



# EY Price Point: global oil and gas market outlook

Q2 | April 2021



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## Q2 overview

At the close of last quarter, we asked two questions. The first was whether oil market confidence could be sustained until COVID-19 vaccination programs started to bend the curve on cases. The second was whether OPEC+ could maintain supply discipline until they did. The answer to both of those questions was a resounding “yes”, at least for now. From the beginning of January until the end of March, WTI and Brent prices increased steadily from near US\$50/bbl on New Years Day, to more that US\$65/bbl at the peak in mid-March. The recovery in prices has been carefully engineered by OPEC+, led by Saudi Arabia and at every opportunity, the organization has resisted the urge to bring production back online prematurely. In early January (and subsequently reaffirmed in March), Saudi Arabia committed to reducing production by 1 million barrels per day, a move that clearly triggered the positive sentiment we have seen since.

Recovery in the sector hasn't been confined to the upstream markets. A combination of refinery shutdowns and recovery in demand pushed margins up by 64% during the quarter. As of late March, the RBOB crack spread was trading above US\$20/bbl. In late October of last year, those contracts were barely trading above US\$11/bbl. The most dramatic story in the energy markets this quarter was the paralyzing cold wave in the US that brought the Texas power grid to its knees, but had only a marginal impact on global oil and gas markets.

The quarter began with high hopes for those who watched LNG markets in anticipation the long-awaited era of sustained pricing that would support new investment had finally arrived. Those market-watchers ended the quarter disappointed.



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## Q2 theme

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The theme for this quarter is **governed**. Apparent market balance at prices that could be sustainable is the product of calculated choices by market leaders and the cooperation of those who follow them. Economics played their customary role as well, with capital scarcity in North America taking about 2 million barrels per day out of the market, about half of the remaining gap in demand. While inventories are close to their pre-COVID-19 levels, there is still uncertainty. The resolution of the pandemic is in sight, but timing is unclear. Vaccine distribution in the US is having an impact but Europe is struggling to contain a third wave of infections. The taps have opened on economic stimulus, but it remains to be seen if policymakers have done enough or if they have overshot the mark.

The shape of the crude oil forward curve has fundamentally changed since the end of the last quarter. In late December of last year, the Brent forward curve was gradually increasing while today, the curve is backwardated. This is a clear sign that the market sees a short-term dynamic that is disconnected from the medium-to-long-term fundamentals. The lasting impact of the COVID-19 pandemic remains to be seen. While many have opined that COVID-19 marks a turning point in energy transition, the IEA recently released a five-year forecast of oil demand that shows steady growth, albeit at rates that are below historical expectations.

Gas markets are a paradox. At the Henry Hub and at LNG destinations, demand grows, investment lags and prices will occasionally attract attention. Traders, so far though, are unconvinced and futures prices don't indicate imminent scarcity at any link in the value chain.



- ▶ How long (if ever) will it take for crude oil demand to return to pre-COVID-19 levels?
- ▶ Will expansionary fiscal and monetary policy have the desired result or will it produce inflation and currency devaluation? How might that impact oil markets?
- ▶ Is upstream gas activity adequate to keep up with demand? What happens if it isn't?
- ▶ Will the market respond to the recent spike in LNG projects with new investment or will it wait and see?

## The journey to normal for crude oil inventories continues

Crude oil supply and demand both increased, but OPEC discipline ensures that the market remains undersupplied in the aggregate. A return to normal inventories is within sight.

## Capital spending higher, but still below sustainable levels

Although higher than 2020, capital spending plans are well below where they were before the COVID-19 pandemic. With demand returning to normal levels, there is a risk that supply won't keep up.

## Refining margins recovering

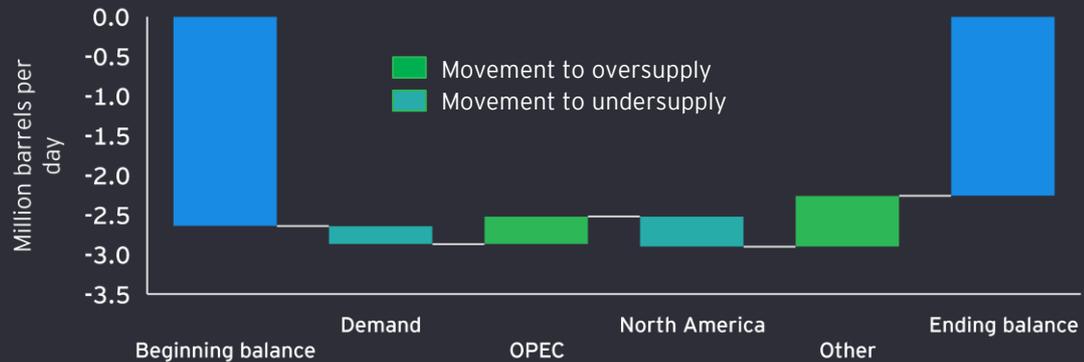
In the last (supply-driven) downturn, downstream businesses were a safe haven. In the latest (demand-driven) downturn, all points on the value chain were adversely impacted. However, refining economics improved this quarter.

