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## **Monetary Easing Competition and Crude Oil Prices**

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On October 6, the West Texas Intermediate crude oil futures price on the New York Mercantile Exchange rose to \$83.23/barrel, the highest level since early May. The benchmark crude oil futures price slipped below \$80/barrel on August 11 and remained below the level for nearly two months before turning up recently. It rose above the \$80/barrel level on October 1. What factors have been behind the recent rapid oil price hike?

Main factors include global macroeconomic and financial situation changes. It may be no exaggeration to say that supply/demand fundamentals (particularly, its current conditions), which are usually primary factors for pricing crude oil, have made little contribution to the recent rapid price hike. Market conditions indicate that oil demand growth has globally been met, with supply remaining abundant. As a result, oil inventories have maintained record levels in the United States and the entire Organization for Economic Cooperation and Development. Crude oil prices have frequently soared even amid an easy supply/demand balance since 2009. But the latest hike might have uniquely stemmed from liquidity-driven markets caused by Japanese, U.S. and other monetary easing measures.

The most symbolic among these measures might have been those that the Bank of Japan decided to take on October 5. The central bank made and announced the decision to (1) lower its policy interest rate from 0.1% to a 0.0-0.1% range (zero interest rate policy), (2) to maintain the zero interest rate policy until an inflation rate of 1% comes into sight, and (3) to purchase 5 trillion yen in such assets as government securities, corporate bonds and exchange-traded funds. These measures represented a far greater quantitative monetary relaxation than expected by market players. Since the termination of its quantitative easing policy in 2006, the BOJ might have believed it would not have to resort back to the zero interest rate policy. Amid the yen's prolonged appreciation, growing deflation fears and rising concerns about an economic downturn, the central bank came up with the monetary easing measures in a manner to cope with an emergency. In a sense, the monetary policy authorities were required to move in step with the government that was considering additional

economic stimulus measures.

We must pay attention to the fact that the BOJ decision came in the context of a global monetary or quantitative easing competition. Particularly in the United States where quantitative easing measures have already been implemented, the Federal Reserve's Federal Open Market Committee is well expected to decide on additional quantitative easing measures at its next meeting set for November 2-3. Under market expectations including the possible additional U.S. measures, the BOJ's monetary easing decision has had a smaller yen-lowering effect than earlier expected. In the future, therefore, the BOJ could implement more additional monetary easing measures while watching developments in the world including the United States. In fact, the BOJ decision covering 5 trillion yen in purchases of a wide range of assets can be interpreted as paving the way for further quantitative easing.

As Japan and other countries in the world race to take monetary or quantitative easing measure to stimulate national economies, huge funds or liquidity are provided to the market. The huge liquidity provisions, though expected to play a key role in supporting the economy, can dramatically change money flows into various financial assets and commodities through a fund flow into riskier assets and growing hedging needs amid currency depreciation fears. We can interpret the recent market developments as indicating that such dramatic changes are now taking place to boost stock and commodity prices. In a typical development, gold has shot up to an all-time high beyond \$1,300 per Trojan ounce.

The benchmark crude oil futures price's recent hike to a five-month high should be understood as part of global market developments. Of course, there are various uncertain factors in the global macroeconomic and financial situations, meaning that future developments are difficult to anticipate. Liquidity-driven markets could lead to asset bubbles. In this sense, market trends and developments may grow more uncertain. For the immediate future, however, ample liquidity provisions are likely to remain as a precondition for market developments as major industrial nations continue their monetary easing race to overcome deflation. Crude oil prices may be formed under such situation. In this sense, the benchmark WTI futures price is expected to remain above \$80/barrel for the immediate future. But whether the ceiling of the recent \$68-86/barrel range could be tested is difficult to predict. Including this possibility, the fate of the liquidity-driven markets may attract much attention.

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