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The Grind Up

Energy Markets Update

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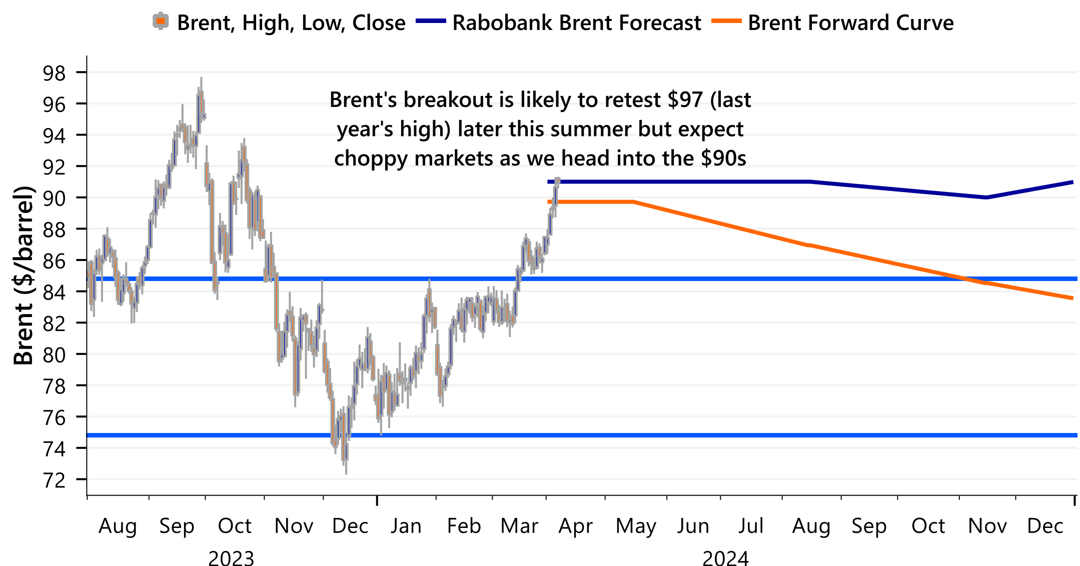
Summary

- A convergence of supply and demand factors are pushing crude oil markets upward. Furthermore, shorting energy is unattractive right now given the asymmetric risks from geopolitical issues. Barring a recession or financial panic, it is likely that crude and products will continue the grind upward. Selloffs are likely to be fast and short-lived.
- We expect Brent prices to average $91 for Q2-Q3 and $90 for Q4 2024, with a full year average of $89.5. We have raised our 2025 yearly average to $93.5 and 2026 to $98.75.
- We forecast WTI prices to average $87.25 for Q2-Q3 and $85.60 for Q4 2024, with a full year average of $85.5. We have raised our 2025 yearly average to $88.9 and 2026 to $93.75.
- Our NY Harbor ULSD estimates are little changed, averaging $2.91/gal for Q2-Q3 and $2.87/gal for Q4 2024, with a full year average of $2.88/gal. Furthermore, we slightly increased our 2025 yearly average to $2.95/gal and 2026 to $3.06/gal.
- Our estimates for ICE Gasoil are adjusted to account for supply concerns, now averaging $876/mt for Q2-Q3 and $860/gal for Q4 2024, with a full year average of $869/mt. As Europe remains reliant on imports and supplies are becoming more fraught, we increased our 2025 yearly average to $882/mt and 2026 to $918/mt.

All Signs Pointing Up For the Crude Complex, But Caveats Remain

Brent crude finally closed above the key psychological marker of $90/bbl, touching $89.99 as of the morning of April 3, then plowing through the next day up to $91/bbl! Additionally, front-month spreads settled on April 2 at $1.03, showing strong backwardation and implying imminent demand for crude at refineries.

Figure 1: Brent's next resistance points are $93 and $97/bbl. We forecast that $100 will be tested this year as supply lags behind demand. A pickup in US drilling will take 12-18 months to affect prices, so OPEC fragmentation around supply cuts is the major counter to the current trend



