

ECONOMIC VIEWPOINT

Oil Market: Should We Expect a Glut and Falling Prices in 2025?

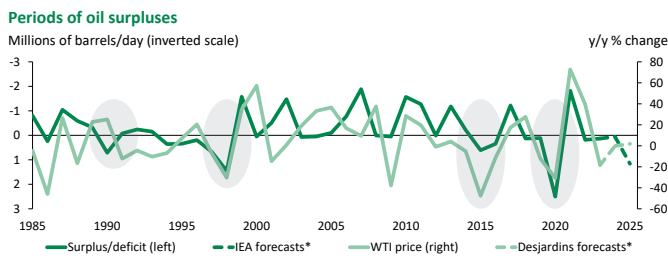
By Marc-Antoine Dumont, Senior Economist

Unless a major crisis in the Middle East disrupts production, a global oil glut is expected in 2025 with supply set to increase despite moderating demand growth. Gasoline consumption is also in the midst of a transformation, with the effects of increased fuel efficiency in combustion engines and the penetration of electric vehicles being felt faster than anticipated. As a result, the price of West Texas Intermediate (WTI) has fallen from US\$85 per barrel in July to US\$70 per barrel at the time of writing. But expectations for next year's oil glut may be overblown. China could continue with destocking and producers, mainly in the West, could end up slashing production in the face of low prices. For these reasons, we expect WTI to approach US\$75 per barrel in the next few quarters.

What's a market glut, exactly?

In economics, a glut is when supply greatly outstrips demand for a commodity. The imbalance tends to drive market prices down significantly. There have been four global oil gluts since 1985 (graph 1). Each time, a significant and lasting surplus occurred amid a combination of rising production and disappointing demand. Although there is no official rule, a glut is typically a surplus of more than 0.5 million barrels per day (MMb/d) lasting for about a year.

Graph 1
Four Gluts Have Occurred Since 1985



IEA: International Energy Agency; WTI: West Texas Intermediate; * For 2024 and 2025. Datastream, Oxford Economics and Desjardins Economic Studies

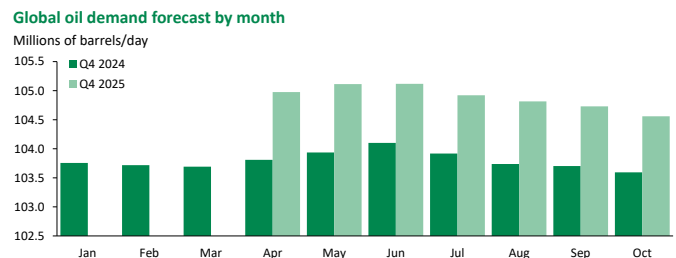
The International Energy Agency (IEA) estimates that there will be a surplus of around 1.2 MMb/d in 2025. This would be the biggest market surplus ever recorded outside of the COVID-19 pandemic. So there's a strong likelihood of excess supply. If

we stopped the analysis right here, we'd likely conclude that oil prices will fall in 2025. But it's not that simple. For a better understanding of the situation, we need to dig deeper.

What's causing weak demand?

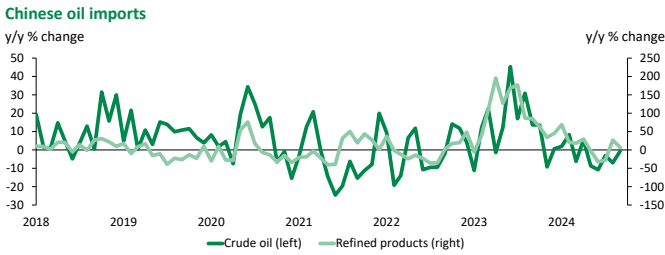
Between June and October 2024, the IEA downgraded its global oil demand forecast by 0.5 MMb/d for Q4 2024 and 0.6 MMb/d for Q4 2025 (graph 2). This revision mainly reflects concerns about China's struggling economy, as troubles in its property market have led to more widespread woes. Both consumer spending and industrial production have slowed since the beginning of the year. Imports of oil and refined products have been declining since May (graph 3 on page 2), which the market has interpreted as waning demand. This contrasts sharply with the massive gains recorded just one year earlier, when the Chinese economy revved back to life following the pandemic.

Graph 2
Demand Growth Has Been Slower Than Expected



International Energy Agency and Desjardins Economic Studies

Graph 3
Following a Sharp Rise, Chinese Oil Imports Have Moderated



Datastream and Desjardins Economic Studies

But there’s something else behind these numbers. Some of the oil imported in 2023 was used to fuel economic growth, but the rest went into commercial and government stockpiles. Even though China doesn’t publish this information, there are [several reasons](#) to believe that the country is currently sitting on outsized oil inventories. Declining imports may therefore be partly attributable to destocking efforts. So while Chinese demand has definitely softened, the perceived decline may be overblown.

