PUBLIC

# Economic Update

NBK Economic Research Department I 7 December 2022

Oil Markets

# Oil prices decline in November on intensifying global economy concerns


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



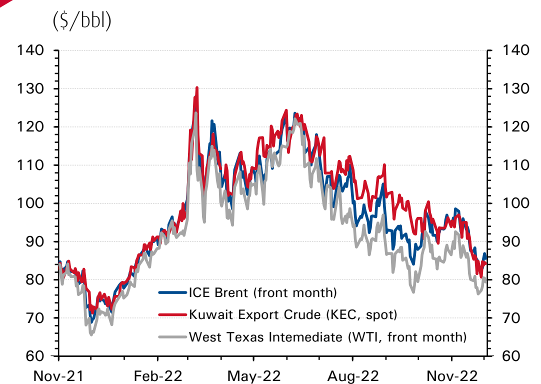
## Summary

**Oil prices closed lower in November, reversing all of October's OPEC+ announcement gains, as global economic recession worries intensified. The focus of concern was China and the economic damage that was being caused by repeated lockdowns. While OPEC+ output was due to be pared back in November, preliminary estimates show a slight increase. The G7/EU finally agreed to cap Russia's crude oil sales at $60/bbl.**


- Oil prices trended lower in November, pressured again by worries over the health of the global economy amid elevated inflation, tightening monetary policy and repeated Covid-19 lockdowns in China, the world's second largest economy and largest crude oil importer. (Chart 1.) By November's close, Brent crude had fallen 10% to $85.4/bbl (+9.8% ytd), shedding all the gains that followed the OPEC+ output cut decision in October and extending the decline from March's post-Ukraine invasion peak of $128/bbl to 32%. US marker West Texas Intermediate (WTI) declined 7% m/m in November to $80.6/bbl. Local blend Kuwait Export Crude (KEC), fell 10.7% m/m to $83.8/bbl (+6% ytd).
- The bearish turn in the oil markets is reflected in the structural shift of the Brent forward curve at the front end from one of backwardation (near-term prices being higher than longer-term prices) to one of contango (near-term prices lower than longer-term prices). (Chart 2.) This phenomenon is usually associated with ample near-term supplies. November saw money managers slash bullish, 'long' positions in favor of bearish, 'short' positions in Brent futures and options contracts. Net length fell by 34% to 138k contracts in the week to 22 November, the biggest weekly decline in eight months, and brings net length to its lowest level since August. (Chart 3.) Behind that week's precipitous decline were uncorroborated rumors of an impending OPEC+ supply increase and China's tightening of anti-Covid curbs.
- The global oil demand picture has worsened, especially in the near term, as western economies and Europe in particular grapple with an energy crisis catalyzed by Russia's invasion of Ukraine and soaring inflation and borrowing costs. A stronger US dollar has also been a factor. China, the key driver of global oil demand growth, remains mired in a Covid-19 infection-lockdown spiral that has severely dented economic activity. According to the International Energy Agency (IEA), oil demand is expected to contract this quarter by 240 kb/d y/y and in 1Q23 by a hefty 1 mb/d q/q to 99.6 mb/d (+0.22 mb/d y/y). (Chart 4.) Looking further ahead, however, the IEA sees oil demand rebounding from 2Q23 to a high of 2.4 mb/d by 4Q23 on an expected resurgence in post-lockdown Chinese economic activity. Average annual growth in 2023 will be 1.6 mb/d, slower than the 2.1 mb/d estimated for this year, though.
- On the oil supply side, October was the first month in which OPEC+ had scheduled a reduction in supply, of 150 kb/d, since the Vienna agreement of April 2020 at the onset of the pandemic. While OPEC-10 production did indeed fall, by 223 kb/d to 25.1 mb/d, according to OPEC secondary sources, output from other OPEC+ members (excluding Mexico), on the other hand, reportedly increased, thanks to rebounding supply from Kazakhstan. Together, aggregate output among OPEC+ group members subject to quotas probably increased by around 27 kb/d over September levels to 38.6 mb/d. Russia's output in October was also seen ranging higher month-on-month, at around 9.85

### Chart 1: Oil prices

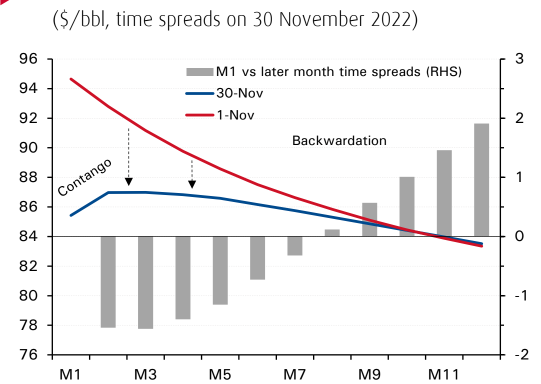
($/bbl)




Source: Refinitiv, Bloomberg

### Chart 2: Brent forward curve and time spreads

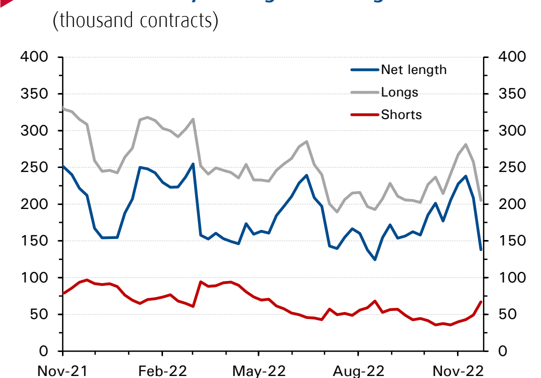
($/bbl, time spreads on 30 November 2022)




