20th National Energy Conference "Energy & Development 2015"

The New Oil Order and the Impact on SE Europe

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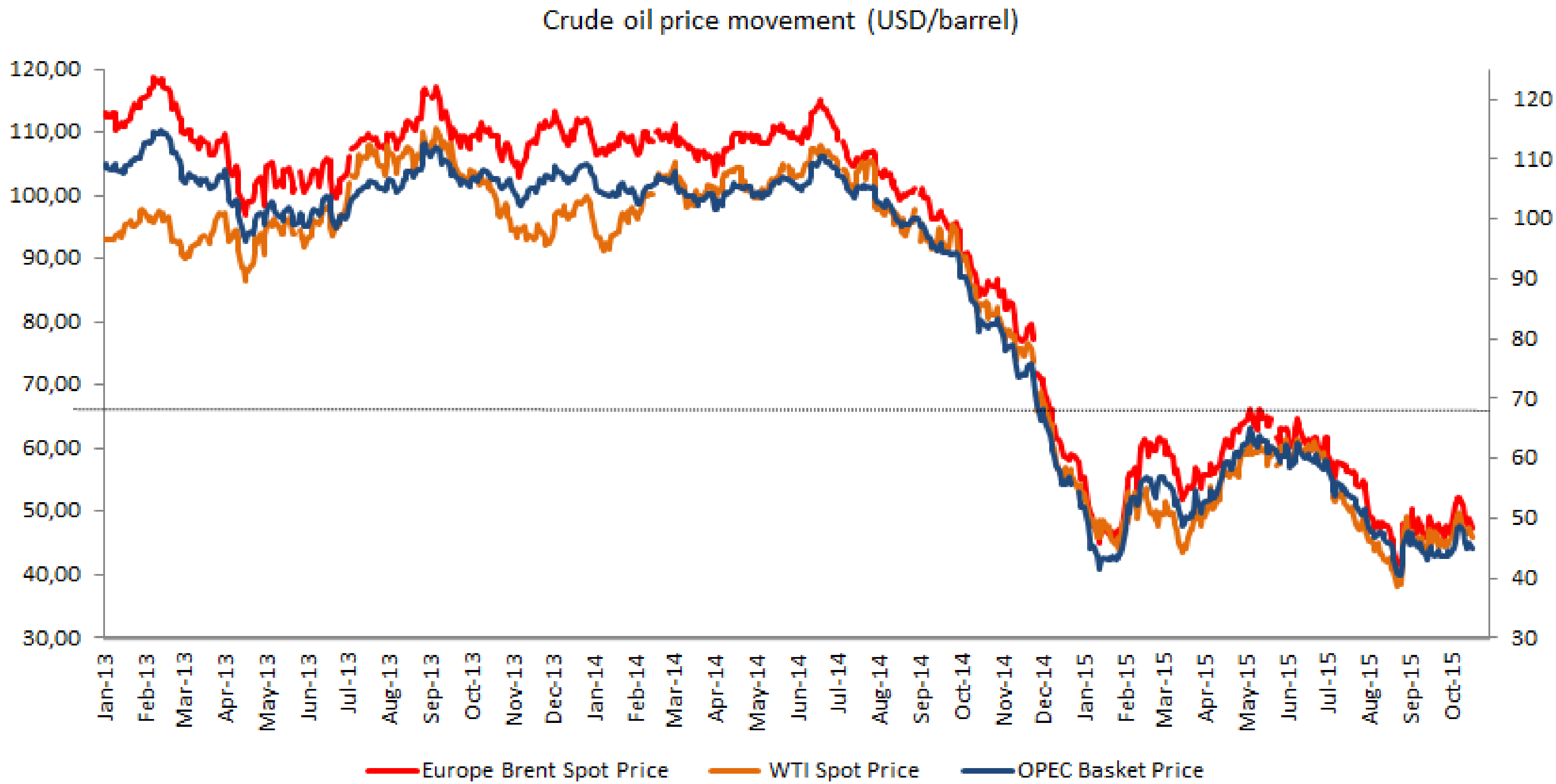
INSTITUTE OF ENERGY
FOR SOUTH EAST EUROPE

Crude oil price movement, January 2013 – October 2015 (USD/barrel)



Descent into an oil abyss?

- It has now been more than a year that international oil prices started their unceremonious descent into the **present lows of $45 to $48** per barrel for Brent
- An upward trend which started in late 2009, had seen average Brent prices maintained well above **$100 per barrel since 2011**.
- While a cluster of geopolitically induced dangers was mounting, from the deepening crisis in Ukraine and war torn Libya and Syria to the emergence of the blood soaked ISIS caliphate in the Iraq-Syria borderlands, **oil prices were** falling largely **unaffected by non market factors**
- A surplus of global oil supply appears to be driving prices downwards, as a number of fully loaded idle VLCC's made their appearance in the Atlantic basin and in the East Med seeking buyers
- At OPEC's historic meeting in Vienna on November 27, 2014, Saudi Arabia refused to lower its own production in order to rebalance prices, thus forcing the other cartel members to accept its position for **defense of market share**
- Since then OPEC's mantra has been that all is well in the market place in spite of accumulated huge losses for producers, i.e. NOC's and IOC's
- By early October stress signs were apparent in Riyadh as Saudi Arabia announced its decision to raise funds from the international markets the first such move in 12 years

Oil glut deepens with 100m barrels at sea

David Sheppard and Neil Hume

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More than 100m barrels of crude oil and heavy fuels are being held on ships at sea, as a year-long supply glut fills up available storage on land and contributes to port congestion in key hubs.

From China to the Gulf of Mexico, the growing flotilla of stationary supertankers is evidence that the oil price crash may still have further to run, as the world's energy infrastructure starts to creak under the weight of near-record inventory levels.

