COVID-19, Lockdown and Market Turmoil – Implications for Energy Markets

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Global markets, and energy markets in particular, hit by a triple whammy
With massive impact of unknown scale and duration

1. The COVID19 virus, with potentially damaging consequences on global health services, supply chains and economies
2. The massive measures to limit the spread of the virus – dramatically reducing travel and transport and killing large parts of the service sectors
3. Supply growth and oversupply of both gas and oil – the latter in particular because of collapse of Opec+ cooperation

- Unprecedented crash of global economies – massive increase in unemployment
- Stockpiling of energy products – with storage approaching tank tops

- How will markets respond over the next quarters?
- What will be the medium- and long-term implications?
COVID-19 shock spins the world into economic recession – a sharp and abrupt contraction

- The virus, and measures to limit its spread, have had a massive impact on economies
  - Will we be able to fight the virus with crashed economies?
- The world has been hit by both a supply and a demand shock
- On top, very low oil prices pose an extra drag on many countries’ economies
- Travel and transport restrictions hitting global supply chains
- Authorities are doing whatever they can to stimulate economies through fiscal and monetary measures
  - But, due to lockdowns, the short-term impact of policy measures on activity levels will be moderate
- For 2020, the IMF two weeks ago expected world GDP to contract by 4.2% in 2020 and to rebound by 5.4% in 2021
  - Most forecasters are becoming more pessimistic
  - Do not be surprised if future forecasts are worse

GDP growth 2017-2021 (% change y/y in GDP)

Source: International Monetary Fund
The outcome space is large – both in terms of scale, duration, and rebound “V”, “U”, “W”, “L”, or?

Key known unknowns, that require scenario analysis:

• How will the pandemic develop (herd immunity, vaccine availability, vaccine deployment, treatment, virus dies)?
• How will measures/(shutdowns) impact economies, and how long will they last?
• How will economies respond to gradual lifting of lockdowns, and how will public adherence be?
• How much can macro policy be stretched before lasting damage is done?
• Will there be a meltdown in credit markets?
• How will international trade be impacted in the rebound – increasing protectionism?
• Will there be medium- to long-term impacts on productivity and growth?

![World GDP, deviation from baseline (%)](source: International Monetary Fund)

- Longer outbreak in 2020
- New outbreak in 2021
- Longer outbreak in 2020 plus new outbreak in 2021

2019 2020 2021 2022
Crash and massive uncertainty about macroeconomic development

Pessimism, volatility, increased risk premiums

Global policy uncertainty index

US VIX index

Manufacturing business sentiment index

Italian/Spanish 10 years bond yields over German bunds (percentage points)

Source: Thomson Reuters Datastream policyuncertainty.com, IHS Markit
Short-term oil and gas markets in turmoil
Negative prices, record low gas prices in Europe, volatility

Oil:
- Unprecedented crash in demand – swift rebound, or?
- Short price war, new global “management” of supply – how will it develop?
- Massive impact in short-term markets:
  - Negative price as storage is near full
  - Very large volatility, large discrepancy between spot and futures
  - Differentials key – shut-ins to be expected
  - Get worse before it gets better

Gas:
- Weak market balances to start with, demand hit by GDP decline
- Oversupply hitting markets – European prices have been below HH!
- A pro-longed oil glut could improve gas balances through lower associated gas
Markets crashing and searching for an anchor...

Sources: ICE and NYMEX
Medium- and long-term energy market development

What could be the impact of the crisis?

Demand for oil and gas:
- Macroeconomic development after the crisis
- Low prices, pent-up demand for travel
- Increased digital communication and new ways of working, increased fear of new pandemics, potential setbacks for globalization
- Accelerated development/use of alternative energy sources as part of crisis support programs

Supply/marginal costs for oil and gas:
- Reduced exploration activities and drilling
- Higher debt, finance costs and risk premiums, lower breakeven requirements in energy companies
- Less cost and efficiency improvements if supply industry crashes
- Increased geopolitical and regional risks following from policy and economic strain among key oil producers

Will energy transition trend speed up or slow down?
- It will not disappear
- Focus on jobs, in the millions
  - Can renewables and batteries deliver?
  - Too capital intensive?
- Availability of finance more constrained?
  - Cash flows in energy companies
  - Governments’ fiscal balances and debt levels
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