# AozoraStep Capital LLP

UK Listed Equity Turnarounds

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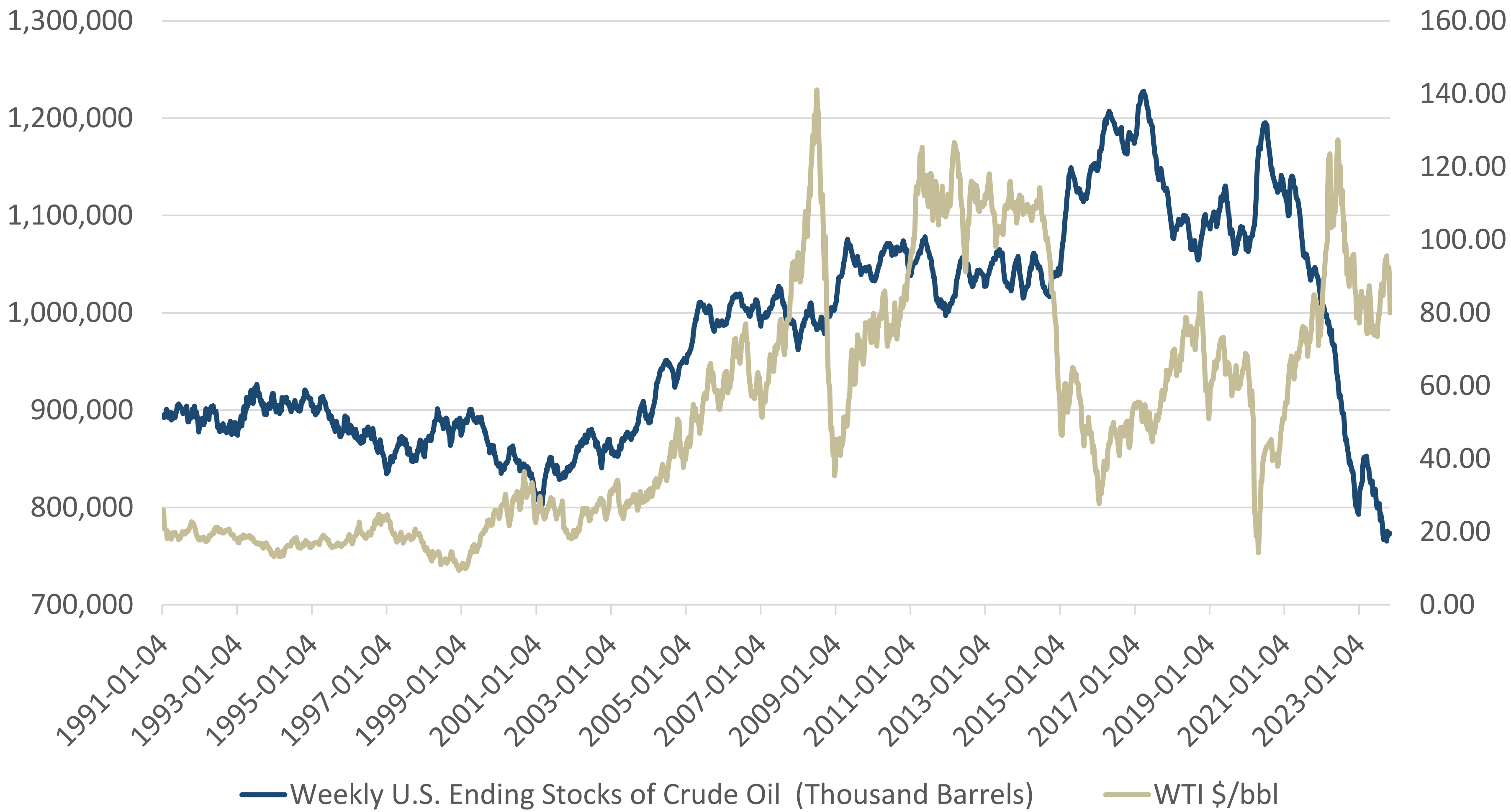
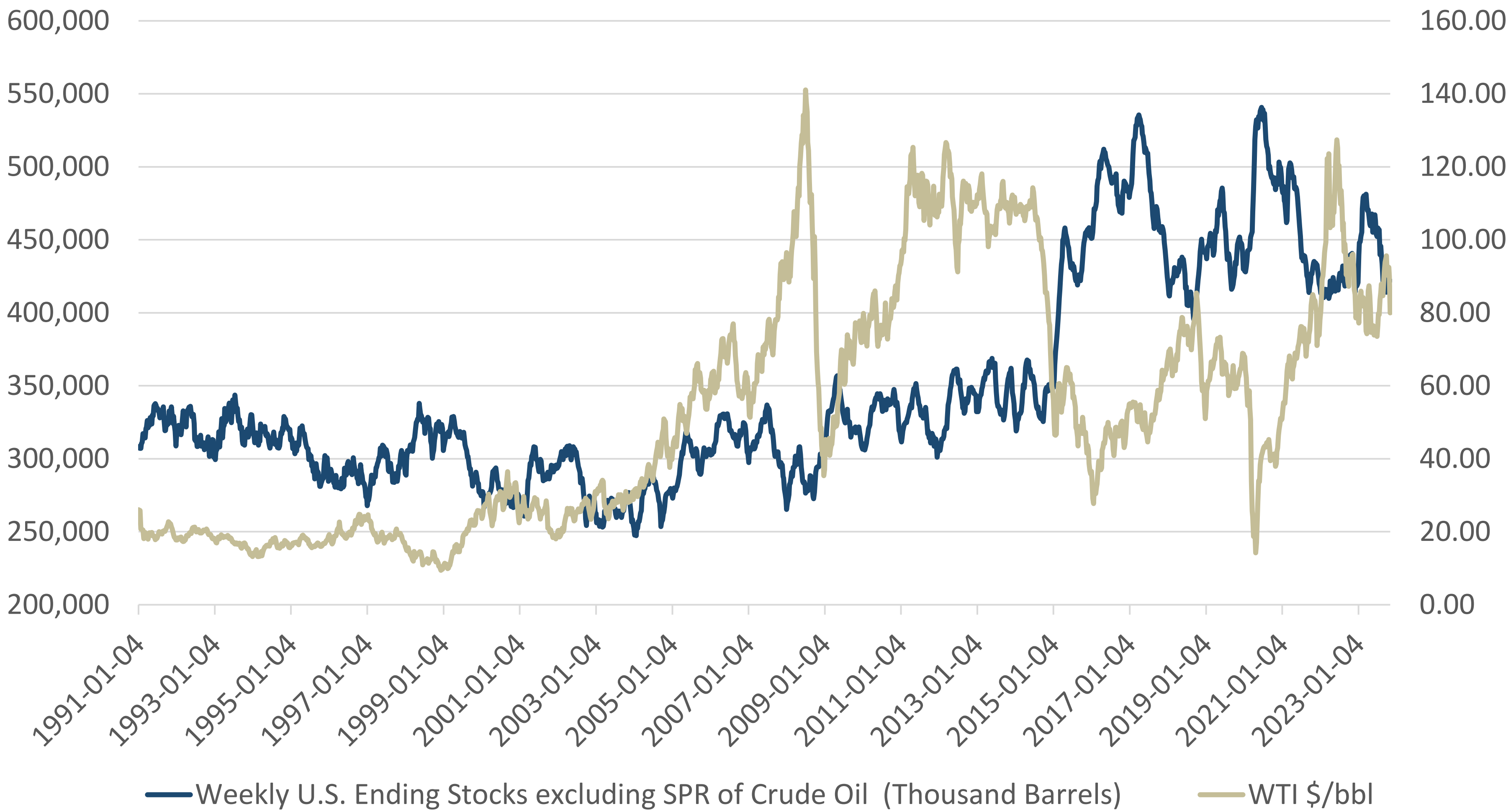
# What is the outlook for oil prices based on multiple supply variables?