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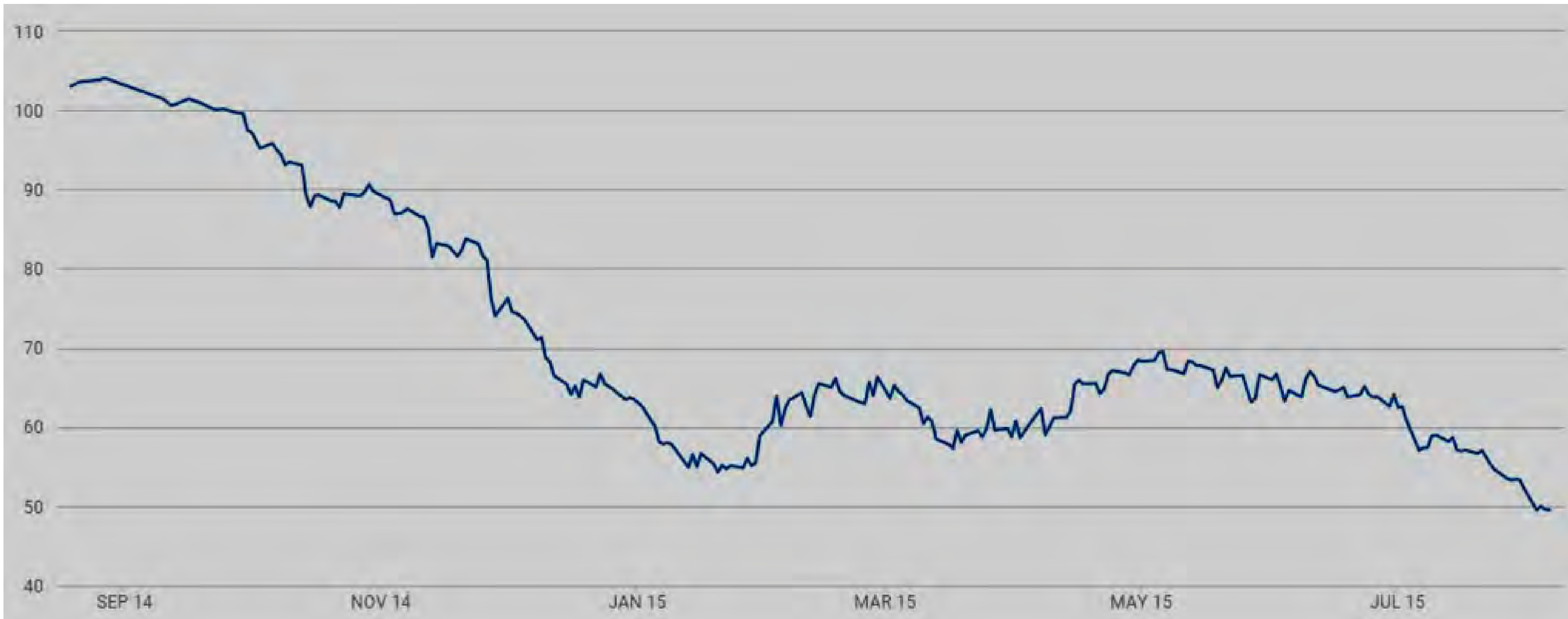
MARKETS DATA — Energy | Metals | Agriculture

Brent Crude	45.20	-1.33%
WTI Crude	42.29	-1.49%
RBOB Gasoline	1.31	-1.11%
Natural Gas	2.26	-0.31%
Heating Oil	1.44	-0.26%

Data delayed by at least 15 minutes

Commodities

ICE Brent Crude Oil Prices (Sep. 2014- July 2015)



Global Oil Demand (2014-2016)

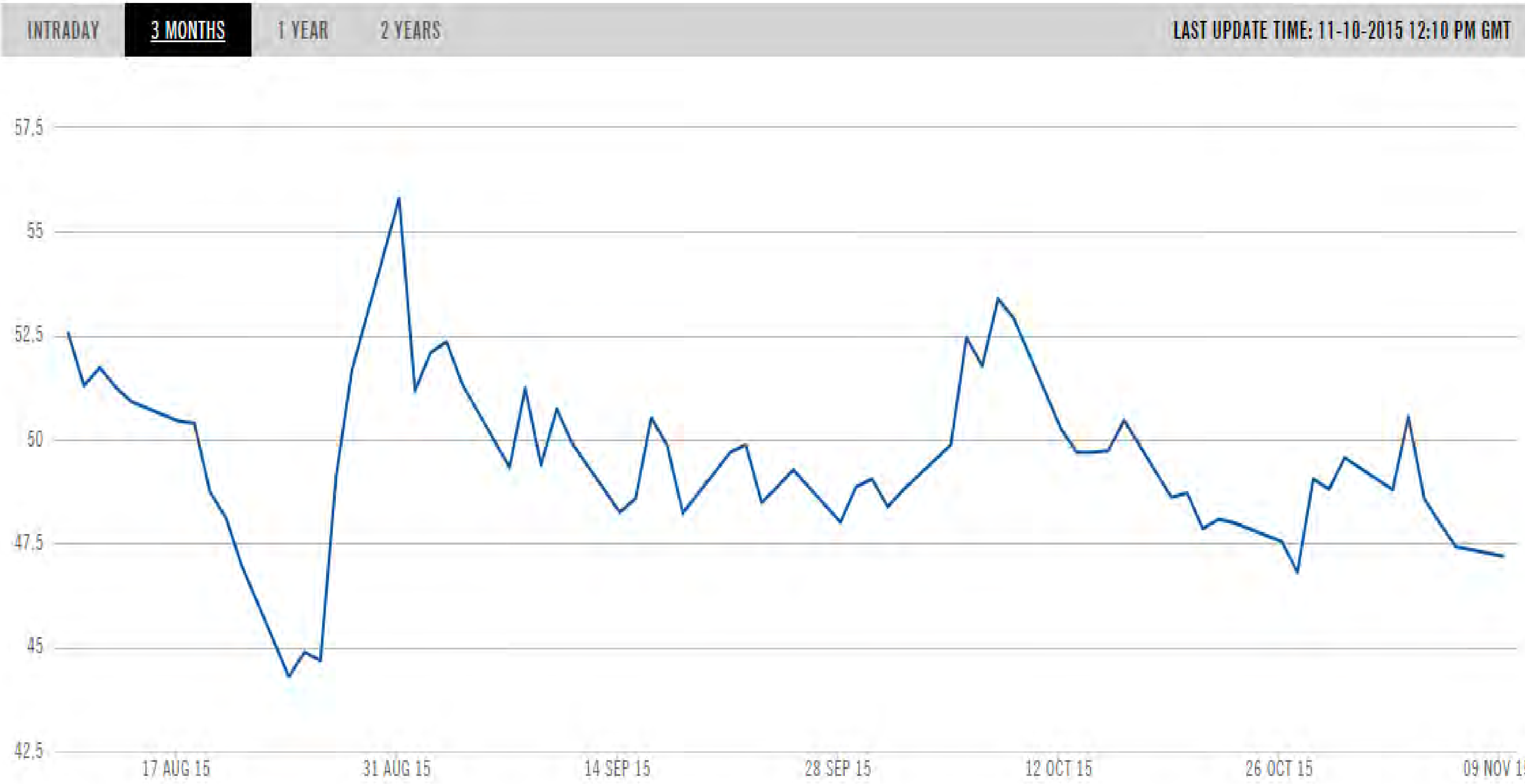
Global Oil Demand (2014-2016)

(million barrels per day)

