



Foreword

The past year has been one of much upheaval as the world faced a massive financial crisis and an ensuing deep economic contraction; one not witnessed since the 1930s. The implications have stretched far and wide, with its ripple effects carrying it far beyond the country where the crisis originated. It has ushered in some extraordinary changes in such a short period of a time.

And of course for the oil market in general and, OPEC in particular, the adverse impacts were dramatic too. This is especially evident when looking at oil price movements over the past year, with the OPEC Reference Basket price hitting highs of over \$140/b in July 2008, before falling by more than \$100 to below \$40 only six months later. And this volatility could have been even more extreme without OPEC taking timely and proactive measures, both when prices were heading up, as well as down.

Few could have predicted the rapid and widespread adverse impacts that resulted from the US sub-prime mortgage crisis. Over-leverage, poor risk management, greed and speculation drove the financial system to the edge of a total meltdown when Lehman Brothers collapsed in September 2008. Whilst it is apparent that the world has now stepped back from the abyss, the lessons need to be taken on board.

From an oil market perspective, OPEC has clearly stated that the high oil prices in the middle of 2008 were not justified by physical supply and demand fundamentals. Price movements were exacerbated by massive direct and indirect investment inflows by non-commercial players looking to gain exposure to commodity markets. This was facilitated, among other things, by the possibility of high leverage and the absence of a cap on speculative activity.

OPEC has repeatedly called for better regulation and increased transparency in these markets, for the benefit of both producers and consumers alike. This call had a prominent place in the foreword of last year's WOO. There is evidently a need for this to be repeated here.

In putting together this year's publication, a number of important questions focused on the current crisis, in particular, just how long and deep this recession may be, and which path the economic recovery might follow. At present, despite the bold fiscal and monetary intervention from governments, global economic conditions remain gloomy, although some 'green shoots' have recently appeared. In addition, the potential impacts of government intervention, especially in the medium-term, in such areas as inflation, interest rates or the actual solvency of some countries, are difficult to predict. Perhaps the most important question, however, is whether this recession is

a game-changer that indeed brings about profound changes in the longer term, much as happened after the Great Depression.

It is not the role of this publication, however, to delve into the details of such important potential developments and their implications. It concentrates on exploring the possible developments of oil supply and demand.

OPEC, as an Organization, has maintained its commitment to ensure stable supplies of crude oil to the market at all times, undertaking an ambitious programme of investment, aware of the importance of responding to the demand for its crude in a timely manner, while offering an adequate level of spare capacity. However, it is not without concern that the Organization observes a repetition of the past, where a large drop in oil demand leads to damagingly high levels of unused capacity.

Nevertheless, we also believe in the widely held view that low oil prices are not sustainable. The levels for most of the first half of 2009 were considerably below that required to attract industry-wide investments and ensure sufficient production capacity to meet future demand. Stable and fair prices should take into account energy supply, demand and investments, including such core issues as costs and human resources, over all timeframes.

And this is obviously true across the entire energy industry. Each energy source, each technology, and each project, has a price when it is viable; and a price when it is not.

The significance of this can be viewed when weighing up expected demand in the longer term. Whilst it is obvious that oil demand levels will drop in the short- to medium-term — leading to a rise in overall spare capacity — looking further out, demand will rebound again, particularly as the global economy recovers. And with oil, and fossil fuels in general, expected to retain their preeminence in the global energy mix it is essential that the petroleum resources, of which there are plenty, are developed in a timely manner. This will provide consumers with required supplies, producers with stable and adequate revenues for their non-renewable natural resources and investors with fair returns.

The WOO 2009 also underscores other drivers of uncertainty concerning future oil demand requirements. This year there are a number of downside risks stemming particularly from the global economy, unreliable market signals and major policy developments.

Whilst OPEC welcomes diversity in the overall energy mix, including renewables and nuclear, we need to give careful thought to how we proceed. The uncertain-

ties are a major challenge for oil producers in general and OPEC Member Countries in particular. This is clearly illustrated in the demand and investment uncertainties explored in this year's WOO.

On the issue of climate change, 2009 is viewed as an important milestone, with the ongoing negotiations within the United Nations Framework Convention on Climate Change and its Kyoto Protocol. This year's WOO illustrates again the historical responsibility of developed countries regarding the state of the Earth's atmosphere. They account for the majority of cumulative greenhouse gas emissions and developing countries should be left to focus on evolving their economies, and eradicating poverty. In addition, developed countries, having the financial and technological capabilities, should take the lead in mitigation and adaptation.

It is also essential for the industry to maintain its commitment to the sector's skills base, the backbone of the industry. The spotlight needs to be on keeping the younger generation interested and motivated. And then there is the importance of remaining committed to advancements in the research, development and deployment of technology. In particular, the focus needs to be on the early development and deployment of cleaner fossil fuel technologies, such as carbon capture & storage.


The overall goal is a stable and enabling environment to continue to develop, produce, transport, refine, deliver and use oil in an ever more efficient, environmentally-friendly and economic manner, to the benefit of both producers and consumers.

With this in mind, it is evident over the past year that the goalposts have shifted somewhat. The growing need for what some term 'counter-cyclical' action to help offset the market's cyclical behaviour has come to the fore, in both the global economy and the international oil market. This can be viewed in the announced stimulus packages to counteract the recession, and OPEC's actions focused on maintaining oil market stability. The upshot is that there is now an increasing consensus that markets need to function more efficiently, in terms of price discovery, risk management and liquidity, and appropriately reflect the true state of the physical supply and demand fundamentals.

Pointing a way forward is never an easy task, and it is important to stress that the WOO is not about predictions, but a means of presenting information and concepts across various key energy issues. It would be impossible to formulate one single direction for the energy future. The WOO 2009 points at increasing interdependencies among all stakeholders. This is one reason that OPEC continues to

stress the importance of a positive and constructive dialogue between producers and consumers.

The publication's goal is to provide a useful reference guide for the coming year: it is an important tool that helps further the common interest among all stakeholders for energy market stability as we look to bring more clarity to the oil market and develop solutions and ways forward in the years ahead.

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Abdalla Salem El-Badri
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