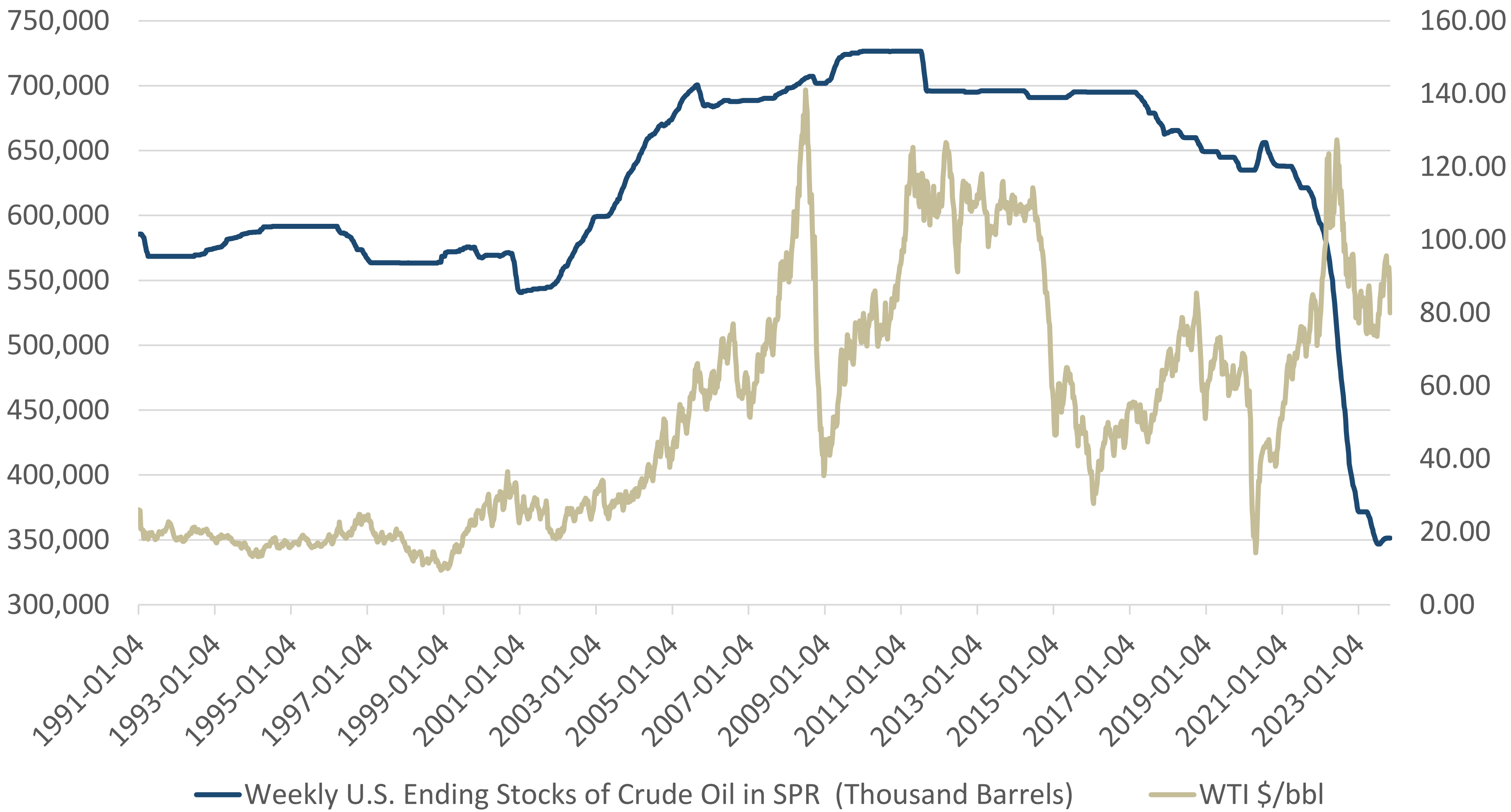
# There is a mostly negative correlation between crude oil prices and US inventories



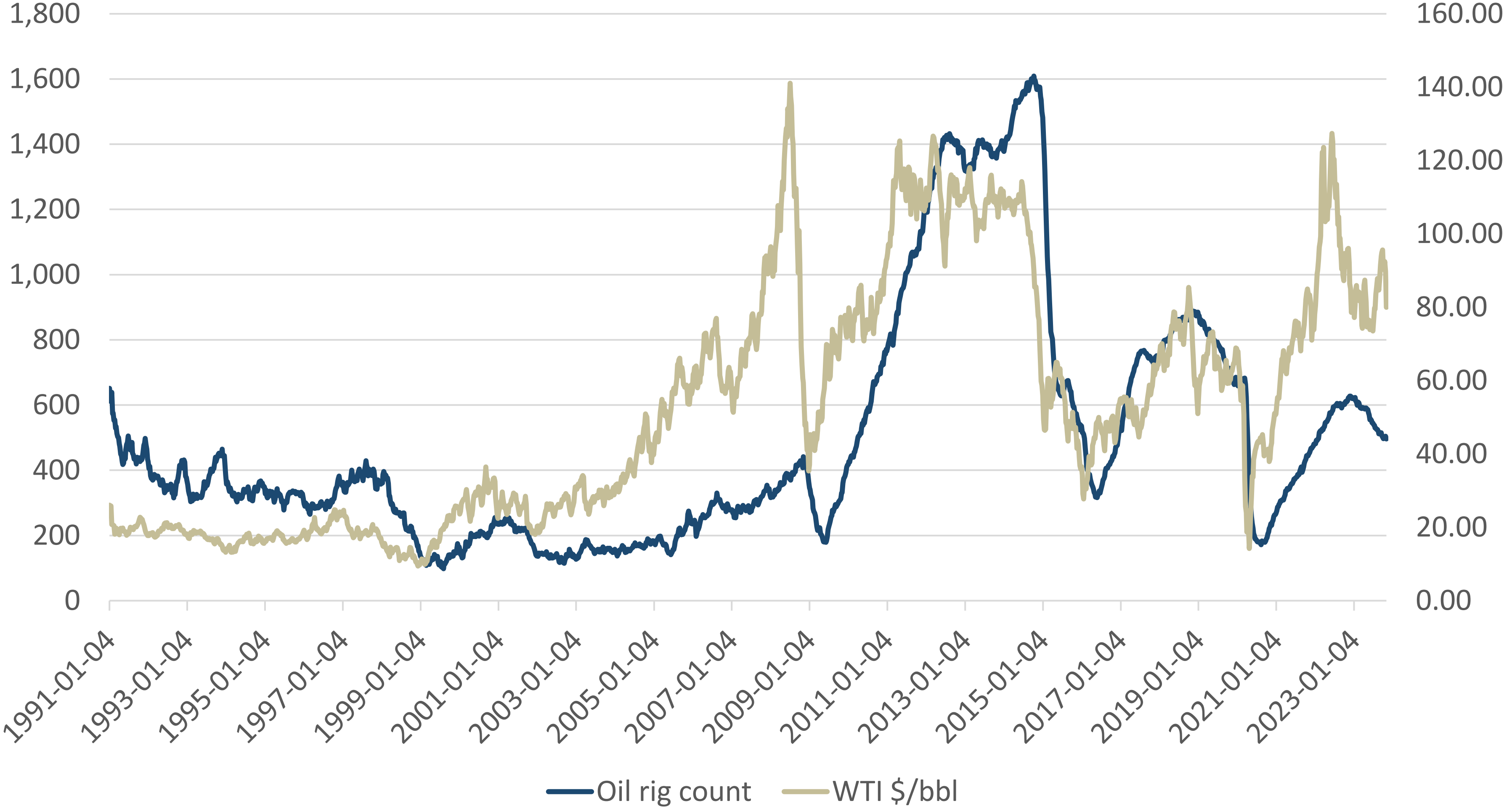
# Commercial inventories generally climb when oil prices decline, and not the other way round