	1Q14	2Q14	3Q14	4Q14	2014	1Q15	2Q15	3Q15	4Q15	2015	1Q16	2Q16	3Q16	4Q16	2016
Africa	4.0	4.0	3.9	4.0	4.0	4.1	4.1	4.0	4.2	4.1	4.3	4.2	4.1	4.3	4.2
Americas	30.5	30.5	31.3	31.5	31.0	30.9	30.9	31.8	31.7	31.3	31.2	31.1	31.7	31.9	31.5
Asia/Pacific	31.3	30.4	30.0	31.5	30.8	32.1	31.5	31.1	32.3	31.8	32.8	32.2	32.0	33.0	32.5
Europe	13.6	14.0	14.5	14.1	14.1	14.1	14.2	14.6	14.3	14.3	14.1	14.3	14.6	14.3	14.3
FSU	4.6	4.9	5.1	5.0	4.9	4.6	4.9	5.0	4.9	4.9	4.7	4.8	5.0	4.9	4.8
Middle East	7.8	8.2	8.5	7.9	8.1	7.7	8.3	8.6	8.0	8.2	7.9	8.4	8.8	8.2	8.4
World	**91.8**	**91.9**	**93.2**	**94.0**	**92.7**	**93.6**	**93.9**	**95.2**	**95.4**	**94.5**	**94.9**	**95.1**	**96.2**	**96.7**	**95.7**
Annual Chg (%)	1.2	0.5	0.8	1.2	0.9	1.9	2.1	2.1	1.5	1.9	1.4	1.3	1.1	1.3	1.3
Annual Chg (mb/d)	1.1	0.5	0.7	1.1	0.8	1.8	1.9	1.9	1.5	1.8	1.3	1.2	1.1	1.2	1.2
Changes from last OMR (mb/d)	0.0	0.0	0.0	0.1	0.0	0.0	0.1	0.2	0.0	0.1	-0.1	0.0	0.0	-0.1	-0.1

Global demand averaged at 95.2 mb/d in the third quarter of the year with global oil demand growth having peaked at 1.9 mb/d on y-o-y base but forecasted to move lower to +1.2 mb/d for 2H15. Yearly average demand is likely to reach 94.5 mb/d. Still projected average demand for 2016 is forecasted at 95.7 mb/d, a rise of 1.2 mb/d, with global demand gains almost entirely from additional non- OECD demand.

ICE Brent Crude Oil Prices (August. 2015 – November 2015)



Upward and Downward Pressures on Oil Prices

- After falling to almost **$45 a barrel in January**, Brent rebounded to more than **$69 a barrel in May**. But since then prices have fallen back by more than 20 per cent with many traders now forecasting a longer period of lower prices. Speculators' bets on rising oil prices have fallen sharply since May.
- Financial turmoil in Greece, Chinese equity market tumult and stronger US dollar all combined to add some pressure to prices. Downward pressures on oil prices was sustained at the end of August when prices fell by another 5% losing more than $3 a barrel to hit **six month low at $44.29**.
- The renewed price pressure came as market participants focused on accelerated production from OPEC countries, such as Saudi Arabia and Iraq, where output reached new records amid a global competition for customers. **The fear of additional Iranian barrels** seeping into the market after July's nuclear deal just added further downward pressure to prices.
- Today, despite new data showing that US oil inventories fell more than expected and Saudi export pricing numbers showing a boost for Asia, the overall environment is still bearish with supply heavily outweighing demand. Analysts at Goldman Sachs reckon **the global oversupply is currently running at 2m barrels a day, compared to 1.8m b/d during the first six months** of the year.
- Fundamentals are weaker today than in 1Q. Global supply **is currently up 3.0 million compared to 2014 b/d** (and averaged up 3.2 million b/d over the past 12 months), driven in large part by a surge in low -cost production from Saudi Arabia, Iraq and Russia.

Reduced Profits for Oil Majors and Cuts on New Projects - I

The sharp drop in oil prices and their stubborn resistance to move higher has caused enormous pain for investors in big oil:

- Chevron's profit was 64 per cent lower than last year's third quarter; Chevron plans to cut capital and exploratory spending next year by one-fourth, with further cuts in 2017 and 2018 depending on the oil industry's condition then.
- Halliburton, Schlumberger and other oilfield-service providers have also cut thousands of jobs.
- Exxon's profit fell 47 per cent, its worst third quarter since 2003. Exxon's profit from exploration and production dropped from $6.5 billion to $1.4 billion, including a loss of $442 million in the U.S. However, so-called downstream earnings from refining and selling petroleum products jumped from $1 billion to $2 billion on higher refining margins.
- The British oil giant BP said late in October that its profit was down sharply in the third quarter as depressed oil prices took a heavy toll. Exploration costs were cut by more than half in the third quarter, to $356 million
- Royal Dutch Shell and Centrica announced in August that they were shedding more than 12,000 jobs between them. Shell cut capital spending 20 per cent, with its chief Ben van Beurden warning of a “prolonged downturn” ahead.

Reduced Profits for Oil Majors and Cuts on New Projects - II

- Reduced capital spending by oil and gas companies, as a result of much lower oil prices, is hurting the oil industry which has entered a downward spiral with wide ranging effects on profitability and employment. Analysis of planned oil and gas projects show that more than **$200 bn of capital spending has been slowed, delayed or ditched**. The impact of differing investement in such projects will delay production of **1.5-2.0 million barrels per day**, which is bound to put pressure on prices from 2017 onwards
- Energy consultancy Wood Mackenzie says that the plunge in crude prices since last summer has resulted in the deferral of **46 big oil and gas projects** with 20bn barrels of oil equivalent in reserves — more than Mexico's entire proven.
- Among companies postponing big production plans while they wait for costs to come down are UK-listed BP, Anglo-Dutch Royal Dutch Shell, US-based Chevron, Norway's Statoil, and Australia's Woodside Petroleum. Research **from Rystad** Energy, a Norwegian consultancy, found in **May that $118bn of projects** had been put on hold, but the Wood Mackenzie study shows the toll is now much greater.

The New Oil Order

- With most analysts agreeing that given present market conditions and Saudi resolve to keep on pumping in spite of lower prices, global oil prices are not unlikely to rebound any time soon. It seems that we have now entered for good **a new price era**.
- The decision to ride out a sustained period of lower prices has put a huge strain on the finances of major oil exporters, including **Saudi Arabia which requires an oil price of $105 a barrel to balance its budget**. The kingdom has drained $65bn of its fiscal reserves over the last 12 months in order to maintain government spending intact
- **The new oil order as dictated by Saudi policies and shaped by the rest of the OPEC country group**, foresees the continuation of weak oil prices with possible momentary rebounds together with high volatility, and the subsequent serious curtailment of exploration activity by the IOC’s in view of much reduced profits and market uncertainty.
- Reduced exploration activity will inevitably lead **to less discoveries over the next couple of years** with NOC’s taking the lead on new ventures. It is doubtfull though if NOC’s will manage during this critical time to further increase their reserves and so counterbalance the anticipated lack of progress by the oil majors.
- Whatever the case may end up to be, **the outlook over the next 2 to 3 years will be for demand to start at one point outstripping supply**, leading once again to a period of higher prices. A classical boom and bust case, but this time with major producers rather than traders calling the shots.

