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[Feeder Cattle](#)
[Stocker Cattle](#)
[Cattle Feeding](#)
[Cattle Processing](#)
[Beef Retail](#)
[Partner Features](#)
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[Stocker Cattle Forum](#)
[Cattle Marketing Symposium](#)
[Cattle Identification Center](#)
[BVD Resources](#)
[Risk Management Center](#)
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[World News](#)
[Cattle Features](#)
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[Partner Feature Stories](#)
[Company News](#)
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 8/13/2007 1:29:04 PM



World Oil Outlook: Rising Consumption & Production Restraints Keep Prices Firm

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World Oil Outlook: Rising Consumption & Production Restraints Keep Prices Firm

Continued production restraint by members of Organization of Petroleum Exporting Countries (OPEC), rising consumption, and moderate increases in non-OPEC supply are keeping oil prices firm. The global oil balance for the remainder of 2007 has tightened since the last *Outlook* due to lower projections for world oil production and a larger projected Organization for Economic Cooperation and Development (OECD) stock draw in the second half of the year. This situation contrasts with conditions last year, when prices weakened in the second half due to slow consumption growth, rising global inventories, and the absence of hurricane-related oil supply losses. EIA projections for 2008 also point to a tight market, with higher consumption growth in 2008 than in 2007, moderate growth in non-OPEC supply, increased demand for OPEC oil, and limited surplus production capacity, held mostly in Saudi Arabia.

These tight conditions leave the market vulnerable to unexpected supply disruptions, especially as oil inventories are reduced over the coming months.

Consumption. World oil consumption grew at a moderate rate of 0.7 million barrels per day (bbl/d) in the first half of 2007 compared with year-earlier levels and was slowed in part by warmer-than-expected weather in Europe and Asia. However, EIA projects that world oil consumption will grow at a year-over-year rate of 1.8 million bbl/d during the second half of 2007 in response to continued economic growth with most of the oil consumption growth expected to come from China, the United States, and the Middle East. Problems with the Kashiwazaki-Kariwa nuclear power plant are expected to increase oil consumption in Japan through mid-2008 by an estimated 150,000 bbl/d. At the same time, EIA lowered its projection for 2008 world oil consumption growth from the last *Outlook* by 0.1 million bbl/d, reflecting the impact of higher oil prices ([World Oil Consumption Growth](#)).

Non-OPEC Supply. Non-OPEC production is projected to grow by about 690,000 bbl/d during 2007 compared with year earlier levels ([International Oil Supply Charts](#)). In 2008, EIA estimates that non-OPEC production will rise by roughly 1.1 million bbl/d. Increased production in the former Soviet Union, the United States, and Brazil are expected to more than offset declining production in a number of countries, including Mexico, Norway, and the United Kingdom. The 2008 non-OPEC supply growth forecast is 100,000 bbl/d higher than in EIA's previous *Outlook*, mostly due to higher growth projections for the United States (50,000 bbl/d) and Brazil (50,000 bbl/d).

OPEC Supply. Despite higher prices, OPEC officials have expressed a reluctance to raise production, pointing to high U.S. crude stocks and attributing high prices to refining bottlenecks, geopolitical tensions, and fund speculation. EIA's projection for OPEC crude production in third quarter 2007 has been lowered by about 0.3 million bbl/d from last month's *Outlook* to 30.5 million bbl/d. The change largely reflects an assumption that OPEC will delay increasing output from the third quarter of this year to the fourth quarter. Iraqi and Nigerian output have been constrained due to militant attacks, and at the end of July, shut-in production in Nigeria stood at 641,000 bbl/d, about 127,000 bbl/d less than a month earlier. OPEC plans to meet on September 11 in Vienna to re-examine its output levels.

The low level of surplus OPEC oil production capacity, which is primarily in heavy crude oil, remains a key reason for the continued tight market conditions. Despite production restraint by OPEC since last fall, the level of OPEC surplus capacity in the second quarter 2007 stood at 2.4 million bbl/d, most of it in Saudi Arabia, Kuwait, and the United Arab Emirates. Low surplus capacity is expected to remain in 2008, as expected increased demand for OPEC oil more than offsets expected capacity gains in a few countries, continuing to leave the market vulnerable to unexpected supply disruptions. Further, the apparent unwillingness by OPEC to use available surplus capacity in the face of rising crude oil prices reduces any downward price impact that additional surplus capacity might have.

Inventories. According to preliminary estimates, total OECD commercial inventories stood at 2.66 billion barrels at the end of June, near the seasonal average but down from the historically high levels seen last year. The shift in the market to backwardation (future prices are lower than current month prices) is a sign of a tight market and a disincentive to hold inventories, supporting an outlook for lower inventories in the months ahead. EIA projects that total third quarter OECD commercial inventories will experience a counter-seasonal 200,000 bbl/d stock drawdown, versus an average 290,000 bbl/d stock build experienced over the past 5 years. EIA projects that OECD commercial inventories (measured on a days-supply basis) will be in the low end of the 5-year range by the end of September. Even if OPEC raises output in the fourth quarter by roughly 0.5 million bbl/d (as we assume in our *Outlook*), inventories at year-end will be at the bottom of the 5-year range and remain there for the remainder of the forecast period ([Days of Supply of OECD Commercial Oil Stocks](#)).

Source: Short Term Energy Outlook

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