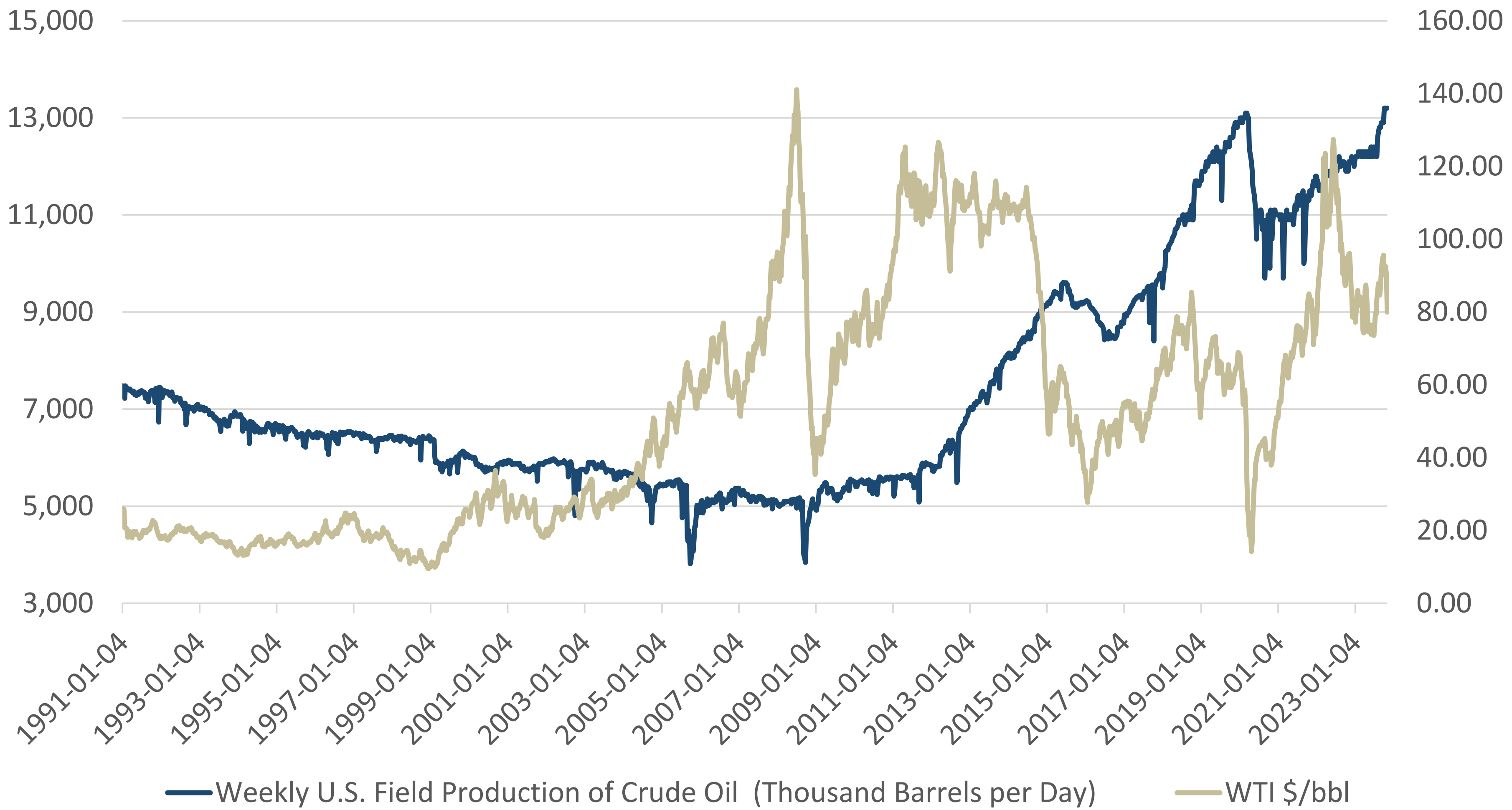
# The filling of the SPR has led to oil price rises in the early 2000s, limited recent oil climb 1st time



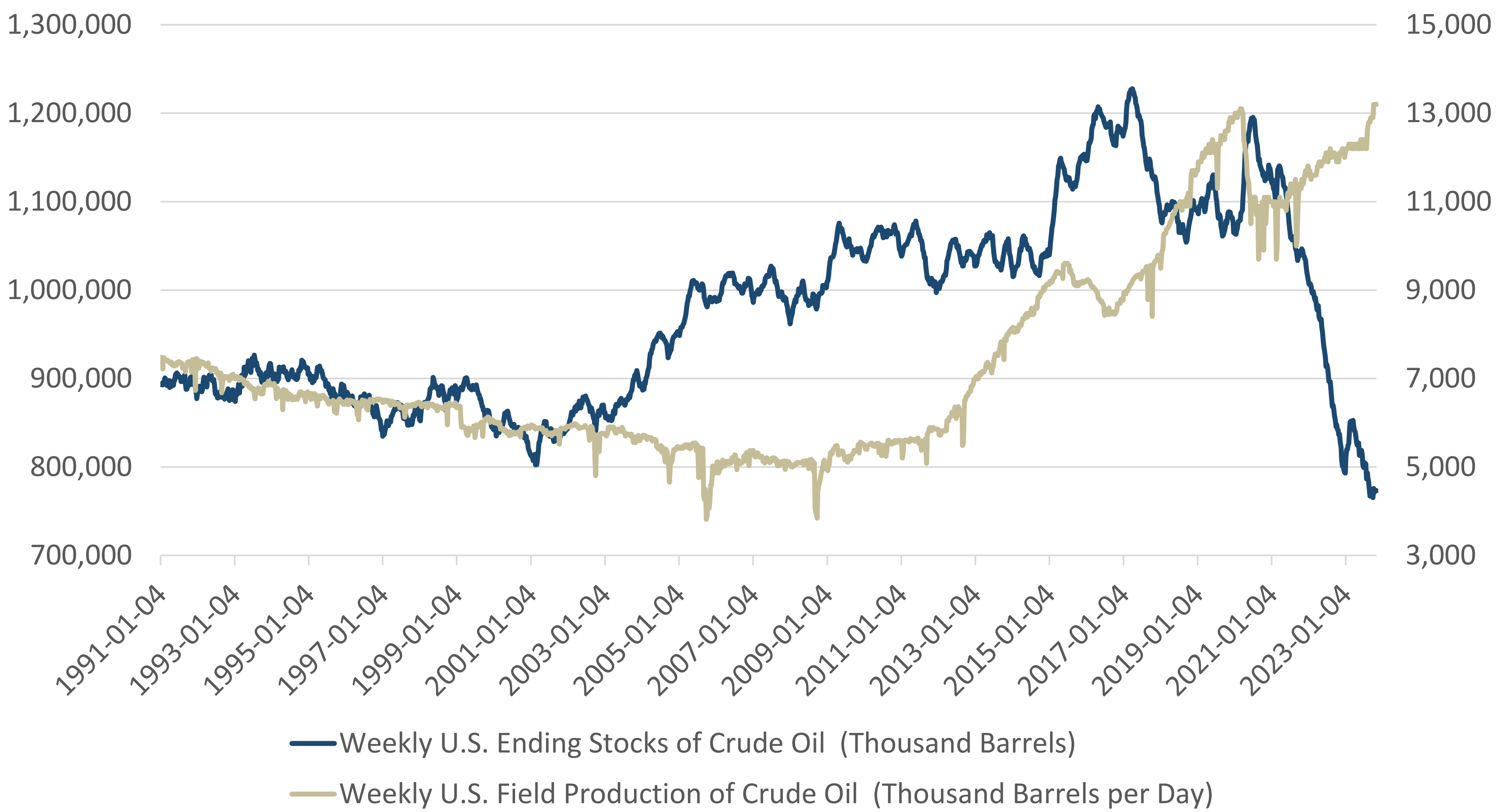
# Similar to inventories, rig count follow oil prices, not the other way round



