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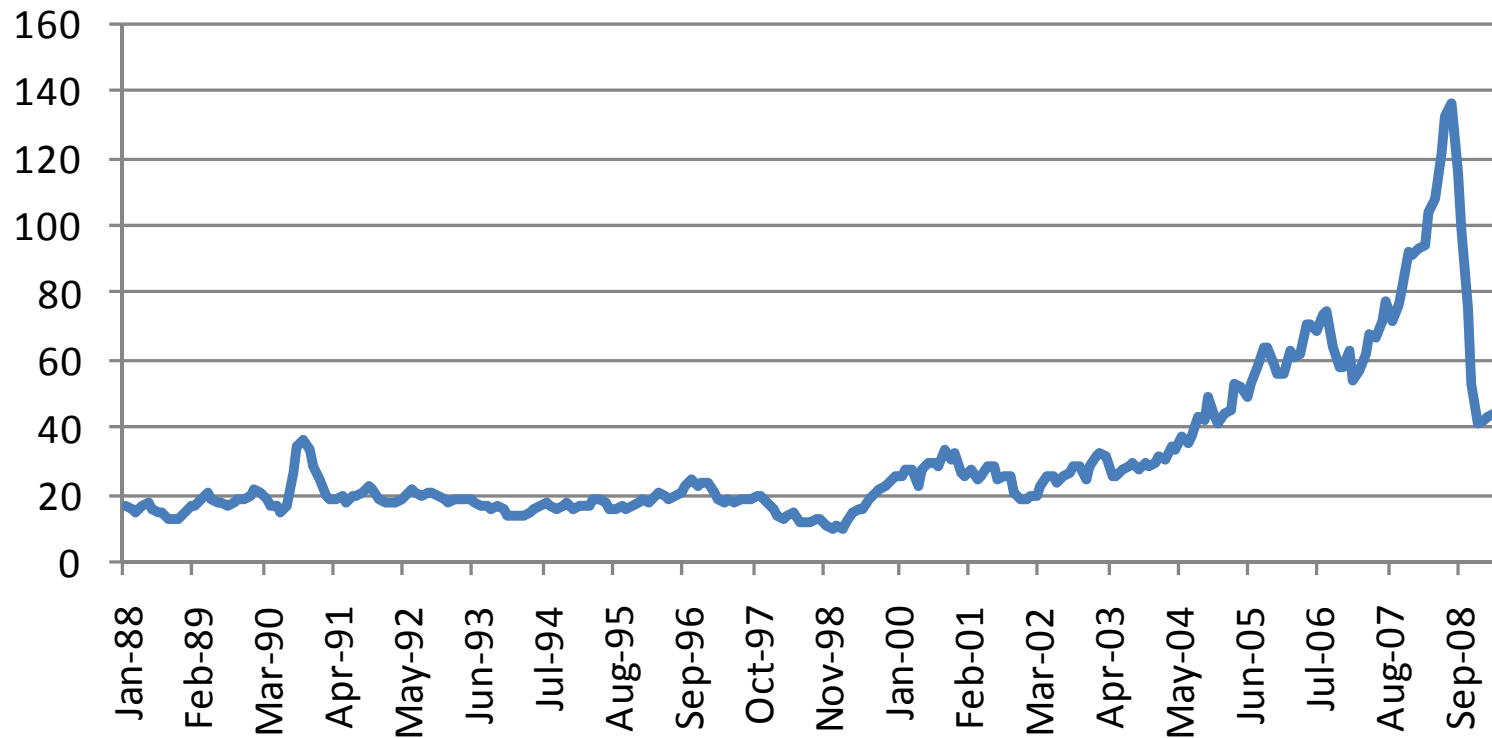
# The \$75/bbl price target – is it really needed?

**Ambassador Jones**  
Deputy Executive Director  
International Energy Agency

**CGES Seminar**  
**24 March**

# Memories are short – is \$75/bbl ‘inevitable’?

Dated Brent, \$/bbl



- Prices for a depleting resource may tend to rise
- But unlikely we are bumping up against resource constraints yet
- There are barriers to expanding supply base, but superseded for now by plunging demand

