The Outlook: Aug. 1, 2018

Oil: what we know, and the market does not.

Here is Conoco's roller-coaster ride, this past three months. The "engine" driving Conoco's roller coaster has been the market's lightning changes in opinion about where on earth the price of oil intends to go. If it looks like the market is terribly uncertain about oil's intentions . . . we are understanding the chart perfectly.

Conoco: 3 Months

The $64,000 Question, of course, is: "Do we know something the market doesn't know?"

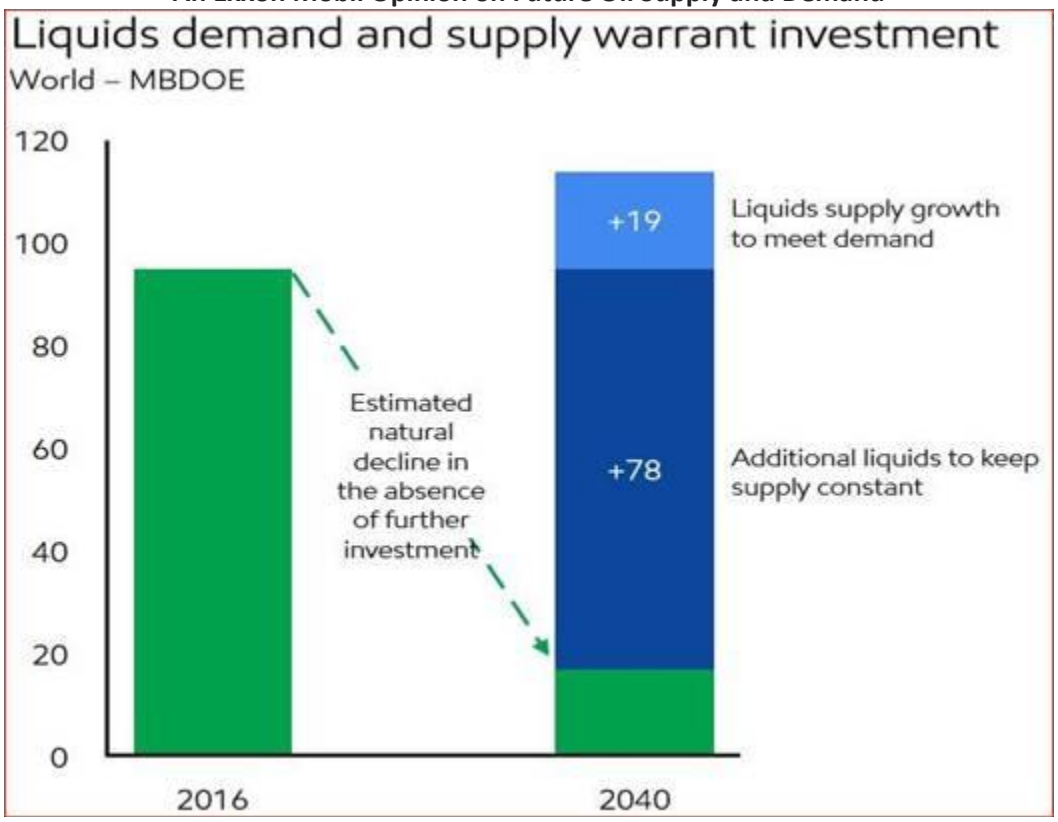
We do. We know several "Big" things. Here's the first. (Keep an eye on the items in red.)

Source	2010	2018 Est	Change
Conventional oil production	44.8 mm b/d	43.5 mm b/d	-1.4 mm b/d
US shale oil	0.9 mm b/d	5.8 mm b/d	+4.9 mm b/d
US shale NGL	0.3 mm b/d	2.7 mm b/d	+2.4 mm b/d
Canadian oil sands	1.5 mm b/d	3.0 mm b/d	+1.5 mm b/d
Bio Fuels	1.8 mm b/d	2.6 mm b/d	+0.8 mm b/d
Refining Gains	2.1 mm b/d	2.3 mm b/d	+0.2 mm b/d
OPEC NGL	5.4 mm b/d	6.9 mm b/d	+1.5 mm b/d
Total Non-OPEC Liquids Production	56.8 mm b/d	66.8 mm b/d	+10.0 mm b/d
Global Demand	87.8 mm b/d	99.8 mm b/d	+12.0 mm b/d
OPEC Crude Production	30.2 mm b/d	32.2 mm b/d	+2.0 mm b/d

Over the past 8 years, "non-OPEC" oil and oil-liquids production grew by 10 million barrels per day. 75% of that growth came from U.S. shale, whose "miracle" hadn't quite appeared yet, in 2010. But global demand grew 12 million barrels. The lesson from the table is very simple, and hardly anyone would disagree with it: "Without the "shale miracle," non-OPEC supplies of oil fell far short of what the world needed to meet growing demand." OPEC would have had to achieve historical records in oil production—major historical records—to keep up with world demand. OPEC and its boss, Saudi Arabia, make lots of statements about how much oil they can produce . . . but their tallest claims don't come close to the $38 million barrels which would have been needed, without the U.S. shale miracle. The skyrocketing oil prices which peaked in 2014 at $107/barrel, if they had stayed in place or even kept rocketing up, would not have called forth that extra production, because it's not within OPEC's grasp.

So our first "big thing" is simply that global demand has grown fairly strongly and steadily, and only U.S. shale oil has been able to keep up—almost. Here is the next "big thing" we know:

An Exxon Mobil Opinion on Future Oil Supply and Demand



All oil fields—everywhere and every kind, from deep-sea to shale—simply plunge in production after Year One . . . unless a great deal of money and effort are spent on them to keep production up; or unless a great deal of money and effort are spent on new discoveries to replace exhausted fields. Exxon Mobil's picture, up there, is actually somewhat terrifying. It's especially terrifying when we consider the next "Big Thing" we know:

The global oil industry's spending on exploration and production fell 50% (roughly 400 billion dollars) from the 2010-2015 period to the 2015-2020 period. Hundreds of exploration projects cancelled after 2014's oil-price plunge are still cancelled.

As Outlook has remarked more than once, that slamming of the spending brakes had to happen. When the sales price of what a company makes falls 75%, massive behavior changes must happen in a hurry, or the company won't be back to fight another day. But the chart above tells us something about "the facts of life" in the oil business, whether a company is back for another day or not: "Oil spending stopped. There will be consequences, period."

Glance at the table with the red items, again. Will U.S. shale save the day again? Another gain of 7.3 million daily barrels would certainly help, over the next 8-year period. But if global demand matches the 12 million daily barrels of the last 8 years, it won't be enough—it will be emphatically short of "enough." Will the extra supply come from a non-OPEC oil industry which slammed its spending brakes for 4 years? (Sound of crickets chirping.) Will the extra supply come from Saudi Arabia, delivering on its occasional assertion that it has a nearly-infinite pool of oil down there, under the sand? (Sound of wind blowing across a barren desert.) In Outlook's opinion, not likely. Saudi oil fields are cursed with the same plunging production arrow as everyone else's oil fields—and most of the rest of OPEC is already showing itself unable to keep production from falling, much less staying flat or rising.

The market which has been acting so nervous about Conoco, and about the direction of oil, will not stop focusing on where oil supply and demand might be next month, or next year for the far-sighted, infinitely patient members of the market crowd. But these oil facts of life will eventually make the market see the long-term problem: more oil demand than possible supply. Oil prices will stay on their roller-coaster, but the ride is heading up over the next 5 – 10 years, not down.

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