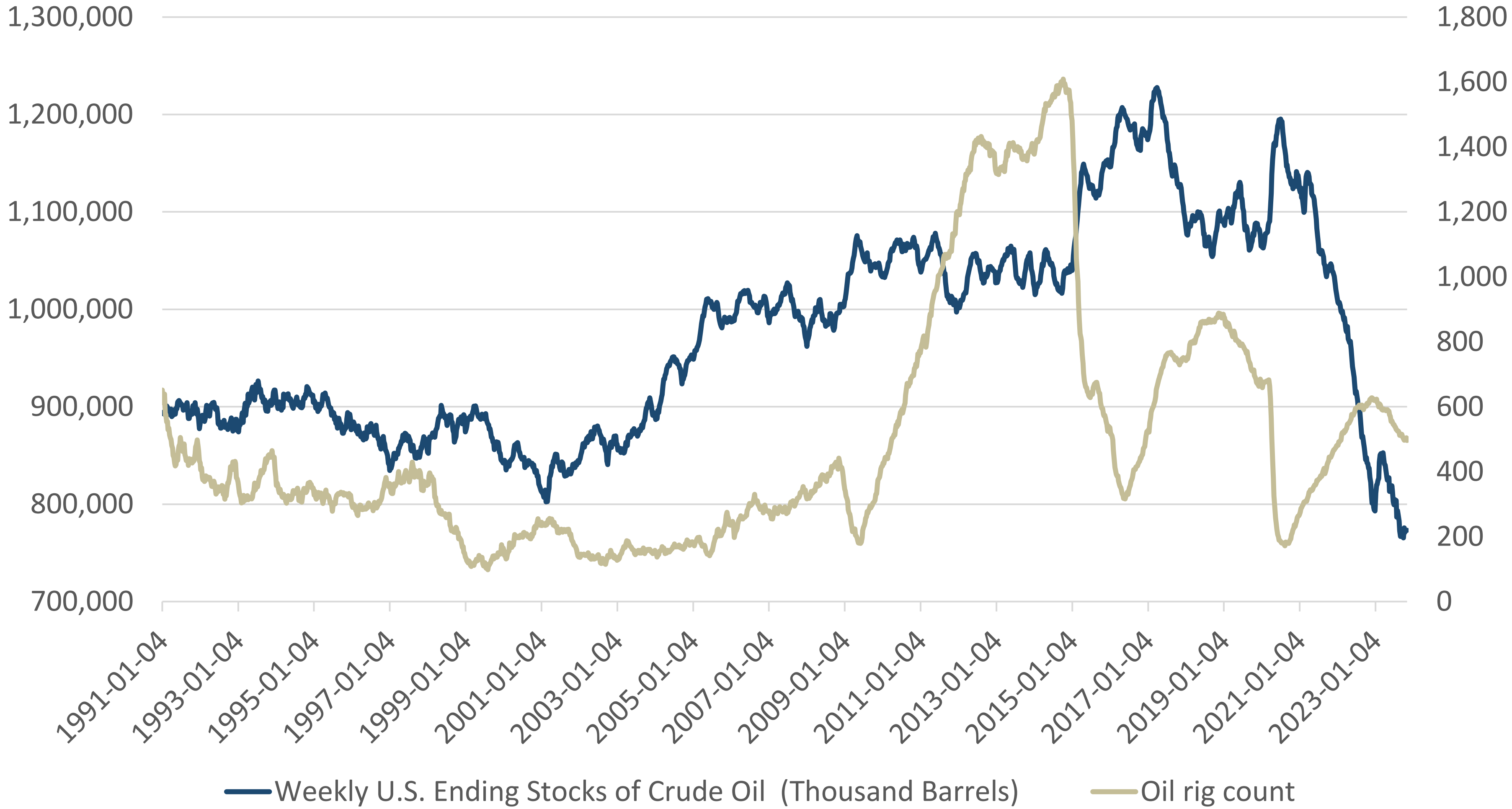
# There is a delayed positive correlation between US oil production and oil prices



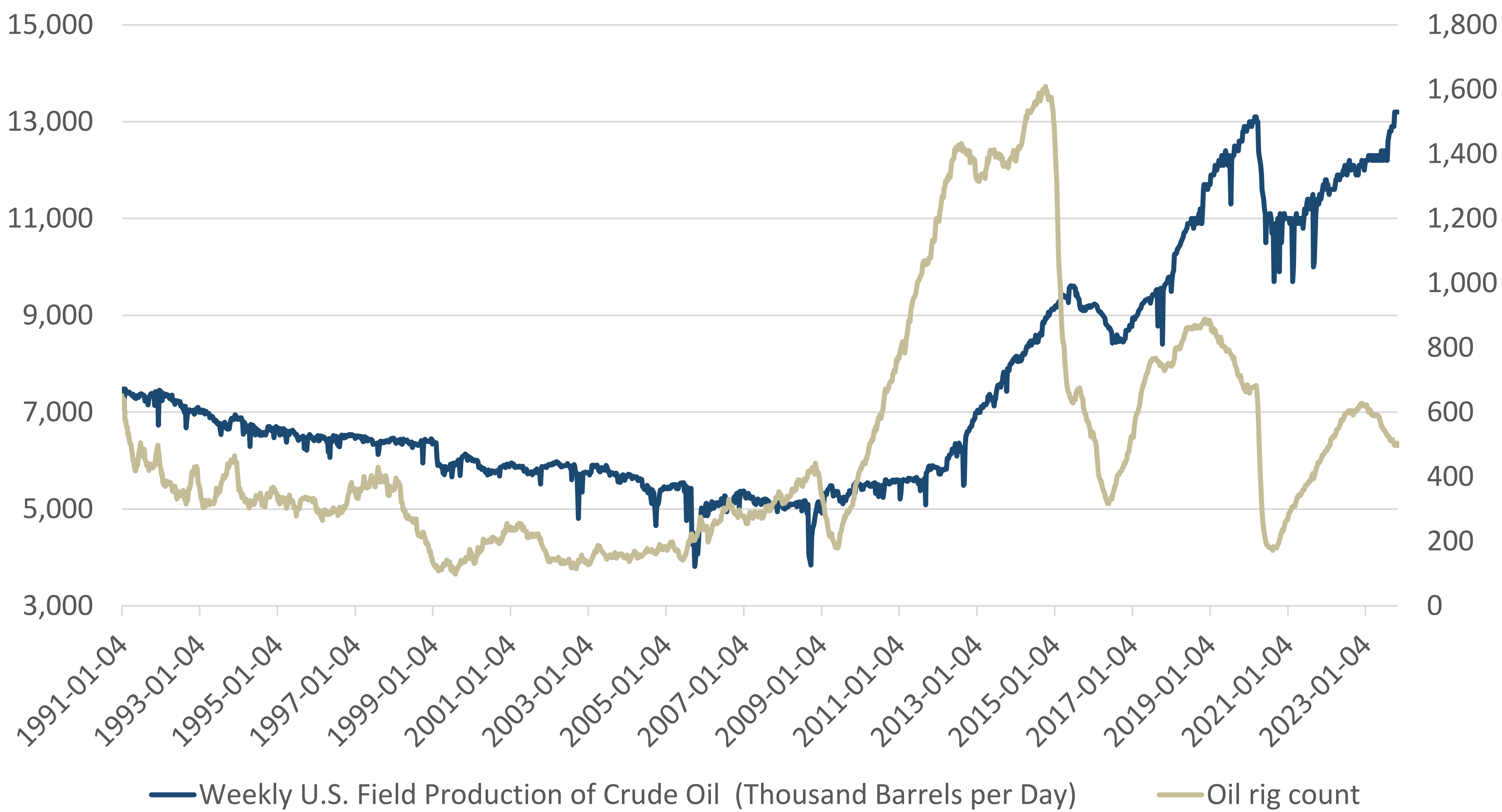
# Big inventory rises generally lead to oil production lower



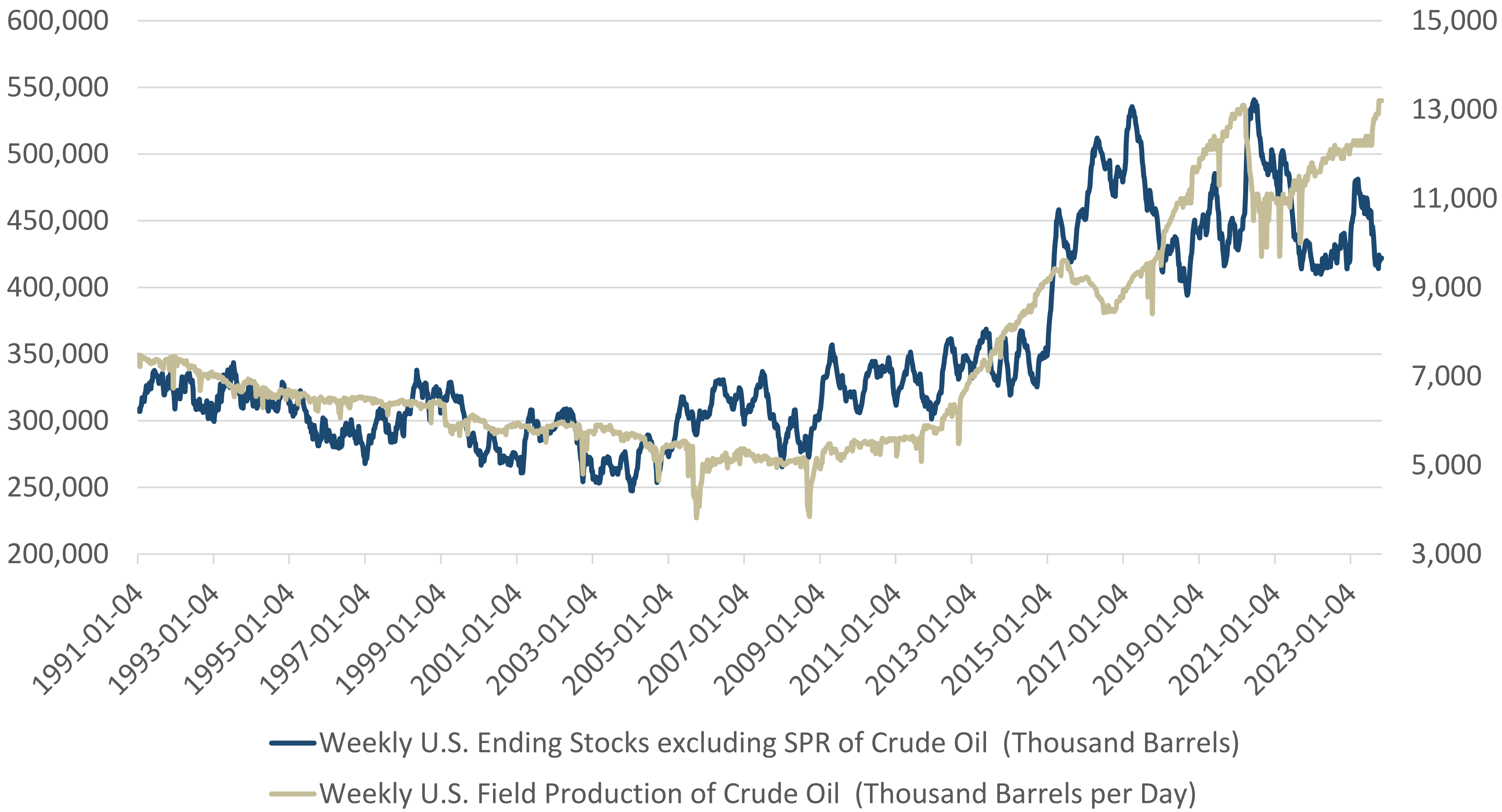
# Sharp declines in rig counts generally lead to instant inventory build ups



