OPEC at 50: Oil Market Modeling and Projections

Dermot Gately

Professor of Economics, New York University
and
Visiting Professor, King Saud University

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Overview

• Provide a quick retrospective of the world oil market for the past 50 years, reviewing the main aggregates: world oil demand, Non-OPEC supply, OPEC output and export levels, and crude oil price – disaggregating Non-OPEC into the OECD, the FSU, and the Rest of the World. We analyze how well OPEC did in achieving its own interests.

• Summarize and compare long-term projections to 2030, from Exxon-Mobil, BP, DOE, IEA, and OPEC: slowly growing demand, even slower growth in Non-OPEC supply, and a growing need for OPEC exports. We argue that projections of Non-OECD demand are too low, especially for the OPEC countries, and that higher prices (and/or slower income growth) will be needed in order to constrain demand growth to equal the slower growth of Non-OPEC supply and OPEC exports.
1. Retrospective: 1960-2010
OPEC and Non-OPEC, 1965-2009

OPEC and Non-OPEC

Ignore OPEC’s own oil consumption, which grew rapidly, from 1 mbd in 1965 to 8 mbd in 2009.

Quick summary:
• 1960-80: spectacular success
• 1981-85: kept price too high for too long, leading to disastrous loss of market share
• 1986-2004: two decades for OPEC to recover
• 2004-2011: big price increases needed to slow demand growth to equal slowly growing Non-OPEC & OPEC supply
World Oil Demand since 1971 in million barrels per day

The OECD and FSU consumed 86% of world oil in 1971, compared with only 61% today. Most of the demand reductions since 1973-74 were due to fuel-switching away from fuel oil (in electricity generation and space heating), especially in the OECD. In addition, the economic collapse of the Former Soviet Union (FSU) reduced their oil consumption substantially. Neither of these can be repeated.
World oil demand, per-capita (liters/day)

OECD

Former Soviet Union

World

Oil Exporters

Income Growers & Other Countries

China
Two oil-price quintuplings: much smaller price-responsiveness of oil demand in 1998-2008 than in 1973-84


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<tr>
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</thead>
<tbody>
<tr>
<td><strong>Crude Oil Price (2007 $/b)</strong></td>
<td>$16.01</td>
<td>$96.62 (1980)</td>
<td>504%</td>
<td>$17.32</td>
<td>$97.26</td>
<td>461%</td>
</tr>
<tr>
<td><strong>OECD</strong>&lt;br&gt;Real Income per capita (Th.$)</td>
<td>$14.3</td>
<td>$17.0</td>
<td>20%</td>
<td>$22.7</td>
<td>$27.3</td>
<td>20%</td>
</tr>
<tr>
<td><strong>Total Oil per capita (liters/day)</strong></td>
<td>7.27</td>
<td>5.98</td>
<td>-19%</td>
<td>6.66</td>
<td>6.33</td>
<td>-3%</td>
</tr>
<tr>
<td>Fuel Oil per capita (liters/day) (a)</td>
<td>3.28</td>
<td>1.89</td>
<td>-42%</td>
<td>1.52</td>
<td>1.06</td>
<td>-30%</td>
</tr>
<tr>
<td>Fuel Oil share of Total OECD Oil</td>
<td>45%</td>
<td>32%</td>
<td></td>
<td>23%</td>
<td>17%</td>
<td></td>
</tr>
<tr>
<td>Transport Oil per capita</td>
<td>2.60</td>
<td>2.71</td>
<td>4%</td>
<td>3.45</td>
<td>3.71</td>
<td>8%</td>
</tr>
<tr>
<td>product share of Total Oil, OECD</td>
<td>36%</td>
<td>45%</td>
<td></td>
<td>52%</td>
<td>59%</td>
<td></td>
</tr>
<tr>
<td>OECD share of Total World Oil</td>
<td>73%</td>
<td>63%</td>
<td></td>
<td>63%</td>
<td>56%</td>
<td></td>
</tr>
<tr>
<td>OECD Fuel Oil share of Total World Oil</td>
<td>33%</td>
<td>20%</td>
<td></td>
<td>14%</td>
<td>9%</td>
<td></td>
</tr>
<tr>
<td><strong>Non-OECD</strong>&lt;br&gt;Real Income per capita (Th.$)</td>
<td>$2.3</td>
<td>$2.9</td>
<td>27%</td>
<td>$3.5</td>
<td>$5.8</td>
<td>66%</td>
</tr>
<tr>
<td>Total Oil per capita (liters/day)</td>
<td>0.78</td>
<td>0.94</td>
<td>20%</td>
<td>0.92</td>
<td>1.14</td>
<td>23%</td>
</tr>
<tr>
<td>Residual Oil per capita (liters/day) *</td>
<td>0.27</td>
<td>0.30</td>
<td>12%</td>
<td>0.21</td>
<td>0.18</td>
<td>-17%</td>
</tr>
<tr>
<td>Residual Oil share of Total Non-OECD Oil</td>
<td>32%</td>
<td>31%</td>
<td></td>
<td>23%</td>
<td>16%</td>
<td></td>
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<td>Non-OECD share of Total World Oil</td>
<td>27%</td>
<td>37%</td>
<td></td>
<td>37%</td>
<td>44%</td>
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<tr>
<td>Non-OECD Residual Oil share of Total World Oil</td>
<td>9%</td>
<td>12%</td>
<td></td>
<td>8%</td>
<td>7%</td>
<td></td>
</tr>
<tr>
<td><strong>World</strong>&lt;br&gt;Real Income per capita (Th.$)</td>
<td>$5.1</td>
<td>$5.9</td>
<td>16%</td>
<td>$7.2</td>
<td>$9.8</td>
<td>35%</td>
</tr>
<tr>
<td><strong>Total Oil per capita (liters/day)</strong></td>
<td>2.37</td>
<td>2.05</td>
<td>-13%</td>
<td>2.05</td>
<td>2.11</td>
<td>3%</td>
</tr>
<tr>
<td>Residual Oil per capita (liters/day) (b)</td>
<td>0.66</td>
<td>0.45</td>
<td>-32%</td>
<td>0.31</td>
<td>0.23</td>
<td>-24%</td>
</tr>
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<td>Residual Oil share of Total World Oil</td>
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<td>22%</td>
<td></td>
<td>15%</td>
<td>11%</td>
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2. Long-term projections to 2030