US oil consumption forecasts have also been downgraded by both the U.S. Energy Information Administration and the IEA. The first factor behind the scaled-back expectations is lackluster industrial growth resulting from the restrictive interest rate environment and weak demand for goods.

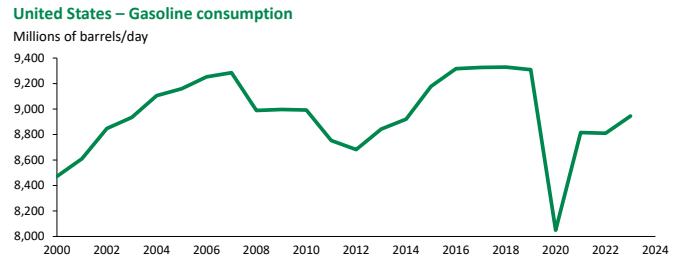
The second factor—and perhaps the most important factor for the future—is the lower-than-expected growth in demand for gasoline. It would be reasonable to assume that demand would be rising based on the various factors that drive it, such as individual wealth (real GDP per capita), road vehicle numbers, population and miles travelled (table). But gasoline consumption is still below its 2018 peak and only slightly above 2013 levels (graph 4). And any advancement of these demand drivers has

Table
Improved Energy Efficiency and Electric Vehicle Popularity Have Weighed on US Gasoline Consumption

Growth factor	Effect on gasoline consumption*	Data over time		
		2013	2023	Change
Real GDP per capita (US\$)	↑	56,172	67,632	+20.4%
Population (millions of people)	↑	316.1	343.5	+8.7%
Number of vehicles (millions)	↑	248.9	292.3	+17.4%
Miles travelled (12-month moving average)	↑	2,974,667	3,235,083	+8.8%
Average vehicle age (number of years)	↑	11.4	12.5	+9.4%
Energy efficiency (miles/gallon of gasoline)	↓	27.6	34.9	+26.2%
Electrification (electric vehicles as a percentage of the total fleet)	↓	0.08%	1.50%	+1.4 % points

* Directional effect of a rise in the growth factor; for example, an increase in real GDP per capita leads to higher fuel consumption.
U.S. Bureau of Labor Statistics, U.S. Bureau of Transportation Statistics, International Energy Agency and Desjardins Economic Studies

Graph 4
Gasoline Consumption Remains Below the 2018 Peak



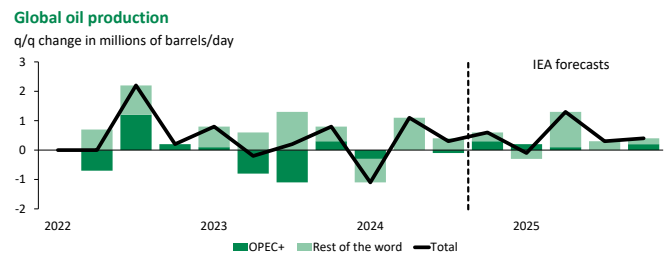
U.S. Energy Information Administration and Desjardins Economic Studies

been offset by major strides in energy efficiency. On average, miles travelled per gallon of gasoline have increased by 26.2% since 2013. This improvement, combined with the growing proportion of electric and hybrid vehicles on the road, means less demand for gasoline. The same thing is happening in China, where the population is declining and the shift to electric transportation is happening much more quickly. Gasoline demand is slowing faster than initially anticipated in the US and other countries, and the adjustments made to 2025 demand forecasts are partially attributable to this moderation.

What’s the 2025 supply forecast based on?

First, it’s important to clarify that the anticipated increases in global oil output for 2024 and 2025 aren’t the doings of the Organization of the Petroleum Exporting Countries and its partners (OPEC+). According to the latest IEA forecasts, the cartel’s production levels are expected to come down this year and only account for 25% of next year’s gain (graph 5). Concerns about OPEC+ have more to do with unused production capacity, which is currently at an all-time high of more than 5 MMb/d. This is equivalent to Canada’s total production. With the cartel already exceeding its production quota and trying to capture more [market share](#), there’s a risk that the group could flood the market in 2025 and send oil prices off a cliff.

