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Why a Shift from Backwardation to
Contango is Looming?”*

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OPEC+ Driving Oil Markets to the Brink: *Why a Shift from Backwardation to Contango is Looming?*

By Sean Evers, Managing Partner, Gulf Intelligence

The End of Backwardation: Understanding the Price Shift

The global oil market is teetering on the edge of a significant structural shift, moving away from backwardation—where immediate oil prices surpass future prices—to a state of contango, characterized by higher future prices relative to current levels. Traders and analysts increasingly believe this transition is imminent, signaling an oversupplied market grappling with weakening demand fundamentals.

Recent data underscores this shift, with Brent crude oil dropping dramatically by 20% over the past month alone—from in the mid \$70s per barrel down to under \$60. This decline highlights growing pessimism about global economic health, exacerbated by sustained trade tensions between the world's two largest economies, the United States and China. Market indicators have begun showing clear signs of contango, suggesting deeper underlying supply-demand imbalances.

Contango typically indicates that markets foresee prolonged weak demand or substantial excess supply, compelling traders to store oil today in anticipation of higher future prices. The re-emergence of this pattern suggests widespread market skepticism about near-term demand recovery, emphasizing structural inefficiencies and excess inventories that have quietly accumulated.

OPEC+ has played a critical role in driving the market toward contango through recent strategic decisions to incrementally increase production. This incremental addition to supply has further reinforced perceptions of surplus, intensifying downward price pressures.

OPEC+'s Strategic Pivot: Managing Market Share Amid Declining Demand

Despite that most multilateral agencies, including the World Bank and the IMF, have recently reported declining global economic growth, OPEC+ announced on May 3rd that it would implement another production increase of 411,000 barrels per day in June. This move represents part of a broader strategy—agreed upon in December 2024—to gradually reintroduce previously withdrawn 2.2 million barrels per day back into the market. OPEC+ justifies this cautious incremental strategy by citing historically low global oil inventories, yet internal dynamics reveal deeper strategic considerations.

This strategy potentially marks a historic pivot away from OPEC's traditional policy of maximizing prices. Instead, OPEC+ now seems focused on maintaining or expanding market share in an environment of anticipated stagnation or declining oil demand. Producers might soon engage in fierce competition to maintain their nominal volumes, risking a damaging price war reminiscent of previous downturns in 2014 and 1997.

Trump's China Tariffs to unleash Supply Shock on US Economy -- will that be bullish or bearish for oil prices?



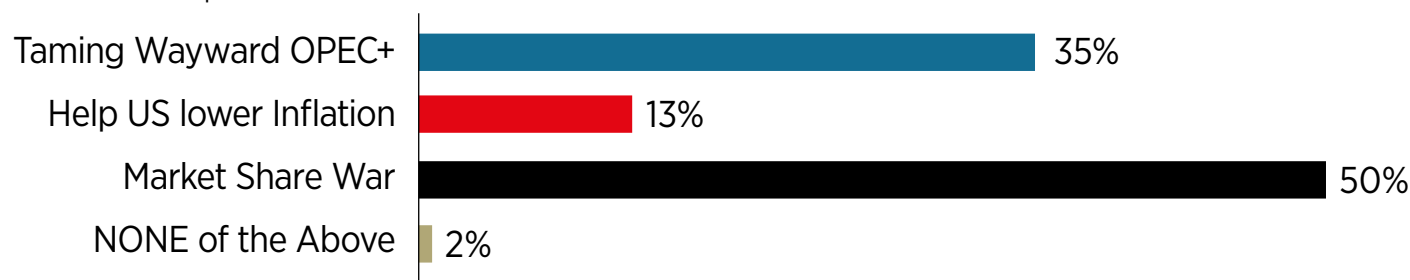
Does the Spain power outage present a cuckoo in the coalmine warning for global infrastructure vulnerability in the era of AI?



