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US decides to Release Oil Reserves to Lower Prices in collaboration with Japan and others

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On November 23, U.S. President Joe Biden announced a decision to release strategic petroleum reserves in an attempt to lower crude oil and gasoline prices that have stayed high. He also offered a policy of cooperating with major oil-consuming countries such as Japan, China, India, South Korea and the United Kingdom to implement the release of oil reserves. On November 24, the Japanese government published a plan to release state-owned oil reserves in a manner to respond to the U.S. announcement. The release, estimated at several millions of barrels, will take the form of moving up the replacement of oil reserves. The U.S. SPR release is reported at 50 million barrels. Japan, the United States and others will consider details of how to release oil reserves in the future.

The oil crises in the 1970s have prompted oil-consuming countries to pile up oil reserves in preparation for emergency events such as disruptions to supply. Developed countries have taken leadership in stockpiling oil reserves. China and India as big oil consumers have also developed state-owned and other oil reserve arrangements in view of their increasing dependence on oil imports. In the past, oil reserves were released in response to emergency events and supply disruptions. In 2005, the United States released its SPR in response to damage from Hurricane Katrina. On the occasion of the 2011 Great East Japan Earthquake, Japan released oil reserves by lowering the obligated number of days to be covered by private sector oil reserves. In 2011, the International Energy Agency led a joint release of oil reserves to cope with the Libyan crisis.

However, the current U.S.-led initiative to release oil reserves is unusual for various reasons. First, the initiative has come to pursue lower oil prices at a time when crude oil prices remain as high as $80 per barrel in the absence of any emergency events such as supply disruptions. The United States implemented an SPR release alleged to seek oil price drops in the absence of any special supply disruption under the Clinton administration in September 2000. However, the initiative to lower oil prices is the first ever for Japan that has designed a release of oil reserves to respond to an emergency event. It is basically the first time for other countries participating in the coordinated release. Major oil-consuming countries have thus agreed to a historic coordinated action to release oil reserves for the purpose of lowering oil prices.

Second, the IEA, which has historically taken leadership in implementing oil market stabilization measures including the joint release of oil reserves, has not been involved in the current international cooperation framework for releasing oil reserves. For the IEA that has positioned an oil reserve release as a means to stabilize the international oil market in response to emergency events such as supply disruptions, it might have been difficult to participate in the current initiative. Another remarkable point of the current initiative is that its participants include not only the United States, Japan, the United Kingdom and South Korea as IEA members but also India and China as non-IEA countries. The six countries accounted for 48% of global oil consumption in 2020. The initiative indicates that major Asian oil-consuming countries have partnered with the United States and the United Kingdom to create cooperative arrangements to lower oil prices. Attention should be paid to the unusual combination of the IEA's absence and the participation by China and India. This is interesting, given the initiative's implications for global energy governance and the U.S.-China confrontation. Third, Japan is releasing its state-owned oil reserves for the first time under the current initiative. In the past, Japan released oil reserves by lowering the obligated number of days to be covered by private sector oil reserves. The government might have considered relations with the United States and agonized over what it can do under the Oil Stockpiling Act.

Attracting global attention is how the unusual international initiative to jointly release oil reserves would influence the future international oil market. Regarding the initiative's objective to lower crude oil and gasoline prices, some announcement effects have been seen. The key West Texas Intermediate crude oil futures price topped $80/bbl in October and hit the year-to-date high of $84.65/bbl on October 26. It stayed high later, closing at $84.15/bbl on November 9. Later, however, the price declined rapidly to $76.10/bbl on November 19, losing some $8/bbl in 10 days. Insecurity about the global economy and the renewed spread of COVID-19 infections in Europe might have contributed to the crude oil price decline. However, I think that the greatest contributor might have been an expected U.S. SPR release and the United States' approach to Japan and other countries regarding the coordinated oil reserve release. As crude oil prices are determined in the futures market, market participants trade in futures contracts while anticipating future supply, demand and market conditions. During the 10-day decline in crude oil futures prices, the most important development for market participants was an indication of the oil reserve release. The price decline can be seen as reflecting the indication.

However, market participants continue to anticipate future developments. On November 23 when Japan, the United States and others officially announced their coordinated oil reserve release, the benchmark WTI futures price rose by $1.75/bbl from the previous day to $78.50/bbl. Factors behind the price hike following the announcement of the oil reserve release may include (1) crude oil futures prices' earlier decline discounting the oil reserve release, (2) the announced oil reserve release falling within anticipation of market participants and (3) market participants' speculations about how the OPEC-plus group comprising the Organization of the Petroleum Exporting Countries and some non-OPEC oil-producing countries would react to the oil reserve release by oil-consuming countries or whether the group would phase down its production cut as earlier planned. Although the coordinated oil reserve release has thus served as a market-moving factor, how it would influence the market in the future is difficult to anticipate. As a matter of course, market participants will closely watch how the announced oil reserve release would be implemented and how much would be released consequently. However, crude oil prices could go up or down depending on other factors including a decision on the production cut at an OPEC-plus meeting on December 2, potential cold waves in the northern hemisphere, COVID-19 infection conditions and global economic trends including Chinese and U.S. trends.

Another important issue is whether or how the current initiative to release oil reserves would contribute to the politicization of the international oil market. As far as any oil reserve release responds to emergency events like large-scale supply disruptions, its implementation may be understandable and transparent. If an oil reserve release is aimed at stabilizing oil prices, however, it would be difficult to decide on specific price conditions and measures for implementing the release. Such decision may become political. Such political decision could risk oil-producing countries' reactive political decision. In this way, oil-producing and -consuming countries could dispute over oil prices and escalate their confrontation. Despite the fact that the stabilization of oil prices is important for both oil-producing and -consuming countries, they could denounce each other and take actions against each other. To avoid such problem, oil-producing and -consuming countries should keep away from any situation for mutual denouncement and promote dialogue for mutual understanding and cooperation to stabilize the market. Japan is positioned to give priority to both the United States and oil-producing countries and should strive to promote dialogue to stabilize the market.

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