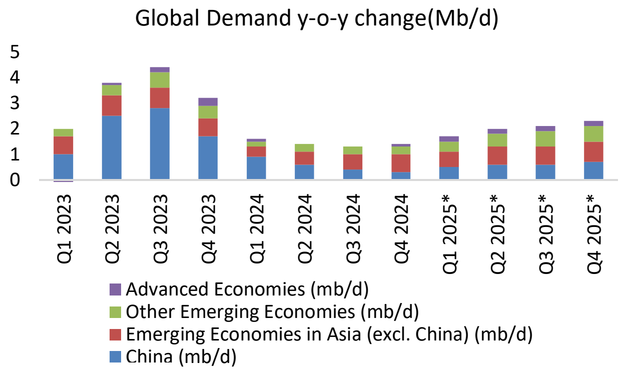
"China's Economic Pulse: Steering Global Oil Markets"

17nd Sep 2024

Oil markets are facing a new world without the Chinese bullish story, and the consequence is leading to Brent prices falling drastically from $82 to $70 as China recovery story delay is disappointing investors. China has been the cornerstone of the growth in global oil demand so far this century. Dynamic factory activity, massive infrastructure investments and rising prosperity across a population of over 1 billion people driving what has, at times, felt like an inexorable expansion in oil consumption.

Over the past decade, the annual increase in Chinese oil demand has averaged in excess of 600 000 b/d, accounting for more than 60% of the total global average increase. Moreover, China's share of global demand growth has expanded since the pandemic.

This year, demand outside China will remain 0.3% below 2019 levels, but in China, consumption will be 18% higher. Now, the world's oil demand growth is slowing sharply from its post-pandemic rebound. This is largely coming from decelerating growth in China- which has long been a driver of global oil demand.



Source: RTRS

China's economic path is deeply interconnected with global oil markets, where economic upswings tend to push oil prices higher, while slowdowns typically result in reduced demand and lower prices. Participants are keeping a close eye on Chinese economic indicators, such as industrial production and GDP growth, to predict potential changes in oil prices. As China faces its economic challenges and explores new opportunities, the global oil markets are expected to react accordingly.

China's economic outlook is bleak, with its property market stagnating and consumer confidence faltering as the country grapples with a slow recovery from the pandemic-induced downturn. Chinese oil demand is currently firmly in contraction, falling by 1.7%, or 280 000 b/d, year-on-year in July, a marked contrast with the 9.6% average pace of growth in 2023. Accordingly, the annual growth is expected of only 1.1%, or 180 000 b/d, in 2024.

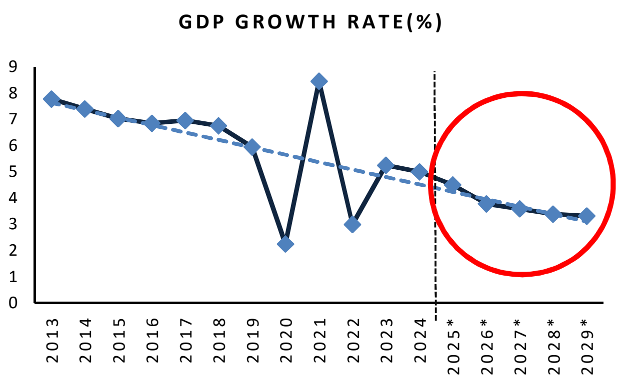
The main areas for slowdown in China:

- The rising domestic sales of vehicles powered by alternative fuels are significantly reducing oil demand for road transportation.
- The expansion of China's vast high-speed rail network is curbing growth in domestic air travel
- The market share of battery and plug-in hybrid electric vehicles has surged, with over half of all cars sold in China during July and August being electric
- A growing number of new trucks are also running on natural gas or electricity. These shifts are expected to cut oil demand growth by around 400,000 Bpd this year alone.

- A slowdown in construction investment, linked to a prolonged real estate slump, is further dampening demand.
- Building activity is gradually tapering off and has impacted gasoil, the primary fuel for construction machinery and material transport, with overall gasoil demand declining nearly 5% year-on-year in Q2 2024

With China's oil demand growth losing momentum and only modest increases or even declines in many other nations, current trends support the view that global oil demand may reach a plateau by the end of this decade. The industrial output growth slowed to a five-month low in August, while retail sales and new home prices weakened further. Oil refinery output also fell for a fifth month, as disappointing fuel demand and weak export margins curbed production.

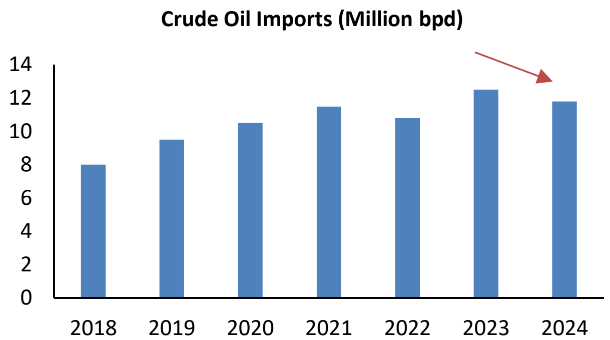
Meanwhile, China boosted crude oil inventories in August by the biggest amount in 14 months, confirming that the rebound in imports was driven by stockpiling and not by any recovery in fuel consumption. These are the biggest flows since July 2023 when 2.1 Mbpd was added to stockpiles, and was also a sharp increase from the 280,000 bpd added in July. Currently, China has added 1.85 Mbpd to either commercial or strategic storages.



Source: RTRS

The only viable option to close gap between consumption and production growth is either by boosting investment, though economy faces challenges in absorbing it due to high levels of debt-fueled, unproductive investments, or by increasing its trade surplus.

However, this second path is becoming less feasible as the rest of world grows increasingly resistant to accommodating larger Chinese trade surplus. If China's long period of economic expansion is indeed slowing down, and with demand in advanced economies currently at 2014 levels and expected to decline, question arises whether any other countries or regions could take China's place as driving force behind global oil demand growth.



Source: RTRS

India, which is projected to have the largest annual increase in oil consumption in 2024 at 200,000 Bpd, is expected to contribute nearly half of medium-term oil demand growth in emerging Asia. However, despite being world's fastest-growing major economy, India's overall oil consumption is relatively limited, reaching only one-third of China's level in 2024. China now looks unlikely to be the behemoth for oil demand and perhaps even for other commodities that it once was and Chinese government will not allow economic growth to collapse, but growth will no doubt be lacklustre for the foreseeable future. Prices are expected to stay lower and correct towards levels of Rs. 5500 in coming months. Prices might get temporary support from triggers like OPEC+ cuts, FED rate cut but demand concerns will continue to dominate the fundamentals and push prices lower.

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