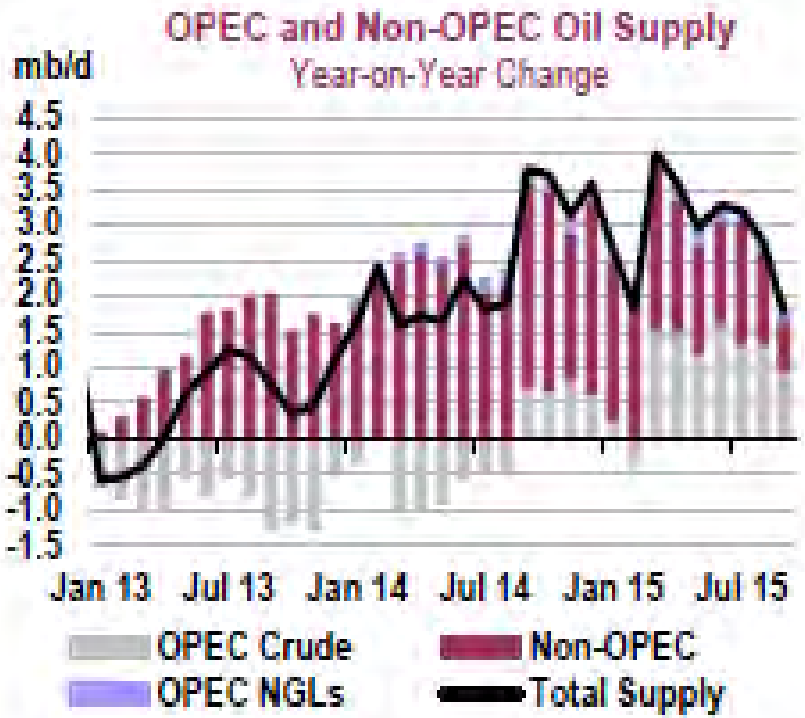
World Economic Outlook, 2016

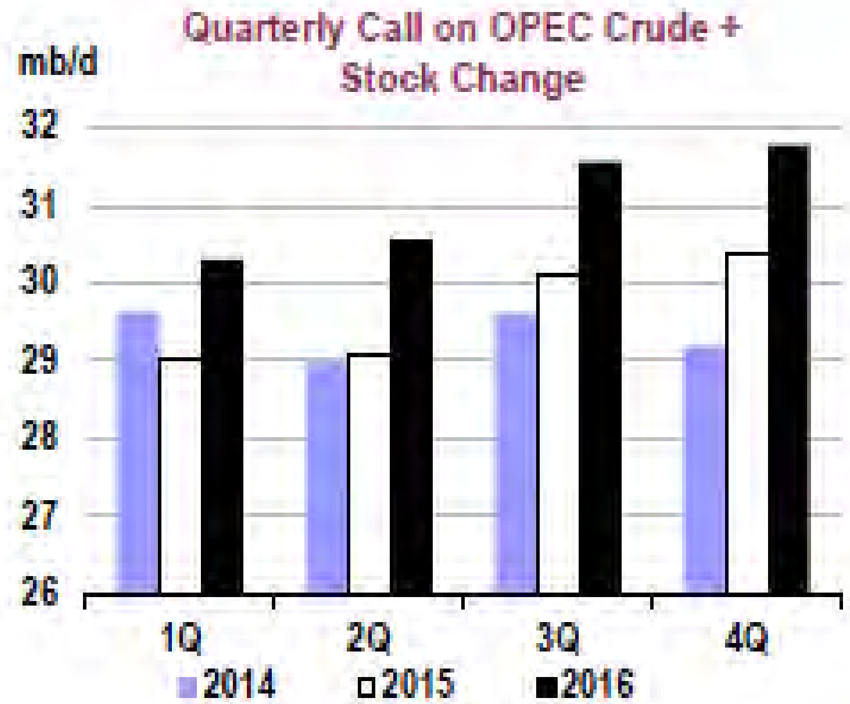
Economic Outlook, 2016

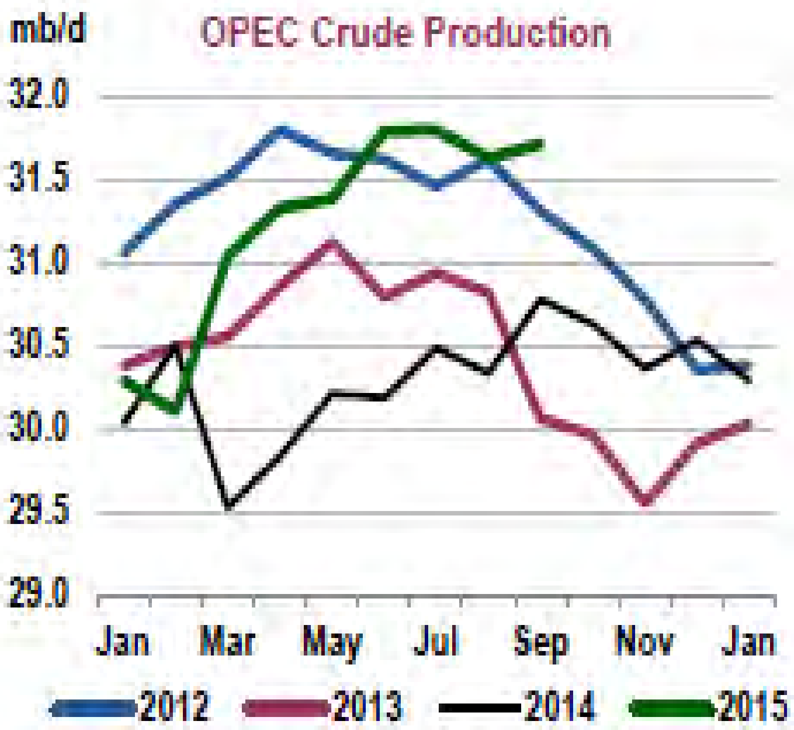
IMF projections

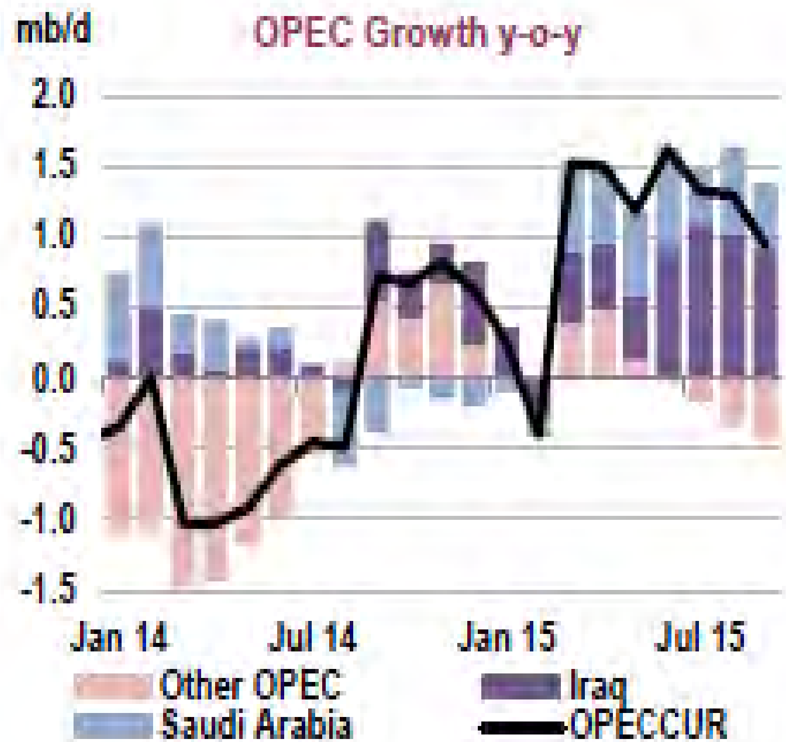
% change	Jul-15	Oct-15
WORLD	**3.8**	**3.6**
US	3.0	2.8
Germany	1.7	1.6
France	1.5	1.5
Italy	1.2	1.3
Spain	2.5	2.5
UK	2.2	2.2
Canada	2.1	1.7
Japan	1.2	1.0
