 8623

Singapore
National Bank of Kuwait SAKP
Singapore Branch
9 Raffles Place # 44-01
Republic Plaza
Singapore 048619
Tel: +65 6222 5348
Fax: +65 6224 5438

China
National Bank of Kuwait SAKP
Shanghai Representative Office
Suite 1003, 10th Floor, Azia Center
1233 Lujiazui Ring Road
Shanghai 200120, China
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

NBK Capital

Kuwait
NBK Capital
38th Floor, Arraya II Building, Block 6
Shuhada'a street, Sharq
PO Box 4950, Safat, 13050
Kuwait
Tel: +965 2224 6900
Fax: +965 2224 6904 / 5

United Arab Emirates
NBK Capital Limited - UAE
Precinct Building 3, Office 404
Dubai International Financial Center
Sheikh Zayed Road
P.O. Box 506506, Dubai
UAE
Tel: +971 4 365 2800
Fax: +971 4 365 2805

Associates

Turkey
Turkish Bank
Valikonagl CAD. 7
Nisantasi, P.O. Box. 34371
Istanbul, Turkey
Tel: +90 212 373 6373
Fax: +90 212 225 0353