

## 2010 OIL OUTLOOK

### *Oil may be headed back to \$60 /b in 2010*

OPEC latest forecast predicts that energy demand in 2010 will increase by 800,000 b/d. This is 70,000 barrels a day stronger than the forecast made by OPEC in November. We believe this news only lends modest support to what still is a weak fundamental position for oil. The fact that the USD is showing signs of a cyclical recovery also suggests that oil prices could be pressured lower in 2010.

Inventories in developed countries have been above the seasonal average for many months. Despite persistently high levels of inventories, oil rallied this year between February and late October in tune with the general upswing in risk appetite. We feel the rise in prices was out of step with the ample supply and suggests that optimism, with respect to the strength of the global recovery, is likely overstated by the price even in consideration of OPEC's latest upwards revision in demand. Unemployment in the US has risen to above 15 mln, this is more than double the 7.4 mln registered in the spring of 2008 while oil prices were only around 30% softer than they were in April 2008. As in many other countries, US unemployment is likely to rise further before recovering. Growth returned to the US in Q3 2009. However, this would have been almost non-existent if it were not for the government's fiscal support. In 2009, the US will be one of just a handful of countries in the G40 to suffer a double digit budget deficit/GDP ratio. Fiscal expenditure will have to be reined back not just in the US, but in the UK and in many Eurozone countries in the New Year. The combination of very high unemployment and the reined back of fiscal incentives is consistent with our view that growth in the US, Eurozone and the UK will remain below trend at least through 2010 and that prospects for a recovery in energy demand by OECD countries in general are low.

The USD index has strengthened by around 5% during December 2009. This coincides with a modest increase in expectations about Fed policy tightening but we believe it is also a response to a generous credit facility by the BoJ and a reaction to bad news related to budget deficits and creditworthiness in the EMU region. We feel there is still a huge amount of political will in the Eurozone and in Japan in favour of a stronger USD which is likely to affect policy decision of both the BoJ and the ECB during 2010 and beyond. It is possible that the USD index will steer away from its recent lows in the coming months 2010 and this should cap upside potential of oil prices and other USD denominated commodities and least through the early stages of 2010. Later in 2010, the likelihood that the Fed will precede the ECB and certainly the BoJ on the issue of interest rate hikes could reinforce the better tone of the USD index.

We think the prospect of a slow recovery in oil demand from OECD nations in 2010 and the prospect that the USD may have begun a cyclical recovery vs. the JPY and the EUR should cap the upside potential of oil prices into 2010 and opens the potential for a downwards correction back towards the USD60 /b.

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