China	6.3	6.3
India	7.5	7.5
Brazil	0.7	(1.0)
Russia	0.2	(0.6)
Saudi Arabia	2.4	2.2

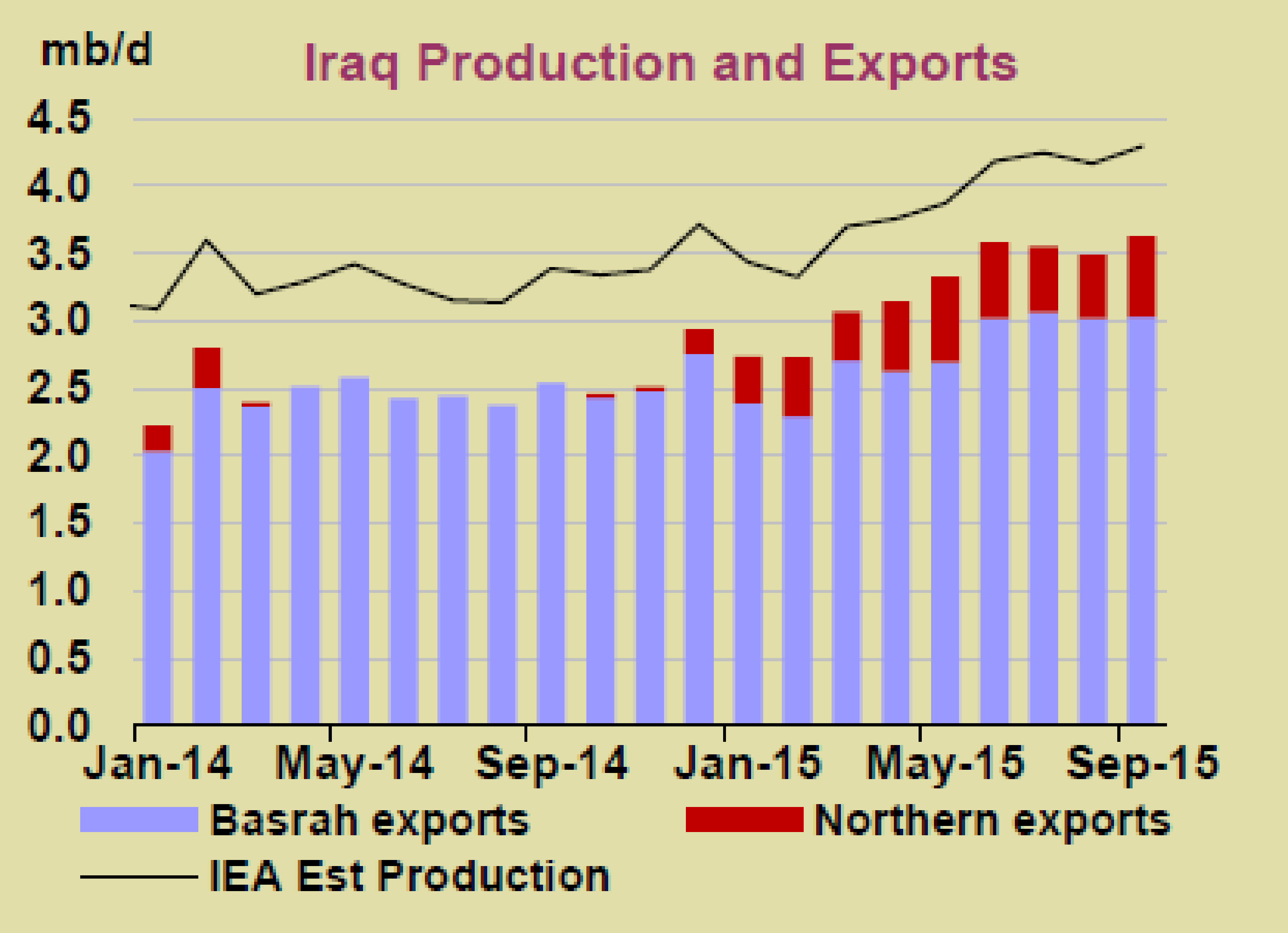
Source: IMF

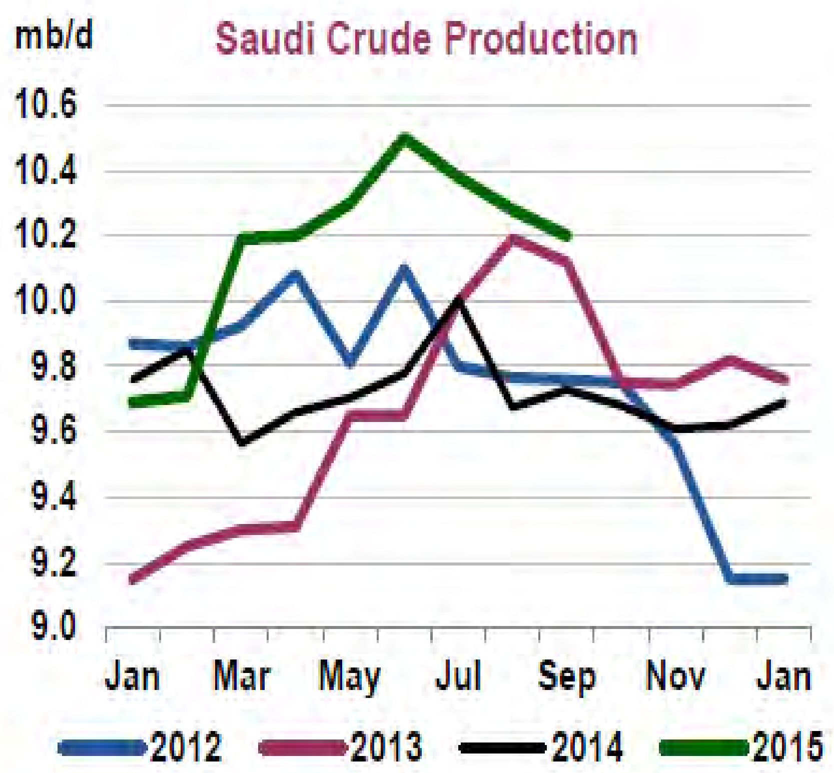

OPEC and Non-OPEC Oil Supply
Year-on-Year Change
mb/d
4.5
4.0
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
-0.5
-1.0
-1.5
Jan 13
Jul 13
Jan 14
Jul 14
Jan 15
Jul 15
OPEC Crude
Non-OPEC
OPEC NGLs
Total Supply