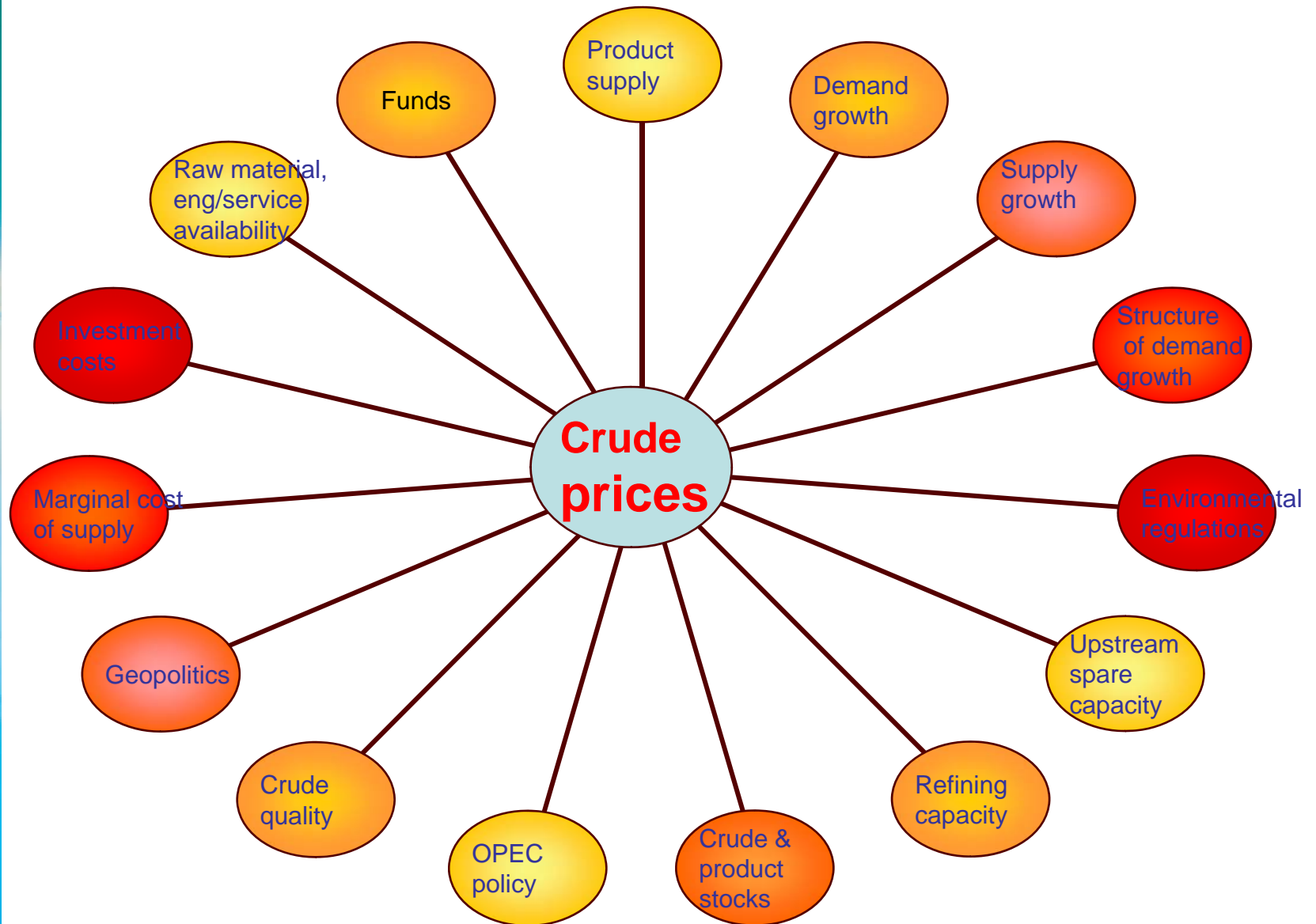
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# Price formation: no single driver

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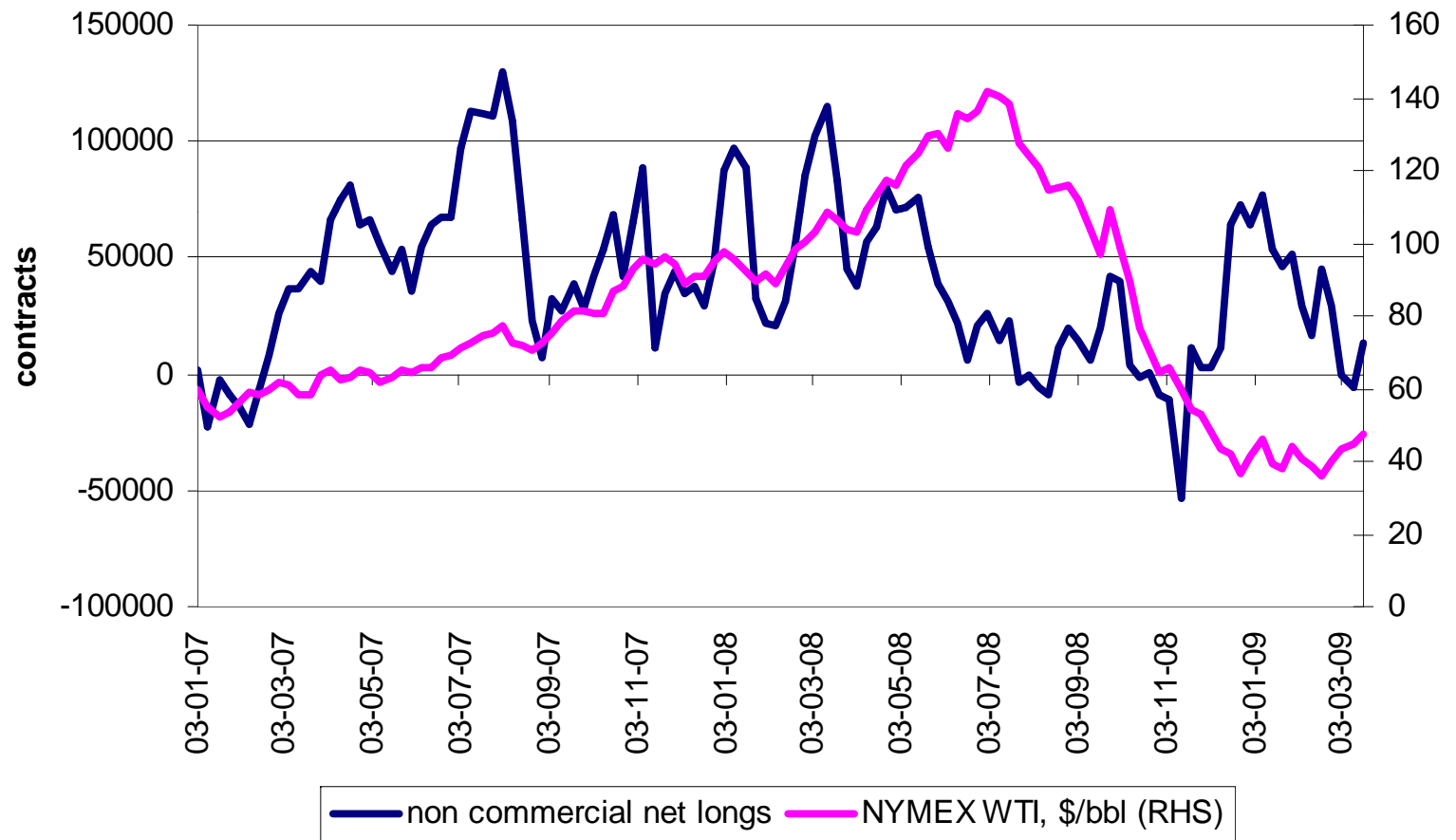