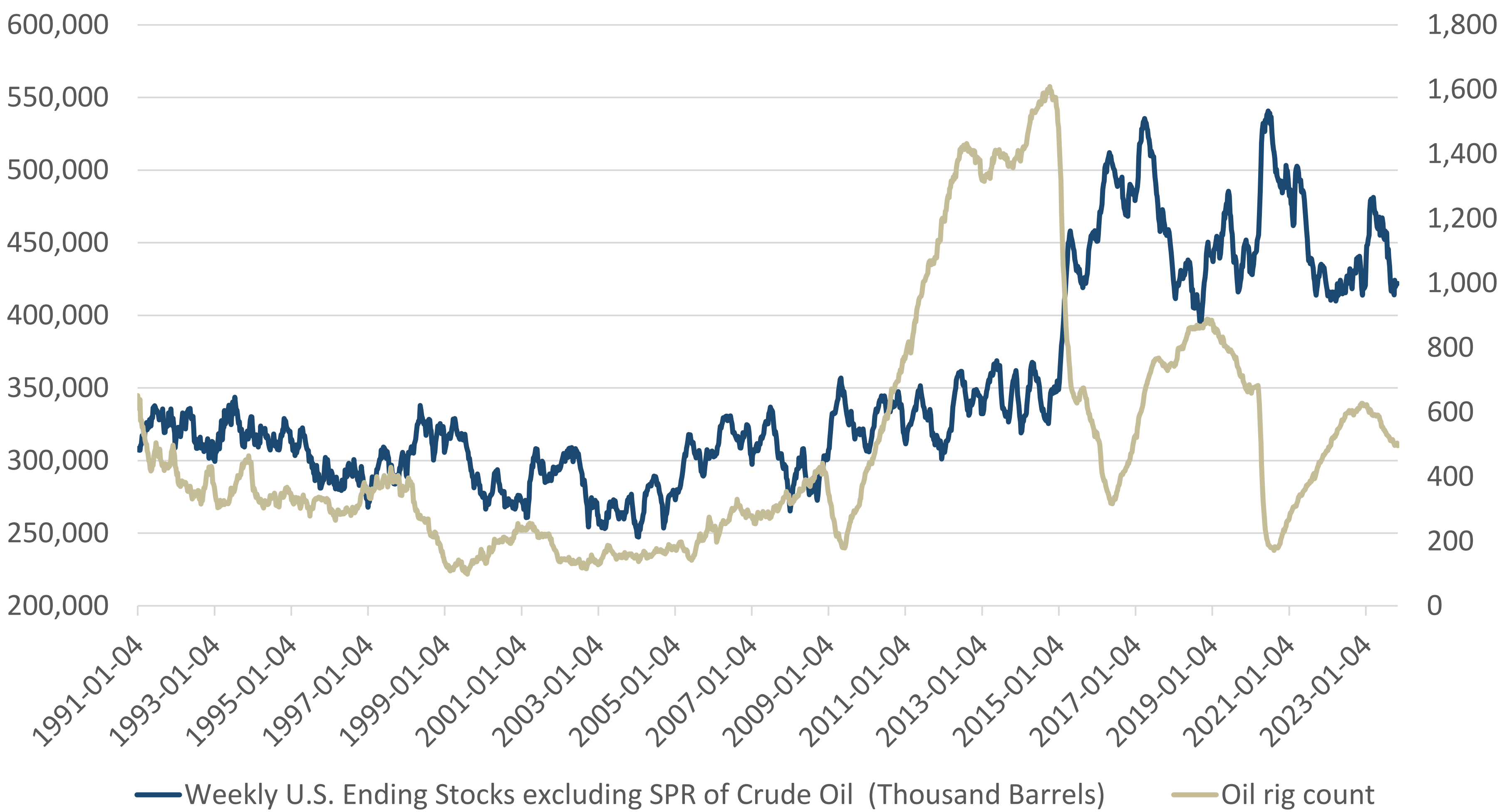
# Due to longer horizontal drilling, only a sharp decline in rig count leads to lower oil production



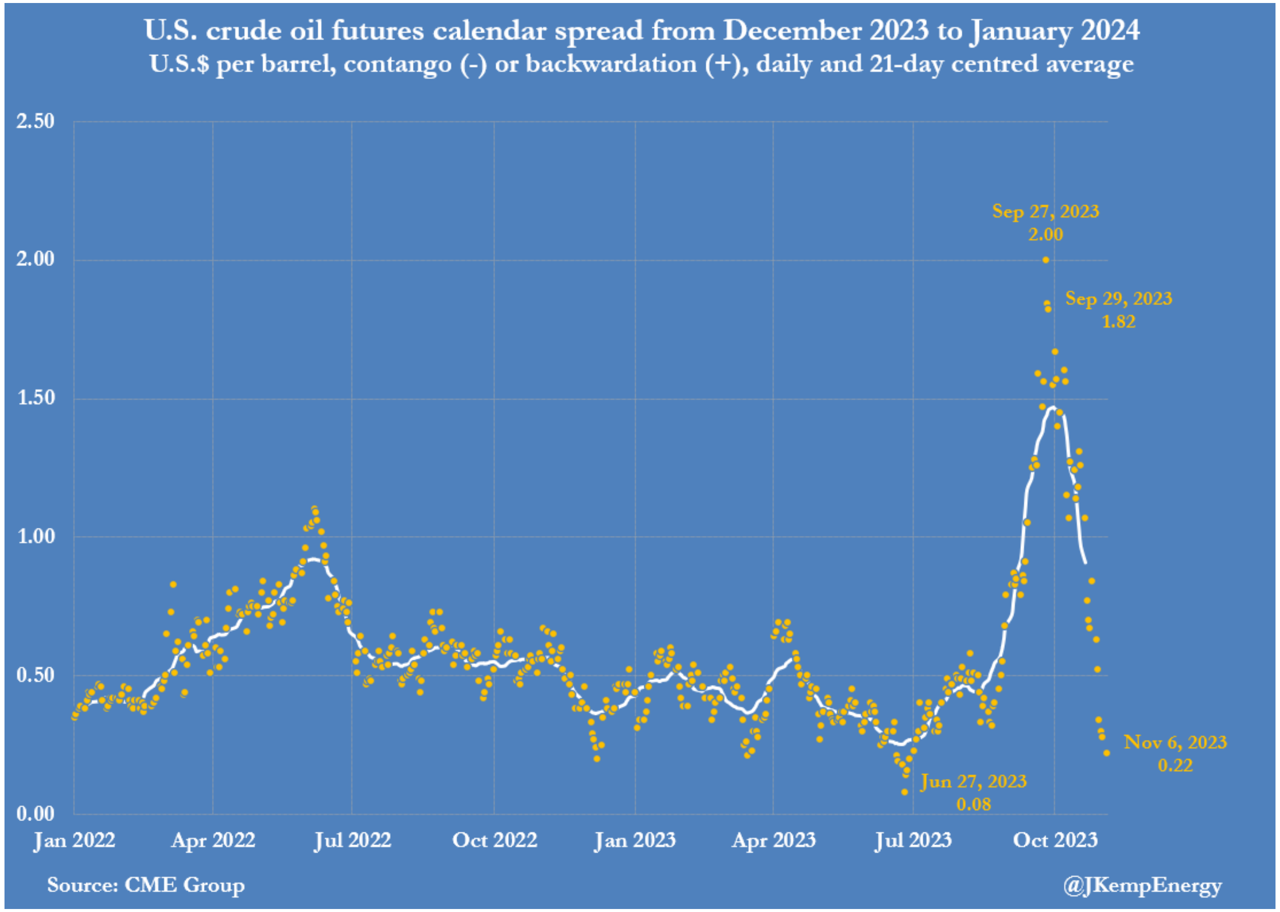
# Only when commercial oil inventories climb rapidly, production gets adjusted lower