Quarterly Call on OPEC Crude +
Stock Change
mb/d
32
31
30
29
28
27
26
1Q
2Q
3Q
4Q
2014
2015
2016

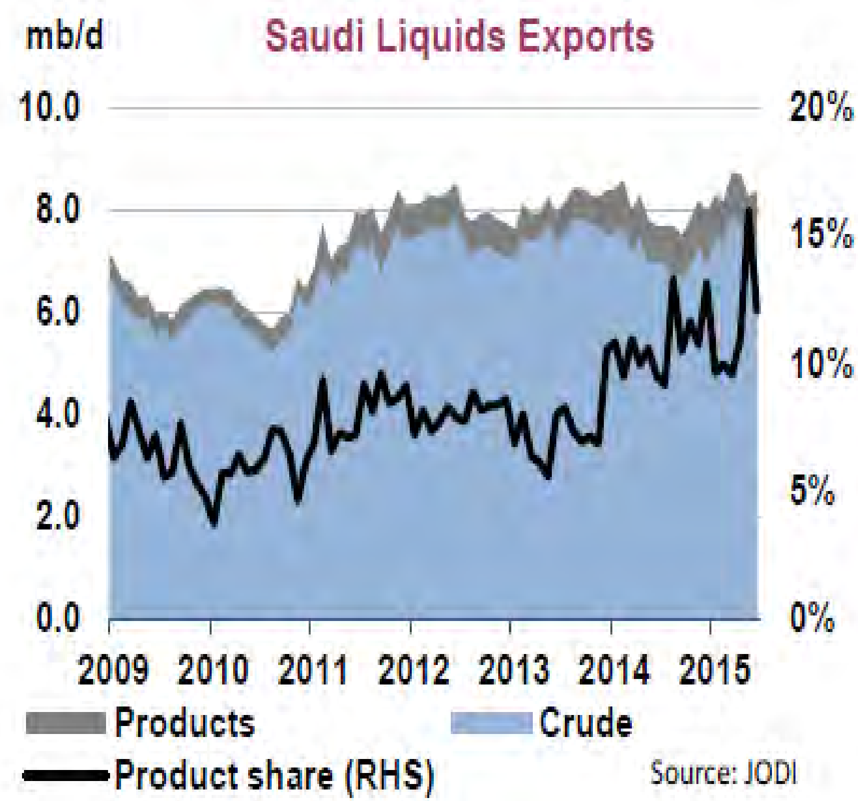

mb/d
OPEC Crude Production
32.0
31.5
31.0
30.5
30.0
29.5
29.0
Jan
Mar
May
Jul
Sep
Nov
Jan
2012
2013
2014
2015


mb/d
OPEC Growth y-o-y
2.0
1.5
1.0
0.5
0.0
-0.5
-1.0
-1.5
Jan 14
Jul 14
Jan 15
Jul 15
Other OPEC
Iraq
Saudi Arabia
OPECCUR

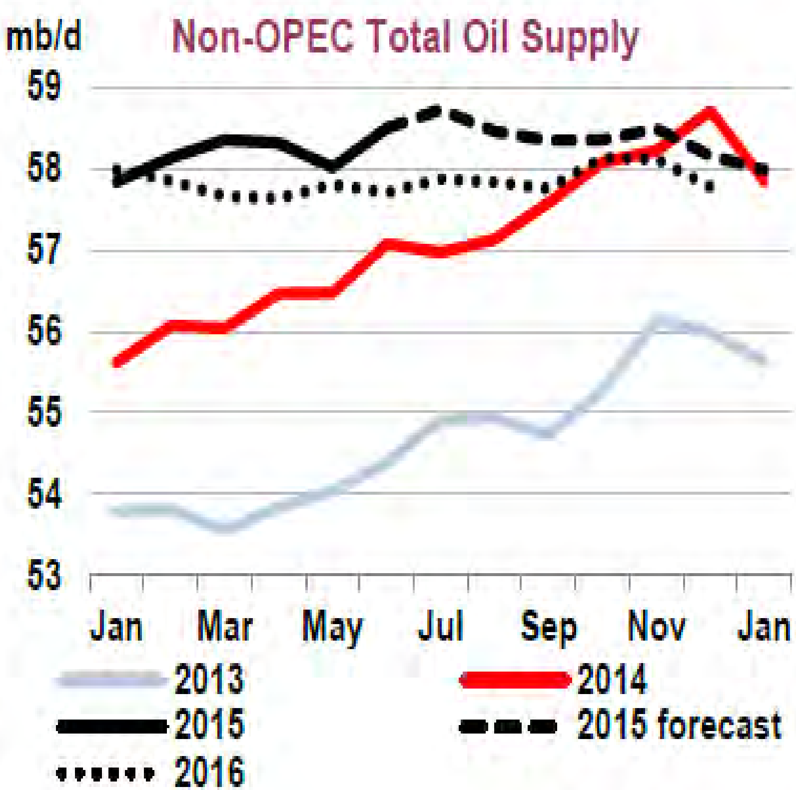

mb/d
Iraq Production and Exports
4.5
4.0
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
Jan-14
May-14
Sep-14
Jan-15
May-15
Sep-15
Basrah exports
Northern exports
IEA Est Production