# Price formation: financial flows' impact inconclusive

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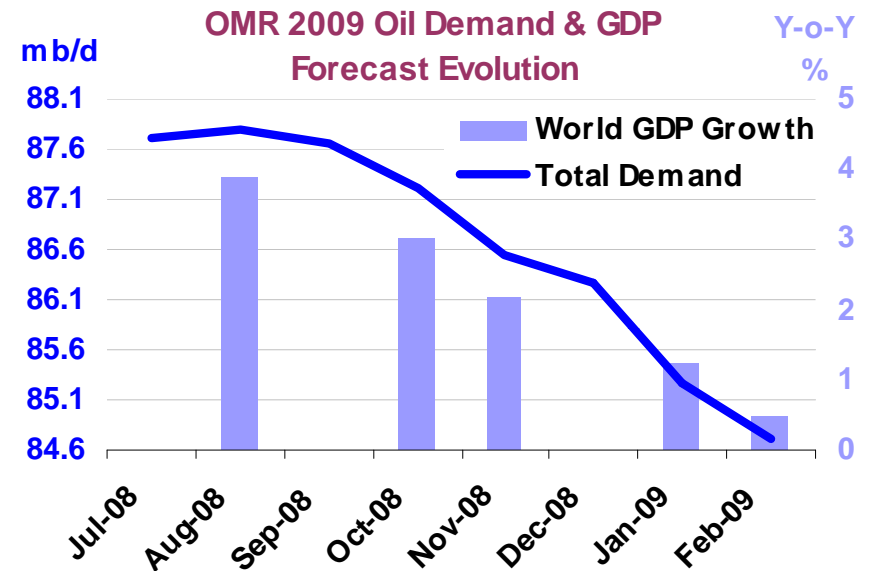
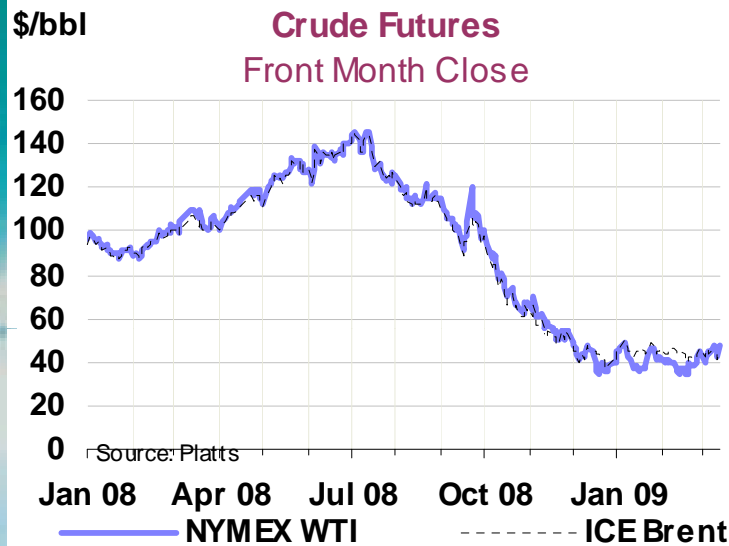
### Non commercial net long positions v NYMEX WTI



# Lower prices – driven for now by economic outlook

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- Two year demand contraction in 08/09 first since early-1980s
- OECD hit hard, but clear signs that non-OECD is slowing now too
- Prices bottoming-out in face of OPEC supply cuts?