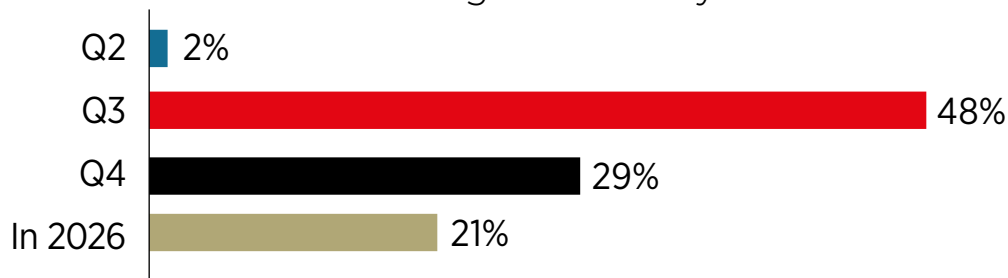
Brent crude fell 20% in the first 100 days of Trump 2.0 – how will it perform in the second 100 days?



What is main reason Saudi Arabia appears keen to drive UP oil supply and push DOWN oil prices:



How soon will China-US reach a Trade Agreement – by end of:



(*nb. Polling conducted with 100+ Energy Market Stakeholders Apr. 28-May 2)

Furthermore, internal tensions within OPEC+ complicate this strategic adjustment. Compliance with production quotas remains inconsistent, with certain member countries regularly surpassing agreed output limits. OPEC's latest adjustments also aim at restoring credibility by addressing these discrepancies explicitly, underscoring a collective commitment to achieve conformity and accelerate compensation for previous overproduction since January 2024.

Global Economic Headwinds: US-China Tensions and Efficiency Gains

Underlying the evolving oil market dynamics are severe global economic challenges, prominently highlighted by the ongoing U.S.-China tariff conflict. Both economic giants have inflicted mutual economic damage through tariffs, sharply reducing trade flows and subsequently depressing oil demand significantly in critical sectors such as shipping and manufacturing. This scenario has created a cycle of mutual economic harm, raising concerns about prolonged economic paralysis.

This trade-induced uncertainty contributes directly to market instability, as businesses struggle to plan effectively amid shifting tariff policies. Considerable economic contractions are anticipated, particularly for the U.S. economy in the near term, driven by reduced cargo traffic and declining consumer inventories. China, facing significant export challenges, is likewise experiencing substantial economic pressures, despite efforts to boost domestic demand.

Adding to this complexity, global efficiency gains continue to structurally depress oil demand growth. Improvements in energy intensity—measured as oil consumption per unit of GDP—have steadily reduced oil usage, independent of short-term disruptions. This presents a significant factor that OPEC+ must navigate, as long-term efficiency gains mean that even economic recoveries might not translate into proportionate increases in oil consumption.

As oil markets adjust to these multifaceted pressures, price levels and investment cycles face significant recalibrations. Historical trends show that prolonged low prices eventually force downward adjustments in production costs, allowing sustained production even in challenging

price environments. Consequently, while short-term oil price volatility may pose risks, the medium-term outlook suggests stabilization at structurally lower price points.

Winners, Losers, and the Road Ahead

As oil markets potentially shift toward contango, clear winners and losers emerge. Immediate beneficiaries of lower oil prices include major importers like China and India, benefiting economically from reduced energy costs. Conversely, oil-exporting nations and their energy sectors face declining revenues, exacerbating economic vulnerabilities.

Despite these pressures, major energy companies are unlikely to rapidly halt investments, given the long-term nature of global oil projects. Countries with significant new oil production, such as Guyana and Brazil, will continue operations despite short-term market pressures. However, U.S. shale oil producers face greater uncertainty, as their responsiveness to price changes remains relatively flexible compared to traditional long-term projects.

Geopolitical uncertainties further complicate the oil market outlook. Potential escalations involving sanctions on Iran or Russia could introduce sudden volatility, making market management increasingly challenging for OPEC+.

Ultimately, the anticipated shift from backwardation to contango represents a significant turning point, indicating market expectations of prolonged oversupply and weaker near-term demand. OPEC+'s incremental strategy reflects cautious optimism tempered by realism about structural market changes. Navigating through internal conflicts, global economic uncertainty, and persistent efficiency gains, the organization's ability to maintain cohesion and stability will be tested rigorously.

The global energy landscape thus stands at a pivotal moment. Whether OPEC+'s flexible adjustments can successfully stabilize markets remains uncertain, but the shift toward contango undoubtedly signals deep-rooted transformations reshaping the future of global oil. ■



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