## Investors increasingly focused on ESG matters

Going forward, attention to long-term value considerations and tangible actions to decarbonize will enable oil and gas companies' access to capital. Investor questions are becoming more frequent and pointed.

# Market fundamentals

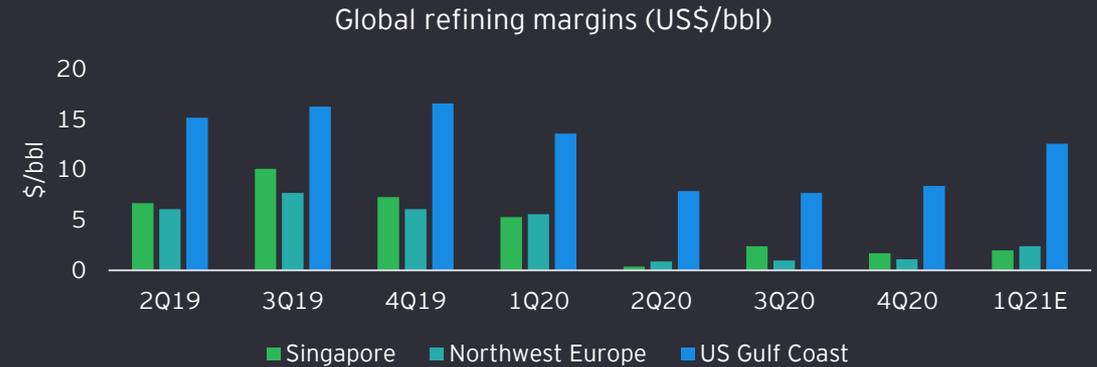
## Oil demand, supply and inventories approaching a balance



Source: US EIA

- ▶ In the first quarter, oil market balance continued to tilt toward an inventory draw. Demand crept up, OPEC and oil producers outside of North America increased output while the capital constrained North American producers reduced output.
- ▶ Going forward, we can expect continued gradual growth in demand and supply. Over time, as inventories draw down to where they were before the pandemic, producers will coordinate supply expansion at rates slightly higher than demand recovery until the market is balanced in real time.
- ▶ Economic forecasts are positive across the board. The most recent OPEC outlook projects the global economy to grow by 5.1%, up from previous forecast of 4.8%. The US Federal Reserve is equally positive, recently raising their estimate of economic growth in 2021 from 4.8% to 6.5%.
- ▶ OPEC expects that global oil demand is expected to expand by 5.9 million barrels per day (mmbpd) this year to reach 96.3 mmbpd in 2021, almost 3 mmbpd less than in 2019.

## Refining margins improving, but unattractive

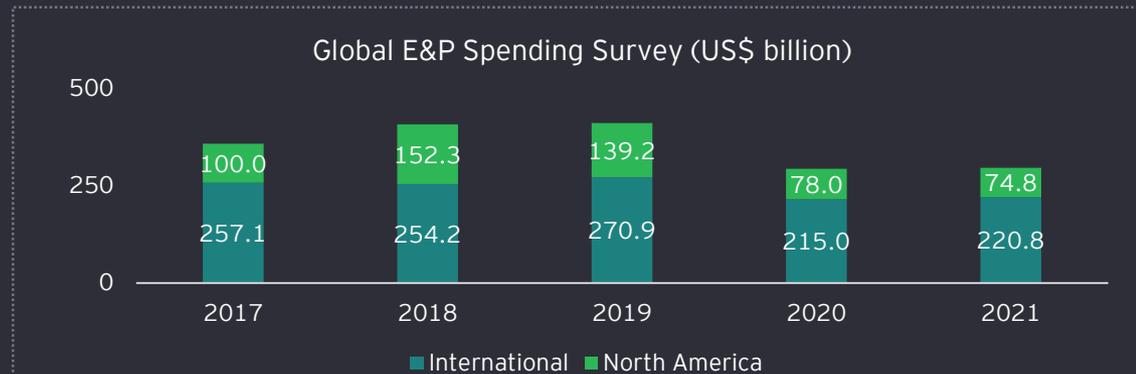


Source: Credit Suisse

- ▶ Fuel demand destruction caused refining margins to fall dramatically during the pandemic. In Q4 2020, refining margins in Europe and Asia were 82% and 77%, respectively, below Q4 2019 levels. The US landscape is slightly more positive. Q4 margins were only 50% below pre-COVID-19 levels, with extensive refinery closures and supply cuts partially offsetting demand reduction.
- ▶ Refining margins are likely to recover gradually in 2021, as the pandemic subsides and the demand for gasoline and (especially) aviation fuel picks up. Demand for liquids is expected to be within 1 mmbpd of pre-crisis levels by the end of 2021, and exports to emerging markets in Africa and Latin America could boost Gulf Coast margins.
- ▶ Recovery in refining margins can be enhanced by increased fuel demand during the back half of 2021, coupled with rationalization of refining capacity. The industry has already announced 4.1 mmbpd of effective and potential closures since 2020, and there could be more to come.
- ▶ The long-term outlook for refining continues to be unclear. The IEA expects liquids demand to grow for the next five years, but the geography and product mix will change.