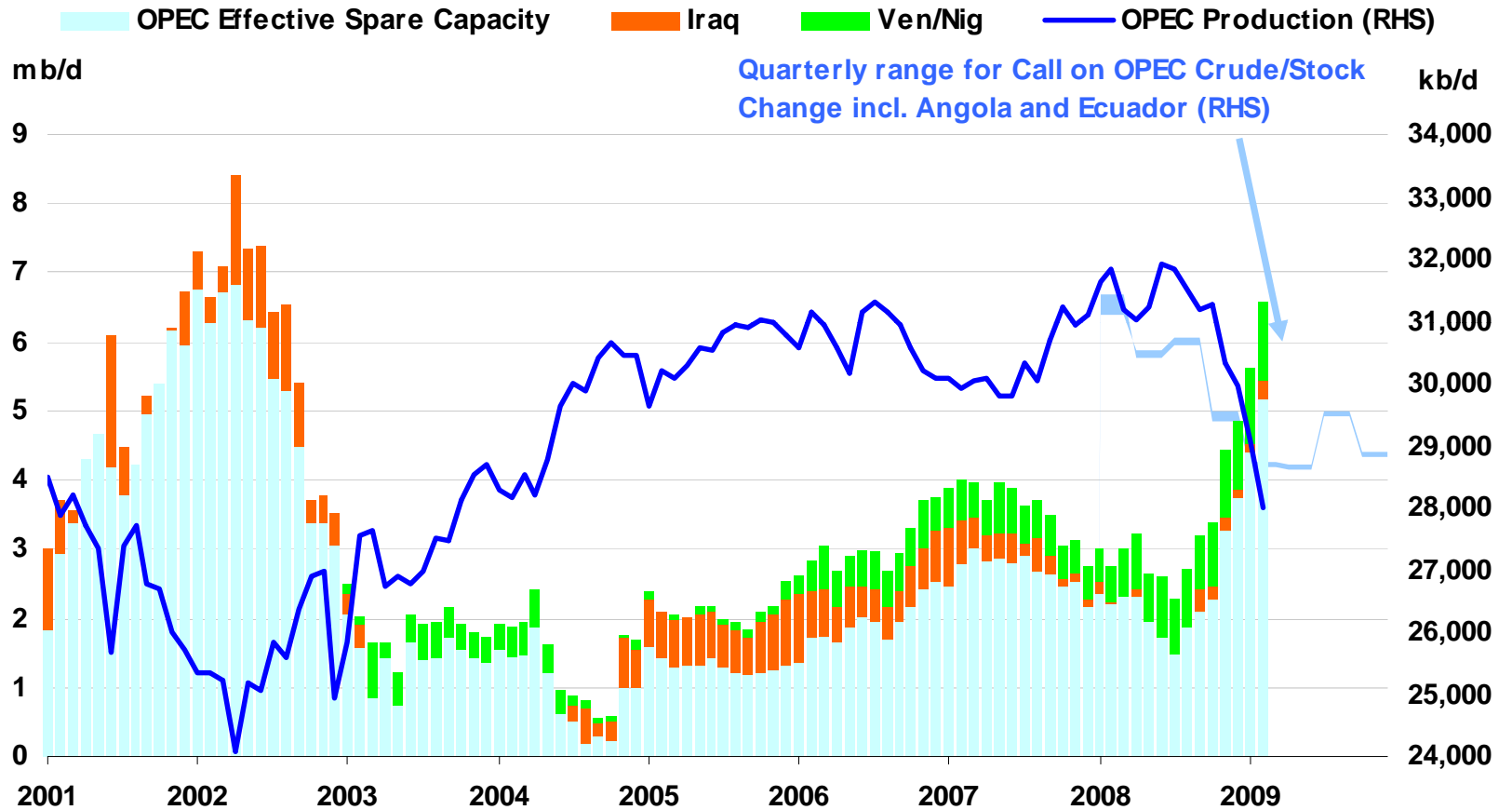


# OPEC reacts by cutting over 3 mb/d since September

*But drives spare capacity to highest since 2002*

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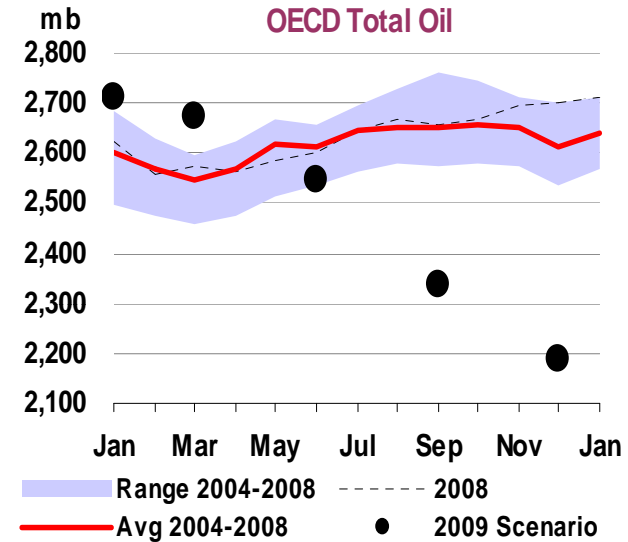
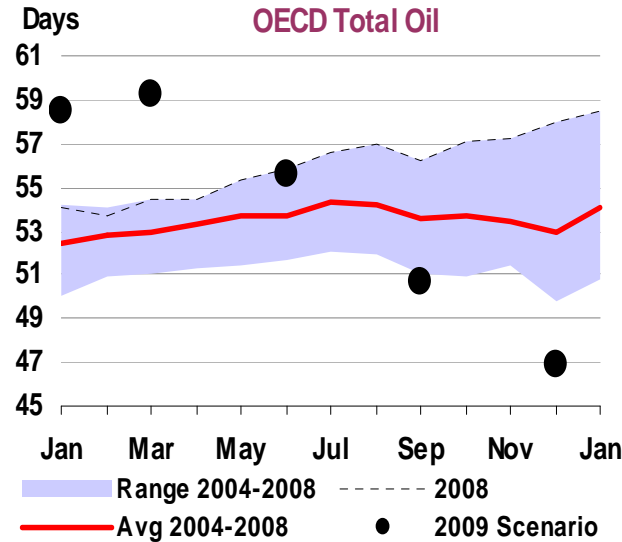
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Effective spare capacity (excl. Iraq/Venezuela/Nigeria) at around 5.19 mb/d in February

