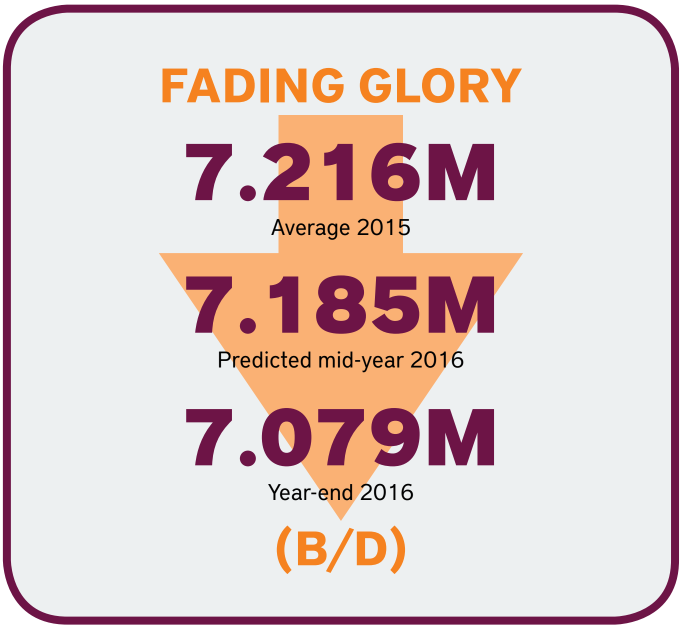
OUTLOOK

Past its peak

China's output will fall this year, the biggest loser as Asia's oil production drifts lower / DAMON EVANS, Singapore

THE INTENSE focus on the price war between Saudi Arabia and higher-cost producers has obscured an important trend elsewhere in the market.

It appears that China's oil production probably peaked at one point in 2015, and will enter structural decline some time over the course of the months ahead.



This is significant as the country is not just a major crude importer, it is also the world's fifth-largest oil producer, trailing behind only the US, Russia, Saudi Arabia and Canada. To give that some context, the country pumps quite substantially more oil than Iran and Iraq.

The country's domestic oil production was up 2.2% to 4.3m barrels a day – or just under 5% of global supply – last year compared with 2014. It was the highest level on record and the culmination of a remarkably constant expansion averaging 1.5-2% every year over the past two decades. But growth has started to falter.

Government data show crude production in December, at 4.293m b/d, was down around 1.5% compared with a year earlier, as Cnooc's rising offshore production was offset by declines at Sinopec's maturing fields.

Daqing down: Asian oil output (m b/d)

Country	Average 2015	Mid-2016	End-2016
China	4.300	4.250	4.124
Indonesia	0.786	0.800	0.810
India	0.890	0.890	0.890
Malaysia	0.650	0.670	0.690
Vietnam	0.330	0.315	0.305
Thailand	0.260	0.260	0.260
Total	**7.216**	**7.185**	**7.079**

Sources: *IEA, Petroleum Economist, FGE, Bernstein*

Last year probably marked the peak in domestic oil supply, as investments are increasingly being cut and high-cost ageing production is shut down, signaling the start of a structural decline for the sector as a whole. The International Energy Agency reckons China's Big Three – CNPC, Sinopec and Cnooc – will be largely unaffected by the downturn in oil prices, with supply edging lower by about 0.7%, or 30,000 b/d. But the agency admits it could be behind the curve, with information on the companies being at a premium.

The age of China's big oilfields – they were discovered in the 1960s and 1970s – means production can only be sustained with strong growth in capital expenditure. Average production costs for China's majors are higher than $40 a barrel. Kang Wu, a Beijing-based China expert at consultancy Facts Global Energy, says he expects 50,000 b/d to be shut down over the course of 2016, as low oil prices close marginal production in ageing fields and exploration activities begin to slow.

But others have a far grimmer outlook. Neil Beveridge, a Hong Kong-based oil specialist at investment and research house Bernstein, expects output to fall 3.5%, or 150,000 b/d, in 2016, if oil prices remain at their current levels. This would mark the steepest drop since the early 1980s, and stiffen demand for foreign crude far more than expected.

Petroleum Economist's analysis foresees production sliding by around 2%, or just under 90,000 b/d, by end-2016 if low oil prices persist. But as the national oil companies' mature fields increasingly need enhanced oil recovery methods – hard to justify in a period of weak prices – to maintain flows, production could drop off even more quickly.

China's largest oilfield, Daqing, which makes up 20% of national crude output, may well be already in a state of managed decline, following a warning by operator CNPC in late 2014. Despite intensified drilling in recent years, production from the field has steadily edged lower. The weaker oil price and cost-cutting drive at CNPC should only accelerate the decline at the field.

SE expectations Meanwhile in Southeast Asia, production is expected to remain fairly stable, as the bulk of output, stemming from onshore and shallow-water fields remains relatively low in cost. Most of the region's producers already implemented measures to counteract falling production well before oil prices plunged.

Still, Indonesia, which reactivated its Opec membership in December, missed its production target, set at 0.825m b/d, again last year. The decline in global oil prices means that

More to come: Shell's Gumusut-Kakap, in Malaysia. The major wants to increase production in the deep-water field

Opec's only Asian member will not meet its target of 0.830m b/d in 2016, unless oil prices average $50/b, according to upstream regulator SKKMigas.

Indonesia's battle to stop its output falling has been underway for well over a decade. But ExxonMobil's Banyu Urip field, which started up in December, and is expected to hit peak output of 165,000 b/d in early 2016, will help boost the country's short-term production forecasts. Petronas also reported the start-up of its Bukit Tua field off eastern Java in November, which will flow 20,000 b/d at peak.

If oil prices average around $40/b, expect Indonesia to pump a little more than 0.8m b/d this year. Should global benchmarks drop further, averaging just $20/b, output will hit only 0.75m b/d as production is shut in.

In neighbouring Malaysia crude volumes will continue to climb as Shell ramps-up production at its deep-water Gumusut-Kakap field, expected to pump 135,000 b/d at peak. Output at the field, which began late-2014, hit 100,000 b/d in October. Oilfields in the Gulf of Thailand, which operate at an average cost of $30-40/b, will maintain stable flows this year, while Vietnam looks set to shut-in some of its more expensive production. Elsewhere, production from India's low-cost onshore and shallow-water fields should remain steady at around 0.89m b/d. **PE**