# Market fundamentals

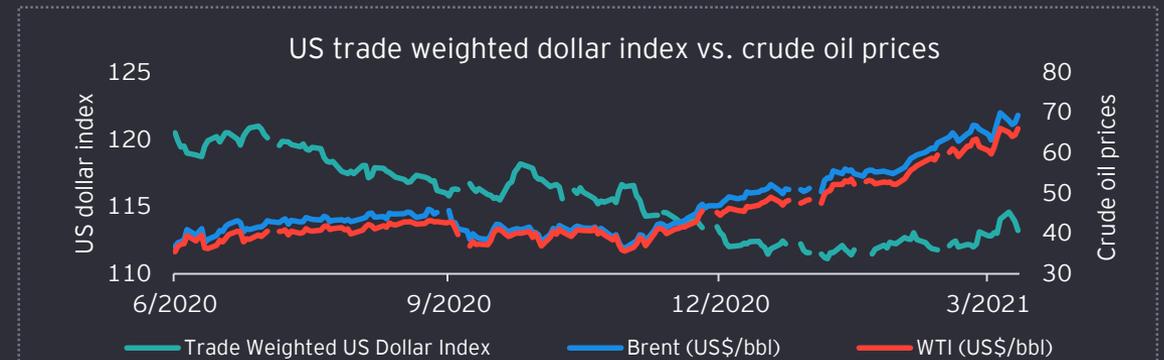
## Global upstream capital spending to marginally increase in 2021



Source: Barclays E&P spending survey, 5 January 2021

- ▶ 2021 will be a transition year as crude oil demand and prices stabilize. However, spending will remain restrained. The industry's benchmark E&P spending survey shows spending increasing slightly (1% up y-o-y) in 2021 after experiencing a 29% decline in 2020.
- ▶ Growth will be entirely driven by international markets such as Latin America (19% up y-o-y) and Russia (16% up y-o-y). North American upstream spending is expected to fall by another 4% in 2021 (after a 44% decline in 2020) with onshore US spending declining to nearly half of its pre-COVID level.
- ▶ Long-term uncertainty and increasing pressure from stakeholders for capital discipline has pushed companies to prioritize capital on critical assets and short-cycle projects. Reinvestment is at historic lows, with upstream spending projected to be less than 60% of 2021 cash flows.
- ▶ Oil and gas demand has recovered substantially and will continue to recover while inventories are expected to return to normal levels. When that happens, the market may be surprised to learn the impact of sustained capital spending reductions on supply capacity. Spot shortages and price spikes are a real possibility in the intermediate term.

## Stimulus, inflation and currency devaluation may impact oil prices

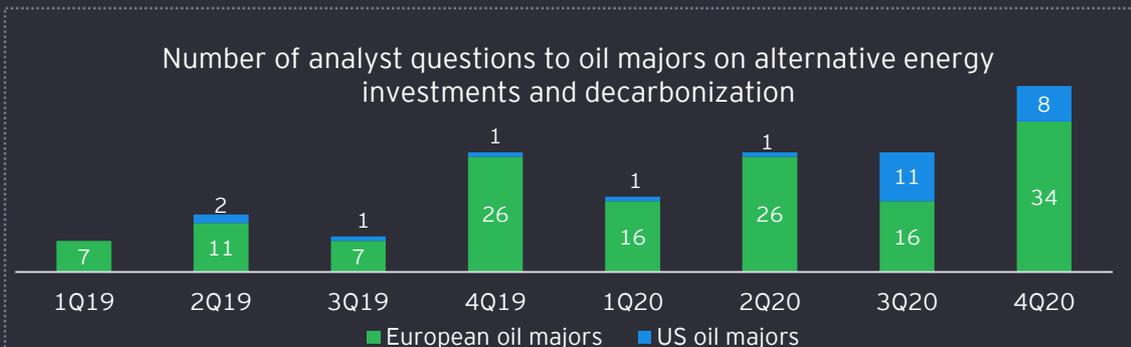


Source: US EIA and Federal Reserve Bank of St. Louis (FRED)

- ▶ Stimulus spending and accommodating monetary policy have been a central feature of government and central bank response to COVID-19 across the globe. In late October, the World Economic Forum reported that total government response has totaled over US\$11 trillion. Between the CARES Act, the most recent US\$1.9 trillion package and everything in between, the total US commitment has been over US\$5 trillion. The US Federal Reserve and its counterparts have bought new government debt liberally and have aggressively supported credit markets.
- ▶ Oil is denominated in US dollars everywhere and a falling dollar reduces the price of oil in local currencies and puts upward pressure on oil prices. In the last quarter of 2020, that effect was evident as the trade-weighted value of the dollar fell by 5.1% and the price of WTI crude increased by 25%. In the first quarter of 2021, the price of oil continued to surge while the value of the dollar stabilized.
- ▶ Economic analysts are still processing the short-run and long-run combined impact of the various economic interventions. Recently, the Federal Reserve raised its inflation forecast for this year from 1.8% to 2.4%, and the inflation rate implied by indexed treasury securities has gone up from 1.5% to 2.5% since the end of Q3 2020. Depending on what happens in other countries, further dollar devaluation could be on the horizon.