# OPEC target compliance could tighten market in second-half 2009

Potential Trend of OECD Stocks: Scenario - OPEC at Current Target April Onwards

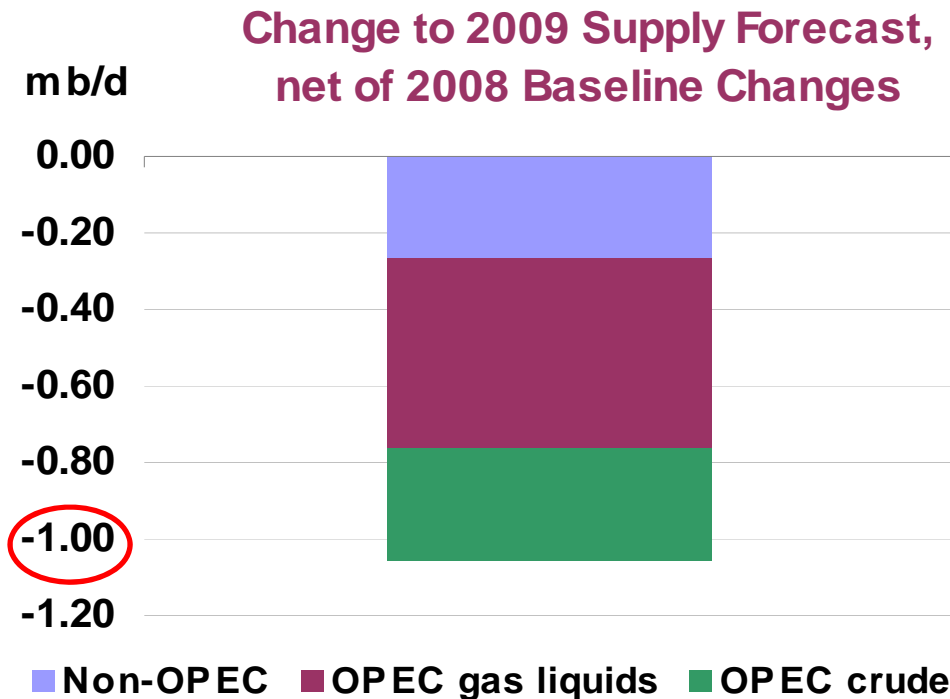


- By adhering to its output targets, OPEC would tighten OECD stocks from late-2Q09...
- ...under the current 2009 demand scenario of -1.2 mb/d
- If demand fall 2mb/d, OECD stocks draws from 3Q09

# Low prices & credit squeeze also hit short term supply

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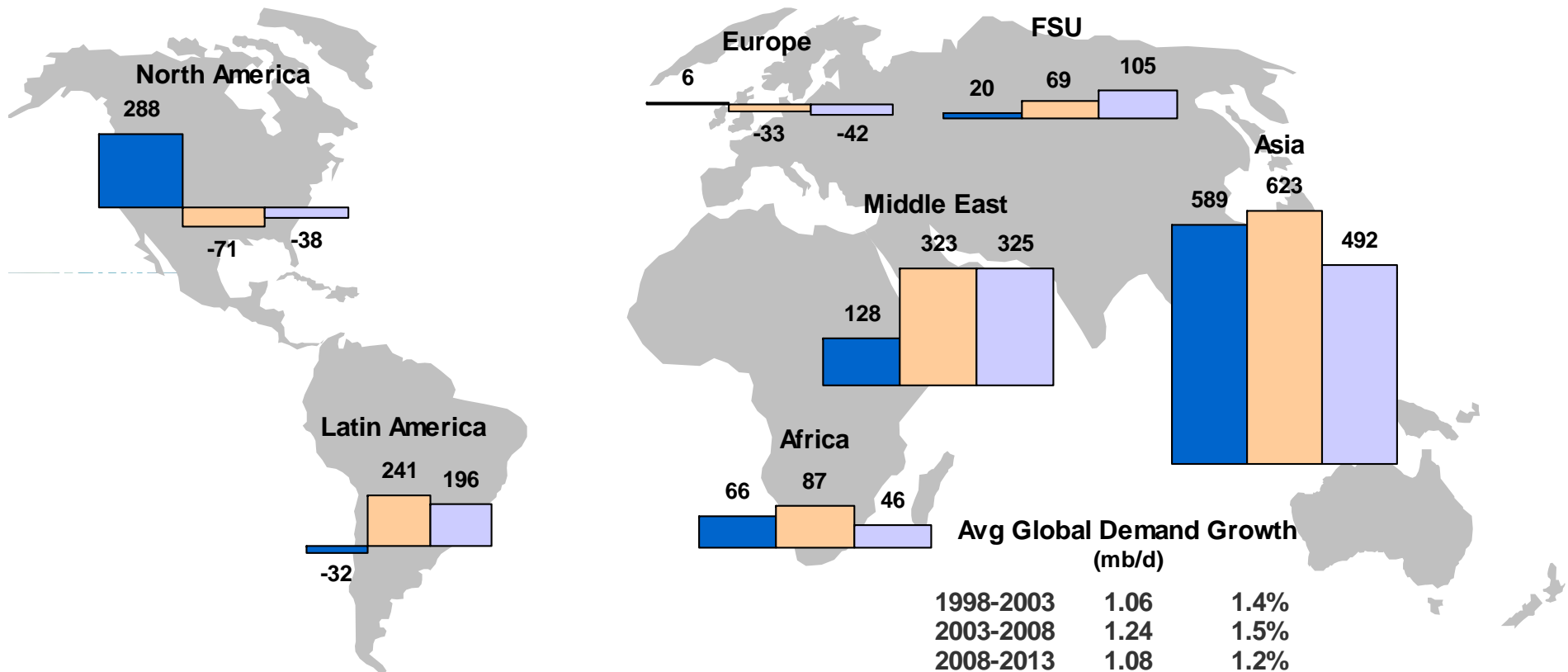


