KAMCO Oil Market Monthly Report

Cloud over global economic growth weighs on oil demand and prices

IEA expects a demand surge during second half of 2019

KUWAIT: In one of the longest running declining streaks in recent months, OPEC crude oil prices plunged 12.3 percent while Brent crude declined 15 percent during the first six trading sessions of August-19 led by intensifying trade dispute.

Recent data releases from various economic agencies across the globe has hinted to an imminent global economic slowdown. This has affected prospects of oil market rebalancing this year as was expected earlier and has forced forecasters to further lower oil demand outlook. On the other hand, the geopolitical issues in the Gulf region that supplies around a quarter of global crude oil has had minimal impact on oil prices as economic concerns weigh on prices.

On one hand, there is the unresolved trade conflict that continues to cast a shadow over world economic growth. The data points have led to investor concerns and a great deal of volatility in financial and commodity markets. On similar lines, India's auto sector recorded an 18.7 percent decline in sale of passenger vehicles, the steepest monthly in 18 years. In Europe, Germany is reportedly on the brink of a recession with its GDP declining during Q2-19, albeit marginally by 0.1 percent. And with Eurozone quarterly growth at 0.2 percent, the ECB is said to be preparing a stimulus package in September-19.

In terms of oil demand, the IEA further lowered its outlook for the year as it reported slowest demand growth since 2008 during the first five months of the year. According to the agency's latest monthly report, demand declined for the second time this year in May-19, and the aggregate demand growth during the first five months stood at 520 tb/d, due to weak demand from India and the US. While stating that demand outlook stays fragile, the IEA lowered full year 2019 demand growth forecast by 100 tb/d to 1.1 mb/d and by 50 tb/d for 2020 to 1.3 mb/d. Nevertheless, the IEA expects a demand surge during 2H-19 that would significantly help in tightening the market. In a similar move, the OPEC also lowered its 2019 non-OPEC demand growth forecast by 40 tb/d citing economic woes but said that supplies would be lesser than previous forecasts. Meanwhile, OPEC continued to lower production during July-19 pumping at just below the 30 mb/d mark.

Oil prices

After seeing marginal m-o-m price improvement in July-19, oil prices plunged during the August-19 with Brent crude reaching as low as 55.03 per barrel as of 7-August-19 when in declined by 6.1 percent in a single day. Prices went below the $60/b mark for the first time since the end of January-19, with average prices for the first half of the month declining by more than 8 percent m-o-m. A bearish view from the IEA as well as to some extent from the OPEC in their respective monthly reports also supported the oil price decline. Concerns continue to weigh on the demand side of the oil market while supply continued to remain above the 100 mb/d mark during July-19 as per IEA report, which also said that it could further lower demand outlook numbers if the trade war continues. Meanwhile, the oil inventory build in the US during the last two weeks further added to pressure on oil prices. After declining for seven consecutive weeks, US crude stocks have gained over the last two weeks by a total 4.0 million barrels to reach 440.51 million barrels. The inventory data came in line with rig count data released by Baker Hughes.

According to the latest weekly US rig count report, active oil rigs increased by 6 last week to reach 770 rigs. Nevertheless, despite lesser number of rigs as compared to last year, US oil production has continued to ramp up due to improving productivity in most of the oil basins this year. Average crude prices witnessed slight improvement during July-19 as declines during mid-month was offset by gains during the first half and last week of the month. Average OPEC crude prices gained 2.8 percent m-o-m to reach $64.7/b while Kuwait crude averaged at $64.9/b recording a slightly higher m-o-m gain of 3.7 percent. On the other hand, Brent crude declined by -0.2 percent to average at $63.9/b during July-19.

World oil demand

World oil demand growth expectations for 2019 were lowered by 0.04 mb/d to a growth of 1.1 mb/d as demand is now expected to average at 99.92 mb/d, according to OPEC's latest monthly report. The revision reflected lower-than-expected oil demand growth estimates for the OECD region during Q1-19 with data being revised downward by 0.05 mb/d for the quarter due to lower demand during March-19 in OECD Americas. Demand growth numbers for the non-OECD region was also revised downward by around 0.13 mb/d for Q2-19 reflecting lower-than-expected demand data for the Other Asia and the Middle East regions. The revision in Other Asia was led by slower construction and economic growth that led to lower demand from India, Hong Kong, Taiwan and Singapore while the Middle East region witnessed the impact of fuel substitution and subsidy reduction policies.