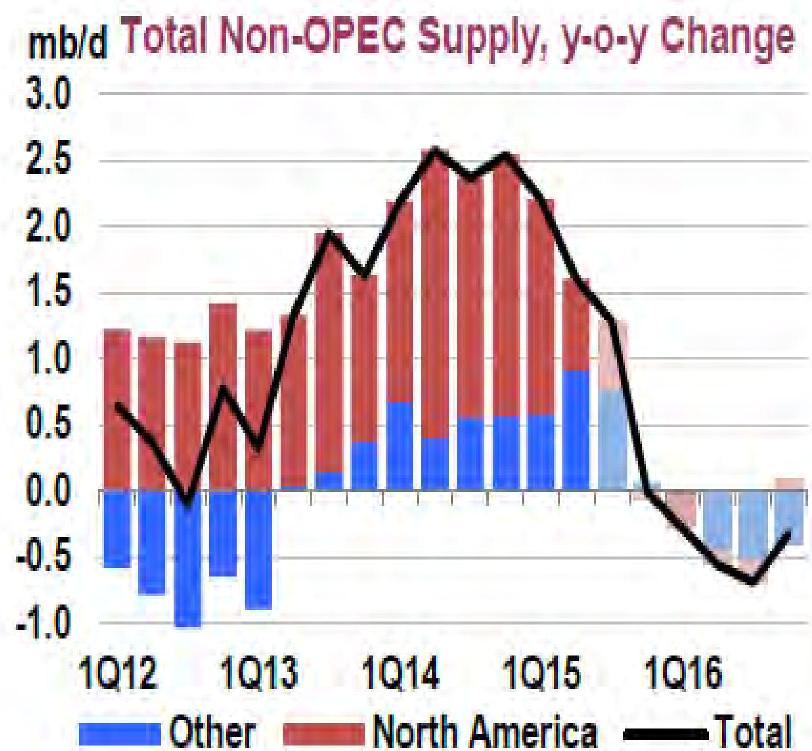


mb/d
Saudi Crude Production
10.6
10.4
10.2
10.0
9.8
9.6
9.4
9.2
9.0
Jan
Mar
May
Jul
Sep
Nov
Jan
2012
2013
2014
2015



mb/d
Saudi Liquids Exports
10.0
8.0
6.0
4.0
2.0
0.0
20%
15%
10%
5%
0%
2009
2010
2011
2012
2013
2014
2015
Products
Crude
Product share (RHS)
Source: JODI


mb/d
Non-OPEC Total Oil Supply
59
58
57
56
55
54
53
Jan
Mar
May
Jul
Sep
Nov
Jan
2013
2014
2015
2015 forecast
2016


mb/d
Total Non-OPEC Supply, y-o-y Change
3.0
2.5
2.0
1.5
1.0
0.5
0.0
-0.5
-1.0
1Q12
1Q13
1Q14
1Q15
1Q16
Other
North America
Total

The Impact on SE Europe

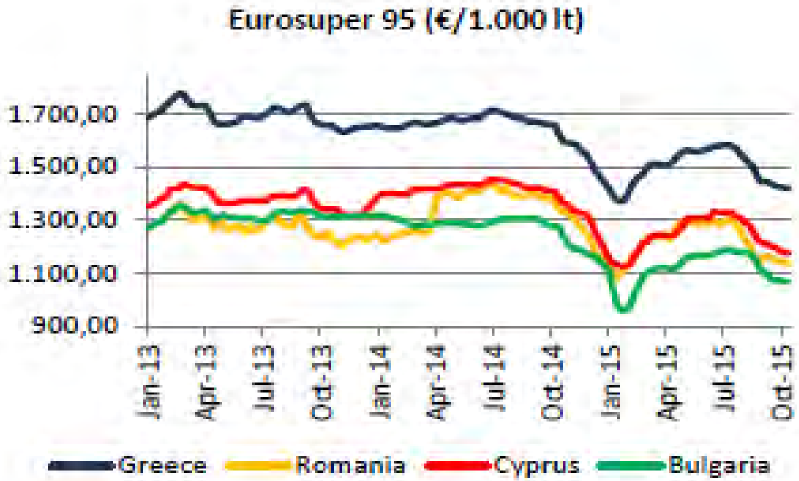
- Lower oil prices can only be beneficial for the group of countries comprising SE Europe. As it is clearly evident from the data presented in Table 2, **SE European countries as a whole are net importers of oil and natural gas.**
- Presuming that prices trade on average at around $50 a barrel over the next 12 months, SE Europe will see a **cumulative reduction of $29 bn in its oil import bill** with major importers such as Turkey and Greece benefiting most (At a $105 per barrel the import bill for the 13 country group of SE Europe had reached $55.50 billion).
- A substantial portion of these saved costs will gradually feed in to consumer pockets who although they may decide to retain most of them they will still divert some funds towards higher spending. This may **help sustain and even strengthen the anaemic economic growth** observed lately in most SE European countries, with the exception of Greece whose economy is now set for yet another contraction of approximately 1.5%-2.0% for 2015.
- In conclusion **lower international oil prices will clearly benefit the economies of the region**, greatly contributing to public deficit reduction, but not to the extent that they will affect drastically other key economic indicators, since consumer oil prices entail a very high degree of taxes. In most cases **government taxes amount between 55-65%** of the pump price. So the much reduced international oil prices will only affect a small segment of the final price. (See Video)

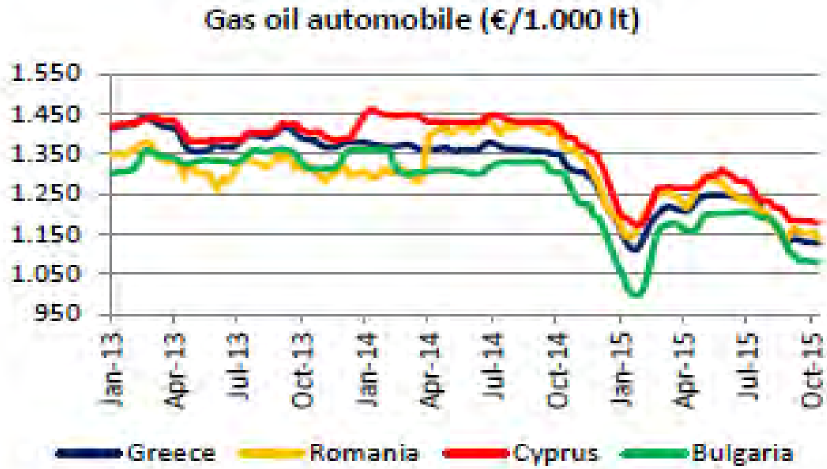
Oil and Gas Production and Consumption in SE Europe (2013)