Source: Refinitiv

### Chart 3: Money manager net length

(thousand contracts)



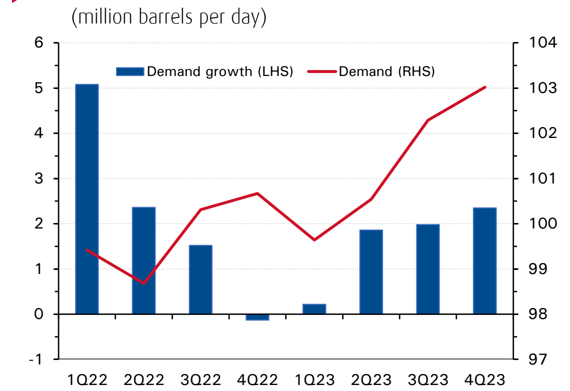

Source: Bloomberg, Refinitiv; *futures and options

mb/d, according to S&P Global. From November 2022 until December 2023, OPEC+ has penciled in cuts totaling 2 mb/d. Effective cuts are not expected to exceed 1 mb/d, though, given that many members, including Russia, Nigeria and Angola, never managed to pump enough crude to hit their targets when supply was being ramped up due to capacity constraints, outages and sanctions.

- OPEC+, at its 4 December ministerial meeting, which was moved to a virtual rather than a physical one, opted to rollover existing production cuts of 2 mb/d. There had been talk ahead of the meeting that, with the global oil demand outlook deteriorating further, the oil exporters' group might announce even deeper output cuts. In the end, though, the group preferred to wait and see how global oil demand, the EU's Russian oil embargo and the G7's price cap on Russian oil sales would affect oil demand-supply balances. The group made it clear that it remained ready to react quickly to changing market conditions.
- Determining a suitable price level above which Russia is prevented from selling its oil had proven increasingly difficult for the G7/EU. The group was looking to impose a price that was low enough to make a meaningful dent on Russia's oil revenues but not so low as to be below Moscow's cost price and shut-in supplies to the rest of the world (the US and its European allies have embargoed Russian oil imports). Within the EU there are divisions between those, such as Poland and the Baltic states that are keen on a lower price, and others like Greece, that prefer a higher price to keep their shipping and maritime interests running. Aside from the practical complexities and non-participation of Russia's largest customers China, India and Turkey that has many doubting whether the plan is workable, the approved price cap of $60/bbl is still higher than the level that Russia's flagship Urals grade is currently trading at. It may therefore be business as usual for Russia.
- The outlook for the oil market is extremely uncertain. In the short term, softening global oil demand and oil inventory builds this quarter are likely to impose a downward bias on oil prices. Demand destruction at the oil product level, with gasoil/diesel, for example, may already be taking place. Moving into 2023, however, and the oil market is expected to tighten significantly, with Russian oil supplies potentially shut in following the EU's crude and refined products embargo, OPEC+ supplies curtailed as per the group's October agreement and, importantly, China's re-emergence from Covid lockdowns that should lead to a normalization of economic activity and increased demand for oil. The market should flip from a surplus at the start of the year to a deficit by the second half. Price pressures should revert to the upside.

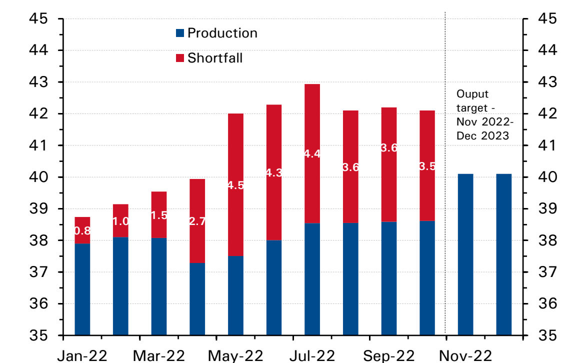
**Chart 4: World oil demand**

(million barrels per day)




Source: IEA

**Chart 5: OPEC+ output and targets**




Source: OPEC, S&P Global

## Head Office

**Kuwait**
National Bank of Kuwait SAKP
Shuhada Street,
Sharq Area, NBK Tower
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

**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

**France**
National Bank of Kuwait France SA
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 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
34h Floor, NBK Tower
Shuhada'a street, Sharq Area
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

**© Copyright Notice.** The Economic Update is a publication of the National Bank of Kuwait. No part of this publication may be reproduced or duplicated without the prior consent of NBK.
While every care has been taken in preparing this publication, National Bank of Kuwait accepts no liability whatsoever for any direct or consequential losses arising from its use. GCC Research Note is distributed on a complimentary and discretionary basis to NBK clients and associates. This report and other NBK research can be found in the "Reports" section of the National Bank of Kuwait's web site. Please visit our web site, www.nbk.com, for other bank publications. For further information, please contact: NBK Economic Research, Tel: (965) 2259 5500, , Email: econ@nbk.com