The latest monthly data for the US as of May-19 showed a decline in oil demand by 0.5 percent y-o-y as diesel fuel and fuel oil demand faltered due to high historical base and fuel substitution with natural gas while gasoline demand declined due to lower miles travelled and weak auto sales. Nevertheless, preliminary demand data for June-19 and July-19 showed positive demand trend led by rising diesel, jet kerosene and LPG/NGL requirements while gasoline demand continue to remain weak partly offsetting the growth.

In OECD Europe, demand data for 1H-19 showed marginal decline in the European Big 4 countries led by weak demand from the road transportation sector as seen from the 3 percent decline in auto sales during 1H-19. and jet fuel in the transportation sector, although auto sales witnessed a 12th consecutive month of decline during June-19. Oil demand growth projections for 2020 remained unchanged at 1.14 mb/d with total demand expected to average at 101.05 mb/d. Nevertheless, with the ongoing economic pressure, the OPEC report said that next year's growth projections are subject to downside risks.

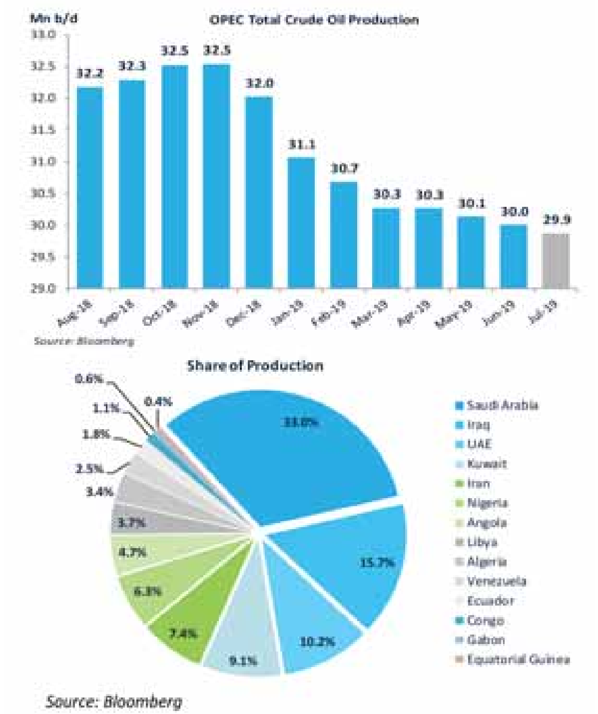
Growth next year is expected to come primarily from non-OECD countries, primarily China and Other Asia, while in the OECD region, OECD Americas are expected to show demand growth while OECD Europe and Asia Pacific regions are forecasted to show demand decline.

World oil supply

According to OPEC, world oil supply continued to increase during July-19 adding 0.23 mb/d as compared to the previous month to average at 98.71 mb/d. The increase was once again primarily on the back of non-OPEC supply that increased by 0.48 mb/d to average at 69.11 mb/d mainly coming from Canada, Norway, The UK, Australia, India, Brazil and Azerbaijan. Higher non-OPEC production pushed down OPEC market share by 30 bps to 30.0 percent during July-19. For the full year 2019, non-OPEC oil supply growth forecast was once again lowered by 72 tb/d to a growth of 1.97 mb/d with total supply expected to average at 64.39 mb/d. The downward revisions reflected lower-than-expected oil production in the US (-35 tb/d), Brazil (-59 tb/d), Thailand (-28 tb/d) and Norway (-16 tb/d) during 1H-19 that was partially offset by higher expected output from Canada (+56 tb/d) for the full year reflecting higher output in Q2-19 after the government of Alberta eased mandatory production adjustments.

OPEC oil production & spare capacity

OPEC crude production once again declined during July-19 reflecting continued efforts from OPEC countries to support prices. This was the eighth consecutive month of decline for the group which saw average monthly production declining by 2.7 mb/d. Production averaged at 29.87 mb/d with a decline of 130 tb/d according to Bloomberg data, while OPEC secondary sources showed average production rate of 29.61 mb/d with a m-o-m decline of 246 tb/d. Based on OPEC's production figures, the compliance to the OPEC+ agreement was around 144 percent during July-19. According to OPEC data, Saudi Arabia undertook a deep production cut of 134 tb/d and produced at 9.7 mb/d while Iran, Libya and Venezuela collectively lowered production by 121 tb/d during the month. Recently, an attack on Saudi Arabia's Shaybah field in the southeast led to a temporary spike in oil prices, but production remained unaffected in the facility. Meanwhile, the sanction-led decline in oil production in Iran and



Venezuela reflected during July-19 output. Iran produced at an average rate of 2.2 mb/d as compared to 2.3 mb/d during the previous month while Venezuela produced at 760 tb/d according to Bloomberg. A Reuters report citing tanker data showed that oil exports from Iran have dropped to as low as 100 tb/d during July-19. Oil production in Nigeria remained flat at around 1.9 mb/d, while the other swing producer, Libya, showed a decline of around 50 tb/d during July-19 after Libya's NOC declared force majeure on crude loadings at the Zawiya port due to a disruption at its Sharara oil field.