Latest projections of prices and quantities published by the major institutions:

Exxon-Mobil, BP, DOE, IEA, and OPEC
Differences & Similarities in Projections:

1. Demand projections are very similar for all.
2. IEA projects lower Non-OPEC supply than others, especially DOE. Hence the demand for OPEC exports is highest for IEA and lowest for DOE.
3. OPEC projects lower prices than others.
2a. Why these long-term projections of demand (& thus of price) may be too low:

DOE has consistently under-predicted Middle East oil consumption
2a. Why these long-term projections of demand (& thus of price) may be too low:

Saudi Arabia’s Domestic Oil Demand

Total Oil

LPG, Naphtha & Other Oil

Resid.

Gasoline, Jet Fuel & Light Fuel Oil

<table>
<thead>
<tr>
<th>Year</th>
<th>Gasoline, Jet Fuel &amp; Light Fuel Oil</th>
<th>Resid.</th>
<th>LPG, Naphtha &amp; Other Oil</th>
<th>Total Oil</th>
</tr>
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<tbody>
<tr>
<td>1971</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1976</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>1981</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>1986</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>1991</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>1996</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>2001</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>2006</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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</tbody>
</table>
Saudi Arabia’s Domestic Oil Demand

Total Oil demand is growing faster than income.

Non-Residual Oil demand is growing twice as fast as income.

2a. Why these long-term projections of demand (& thus of price) may be too low:
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DOE projects OPEC oil consumption to grow to 10.8 mbd in 2030, less than half as fast as income – much more slowly than in the past.

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![Graph showing OPEC oil consumption and OPEC Real Income over time with projections for 2030.](image-url)
2a. Why these long-term projections of demand (& thus of price) may be too low:

Projections of per-capita oil liquids demand to 2030 using DOE Ref. Case assumptions for crude oil prices & income growth:

DOE projections (104 mbd in 2030)

DOE: Next time it’s different.

Annual % growth in per-capita demand: 2.54% historically, but only 0.56% in future (despite faster income growth)
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Projections of per-capita oil liquids demand to 2030 using DOE Ref. Case assumptions for crude oil prices & income growth:

DOE projections (104 mbd in 2030) and Dargay-Gately projections (134 mbd)

DOE projections:

- Next time it’s different.
- Annual % growth in per-capita demand: 2.54% historically, but only 0.56% in future (despite faster income growth)

Dargay-Gately: Next time will be like last time: 2.5% annual growth.


King Saud University and KAPSARC
Dermot.Gately@NYU.edu
2b. How well have consensus long-term projections done in the past – say projections to 2020 from 2001 – how well did they do?
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Projections to 2020 from 2001: how did they do?

Projections to 2020 from 2001: DOE Reference Case
What was my reaction in 2001 to these projections – of OPEC doubling its output to 60 mbd by 2020, with flat or declining prices – by all the most authoritative institutions?
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Wimbledon, 1981

http://www.youtube.com/watch?v=ekQ_Ja02gTY

What was wrong with the long-term projections from 2001 – in which OPEC would double its output to 60 mbd by 2020?

These institutions did **NO** analysis of whether the projected doubling of OPEC output levels made sense for OPEC.

- What incentive did OPEC have to expand its output as rapidly as projected? It was NEGATIVE!
- Might OPEC be better off if instead it did not expand its output so rapidly and just let price increase? Yes, definitely.

See articles by Gately in **Energy Journal**:

(2001): “How Plausible is the Consensus Projection of Oil below $25 and Gulf Output Doubling by 2020?”

(2004): “OPEC’s Incentives for Faster Output Growth”

(2007): “What oil export levels should we expect from OPEC”
Conclusions about OPEC exports

• We should not rely upon OPEC’s export-share of non-OPEC demand increasing, or even remaining constant.
• We might not even be able to count upon OPEC being able to maintain its level of oil exports.
• OPEC’s own oil consumption is likely to grow much faster than is projected by DOE and IEA, perhaps as fast as OPEC income. Now at 8 mbd (nearly 25% of OPEC output), it could grow to 18 mbd by 2030 if it grows as fast as OPEC income, as it has since 1987. That would be 40% to 50% of OPEC production by 2030, greatly constraining OPEC’s ability to increase oil exports.
Conclusions about OPEC exports

• We could see a future in which OPEC investment in capacity expansion is too slow and the world’s need for OPEC oil goes unmet.

• Sharply higher prices that overshoot a long-term equilibrium path could be the short-term result, together with lower economic welfare worldwide.

• We could witness low-cost oil reserves in OPEC remaining underutilized while high-cost substitutes are over-utilized elsewhere – in economically wasteful cycles.
Thank you