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CRUDE OIL: WHY PRICES WON'T FALL OFF THE SHELF

A Generational Moment for Commodity Trading Strategies
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Why Crude Oil Prices Won't Fall off the Shelf

As U.S. shale revolution ebbs, battle-scarred oil producers are protecting their free cash flow

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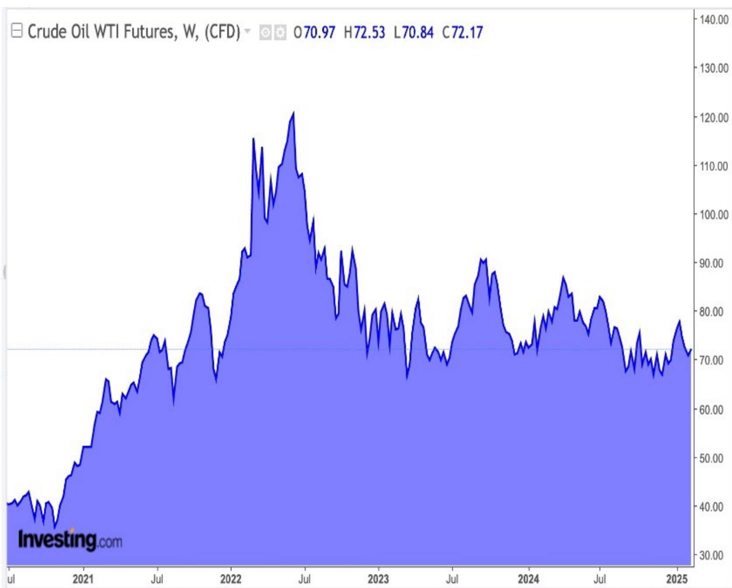
It's no surprise that surveys reveal energy market participants expect lower oil prices this year.[1] After all, Donald Trump campaigned on a platform of "Drill, Baby, Drill," promising to cut energy prices by 50% within 18 months of taking office. Since then, Treasury Secretary Scott Bessent has championed a U.S. production hike of 3 million barrels per day as the final prong of his "3-3-3" fiscal recovery plan. So, it seems only a matter of time before crude prices — having already slipped from $130 a barrel to a recent $71 over the past three years — crash below the $65 level that has formed a shelf on the price chart where buyers have repeatedly stepped in to support WTI crude since late 2021.



Upon a closer look at the economic and geopolitical dynamics of the global energy market, the shelf looks more like a price floor. The level of oil exploration is sharply declining. Oil producers have locked their wildcatter proclivities in the basement, while production levels turn flattish. Foreign oil-producing nations need higher prices just to cover monthly overhead. Oil consumption is forecast to rise. And despite the new president's talk of flooding the zone with cheap oil, crude's price is still pretty much where it was on Election Day. We believe oil prices are more likely just testing the lows of their four-year trading range, with potential upside to $90+.

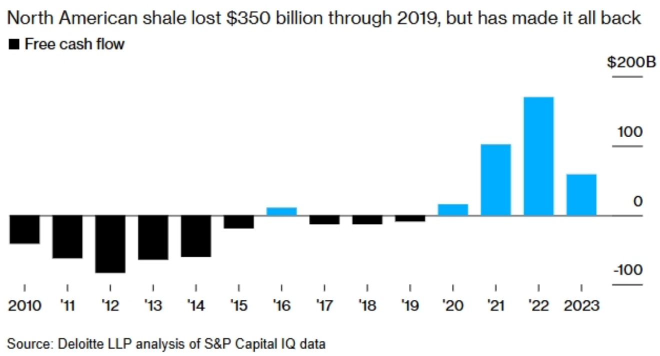
President Trump regards much lower energy costs as a critical catalyst to accelerate economic growth. The resulting jump in tax revenue would be available to service a mounting interest expense burden that now exceeds defense spending. To stoke oil supply, he intends to:

- revoke President Biden's block on oceanic drilling on the West and East coasts
- bolster Alaskan oil development
- expedite permitting, and
- curtail some endangered species and Corps of Engineers limitations. [2]

[1] "Wall Street Banks Raise Oil-Price Forecast Amid U.S. Policy Uncertainty," Wall Street Journal, Jan. 31, 2025