# Market fundamentals

## US majors respond to analyst concerns about energy transition

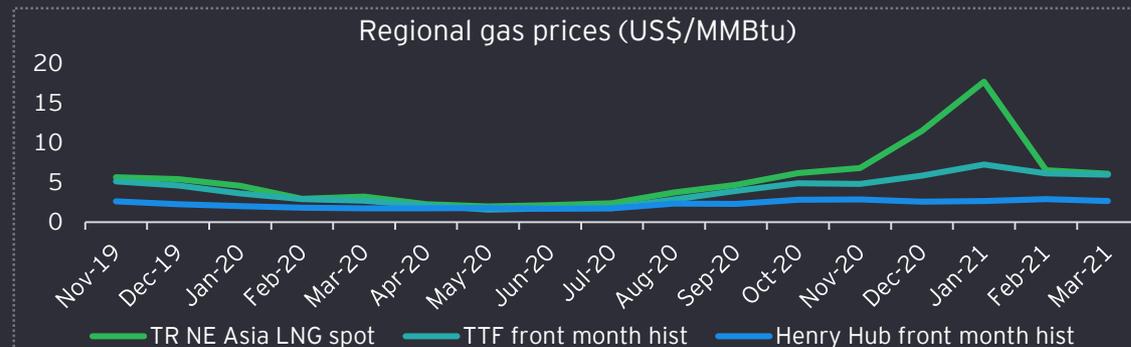


Source: EY analysis of quarterly earnings call transcripts  
 Note: Oil majors include BP, Chevron, ExxonMobil, Shell, Eni, Total and Equinor

- ▶ Until very recently, the oil industry's response to the energy transition has been a "tale of two hemispheres," with European majors acting aggressively to diversify into low-carbon businesses and US-based majors standing by their core business.
- ▶ Pressure on the US majors to change course comes from multiple directions. The Biden administration has announced that it intends to re-join the Paris Agreement, the US Energy Secretary used her first public appearance to urge companies to embrace energy transition, investment funds have stated their intention to redirect capital based on companies' performance against Environmental, Societal and Governance (ESG) metrics. Additionally, in the last round of earnings calls, the number of analyst questions to US oil majors related to decarbonization or alternative energy investments went from 1 in both 1Q20 and 2Q20, to nearly 10 in each of the last two quarters.
- ▶ Companies have responded to the pressure by announcing targets for scope 1 and scope 2 emissions. Time will tell how much of a difference these announcements will make. No US majors announced scope 3 targets or plans to make significant investment in low-carbon businesses.

Note: Scope 1 includes direct emissions such as fuel combusted at a refinery, Scope 2 includes indirect emissions from finished energy purchases such as purchased electricity used in facility operations. Scope 3 includes indirect emissions that are not included in scope 1 and 2, such as emissions due to the produced fuel used by end customers.

