Surge in oil demand could lead to crude shortage

Fuelled by three years of rock-bottom prices, the demand for oil in the industrialized countries is roaring back, leading some analysts to warn that the world will soon shift from a crude surplus to a shortfall.

The industry has seen three consecutive years of declining capital investment, and may find it difficult to boost production quickly enough to keep up with rising consumption, Ben Luckock, co-head of market risk at oil trader Trafigura Group, told a conference in Singapore on Tuesday.

"We are nearing the end of 'lower for longer' oil," he said, referring to the term used to described the extended period of depressed crude prices. Geneva-based Trafigura is one of the world's largest oil trading firms.

In a presentation, which was provided to The Globe and Mail, Trafigura's Mr. Luckock predicted a significant shortage of oil productive capacity in 2019 due to industry budget cuts and rebounding demand, a gap that could reach five million barrels per day.

Mr. Luckock joins analysts from Citigroup Inc. and London-based Energy Aspects Ltd. in forecasting a more rapidly tightening crude market due to stronger-than-anticipated demand. With buoyant growth in consumption expected to persist, the real question becomes the degree to which supplies keep pace, Energy Aspects analyst Amrita Sen wrote recently.

"Investors remain transfixed by an as-yet unrealized energy revolution, and they are not paying attention to the supply side's ability to meet today's demand for oil," she said.

However, Citigroup said in a recent report that there is still plenty of capacity for increased production from the Organization of Petroleum Exporting Countries and the United States and that should temper any concern about supply shortfalls.

Crude prices have risen sharply higher in recent weeks. North America's benchmark, West Texas intermediate, fell slightly Tuesday to $51.88 (U.S.) a barrel, 20 per cent higher than its summer lows, while International Brent prices have been even stronger, closing Tuesday at $58.44 a barrel, nearly 30 per cent above its summer low.

Canadian producers have not benefited as much from the global rebound, thanks to the rising loonie. An increase in the Canadian dollar means producers receive a lower price in their home currency than they would otherwise see.

Still, the Toronto Stock Exchange energy sub-index, comprised of major producers and their service providers, has climbed nearly 16 per cent since early July.

Investors have bid up shares as crude oil prices climbed, though many remain skeptical that a short-term rally will evolve into a lasting recovery after several false starts earlier this year, said Jeremy McCrea, analyst at Raymond James Ltd. in Calgary.

"We've seen this a few times, and guys are trying to determine if this is just another head fake or if this is the real thing," he said on Tuesday. Institutional clients that pared their energy exposure through the downturn are wondering if it's "finally time to get back in the market here.

"Even if we aren't quite at the bottom, the valuations are starting to look appealing, especially relative to other things in their portfolio in other sectors."

The low oil prices that have prevailed since the 2014 slump are having a big impact on the global vehicle market, increasing the popularity of larger sports utility vehicles.

In the United States., the sale of SUVs and light trucks jumped from 7.9 million in 2013 to 10.3 million last year, 58 per cent of the market. Chinese SUV sales, meanwhile, have jumped from 11 per cent to 42 per cent of the market in just five years, while India has seen a 38-per-cent growth in oil consumption in five years with tremendous potential for an increase in vehicle sales there.

The International Energy Agency recently upgraded its forecast for crude demand growth this year after seeing a 2.4-per-cent increase in the second quarter compared to the same period in 2016. The Paris-based agency is now expecting crude demand to grow by 1.6 million barrels per day (b/d) this year, up from a 1.3 million b/d increase last year.

Oil demand, including biofuels, is expected to hit 100 million b/d by the end of 2018, up from 95 million in early 2016, it says.

It is the developed world – especially the United States and Europe – that is leading the charge, IEA analyst Christophe Barret said in an interview Tuesday.

Crude demand in industrialized world peaked in 2005 and fell steadily until 2014, when it began to rebound in response to lower prices. The IEA forecasts the growth consumption will moderate as crude prices rebound. "All the support we got from the very sharp fall in prices after 2014 will not be reproduced so I think we should expect some kind of slowdown in growth in the next few years," Mr. Barret said.

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