- 2009 forecast already down over 1 mb/d since July, excluding 2008 baseline changes
- Canada & Russia taking a hit in terms of investment & likely output
- Prices of likely sub-\$30/bbl before substantial shut-ins of current output occur
- Revision due to weak demand, low prices, credit crunch & investment slippage
- If this continues, Implies further substantial impact by 2013, lower OPEC spare capacity & tighter market v prevailing forecast



# Looking longer term - demand growth resumes

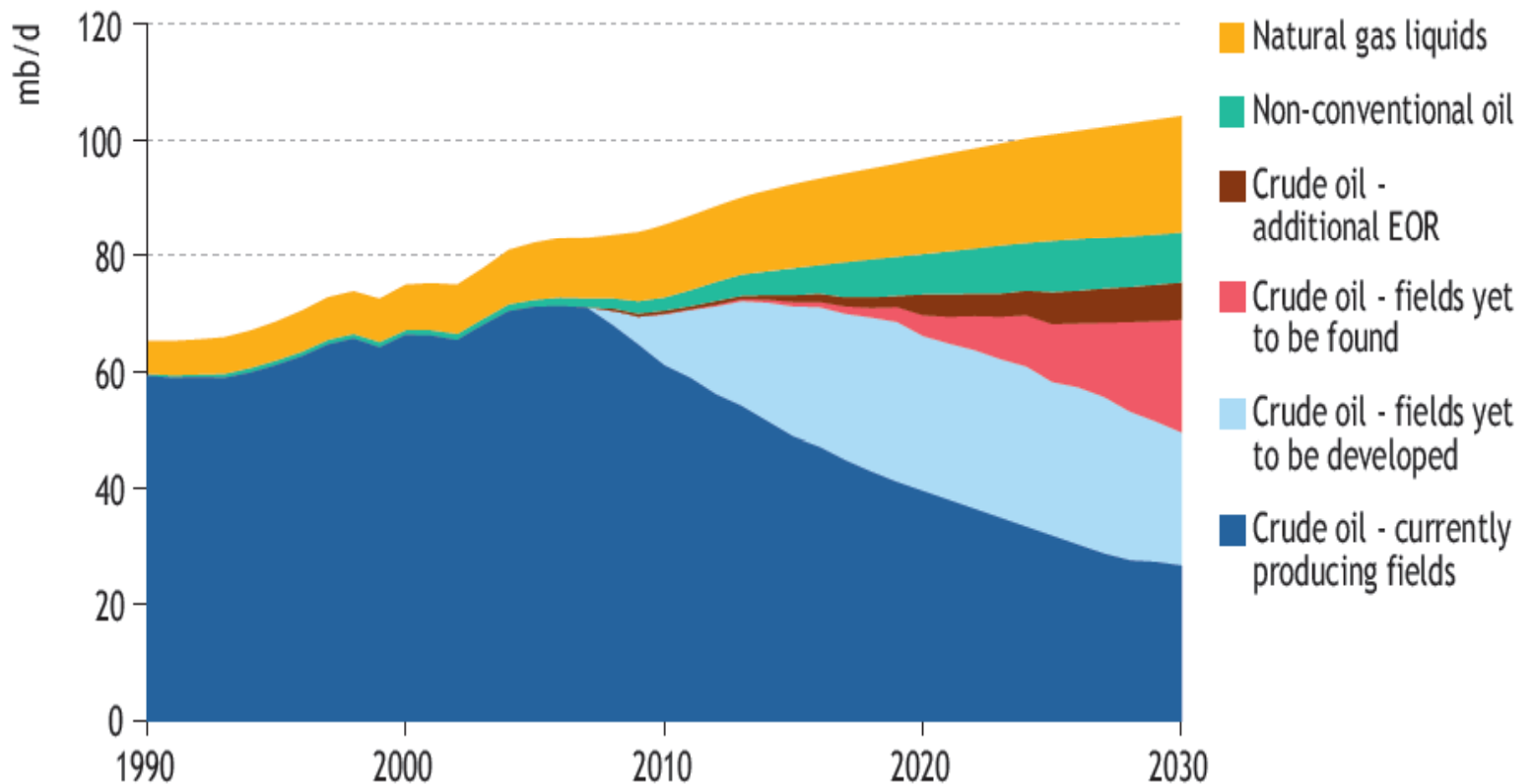
Average Global Demand Growth **1998-2003**/**2003-2008**/**2008-2013**  
thousand barrels per day



Asia and the Middle East **will dominate oil demand growth over the next five years**