## Regional gas price spreads back to pre-pandemic levels

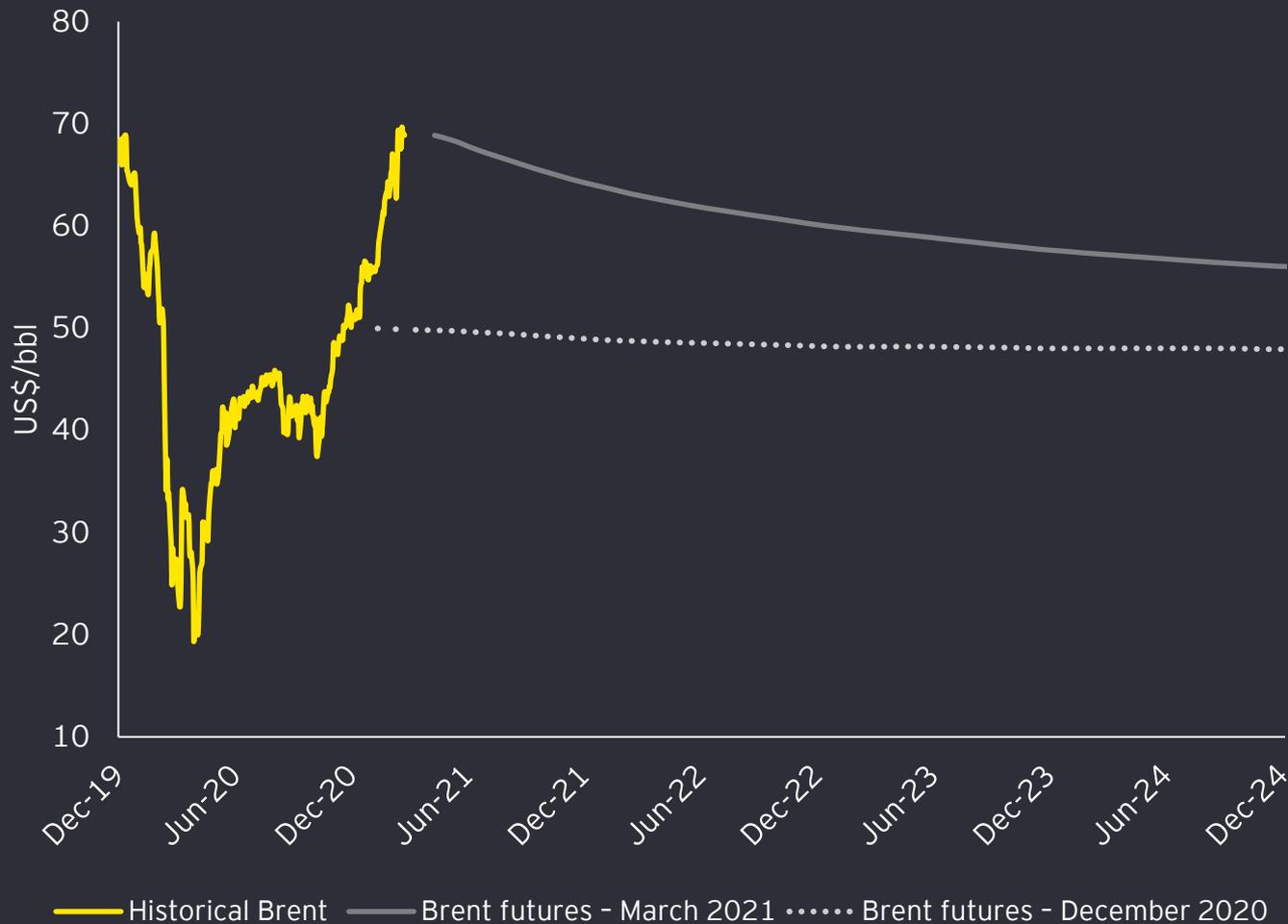


Source: Refinitiv

- ▶ The global LNG market is showing signs of rebalance. Regional gas price spreads reached record highs in January before returning to pre-pandemic levels in February and March. The spread between Asian LNG spot prices and US Henry Hub prices increased ~75x from US\$0.2/MMBtu in May 2020 to US\$15/MMBtu in January 2021 (the highest since 2016) and settled at US\$3.4/MMBtu in March 2021.
- ▶ The Asian market was driven by supply disruptions in January and lower-than-expected temperatures fuelling a surge in demand. Soft demand in February and March ensued and spot prices averaged US\$6.5/MMBtu and US\$6.1/MMBtu, respectively. Gas stocks in Europe have declined to 31% full (below the 5-year average), largely driven by LNG exports diverted to Asia. In contrast, the US gas prices have been stable for the past three months at an average price of ~US\$2.7/MMBtu.
- ▶ US LNG exports are expected to head to Europe in coming months as depleted European stocks have narrowed the spreads between Asian and European markets.
- ▶ Based on the financial statements of major LNG suppliers, we have estimated that a US\$6/MMBtu spread is necessary to support new investment. Notwithstanding, the post-pandemic price environment seems to be stimulating interest in new LNG projects, including the recent sanctioning of a large (32 mtpa) project in Qatar.



# Brent futures



Brent futures have increased in the short term given global COVID-19 vaccination programs coupled with the continued supply discipline of the OPEC+.

Going forward, there will be continued scrutiny on global vaccine distribution, changes in mobility patterns, decarbonization and actions by OPEC+ that will continue to impact medium- to long-term oil demand.

Futures data is effective as of 15 March 2021.

Source: Bloomberg

# Oil price outlook

**For both benchmarks, consultants (on average) forecast higher oil prices throughout the forecast period.**

Consultants focus primarily on the analysis of a long-term sustainable oil price, whereas banks and brokers balance their views on the basis of current market conditions.

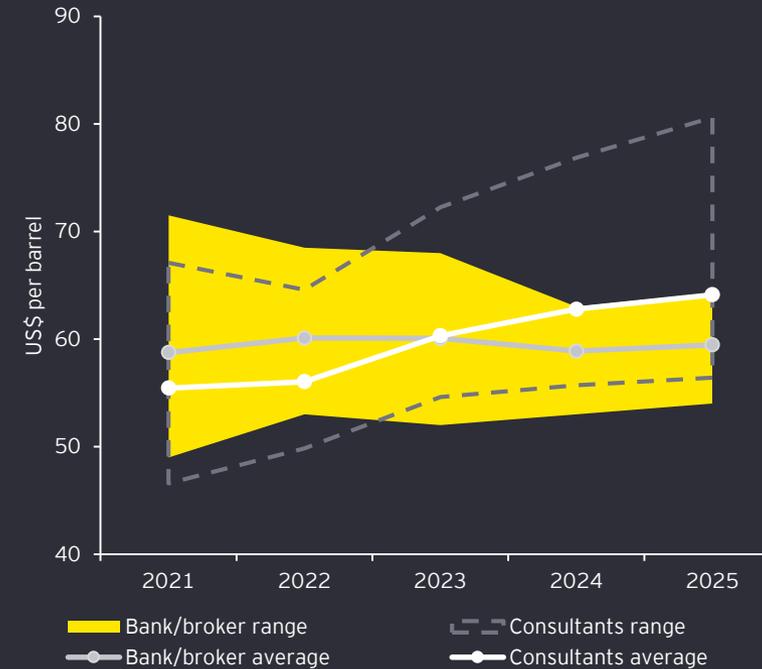
Consultant ranges include estimates of recognized market consultants. Where consultant estimates are updated only annually (for example, the EIA and the IEA), such estimates are included within the range of estimates from 2023 onward (or combined with short-term estimates published by the same consultant) to prevent near-term ranges being impacted by estimates that are not considered to reflect current market dynamics. Brent price estimates derived under the IEA's "Stated Policies" and "Sustainable Development" scenarios (inflation adjusted to reflect nominal pricing) are reflected within the consultant ranges from 2023 onward.