Source: Bloomberg, Rabobank

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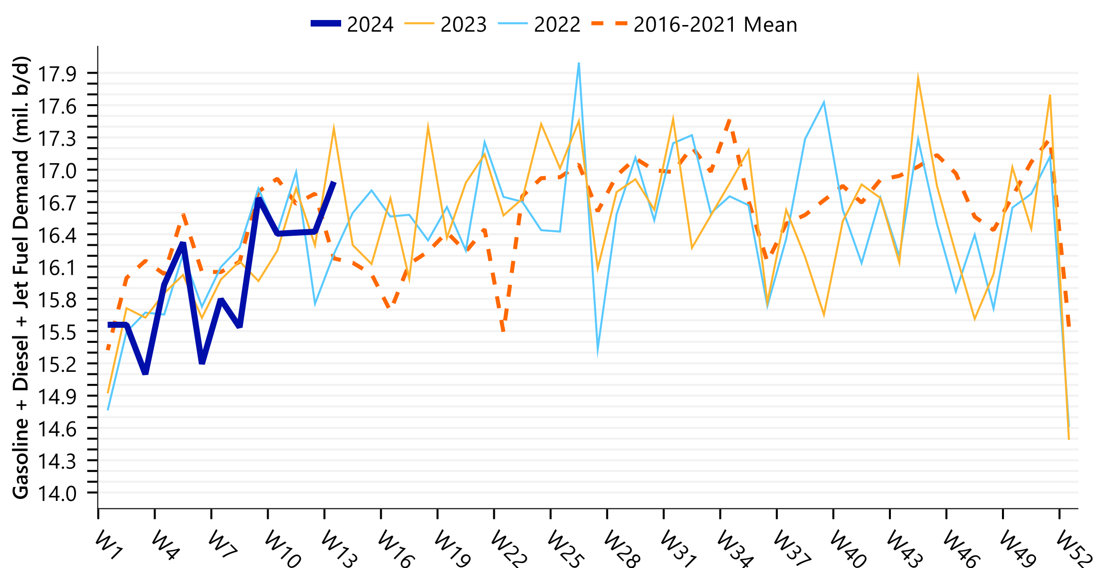
The constant grind upward since early December has been supported by OPEC+'s continued suspension of production and exports (2.2 million barrels a day), recently extended until the June 1st meeting. We believe the current cuts will be extended through the end of the year, one major part of our long term bullish thesis. A third factor is that US and Chinese gasoline demand data over the last weeks has been strong enough to push gasoline cracks close to $30/bbl, and we have seen corresponding draws in inventories. Jet fuel demand has recovered since the pandemic, hitting 6.5m b/d in the first week of April compared to 6.04m b/d for the same period in 2023 (figure 2).

Figure 2: After a rough January, recent overall US product demand is looking healthy, furthering support for higher prices across the complex



Source: Bloomberg, EIA, Rabobank

Due to the rise in prices, during the first week of April, the US Strategic Petroleum Reserve announced a delay to purchase 3 million barrels amid rising oil prices. The original plan from mid-March was to take delivery of crude for a Louisiana storage site in August and September when WTI was trading in the high $70s per barrel. Since the announcement, WTI and Brent have appreciated about $8. The Biden administration has a target to buy oil at $79 or lower to refill the strategic reserve, but it seems increasingly unlikely that they will be able to realize these targets.

For context: the Energy Department has attempted to replenish the emergency oil stockpiles after they reached a 40-year low in July 2023. This situation arose following the administration's sales of a record 180 million barrels in response to Russia's invasion of Ukraine throughout 2022 and 2023. As per EIA data, the current stockpile stands at about 363 million barrels, a significant decrease from nearly 600 million at the start of 2022. Since many SPR barrels were sold in the $90-100s/bbl range, it has been a solid trade for the government in the face of volatile market conditions. Going forward, this will likely keep the bottom in for the WTI market in the low $70s until levels are re-evaluated by the government.

Complicating the US balances is the recent announcement from Pemex, the Mexican state-controlled oil company, that cancelled contracts to supply its flagship Maya crude oil to refiners in the US, Europe, and Asia. The export cut coming at a time when OPEC and its allies are already curbing production. Many OPEC producers, we believe, are only able to keep production flat or declining slowly, and physical supplies of heavier, sour grades such as Maya or Arab Heavy from Saudi Arabia are in demand at the US Gulf Coast. This long term decline of conventional oil plays is a major pillar of our multiyear bullish forecasts for oil and products. Shale (tight) oil is the only source of growth from 2010 to the present, and total Estimated Ultimate Recovery (EUR) for shale wells has declined by nearly 50% since 2019. The scramble for oil is only just beginning.