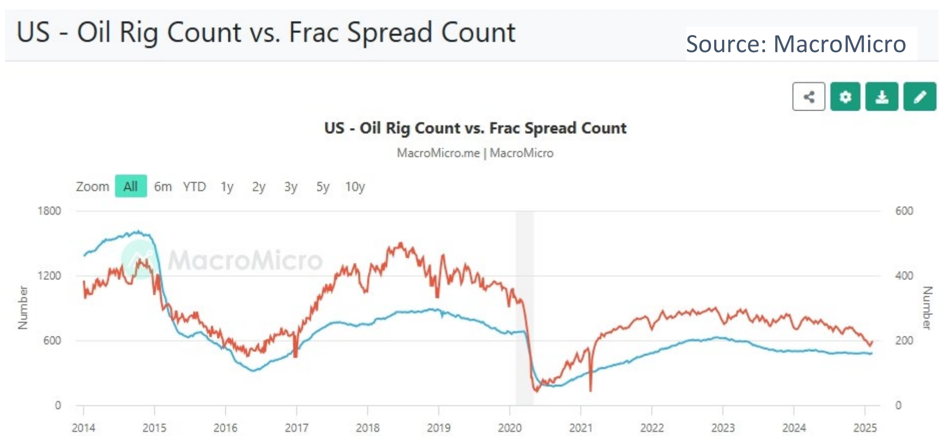
[2] "Declaring a National Energy Emergency" Executive Order, The White House, Jan. 20, 2025.

To lower producers' breakeven costs — variously estimated between $60 and $70 per barrel — Trump issued an executive order revoking 13 EOs issued by previous administrations that raised the oil industry's cost of doing business.[3] He intends all these initiatives to stir the animal spirits among oil producers, who last year were waiting for clarity that would come with the November 5 election.



However, oil company executives still have the 2010s on the brain: That's when they lost a couple OPEC price wars, collectively amassed $350 billion in losses (see graph), and experienced a sobering thinning of their ranks. Today, they are positively tight-fisted on costs and are all about "capital discipline, digital transformation, and strategic acquisitions to grow profitably," says Deloitte's 2025 industry outlook report.[4] Or, as Quantum Energy Partners CEO Wil VanLoh told Bloomberg, "Investors have put oil companies on a tight leash and want a big portion of free cash flow in the form of share buybacks and dividends."[5] As a result, the U.S. Energy Information Administration (EIA) predicts U.S. crude production flattens in 2026, after edging only slightly higher this year.[6]

There are many reasons to be pessimistic about intermediate-term growth in the U.S. oil industry. Due to declining average productivity of wells in the Permian Basin region that accounts for close to half of all U.S. oil production — plus a falling number of fracking units in the field (see graph) and an unusually low number of wells that are drilled but not developed[7] — prospects for a hike in domestic production are remote. The introduction of fracking and horizontal drilling raised U.S. production 2.5-fold since 2010, but now depletion of more easily accessible oil is making it dicier for total production gains to offset



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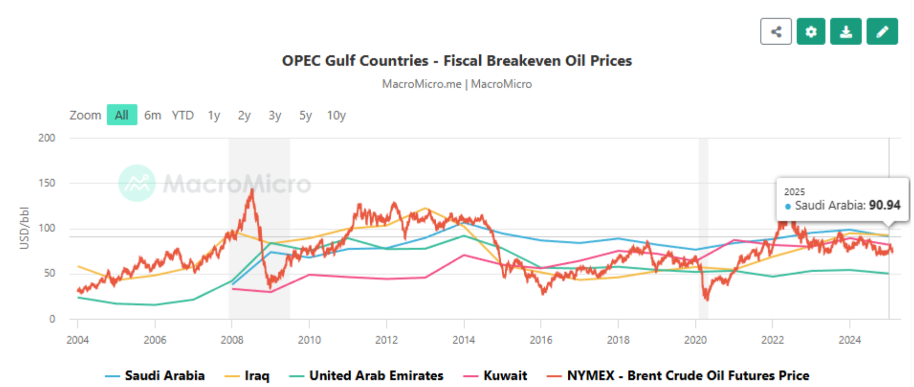
[3] "Executive orders move oil & gas development, permitting reform to top of Trump-Vance energy agenda," Morgan Lewis, Jan. 27, 2025.
[4] "2025 Oil & Gas Industry Outlook," Deloitte, p.2.
[5] "U.S. shale revolution has run its course," Bloomberg video and article, Sept. 23, 2024.
[6] "EIA extends five key energy forecasts through December 2026," U.S. EIA, Jan. 15, 2025.
[7] "2025 Oil & Gas Industry Outlook," *op cit*, p. 3.