Consultant forecasts result in averages of US\$64.1/bbl and US\$59.2/bbl for Brent and WTI, respectively, in 2025.

This data is effective as of 15 March 2021.

## Brent

Bank/broker and consultant price estimates, ranges and averages



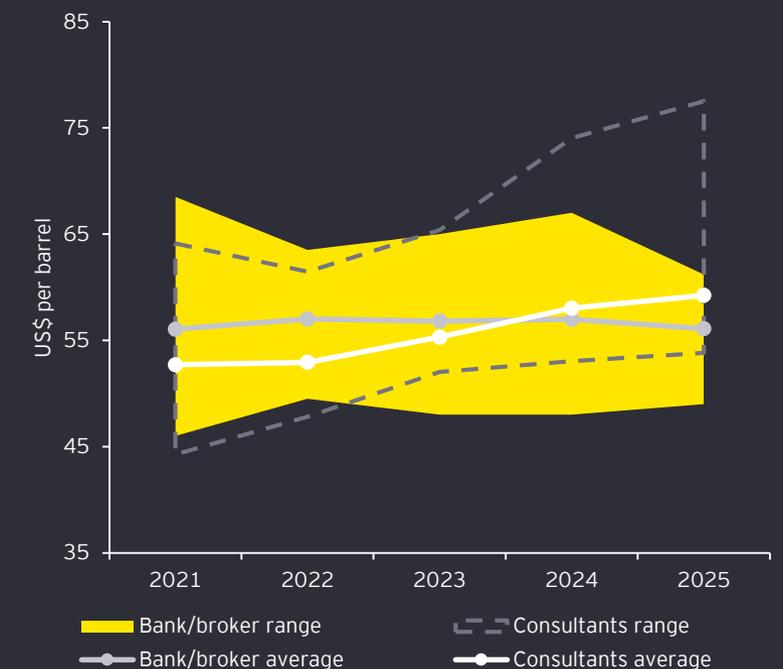
**Brent: US\$64.1**

Average price per bbl forecast in 2025 – consultants

Source: Bloomberg; bank/broker reports; consultants' websites and reports

## WTI

Bank/broker and consultant price estimates, ranges and averages



**WTI: US\$59.2**

Average price per bbl forecast in 2025 – consultants

Note: The wide range of long-term price estimates reflects the degree of uncertainty within the market. Both the lower and upper end of the range provided are supported by the estimates of credible market participants. Given the width of the range, the average of estimates should be used as a starting point for the assessment or generation of estimates.

# Gas price outlook

The banks and brokers forecasts (on average) are wider in the short-term than consultants for Henry Hub and NBP. The trend is reversed starting in 2024.

Consultants focus primarily on the analysis of a long-term sustainable gas price, whereas banks and brokers balance their views on the basis of current market conditions.

Consultant ranges include estimates of recognized market consultants. Where consultant estimates are updated only annually (for example, the EIA and the IEA), such estimates are included within the range of estimates from 2023 onward (or combined with short-term estimates published by the same consultant) to prevent near-term ranges being impacted by estimates that are not considered to reflect current market dynamics. Henry Hub price estimates derived under the IEA's "Stated Policies" and "Sustainable Development" scenarios (inflation adjusted to reflect nominal pricing) are reflected within the consultant ranges from 2023 onward.

NBP price estimates are scarce, with only six and four forecasts released by banks and brokers and consultants, respectively.

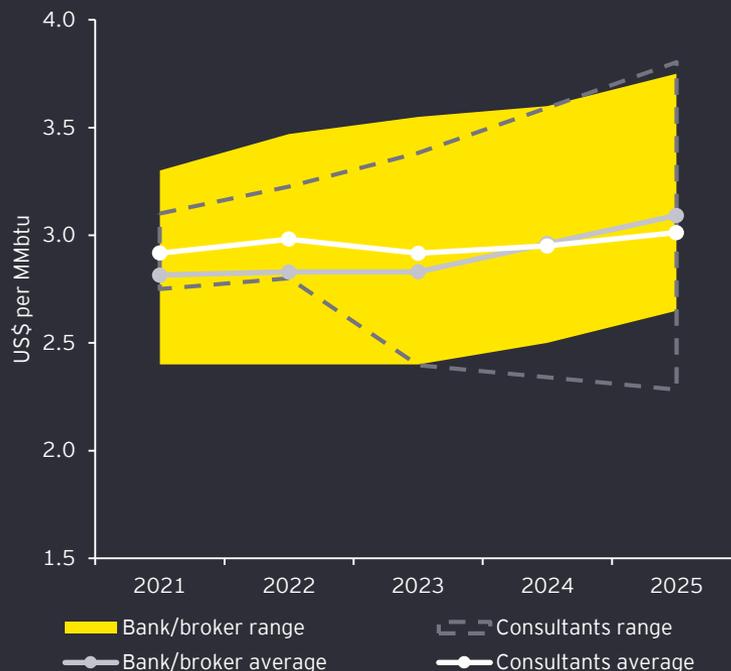
This data is effective as of 15 March 2021.