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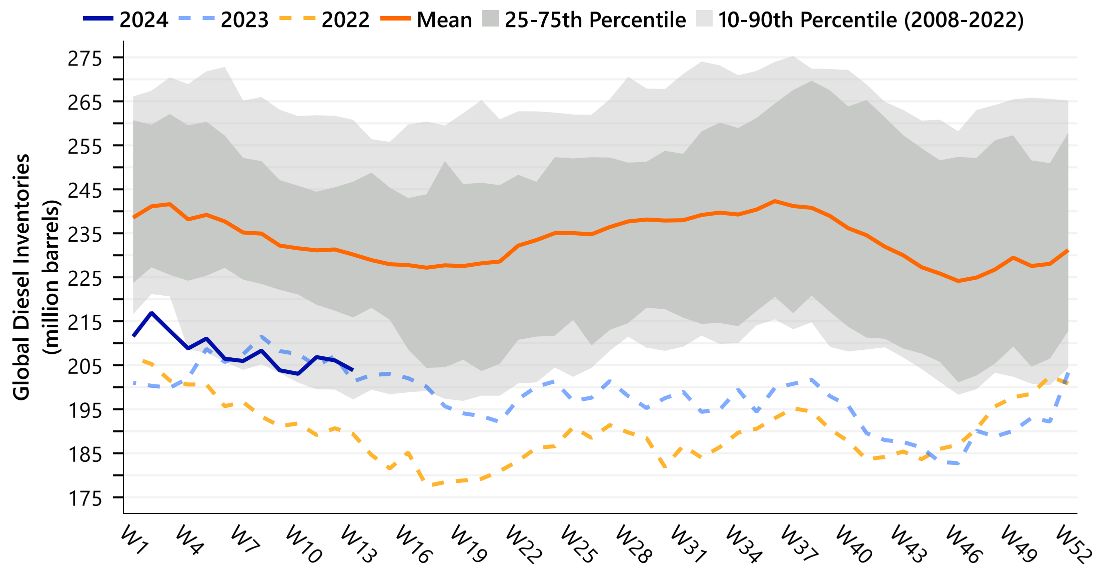
On the other side of supply, Russian is the ever-present grey area. Russian crude oil exports of 3.0-3.5m b/d remain concentrated, with the majority of tankers headed to China (1.3-1.5m b/d), India (1.1 to 1.5m b/d), and Turkey (400k b/d). The recent Ukrainian attacks on Russian refineries will hamper Russian diesel exports to these countries. This effect that will be more pronounced as the attacks continue and flows are redirected, pulling more Middle Eastern and US barrels to Brazil and other countries that do not take participate in the current sanctions.

Figure 3: Global diesel inventories remain ~23 million barrels below the long-term average, which keeps crack spreads elevated and crude demand robust



Source: Bloomberg, EIA, Intl. Enterprise Singapore, Insights Global, Japan Ministry of Economy, SHFE, Rabobank

Brent has some legs to continue running up, and we target $93 and $97 as the next ceiling. We expect a short-lived selloff within the next weeks, as long positions are close to multi-year highs and some profit-taking is in order. But the wider picture is bullish. Brent's 50-day moving average closed above the 200-day average on April 3, which is a classic technical indicator that will draw many CTAs and algos into the space. Further strength in gasoline, jet fuel, and diesel demand will continue to lift products prices, as all remain in deficit to seasonal averages, especially diesel (see figure 3).

Our forecasts have been revised due to these factors, and we expect Brent prices to average $91 for Q2-Q3 and $90 for Q4 2024, with a full year average of $89.5. We have raised our 2025 yearly average to $93.5 and 2026 to $98.75. We forecast WTI prices to average $87.25 for Q2-Q3 and $85.60 for Q4 2024, with a full year average of $85.5. Additionally, we have raised our 2025 yearly average to $88.9 and 2026 to $93.75.

The bull market for diesel will continue, and our NY Harbor ULSD estimates are little changed, averaging $2.91/gal for Q2-Q3 and $2.87/gal for Q4 2024, with a full year average of $2.88/gal. Furthermore, we slightly increased our 2025 yearly average to $2.95/gal and 2026 to $3.06/gal. We see opportunity in the highly backwardated market to take advantage of the gulf between the forward curve and our forecasts, given that new refinery supply coming online in the next years will have trouble meeting the consistently growing demand.

Our estimates for ICE Gasoil are adjusted to account for near-term supply concerns with European refineries, now averaging $876/mt for Q2-Q3 and $860/gal for Q4 2024, with a full year average of $869/mt. As Europe remains reliant on imports and supplies are becoming more fraught globally with the Ukrainian attacks on Russian refiners, we increased our 2025 yearly average to $882/mt and 2026 to $918/mt.

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