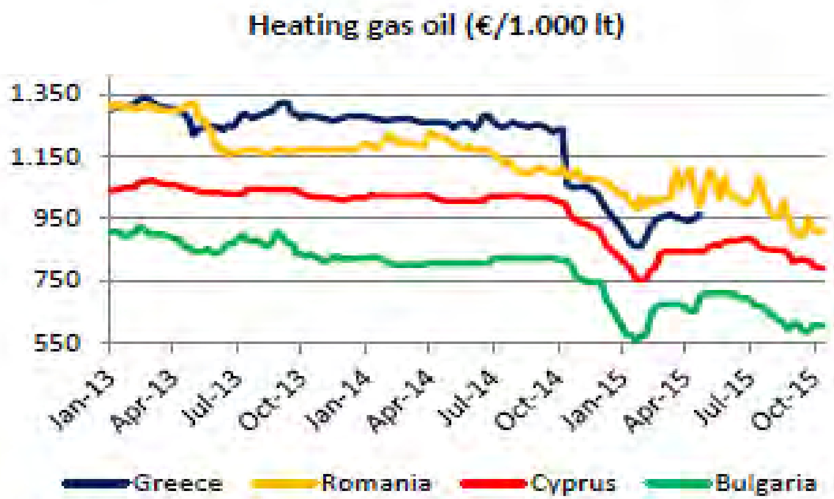
Country	Total Oil Production (bbl/day)	Crude Oil Production (bbl/day)	OilConsumption(bbl/day)	GasProduction (bcm/year)	GasConsumption(bcm/year)
ALBANIA	17.040	17.010	28.000	0	0
BOSNIA AND HERZEGOVINA	0	0	36.000	0	0,24
BULGARIA	3.380	1.000	94.000	0,08	3,07
CROATIA	20.240	12.000	84.000	1,91	3,25
CYPRUS	0	0	58.000	0	0
FYROM	41	0	16.670	0	0,10
GREECE	7.074	1.247	284.015	0,01	3,86
MONTENEGRO	0	0	4.460	0	0
ROMANIA	103.700	84.990	215.250	10,63	13,48
SERBIA	21.220	16.500	77.200	0,56	2,91
TURKEY	58.140	46.240	719.270	0,54	45,65
TOTAL	**230.835**	**178.987**	**1.616.865**	**13,72**	**72,56**

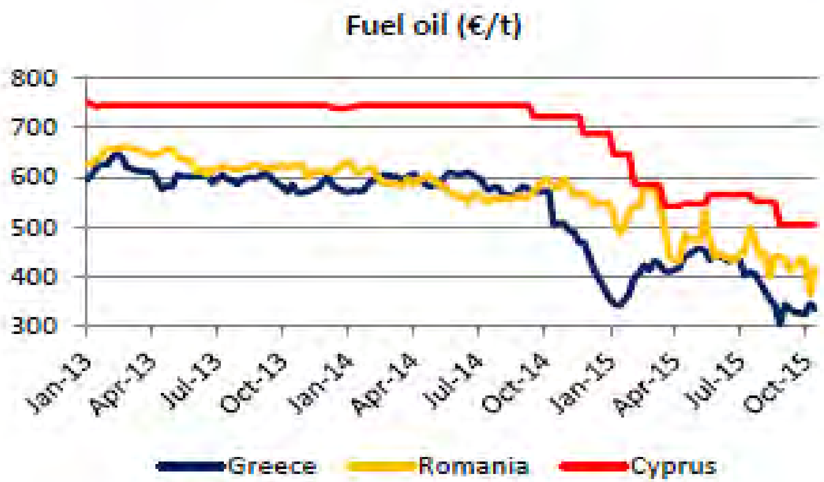
Source: U.S. Energy Information Administration

Oil Products Prices: Greece, Romania, Bulgaria, Cyprus



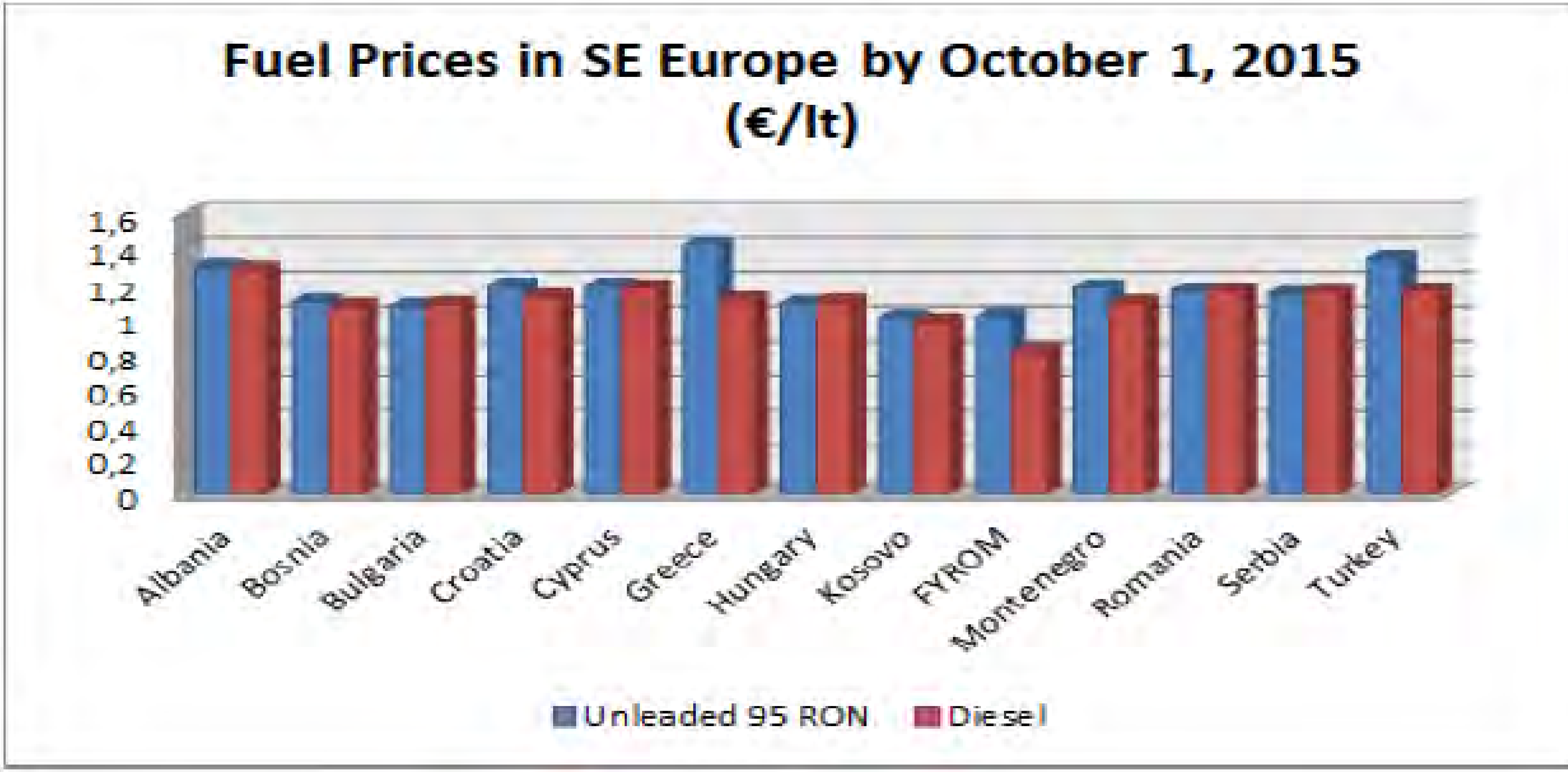






Source: ec.europa.eu

Fuel Prices in SE Europe by October 1, 2015



Thank you for your attention

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