Note: The wide range of long-term price estimates reflects the degree of uncertainty within the market. Both the lower and upper end of the range provided are supported by the estimates of credible market participants. Given the width of the range, the average of estimates should be used as a starting point for the assessment or generation of estimates.

\*NBP: National Balancing Point

## Henry Hub

Bank/broker and consultant price estimates, ranges and averages



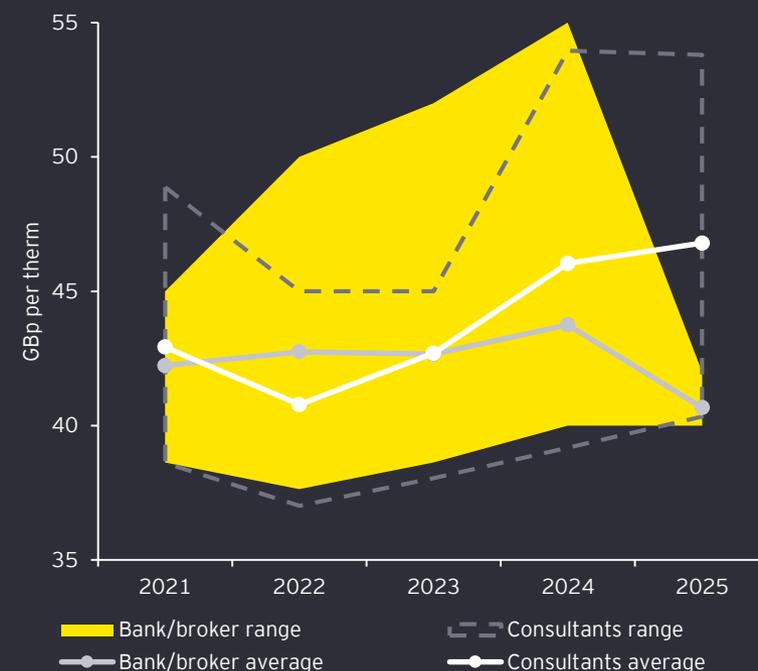
## Henry Hub: US\$3.0

Average price per MMBtu forecast in 2025 – consultants

Source: Bloomberg; bank/broker reports; consultants' websites and reports.

## UK NBP

Bank/broker and consultant price estimates, ranges and averages



## UK NBP: GBp46.8

Average price per therm forecast in 2025 – consultants

# Appendix

## Brent oil price estimates

This data is effective as of 15 March 2021.

Bank/broker	2021 (US\$/bbl)	2022 (US\$/bbl)	2023 (US\$/bbl)	2024 (US\$/bbl)	2025 (US\$/bbl)
High	71.5	68.5	68.0	63.0	64.3
Average	58.7	60.1	60.1	58.9	59.5
Median	58.9	60.5	60.0	60.0	62.0
Low	49.0	53.0	52.0	53.0	54.0

Source: Bloomberg; bank/broker reports

\*Certain price estimates included within the summary above may reflect real vs. nominal pricing as the bank/broker assumptions are not explicitly stated within Bloomberg or the respective reports.

Consultant	2021 (US\$/bbl)	2022 (US\$/bbl)	2023 (US\$/bbl)	2024 (US\$/bbl)	2025 (US\$/bbl)
High	67.1	64.6	72.2	76.9	80.6
Average	55.4	56.0	60.3	62.8	64.1
Median	55.6	55.0	58.5	60.7	62.0
Low	46.6	49.8	54.6	55.7	56.4

Source: Consultants' websites and reports; Oxford Economics

Note: Consultant ranges include estimates of recognized market consultants. Where consultant estimates are updated only annually (for example, the EIA and the IEA), such estimates are included within the range of estimates from 2023 onward (or combined with short-term estimates published by the same consultant) to prevent near-term ranges being impacted by estimates that are not considered to reflect current market dynamics. Price estimates derived under the IEA's "Stated Policies" and "Sustainable Development" scenarios (inflation adjusted to reflect nominal pricing) are reflected within the consultant ranges from 2023 onward.

# Appendix

## WTI oil price estimates

This data is effective as of 15 March 2021.

Bank/broker	2021 (US\$/bbl)	2022 (US\$/bbl)	2023 (US\$/bbl)	2024 (US\$/bbl)	2025 (US\$/bbl)
High	68.5	63.5	65.0	67.0	61.2
Average	56.1	57.0	56.8	57.0	56.1
Median	56.8	57.0	57.0	58.0	60.0
Low	46.0	49.5	48.0	48.0	49.0

Source: Bloomberg; banks and brokers reports

\*Certain price estimates included within the summary above may reflect real vs. nominal pricing as the bank/broker assumptions are not explicitly stated within Bloomberg or the respective reports.

