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POTEN TANKER OPINION

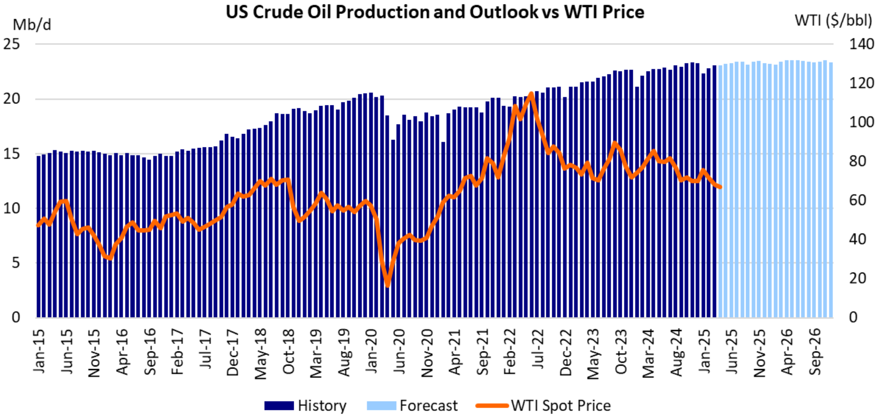
'Drill, Baby, Drill' With Low Oil Prices?

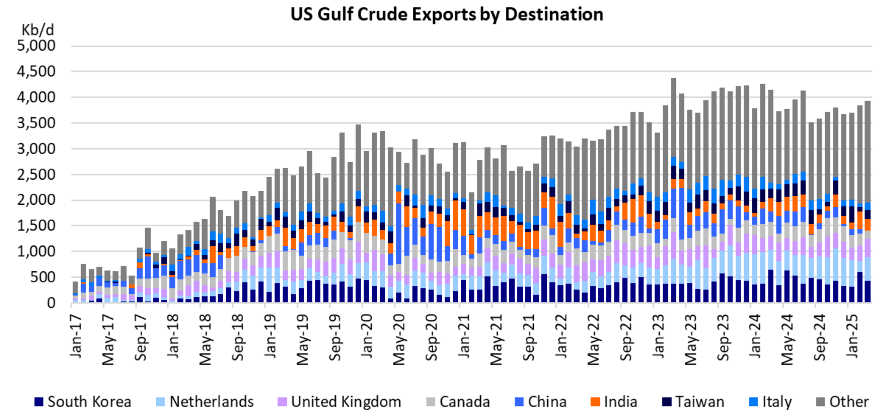
How will U.S. goal of energy dominance deal with low oil prices?

U.S. crude oil production has grown rapidly over the last decade, even though there were some setbacks along the way. During the COVID driven demand and oil price crash, which was further exacerbated by Saudi Arabian production increases, U.S. production dropped from around 20.5 million barrels per day (Mb/d) in January 2020 to 16.2 Mb/d by April 2020. While the current situation is very different from 2020, the combination of growing uncertainty about short term oil demand, due to economic uncertainty and the production increases announced by OPEC+ have caused oil prices to decline by more than $12 over the last week. This weekly opinion will take a look at what this might mean for U.S. crude oil production and exports.

President Trump came into office with a promise to increase energy production by loosening regulations that slow production growth and by other measures, such as providing easier access to Federal lands for oil and gas production. He is trying to implement these policies through executive orders, some of which may be challenged in courts. However, in contrast to some other oil producing countries, the U.S. government does not drill wells and produce oil and gas. In the U.S., private companies are the ones performing such work and they will only do so if these activities are profitable. Prior to the COVID price crash in 2020, many of these companies were focused on maximizing production as investors rewarded growth over profitability. However, they learned a lesson during the crash as many of the producers went bankrupt and assets were sold to competitors. So, during the recovery after 2020, the focus switched to profitability and shareholder returns. Cash flow was returned to investors in the form of dividends and share buybacks, rather than reinvested into maximizing production growth.

The oil price decline over the last week was caused by the fallout of the tariff announcement by President Trump that triggered panic in the financial markets and heightened fears of a recession in the U.S. and other countries. This tariff announcement was followed by a statement from OPEC+ that they would increase oil production by 411 Kb/d in May, about three times the anticipated increase. On Wednesday, President Trump announced that he would pause the implementation of the 'Reciprocal tariffs' by 90 days on most countries, which led to a partial recovery of oil prices, but on Thursday WTI had fallen back to $60/bbl. Overall, the risk of a recession remains elevated due to increased policy uncertainty, which makes it hard for companies to decide on investment and hiring strategies. Under these circumstances, many companies decide to hold onto their cash and wait.





Source: EIA, Vortexa

Several oil analysts have revised down their oil demand outlook for 2025. The EIA delayed the publication of their Short-Term Energy Outlook to recalculate their demand outlook. In their April edition, they lowered the global oil demand outlook by 400 Kb/d for 2025 and their WTI price for 2026 is now $57/bbl, down from $65/bbl. Morgan Stanley also reduced their base case demand outlook by 550 Kb/d.

Shale oil production is more sensitive to oil prices than most conventional fields as the decline rate is higher so continuous investments are required to maintain or increase production levels. The Dallas Fed regularly surveys oil producers and asks them what oil price they need to drill new wells. In the latest survey the average response was a WTI price of $62 per barrel, which is higher than the current price. Low prices put current production levels at risk and makes it likely that U.S. production will decline in the second half of this year.

Lower shale oil production would put U.S. oil exports at risk. However, some countries may be looking at energy purchases from the U.S. to improve their trade balance and limit tariffs on their exports to the U.S. As a result, more crude could be shipped to Korea and to Japan, while exports to China might be reduced. Lower U.S. production and exports would balance the OPEC+ increases that are planned. Trade flows will change as a result. However, there are too many variables and uncertainties to draw any clear conclusions with respect to the implications for the freight market.