Opinion **Markets Insight**

Oil industry faces biggest crisis in 100 years

Producers are facing up to the crash in oil demand as coronavirus forces economies into hibernation

DAVID SHEPPARD

The oil price crash has come at the worst time possible for an industry that was already out of favour with investors © AP

David Sheppard 6 HOURS AGO

It is no exaggeration to say the oil industry faces its gravest crisis of the past 100 years.

As western economies go into hibernation, hoping to snuff out the first wave of coronavirus through lockdowns and isolation, the industry is facing up to the fact that fuel demand is going to fall faster than ever before.

Already prices have roughly halved since the start of this month as airlines have been grounded and millions of commuters eschew the car for a short walk to a laptop on their kitchen table.

For an industry long aware that a 1-2 per cent swing in the balance of supply and demand can be the difference between prices soaring or collapsing, the extent of the fall in consumption is hard to process.

As Europe and North America hunker down, the latest estimates suggest 10 to 25 per cent of global consumption could vanish in the coming few months. In normal times the world consumes some 100m barrels a day.

Such is the scale of the demand collapse that it risks overshadowing the price war between Saudi Arabia and Russia, who are flooding the market with unnecessary barrels after falling out over how to respond to the crisis. But there is little doubt their actions have exacerbated the crash and lengthened the timeline of recovery.

The result is likely to be storage tanks being filled to the brim within months. Even supertankers at sea, called into action as emergency storage vessels, could be maxed out by the end of summer.

Respite will come only once the most expensive oil production starts to shut down, or the weakest producers go bust.

But oilfields cannot be turned off and on like the flick of a light switch. The cost and the risk of shutting down active production is more likely to lead to a war of attrition.

Crude dipped below $25 a barrel last week, its lowest level since 2003, before regaining some ground to trade around $28 on Tuesday. Analysts are starting to predict the price could fall to the teens or even into single digits.

Large-scale lay-offs, already shooting higher in leisure industries, will not be far behind for the energy sector, with scattered reports of contractors already being let go.

The crash has come at the worst time possible for an industry that was already out of favour with investors, who fear that oil demand will peak in the next decade or so and worry about environmental impacts.

The few hardy investors who stuck with the energy majors have been burnt once again. BP's share price is down more than 50 per cent this year to a level last seen in 1995, sinking below even the depths of the Macondo disaster when the company's very survival was in doubt.

ExxonMobil, once the world's biggest publicly listed company, has lost 70 per cent of its market value over the past six years.

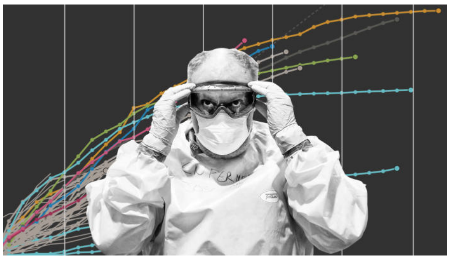
If the short-term outlook for the industry is, frankly, a hellscape, the long-term outlook is arguably not that much better. The pandemic could leave a mark on already stuttering oil demand growth. International travel will take time to recover. Companies and employees who adapt successfully to working from home are likely to make it a bigger part of their future, keeping more cars off the road.

That leaves the industry with little to pitch beyond medium-term hopes that the sheer size of the price crash will ultimately starve competitors of so much investment that production falls short and prices rise.

But a recovery bookended by disaster, from the latest crash to peak demand, is unlikely to be considered particularly compelling.

In that context BP's decision to stick with its commitment to accelerate into the energy transition makes perfect sense, despite naysayers arguing the price crash would weaken the company's resolve. To attract new investors it is no longer enough to defend the dividend. The industry needs a new narrative.

Editor's note



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National oil companies, too, are left surveying the ashes.

Saudi Arabia has pretty much torched its own carefully cultivated image as a reliable steward of the oil market. Even if the kingdom emerges victorious from the price war with a bigger share of a soon-to-be-shrinking market, political allies will see confirmation that warm words about stability mean little under the leadership of Crown Prince Mohammed bin Salman.

For some the oil industry might seem a deserving victim. Its arrogance over climate change — only partially reversed in recent years — has cost it many sympathisers. But you do not have to think charitably towards the sector to realise there is a tragedy in waiting.

Opec's weakest members, such as Iraq and Nigeria, haunted by the oil curse that has sown corruption and inefficiency throughout their economies, face a huge cash crunch.

If the price slump means these poorest producers struggle to fund their own national responses to the pandemic, the crisis for them will be felt most keenly of all.