annual well declines. "The U.S. shale revolution has run its course," Quantum's VanLoh says. Fitch projects a 0.4% year-on-year decline in aggregate global oil and gas capex.[8]

Arguably more important than America's 22% piece of global production is the 40% controlled by the OPEC+ countries. Earlier this month, OPEC+ defied Trump's pleas to hike production. Banks following the energy sector now expect OPEC will cancel plans to end their withholding of 5.85 million barrels a day (5.7% of global supply) that they have done since 2022.[9] Saudi Arabia, with just half the oil production of the U.S. but the largest contributor to OPEC output, has a keen incentive to fend off lower prices: The International Monetary Fund calculates the Saudi government needs $91 oil to cover social services, monthly payments to citizens, and infrastructure projects in 2025 (see graph).

OPEC Gulf Countries - Fiscal Breakeven Oil Prices Source: MacroMicro



While the supply side of oil looks tight, demand is plugging along. Road transportation, which accounts for 45% of annual fuel use, holds solid popularity around the world. Even though last summer's driving season proved a bit disappointing, a Reuters report that 2024 new car sales in the U.S. increased to five-year highs augurs well for the 2025 driving season.[10] Auto sales were helped by 2.8% growth in real U.S. GDP. While GDP deceleration in China has stirred up angst about a possible global oil glut, the world's second-largest economy is reportedly growing at a 5% clip. Number four India — the leading source of global oil demand growth — has GDP growth approaching 6%. Taking all this into account, the U.S. EIA forecasts global consumption of liquid fuels to rise 1.3 million barrels/day this year, versus a 0.9 million increase in 2024.[11]

Higher consumption will likely collide with supply constraints instigated by new tariffs. Earlier this month, Trump initiated his "maximum pressure" campaign on the Islamic Republic of Iran by enacting an embargo on any shipowners, managers and tanker captains involved with a "shadow" fleet facilitating the delivery of millions of barrels of Iranian oil to China. In his first term, Trump cut Iranian shipments from 2 million barrels/day to 400,000, but shipments rebounded to 1.6 million barrels during Biden's tenure because of sanctions evasion and lighter U.S. enforcement.[12] Some Trump officials have discussed the possibility of stronger sanctions

[8] "Oil & Gas Global Capex Outlook," BMI/Fitch, December 2024, summary.
[9] "OPEC+ unlikely to change output policy when panel meets on Monday," Reuters, Jan. 31, 2025.
[10] "Crude oil: the reality of 'drill, baby, drill' for the 2025 driving season," by Dan Dawson in Barchart.com, Jan. 20, 2025.
[11] "Short-Term Energy Outlook," U.S. EIA, Jan. 14, 2025.
[12] "New sanctions aim to curtail Iran's oil revenue flow to China," by RFE/RL on OilPrice.com, Feb. 10, 2025.

on other oil-producing adversaries, including Russia and Venezuela. On the other hand, Trump's tariff threats on Canadian oil seem less likely to take effect, since U.S. refiners depend on the heavier and cheaper Western Canadian Select grade to produce diesel fuels, chemicals, and plastics.[13]

Whether or not there are tariffs that imbalance the supply/demand relationship enough to spark a major rally in the oil markets depends on the notoriously unconventional 47th U.S. president. Still, with demand steadily rising and oil producers so disinclined to ramp up production, we believe the downside from current oil prices is very limited. Throw in respectable economic growth and the possibility of sanctions on other oil exporters, and WTI crude not only should hold above its $65 floor, but it could be poised to post its first meaningful gain in four years.

This report is part of an ongoing series from Titan Advisors that analyzes the opportunity set in the commodity sector.

[13] "The limits of 'drill, baby, drill" with Tracy Shuchart on the "Gold, Goats 'n Guns" podcast, Jan. 27, 2025.