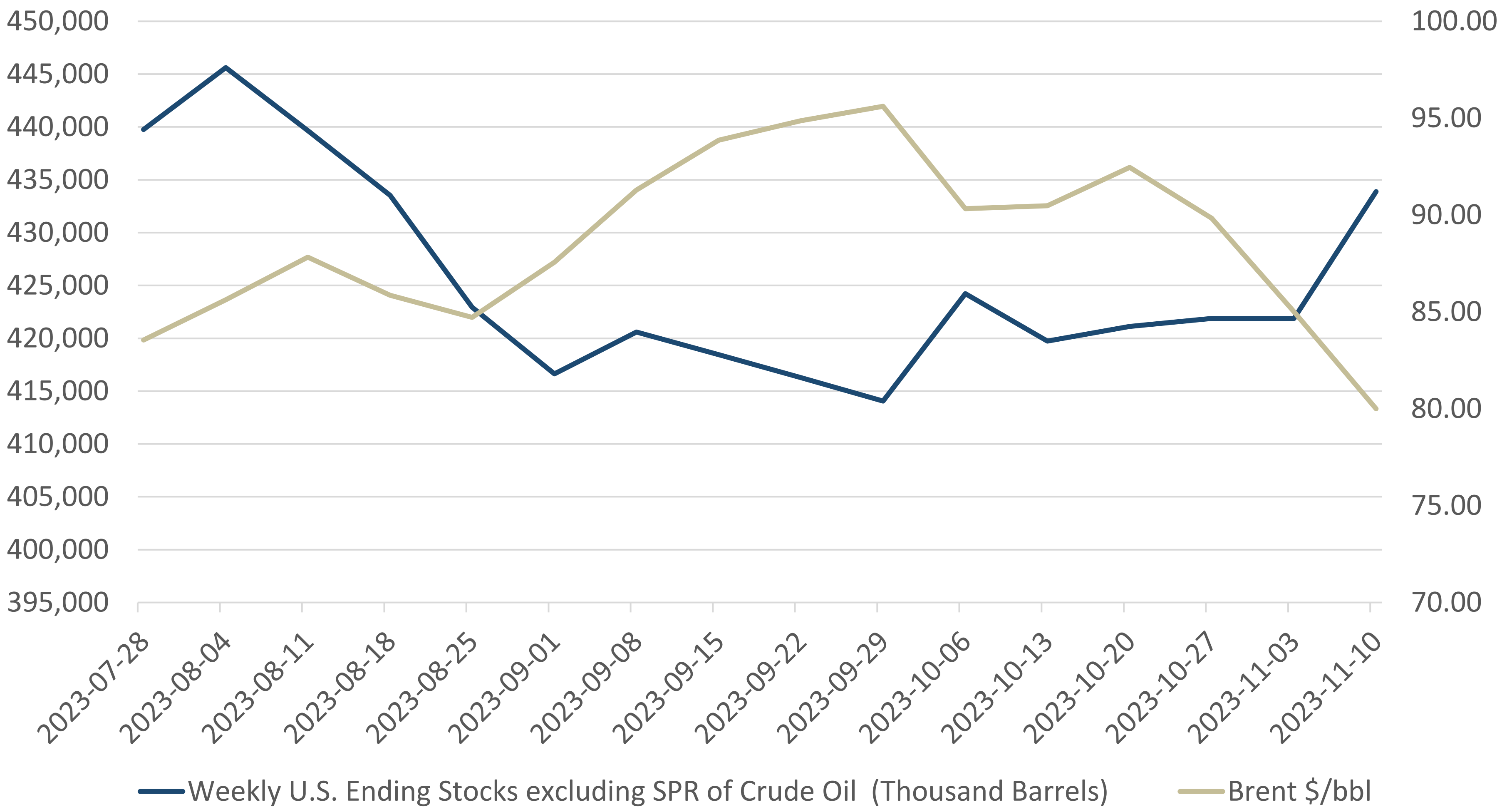
# Abrupt commercial oil inventories rises causes rig counts to decline equally fast



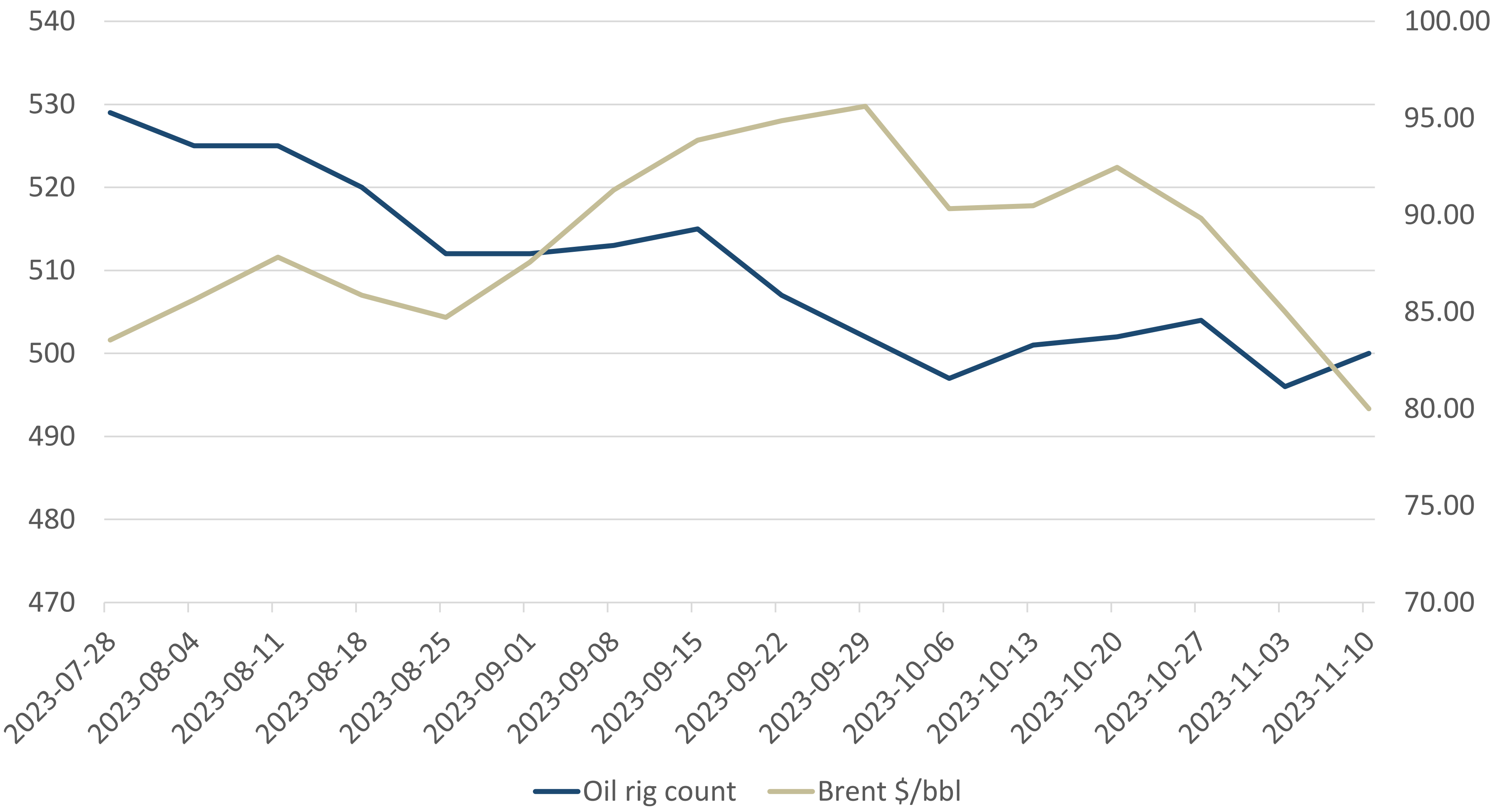
# Oil calendar spreads reach cycle lows and are currently at 20 cents for Dec 23-Jan 24