Consultant	2021 (US\$/bbl)	2022 (US\$/bbl)	2023 (US\$/bbl)	2024 (US\$/bbl)	2025 (US\$/bbl)
High	64.1	61.5	65.4	74.0	77.5
Average	52.7	52.9	55.3	58.0	59.2
Median	53.5	52.0	53.7	56.5	55.8
Low	44.3	47.8	52.0	53.1	53.8

Source: Consultants' websites and reports; Oxford Economics; EY analysis

Note: Consultant ranges include estimates of recognized market consultants. Where consultant estimates are updated only annually (for example, the EIA), such estimates are included within the range of estimates from 2023 onward (or combined with short-term estimates published by the same consultant) to prevent near-term ranges being impacted by estimates that are not considered to reflect current market dynamics.

# Appendix

## Henry Hub gas price estimates

This data is effective as of 15 March 2021.

Bank/broker	2021 (US\$/MMBtu)	2022 (US\$/MMBtu)	2023 (US\$/MMBtu)	2024 (US\$/MMBtu)	2025 (US\$/MMBtu)
High	3.3	3.5	3.6	3.6	3.8
Average	2.8	2.8	2.8	3.0	3.1
Median	2.8	2.8	2.8	2.9	3.0
Low	2.4	2.4	2.4	2.5	2.7

Source: Bloomberg; banks and brokers reports

\* Where brokers have reported figures in US\$/mcf, we have used a conversion ratio of 1.037 for mcf conversion to MMBtu.

\*\*Certain price estimates included within the summary above may reflect real vs. nominal pricing as the bank/broker assumptions are not explicitly stated within Bloomberg or the respective reports.

Consultant	2021 (US\$/MMBtu)	2022 (US\$/MMBtu)	2023 (US\$/MMBtu)	2024 (US\$/MMBtu)	2025 (US\$/MMBtu)
High	3.1	3.2	3.4	3.6	3.8
Average	2.9	3.0	2.9	3.0	3.0
Median	2.9	3.0	2.9	2.9	3.0
Low	2.8	2.8	2.4	2.3	2.3

Source: Consultants' websites and reports; Oxford Economics

Note: Consultant ranges include estimates of recognized market consultants. Where consultant estimates are updated only annually (for example, the EIA and the IEA), such estimates are included within the range of estimates from 2023 onward (or combined with short-term estimates published by the same consultant) to prevent near-term ranges being impacted by estimates that are not considered to reflect current market dynamics. Price estimates derived under the IEA's "Stated Policies" and "Sustainable Development" scenarios (inflation adjusted to reflect nominal pricing) are reflected within the consultant ranges from 2023 onward.

# Appendix

## NBP gas price estimates

This data is effective as of 15 March 2021.

Bank/broker	2021 (GBp/therm)	2022 (GBp/therm)	2023 (GBp/therm)	2024 (GBp/therm)	2025 (GBp/therm)
High	45.0	50.0	52.0	55.0	42.0
Average	42.2	42.7	42.7	43.8	40.7
Median	42.9	42.0	40.0	40.0	40.0
Low	38.6	37.6	38.6	40.0	40.0

Source: Bloomberg; banks and brokers reports

\* Where brokers have reported figures in US\$/mcf, we have used a conversion ratio of 1.037 for mcf conversion to MMBtu and the brokers' forecasted FX rates.

\*\*Certain price estimates included within the summary above may reflect real vs. nominal pricing as the bank and broker assumptions are not explicitly stated within Bloomberg or the respective reports.

Consultant	2021 (GBp/therm)	2022 (GBp/therm)	2023 (GBp/therm)	2024 (GBp/therm)	2025 (GBp/therm)
High	48.9	45.0	45.0	54.0	53.8
Average	42.9	40.8	42.7	46.0	46.8
Median	42.1	40.6	43.9	45.5	46.5
Low	38.6	37.0	38.0	39.2	40.3

Source: Consultants' websites and reports; Oxford Economics

\*Where consultants have reported figures in US\$/MMBtu, we have used the particular consultants' forecast FX rate for the purpose of our conversion.

Note: Consultant ranges include estimates of recognized market consultants. Where consultant estimates are updated only annually, such estimates are included within the range of estimates from 2023 onward (or combined with short-term estimates published by the same consultant) to prevent near-term ranges being impacted by estimates that are not considered to reflect current market dynamics.

# Key contacts

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## Important notice

Price outlook data included in this publication is effective as of 15 March 2021. Given the rapidly evolving nature of the market and views of market participants, analysis can quickly become outdated. It should be noted that EY analysis is not for the purpose of providing an independent view of the outlook for oil and gas prices. Instead, we are collating the views of market participants.

Price outlook data should not be applied mechanistically. Instead, careful consideration should be given to the purpose of any value assessment, with price forecasts assessed in the context of other key assumptions, such as resources and reserves classification, production rates, discount rates and cost escalation rates, together with an appreciation of the key sensitivities in any such analysis.



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