Transport & petrochemicals **the focus of growth**

## Mature field decline is ever-present

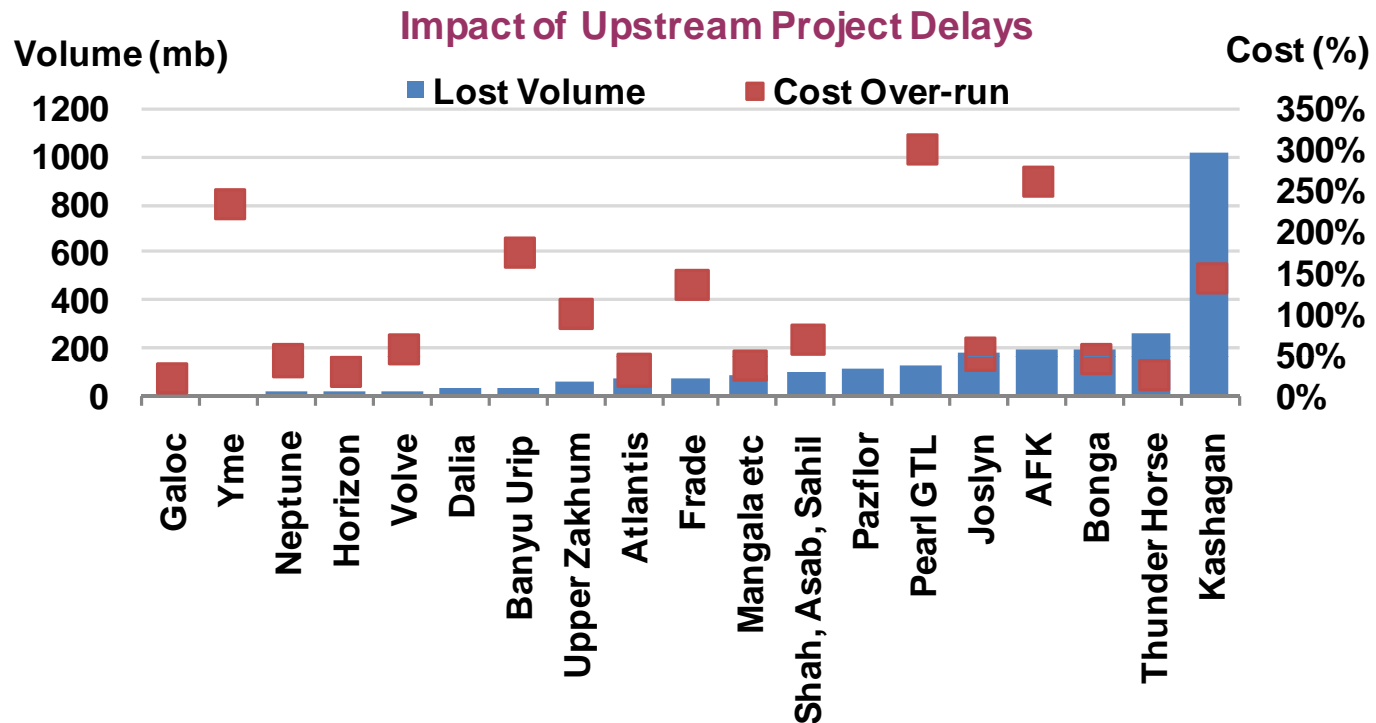


- Global net decline around 5% pa for medium and longer term
- Implies that over 3.5mb/d of new start-ups needed every year just to stand still (plus 1.0 mb/d for demand growth)
- OECD producers facing mature field decline >10% pa, but many OPEC producers face much slower pace of decline

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# Project slippage is endemic, and exacerbated by weaker prices & credit squeeze



- July MTOMR found slippage the key constraint on supply growth
- Typical doubling of investment costs & 12-15 months delays
- Economic slowdown, weaker crude & credit squeeze intensify delays?
- Current Russian & high cost North American production to be affected
- Prospect of “strategic slippage” by OPEC?
- Eventual offsets via lower costs & “distressed producer” policy shifts?

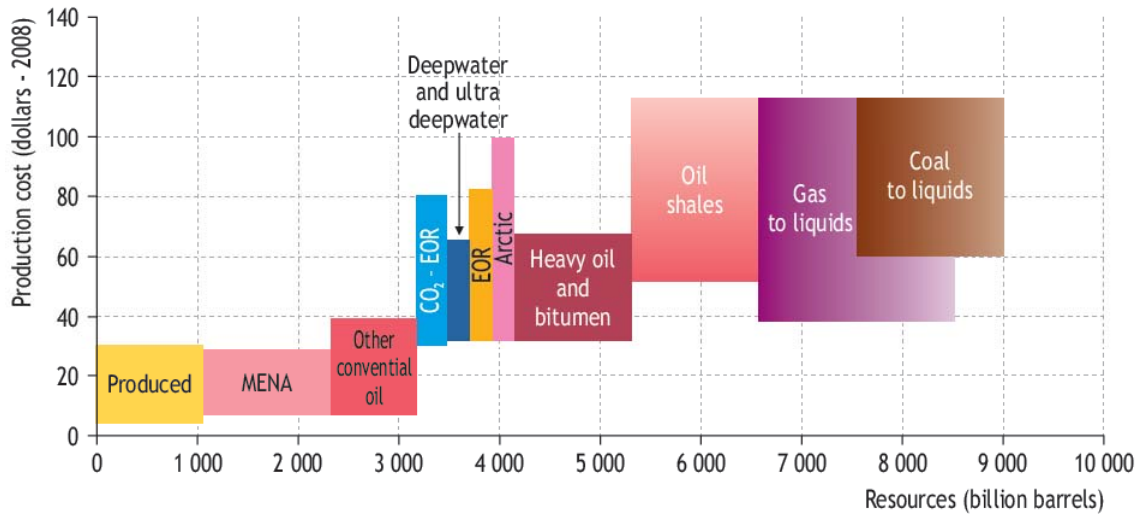
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# Structural shift to difficult oil (opportunity constraints) ...but *cyclical* element to costs too