Oil production in Kuwait remained stable at around 2.7 mb/d, however, the country is reportedly in talks with Saudi Arabia to start production from the Neutral Zone which has a production capacity of around 0.5 mb/d. Similar talks are reportedly initiated between Kuwait and Iraq after the two signed a contract last month to conduct a technical study for joint frontier oilfields. Nevertheless, the oil minister of Kuwait said that the country is fully committed to the OPEC+ cuts with its share of compliance reaching as high as 160 percent during July-19. He added that the concerns regarding global economic slowdown are exaggerated and that oil demand would pick up during 2H-19 and would help reduce the glut of oil inventories gradually.

Japan Inc backs Abe's tough trade stance vs S Korea

TOKYO: Japanese companies broadly support Prime Minister Shinzo Abe's tough trade stance against South Korea, a Reuters poll found. Three-quarters of companies in the monthly Reuters Corporate Survey approved of Abe's explanations for curbing exports to South Korea of materials used to make computer chips. More than nine in 10 predicted Japan would win if Seoul takes its complaints to the World Trade Organization (WTO).

The acrimonious trade dispute between the Japan and South Korea, two US allies, grew out of a row over wartime forced labor. Abe last month tightened curbs on exports to South Korea of three high-tech materials needed to make memory chips and display panels. The government this month cancelled South Korea's fast-track trade status.

Removing South Korea from a "white-list" of favored export destinations means some Japanese exporters face more paperwork and on-site inspections before they can win permits, which could slow Korea-bound exports for a wide range of goods. In the survey, companies were split on whether the trade curbs will affect the Japanese economy. Some companies said they won't be affected as they don't directly engage in business with South Korea.

Those seeing an impact from the export curbs expressed concerns including the global slowdown and spreading trade frictions, worsening Japan-South Korea ties, weaker corporate profits and long-term competitiveness of their firms. "As we stand on the brink of a recession amid trade frictions, it's undesirable to take such steps that could accelerate the downtrend," a manager at a wholesale firm wrote in a survey response.

Others disagreed. "It's obvious that the Moon (Jae-in) administration is putting its utmost priority on reconciliation with North Korea at a time when North Korea proceeds with nuclear development," wrote a manager at an electric machinery maker. "It's only natural to deprive South Korea of most-favored-nation status."

In opinion polls last month, the liberal Asahi newspaper found 56 percent of the public felt Abe's trade moves were "reasonable", while the conservative Yomiuri found 71 percent supported the measures.

Seoul sees the export curbs as retaliation over a dispute about wartime forced labor, while Tokyo cited unspecified security reasons. Asked how they evaluate Japanese government's explanation for its export curbs against South Korea, about three-quarters of companies in the Reuters poll said it has been explained fully or to a degree. The survey, conducted July 31-Aug. 14 for Reuters by Nikkei Research, canvassed 504 midsize and large Japanese manufacturers and non-manufacturers. Managers respond to the survey on condition of anonymity to voice their opinions more freely.

Forced labor dispute

A fresh dispute over wartime forced labor was triggered last year when a South Korean court ordered Japanese firms to compensate some of their former laborers. The dispute brought bilateral ties to their lowest point in decades. Japan argues the issue was settled by a 1965 treaty normalizing bilateral ties. South Korean President Moon said on Friday that Seoul would be open to dialogue with Tokyo as needed, in a carefully choreographed message at his address marking Korea's independence from Japan's 1910-45 colonial rule. If South Korea brings its complaints against Japan's export curbs to the WTO, an overwhelming 94 percent of companies in the Reuters poll said Japan would win.

"Japan's argument stands to reason. No other country including the United States is siding with South Korea," one manager wrote. "Still, Japan needs to lobby hard to win the backing of other countries," the manager said, given that South Korea in April won the bulk of its appeal in a dispute at the WTO over import bans and testing requirements it imposed on Japanese seafood. — Reuters

TOKYO: A crane unloads a container from a cargo ship at the international cargo terminal at the port in Tokyo on Monday. — AFP

Argentina's new economy chief: Peso stability is top priority

BUENOS AIRES: Argentina will stand by the 2019 fiscal targets it has agreed with the International Monetary Fund and work to stabilize its currency, which lost 18% of its value last week, new Treasury Minister Hernan Lacunza said yesterday.

