Market overview

Adapting to a new oil price environment

In the oil and gas sector, the significant advancement in shale oil production in the United States and recovering production in Iraq and Libya, combined with slower than expected economic growth across the globe, has created an excess supply situation prompting a marked decline in the oil price in recent months.

Oil price

2014 was a volatile year for the oil and gas industry as the oil price dropped in the second half to its lowest levels in six years, exiting the year at US$60.22 per barrel, a 42% decline year-on-year. The new oil price environment and abrupt nature of the drop was a reality that surprised economists and oil analysts alike whilst creating uncertainty for an industry that had committed billions of dollars in global upstream development projects.

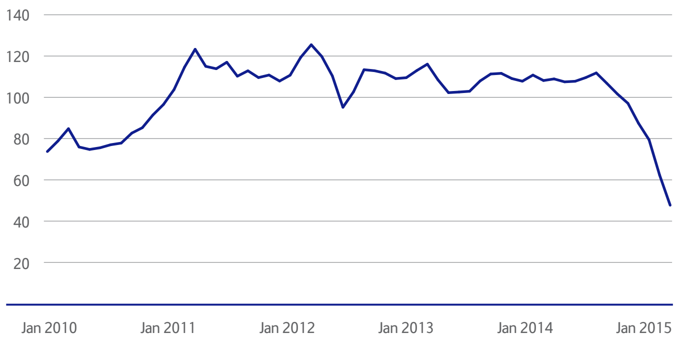
It is widely thought that a major contributor to the oil price decline was the rapid growth in fracking production in the United States that added about 4.5% to global supply, coinciding with a time when global oil demand was rising at a slower rate than in recent years. The glut of supply in the market did not provoke a cut in output by OPEC – reversing its traditional behaviour in periods of excess supply – but instead the organisation saw it as an opportunity to crowd out those expensive producers, notably those shale producers in the US, thus protecting their share of global production in the medium term. Another important catalyst to oil price markets remains the geopolitical situation across the Middle East and North Africa, most notably Libya and Iraq. Events in both these countries could produce significant swings in daily global production and the market will watch both countries with interest in the coming year.

The oil price instability witnessed in 2014 has impacted the oil and gas sector dramatically within a short space of time, with E&P companies large and small responding by adjusting costs and investment plans accordingly, especially those companies operating in more complex and higher cost locations such as deep-waters offshore.

Global economy

Economic and population growth are the principal drivers of global energy demand. In 2014, the world's population surpassed 7 billion, and is expected to reach 8.1 billion by 2025 and 9.6 billion in 2050, with levels of international economic growth likely to move in a similar upward trajectory. As such, the overall long-term trend for energy demand is likely to continue increasing despite the pace of output growth meaning we exited 2014 with a glut of supply in the market contributing to a near 50% fall in oil prices. Despite the slowdown of growth in Asia, the continued economic expansion in China and India will underpin growth in demand for energy over the next 20 years. According to BP's Annual Long-Term Energy Outlook Report, global energy demand is projected to rise 37% from 2013 to 2035, an average of 1.4% a year.

Brent oil price (Dollars per barrel)



Source: Thomson Reuters

Nigerian economy

2014 was a marked year for Nigeria as it overtook South Africa to become not only Africa's largest economy, but also the 26th largest in the world. This followed the publication of recalculated figures that almost doubled estimates for the country's GDP. Nigerian GDP for 2013 was US$509bn, 89% larger than previously recorded. Nigeria's oil industry remains the largest contributor to national GDP; however, the economy has diversified into consumer-focused industries such as financial services, telecommunications and consumer goods, demonstrating the growth of Nigeria's consumer base and the rise of a domestic market across all sectors and most notably energy.

However, the Nigerian economy's exposure to the oil sector will have an impact in the near and long term, with the oil price decline already devaluing the Naira significantly and provoking a rise in interest rates to record levels.

Equity markets

2014 was a challenging year for global equity markets with a divergence of index performance clearly visible across the major geographies. In Europe, demand for equities was particularly strong during Q1 and early Q2 2014, before tapering down primarily caused by economic uncertainty in the Eurozone. US markets represented the most consistent story of the year, performing strongly on the back of a continuous flow of positive economic data. The S&P 500 ended the year 11.4% higher.

In the UK, the FTSE 100 index fell 2.7% over 2014 and was outperformed by mid-cap stocks as the FTSE 250 rose 0.9%. The O&G sector saw a sharp decline in the second half of the year as the market witnessed a general commodity selloff, with the oil price also driven down by the decision by OPEC not to cut output, which left the FTSE O&G producing stocks on the back foot and ultimately closing the year 13.4% lower. The NSE also fell by 16.1% in 2014, as the index was hindered by concerns surrounding the negative impacts on an oil dependent economy caused by falling oil prices and pre-election uncertainty. Seplat's London line ended the year 31.4% lower at 144p whilst the Nigerian line closed down 35.6% at 371 Naira.