

Energy market outlook hinges on the Middle East

The key factor for energy markets remains developments in the Middle East. The only way energy prices move lower is the resumption of flows through the Strait of Hormuz. In the absence of this, prices will only move higher



Dated Brent crude oil prices hit \$144.46 a barrel recently, an all-time high

Oil futures don't fully reflect the scale of supply disruptions

Oil flows through the Strait of Hormuz remain largely cut off, which continues to tighten the oil market. However, despite this significant tightening, the futures market appears to be responding more to headlines over how the war may evolve, with hopes that we could see a resolution in the coming weeks. However, we just need to look at the physical market to get a better idea of the reality of the supply disruption. Dated Brent has traded as high as \$144/bbl recently and is trading at around a \$30/bbl premium to Brent futures. Clearly, the longer supply disruptions persist, the more likely we will see futures needing to catch up with the physical market.

We estimate that around 13m b/d of oil flows from the Persian Gulf are being disrupted due to the Strait of Hormuz blockade. This is after taking into account pipeline diversions, Iranian tankers still moving through the Strait (although this could change with the recent US blockade), as well as some other tankers transiting this key chokepoint. While releases of government stocks and the

drawing down of floating storage have helped the market, the shortfall is still significant. Therefore, there is a need for demand destruction. We are already seeing signs of this, particularly in parts of Asia, with several governments in the region announcing measures to reduce energy consumption. Clearly, the longer this persists, the more demand destruction we will need to see, and this will have to occur across other regions as well. To drive further demand destruction, we will need to see higher oil prices.

For now, our base case is that energy flows will start to make a gradual recovery through the second quarter. However, flows will remain below pre-war levels until at least year-end. This would see Brent averaging \$96/bbl over 2Q26 and \$89/bbl over the full year 2026. A more extreme scenario would be where Persian Gulf flows remain mostly cut off, while escalation sees extensive infrastructure damage, and risks to Red Sea oil flows also grow, which could see Brent trading over \$150/bbl.

The LNG market continues to tighten

The global LNG market also continues to tighten with developments in the Persian Gulf, and the market is set to see supply disruptions persist for longer, even if we were to get a quick resumption of vessel movements through the Strait of Hormuz. Firstly, restarting Qatari LNG capacity will take some time, while 17% of Qatari LNG capacity will also be offline for the foreseeable future after an Iranian attack. As a result, we are seeing the Asian and European gas market increasingly pricing in a tighter market until 2027. A delay in the start of new Qatari capacity only adds to a tighter-than-expected outlook.

There is little in the way of supply alternatives for the market to offset the sizeable volumes we are seeing disrupted from the Persian Gulf. The ramp-up of new US LNG capacity is simply not enough. Therefore, demand destruction will be key to balancing the gas market. This will likely be evident in the power sector, where we expect the industry to lean more on coal, particularly in Asia. But even in Europe, it makes more sense to burn coal rather than gas, even when taking into consideration carbon prices.

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