Flash by EIC

SCB Economic Intelligence Center

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EIC believes the increase in crude production from OPEC to be insufficient to match demand in the second half of the year.

Event

- **Oil producers at the 4th OPEC and Non-OPEC Ministerial meeting reached a deal to raise crude supply.** On June 22nd, 2018, at a joint meeting in Vienna, Austria, oil producers have reached an agreement to raise crude supply by cutting compliance rate from 152% in May 2018 down to 100% by 1 July 2018. This will help maintain balance between global demand and supply of crude, and hence ensure stability of crude price. This agreement is expected to add around 1 million barrels of crude supply per day, or roughly 1% of the global supply.

Analysis

- **EIC believes that Brent will remain elevated within a range of 70-75 USD per barrel in 2H2018, as the additional supply is likely insufficient to substitute for expected shortfall from Iran and Venezuela.** The United States' sanction against Iran is expected to cut global crude supply by between 200 thousand to 1 million barrels per day. In addition, Venezuela, the producer with largest crude reserve, is facing an economic crisis that forces it to scale back production from 2 million barrels per day in January 2017 to 1.4 in April 2018. The International Energy Agency (IEA) has predicted that the country would produce no more than 800 thousand barrels per day by the second half of 2018. Although this OPEC meeting has led to expectations that around 1 million barrels of crude per day will be added to the global supply to make up for the deficit, but in practice the existing limits on each country's quota may cap additional output to only 600-800 barrels per day. For example, producers with excess capacity such as Saudi Arabia, United Arab Emirates, and Kuwait are already producing at close to their quotas. Hence, the actual increase in supply may be lower than expected.

- **EIC expects global demand for crude oil to increase steadily in 2H2018,** particularly during 4Q2018, which is the high season of oil consumption. Our prediction is in line with OPEC's projection that strong global economic growth will add 1.63 million barrels of extra demand per day. Strong demand for crude is confirmed by the level of oil inventory in the Organization of Economic Cooperation and Development (OECDcountries, which account for roughly 50% of the global oil consumption. In March 2018, the group's inventory has fallen to 2,812 million barrels, the lowest level in 3 years which is also below 5-year historical average. This demand for crude will support a higher price in the coming periods.

- **Moreover, the agreement to raise production is in line with Saudi Arabia's policy to stabilize crude price.** Saudi Arabia aims to maintain the price of oil within 70-80 USD per barrel. This range is deemed conducive to promoting economic stability, as part of the reform plan to reduce reliance on oil and transform the country into a Middle Eastern trade hub. At the same time, the target range is set not too low, as Saudi Arabia is planning for a Saudi Aramco IPO in 2019, and is eager to assure investors that it is capable of managing the balance of supply and demand and thus limit volatility of crude price.

Implication

- **If crude price remains high, big players in the oil-related industries as well as Thai exporters will stand to benefit.** Oil-related industries, particularly upstream ones such as oil exploration and production companies, will enjoy higher profits from the improvement in oil price. At the same time, biofuels such as B20 will see a higher demand as more consumers make a switch following government incentives. Petrochemical companies will earn more revenues as their products' prices increase by more than their costs. As for exports, the higher crude price will support further expansion of export value via the price effect. Thus, EIC expects the value of Thai exports to expand by 8.5% in 2018. Recently in May 2018, exports of oil related goods such as finished oil, and chemicals and plastics recorded 30.7% and 29.5% YOY growth, respectively. However, the high price of oil will negatively impact businesses whose production costs consist largely of the cost of oil, such as airlines, transportation, and logistics companies. Due to their cost structure, these businesses will face higher production costs. Similarly, car owners will have to spend more on gasoline, as the retail oil price remains elevated. However, fuel subsidy from the state oil fund will help cushion part of the impact on businesses and households. In addition ,the value of fuel imports in May 2018 rose more than 25%YOY ,in line with the rise in oil price.

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