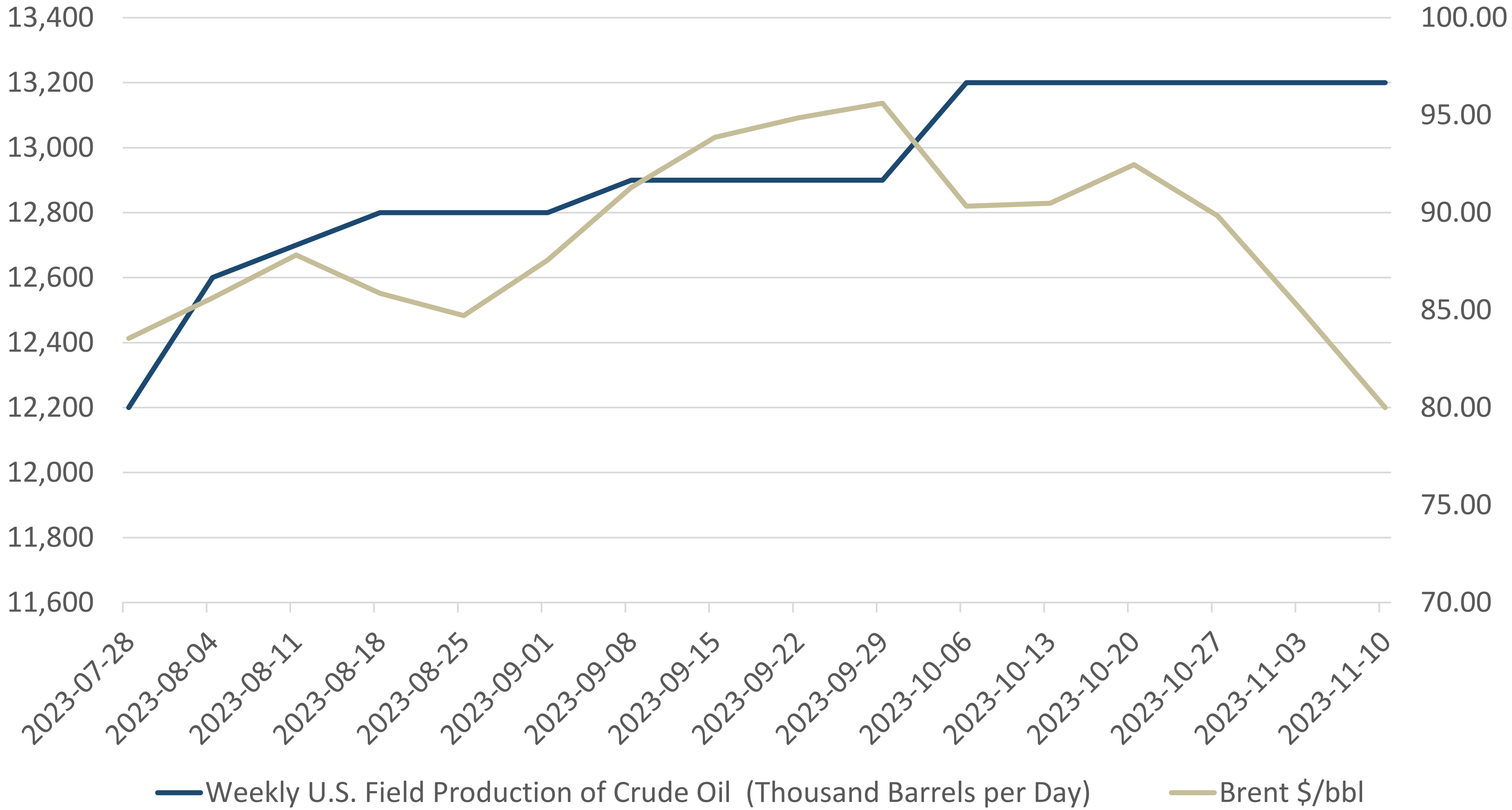
# Since September US commercial oil inventories have stabilised and climbed



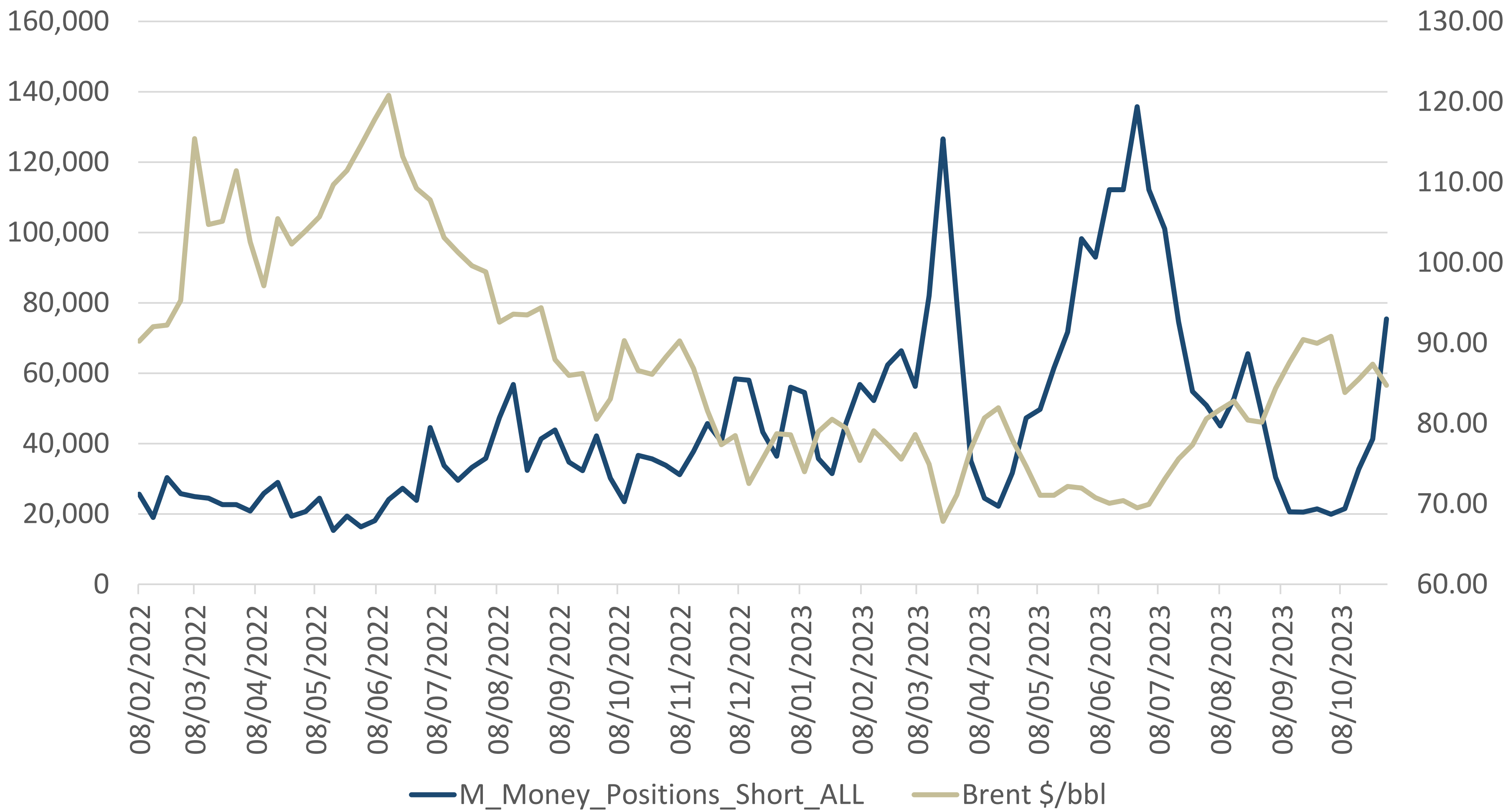
# The rig count continued its decline, although some stabilisation is seen