**Figure 9.10 • Long-term oil-supply cost curve**



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- Cost curves moved higher
- \$80/bbl for some oil sands projects
- Deep water not far behind
- Some cyclical downside now?

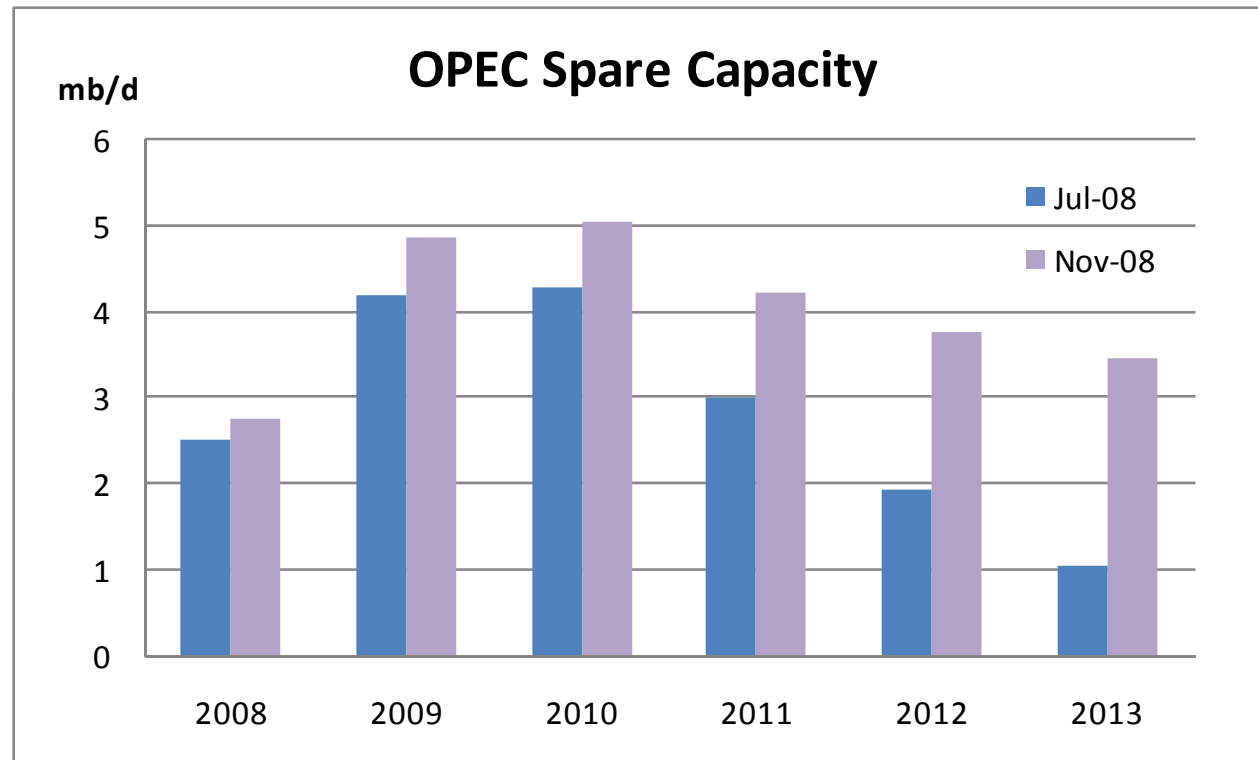


source: SG Equity Research, SG Commodities Research, IEA

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Source: IEA Oil Market Report

## OPEC spare capacity now higher than *MTOMR* but market easing could be short lived



- OPEC effective spare capacity at 3.5 mb/d in 2013, vs. 1 mb/d seen in July
- But does not fully reflect impact of lower price & credit squeeze on investment
- Also assumes OPEC does not further slip key capacity expansions
- Spare capacity could be much lower than the new projection suggests, and even if not, longer term trend unchanged - 3% spare is tight by any measure
- Oil market pause for breath rather than permanent reversion to lower prices

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## Summing Up

- Post-2004 price surge was due to many and varied factors
- Opportunity constraints drive structural increase in costs, but likely cyclical cost reduction from the current market lull
- Duration of weaker market conditions highly uncertain and depends on shape of the economic recovery curve...
  - ...although OPEC cuts to tighten oil market by later in 2009
- Longer term, demand should recover, driven by non-OECD, notably transportation/petrochemical sectors
- “Sluggish” supply response likely to persist however, largely due to above ground factors, rather than resource scarcity
- Prices can be expected to rise anyway, attempting to impose an ‘ideal’ price could lead to excess supply and prolonged low prices
- Better for the market to decide an appropriate price, albeit we need much greater transparency in physical and financial markets

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