Minutes after being sworn in by President Mauricio Macri, Lacunza told reporters the government will stick with the goal of erasing its primary fiscal deficit this year, despite a series of spending measures announced last week aimed at spurring growth in the recession- and inflation-racked economy.

BUENOS AIRES: Argentina's Central Bank president Guido Sandleris leaves after offering a press conference at the Central Bank headquarters in Buenos Aires yesterday. — AFP

He said his top priority will be to stabilize the peso, which tumbled after Macri, who has run a business-friendly government, was drubbed in an Aug. 11 primary election by Alberto Fernandez. The center-left Peronist candidate is now expected to defeat Macri in an Oct. 27 general election. The peso opened 1 percent weaker on Tuesday at 55.55 per US dollar. Argentina's economy is expected to shrink 1.5 percent this year, according to the latest central bank poll of analysts. The analysts expect growth for 2020 to be 2.0 percent. "This is a complicated time for Argentina," said Lacunza, formerly the chief of economy for Buenos Aires province.

"We want to leave a solid economic platform for whichever candidate wins" the presidential election, he said, adding that Argentina had a primary fiscal surplus in July and that he expected a surplus in August as well. Macri, struggling to revive his campaign for a second term, is betting that the new treasury chief can help stabilize the economy. Last week, Macri announced a cut in taxes on food and personal income along with increased welfare spending, raising concern his administration will miss its fiscal targets. "We are closely following recent developments in Argentina and are in ongoing dialogue with the authorities as they work on their policy plans to address the difficult situation that the country is facing," the IMF said in a statement. "An IMF staff team will travel to Buenos Aires soon," said the statement, which was signed by IMF spokesman Gerry Rice. The IMF's next review of Argentina's economy on Sept. 15 should provide a sign of whether the lender of last resort still thinks the country can pay its debt obligations. Government bonds denominated in dollars are harder to pay when the peso weakens.

A crunch point will come in the second quarter of 2020, when Argentina is scheduled to make $20 billion in debt repayments, up sharply from $5.6 billion in the first quarter of next year. Nicolas Dujovne, the former treasury minister, quit on Saturday, saying he believed the country needed "significant renewal" of its economic team. Central bank chief Guido Sandleris also told reporters yesterday that the bank would continue to sell reserves in an effort to halt the peso's slide. — Reuters

Inverted what? Searches for obscure financial term spike on Google

NEW YORK: Searches on Google for "inverted yield curve" have spiked after the unusual bond market phenomenon presented itself last week for the first time in over 12 years and helped tank Wall Street amid chatter that an economic downturn was imminent. Following a tweet from US President Donald Trump referencing the "CRAZY INVERTED YIELD CURVE!", the term made its way onto news websites and radio and television reports that rarely delve into financial topics. Even late-night TV star Stephen Colbert devoted a portion of his show trying to decipher what it means when the yield on 10-year US Treasury notes falls below those for 2-year notes.

As it happens, that abnormal bond market dynamic often precedes US recessions, and when it appeared last Wednesday for the first time since 2007, it rattled investors worried that a US-China trade war might kill both a record-long economic expansion and a decade-long bull market for stocks. US web searches for "inverted yield curve" are on track in August for their highest month on record, and more than double the next highest month December 2005, according to Google's Google Trends analysis tool. December 2005 was the last time 2-year and 10-year Treasury notes entered an inversion trend, one that would continue through 2007 and be followed by the global financial crisis and the harshest recession since the Great Depression.

Bond yields are a main measure of the return the securities deliver to investors, and they are also a proxy for interest rates. When the yields on bonds of different maturities are plotted on a graph, it produces a curve that typically has an upward slope because investors expect greater compensation for the risk of owning longer-maturity debt. An inversion, when shorter-dated yields are higher than longer-dated ones, implies that investors see greater risks in the near future.

Google Trends provides data on the frequency of searches during a time period relative to other time periods. It does not provide actual numbers of web searches. After Google searches for "inverted yield curve" spiked in 2005, searches for the term entered a lull for over a decade until December 2018. That is when yields on 5-year notes dropped below yields on 2-year notes, setting off talk of a potential recession and questions about whether the more closely watched 10-year yield would invert, as it eventually did last week. The US yield curve has been slowly flattening since 2013 or earlier, and while economists and central bank policy makers have hotly debated its significance, the trend has mostly gone unnoticed by the public. The spread between US 2-year and 10-year note yields has slipped below zero before each of the last five US recessions, although it has taken anywhere from 12 to 24 months for the recession to occur. — Reuters