CIO continues to advise risk-taking investors to add long exposure via first-generation indexes or longer-dated Brent contracts, or to sell Brent's downside price risk. (ddp)

Upside in oil remains amid an undersupplied market

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Oil prices have remained under pressure over the past month, with Brent crude falling 13.6% amid recession fears in the US and weaker-than-expected economic data out of China.

Still-elevated Russian exports and the sizable inventory build at the start of this year due to a milder winter in the Northern Hemisphere have also played a role.

We now see the Brent price reaching USD 95 a barrel by the end of this year, down from our previous forecast of USD 105/bbl, as we expect Russian oil output to stay at around 9.6 million barrels per day (mbpd) instead of 9mbpd in the second half of this year.

However, this means an upside of over 25% from current levels. We still see several main reasons to expect the oil market to be under supplied in coming months:

The International Energy Agency sees robust global oil demand. In its latest monthly oil market report published this week, the Paris-based agency raised its forecast for global 2023 oil demand by 100,000bpd to 102mbpd. It also anticipated tighter market balances in the second half of the year, "when demand is expected to eclipse supply by almost 2mbpd." While our own forecast puts current global demand at around 101mbpd, we see higher demand in June, boosted by the driving season in the US and more oil being used to generate power to cool down buildings in the Middle East. In fact, we expect the oil market to be undersupplied by nearly 1.5mbpd next month.

Inventory draws are set to be more visible in the months ahead. The US Department of Energy said earlier this week that it plans to purchase 3 million barrels of crude oil for the Strategic Petroleum Reserve for delivery in August, after a record sale last year that pushed the level of the reserve to the lowest since 1983. It remains to be seen whether

the tender will be concluded, but we expect to see larger inventory draws as the Northern Hemisphere enters summer while the impact of strategic oil reserve release fades.

OPEC+ cuts should tighten the market further amid other supply constraints. The voluntary output cut by nine OPEC+ members this month should continue to tighten the market, while wildfires in Canada's primary oil producing province Alberta has forced shutdowns of oil and gas production. Iraq's total oil exports this month are also likely to be limited amid continued suspension of production in the north. We anticipate oil production will fall back toward 100mbpd in May from around 101mbpd in 1Q23.

A tighter market should convince financial investors to return to the oil market, thus supporting prices. So, we maintain our most-preferred rating on oil alongside our positive stance on broad commodities. We continue to advise risk-taking investors to add long exposure via first-generation indexes or longer-dated Brent contracts, or to sell Brent's downside price risk. We also see value in emerging market energy bonds for an attractive yield pickup versus developed market government and investment grade debt.

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