Graph 5
OPEC+ Isn’t Driving Most of the Growth in Global Oil Supply



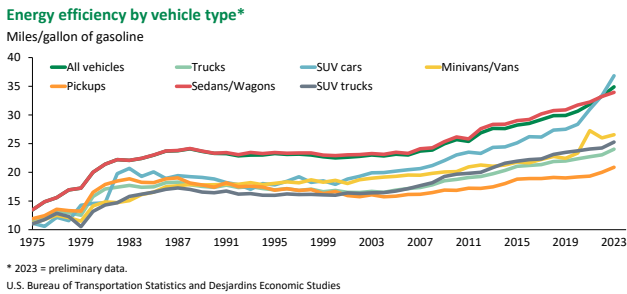
OPEC+ Organization of the Petroleum Exporting Countries and its partners
International Energy Agency (IEA) and Desjardins Economic Studies

STRUCTURAL CHANGE IN GASOLINE DEMAND

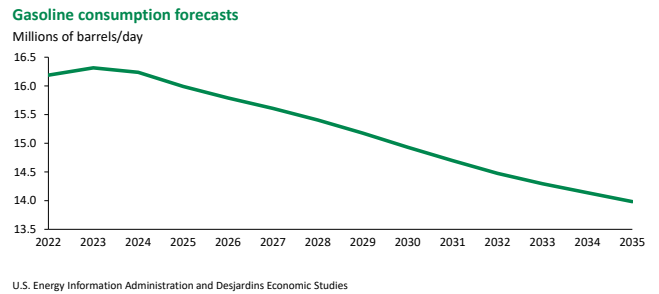
For decades, the oil and gas market developed without any competition. Of course there was competition between oil producers, but there were no viable substitutes for combustion engine technology. Things changed when electric and hybrid vehicles were introduced in the 2000s. These greener alternatives forced gas-powered engines to become more energy efficient. Added pressure then came from government incentives, rising gas prices, stricter environmental standards and greater consumer awareness of climate change and the risks associated with getting oil from the Middle East.

Energy efficiency improved throughout the 2010s, with more notable gains occurring since 2019 (graph A). With further advancements expected, demand for gasoline has probably already peaked in the US and other developed countries. In fact, this is the basis for the U.S. Energy Information Administration’s forecast (graph B).

Graph A
Passenger Vehicles Have Become Significantly More Energy Efficient



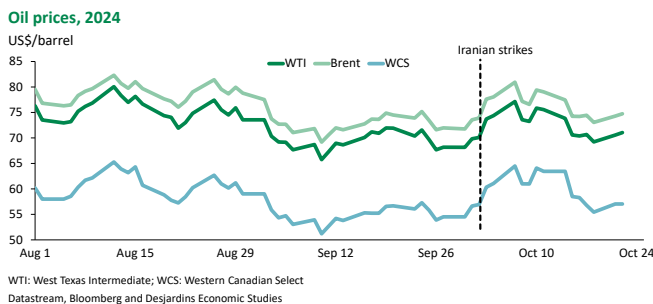
Graph B
US Gasoline Consumption May Have Already Peaked



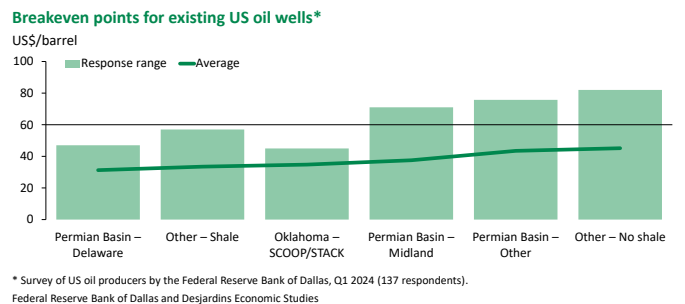
But this could also be a strategic message that OPEC+ wants Western oil producers to hear. After the cartel confirmed that it would ramp up production in December, crude oil prices started coming down, with the exception of an uptick sparked by tensions between Iran and Israel (graph 6). OPEC+ initially postponed the production increase from October to December, and the market had hoped it would be postponed again. Having prices remain sustainably between US\$60 and US\$70 per barrel

would have two effects on Western supply. First, the producers with the highest operating costs would be gradually shut out of the market. Some US producers in the Permian Basin have a breakeven point of more than US\$60 per barrel for existing wells (graph 7). Next, producers could also end up scaling back any plans to increase output. In both cases, supply would gradually be reined in over a few months and the oil surplus would ease.

Graph 6
Oil Prices Surged After Tensions Escalated in the Middle East



Graph 7
Some US Oil Producers Have a Breakeven Point Above US\$60 per Barrel



What does this all mean for crude oil prices?

Unless a major crisis in the Middle East disrupts production, an oil surplus is expected on the market in 2025 with supply set to increase despite moderating demand growth. But as we've explained, the surplus may be overestimated. For this reason, we expect WTI to approach US\$75 per barrel in the next few quarters. However, considerable uncertainty hangs over the oil market. On the one hand, there's a risk that oil prices could plummet. On the other hand, the market's sensitivity to the geopolitical situation in the Middle East means there's also a possibility that prices could spike.