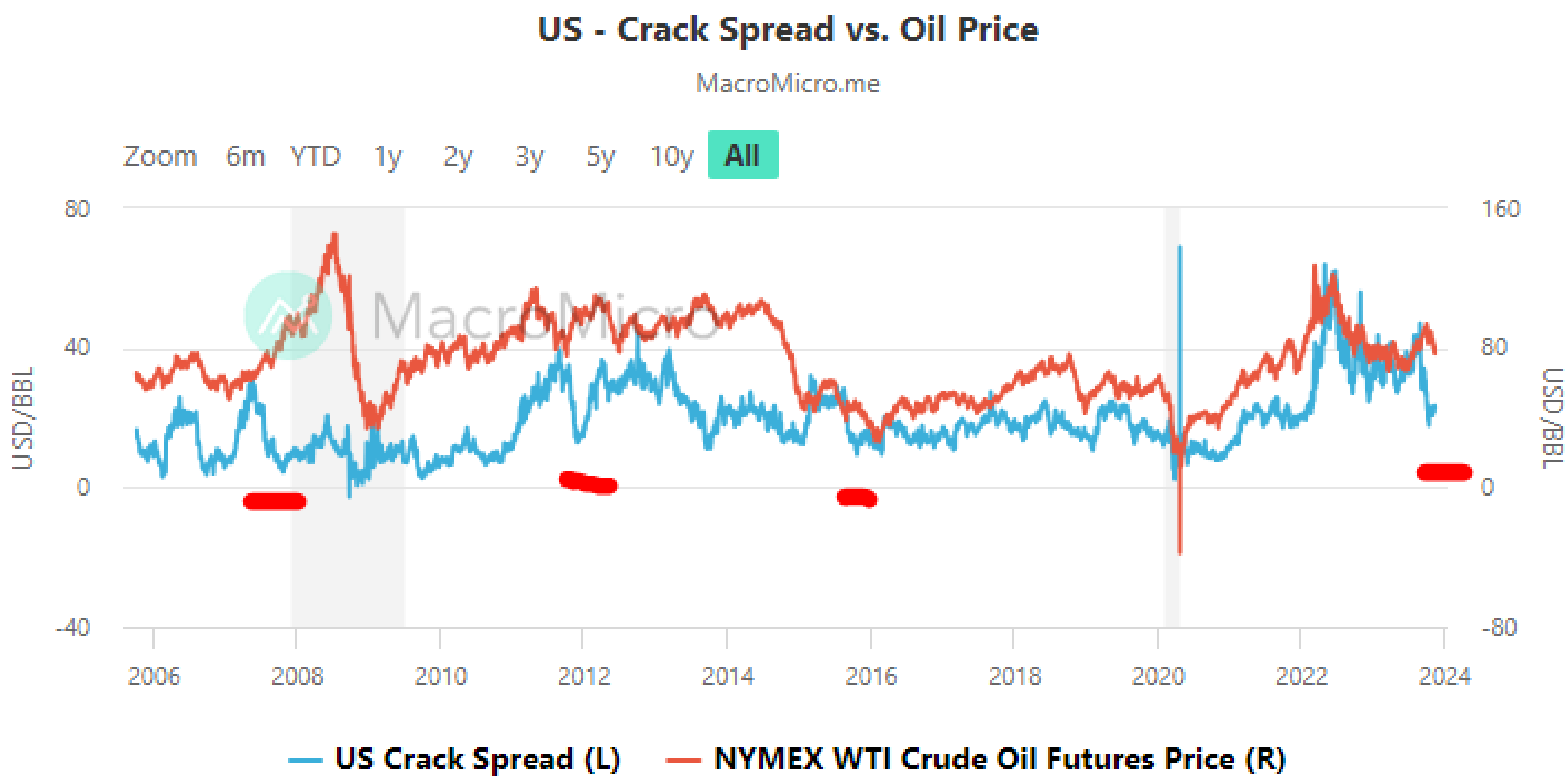
# US field oil production increased by 1mio bopd since end July



# A rise in NYMEX physical short oil positions generally led to oil price decline - temporarily



# Abrupt declines in the crack spread generally led to higher crude oil prices in the past



# How about the non-US oil producers?

- Iran currently produces just above 3mio bopd compared to 2.5mio bopd at the beginning of the year → Iran added the equivalent of the Kurdistan-Turkey pipeline, which is offline, to their production
- Saudi Arabia's oil production peaked at 11mio bopd in Q3 2022 and is now at 9mio bopd (including 1mio bopd voluntary cut)
- Russia's oil production was 10.5mio bopd before Covid, 10mio bopd before the Urkaine invasion, and is now at 9.5mio bopd
- Venezuela used to produce 2.5mio bopd, which declined to 500k-1mio bopd after the Trump sanctions. Currently, Venezuela produces around 750k bopd and is expected to rise to 1mio bopd next year
- Guyana produces 400k bopd and is expected to produce 600k bopd next year
- Nigeria is producing around 1.4mio bopd compared to 1.8mio bopd pre-pandemic

→ If Saudi Arabia and Russia maintain their voluntary production cuts, there would be around 1mio bopd growth from other participants in 2024 (bar US)

→ During the early 1980s Saudi Arabia has cut their production from 10mio bopd to nearly 2mio bopd, which still led to a decline in oil prices, yet a slow one



Production data from Trading Economics

# Historic declines when two subsequent weeks lost more than 10% in oil's value and WTI was above $60/bbl

| Observation Date | WTI $/bbl | Weekly change | Sell off |
|---|---|---|---|
| 2008-09-18 | 96.62 | -7.0% | Y |
| 2008-10-09 | 89.54 | -9.7% | Y |
| 2008-10-16 | 76.30 | -14.8% | Y |
| 2008-10-23 | 70.27 | -7.9% | Y |
| 2008-10-30 | 64.26 | -8.6% | Y |
| 2010-05-20 | 69.85 | -7.7% | Y |
| 2011-05-12 | 99.40 | -8.9% | Y |
| 2011-08-11 | 83.20 | -10.2% | Y |
| 2014-12-04 | 67.19 | -10.4% | Y |
| 2021-12-02 | 67.02 | -13.4% | Y |
| 2022-04-07 | 99.41 | -7.3% | Y |
| 2022-06-23 | 108.01 | -9.0% | Y |
| 2022-11-24 | 79.64 | -7.2% | Y |
| 2023-11-09 | 75.92 | -7.8% | Y |

# Conclusions

- Inventories, rig count, and production are generally lagging oil prices. Hence, they are not a great indicator in predicting oil prices
- However, low SPR inventories point towards higher oil prices due to the US filling up their SPR when oil <$79/bbl (as the early 2000s show, this can lead to higher oil prices)
- The decline in rig count and increasing US production show that there are risks for oil prices to decline, if history is a guide
- Calendar spreads indicate that we might have reached a price bottom at this moment
- Rapidly rising NYMEX physical oil short positions generally leads to oil price declines, but very high short positions are often a good oil bottom price indicator
- Recent commercial oil inventory rises might be temporary, as there are a record number of crude oil tankers heading to the US to export more oil (1)
- Crack spreads decline indicates higher oil prices, while OPEC+'s spare capacity leaves room to the downside
- Pricing dynamics suggest this is the beginning of a wider oil selloff



(1) https://www.bloomberg.com/news/articles/2023-11-06/a-record-number-of-supertankers-is-headed-to-collect-us-oil

# Appendix: Impact of Panama Canal drought on LNG markets

- Panama Canal drought could have big market impact
- Slots are reduced from 36 per day to 25 per day from 3 Nov, and gradually to 18 per day from 1 Feb (1)
- Oil tankers are minor participants, but up to 67% of Panama Canal users are LNG tankers (as of 2019)
- This could lead to more gas being diverted away from Asia to Europe, while Europe gas inventories are already at record highs of nearly 100%



(1) https://reuters.com/business/panama-canal-says-will-slash-booking-slots-due-drought-2023-10-31/#:~:text=Booking%20slots%20will%20be%20cut,18%20slots%20from%20Feb.%201.