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# A Review of First-Half 2011 Crude Oil Prices

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In the first half of 2011, the benchmark West Texas Intermediate crude oil futures price (the closing price of the front-month contract) averaged \$98.5/barrel, ranging from \$84.3/barrel (February 15) to \$113.9/barrel (April 29). From the same period last year, the average rose by \$20/barrel. During this year's first half, the price deviated by up to some \$15/barrel up and down from the average. The price fluctuations in this year's first half were wilder than in the year-before period when the price deviated by up to about \$10/barrel above and below the average.

What were the factors behind the higher prices and wilder fluctuations? The two most influential factors were (1) the destabilized Middle East and North African situation and Libyan crude oil supply disruptions, and (2) changes in views about the future world economy.

As I noted several times in "A Japanese Perspective on the International Energy Landscape," the emergence of geopolitical risks and subsequent oil supply disruptions in the Middle East and North Africa as the center of gravity of world oil supply shook the international oil market greatly, becoming the biggest factor behind crude oil price spikes in the first half of 2011.

The Egyptian crisis led to "fears" of oil supply disruptions regarding passage through the Suez Canal, which triggered crude oil price hikes. Subsequently, the Libyan crisis brought about "actual oil supply disruptions," which exerted a great impact on the market. Crude oil price spikes since the second half of February were attributable to the direct impact of the oil supply disruptions. Particularly, the market lost 132 million barrels in high-quality Libyan crude oil by the end of May. The loss, though made up for partially by an increase in Saudi oil supply, was significant.

Amid the chain of Tunisian, Egyptian and Libyan crises, how the destabilization would expand became a great matter of concern to market participants. As worst scenarios were factored into the market, psychological fears worked to accelerate crude oil price hikes. Crude oil prices soared in sensitive response to relevant developments including European and U.S. military attacks on Libya, the destabilization of the Bahrain situation, spreading relevant anti-government protests and growing tensions between major Middle Eastern countries.

In some sense, the market now has a great capacity to masticate and absorb factors, leading to shorter periods of time where factors remain influential on the market. While the Middle East and North Africa situation remained essentially serious and far from real solutions to problems, the absence of new developments amid the deadlocked situation led crude oil prices to lose their upward momentum, with the serious situation interpreted as factored into the market.

Then, fears about the future world economy emerged as a new market-moving factor. Earlier, the world economy, though plagued with various destabilizing factors, was supported by economic recovery expectations in industrial countries and high growth in emerging economies. Stock prices as a mirror of future economic conditions were firming up. In May, the 30-issue Dow Jones industrial average on the New York Stock Exchange topped 12,800, demonstrating a robust stock market upsurge. Crude oil prices then retained their upward trend in line with the stock market strength. Since May, however, factors leading to fears about the future world economy have emerged one after another, leading the benchmark WTI crude futures price to slip below $100/barrel. These factors include sluggish U.S. economic conditions, the European sovereign crisis including the Greek debt problem, downside risks for the Chinese economy, and adverse effects of the Great East Japan Earthquake on the Japanese economy. We must also pay attention to the fact that crude oil price spikes have become a matter of concern indicating a downside risk to drag down the world economy.

Geopolitical risks and oil supply disruptions drove up crude oil prices before the prices fluctuated depending on changing relations between the growth of the risks and fears about the future world economy. The first half of this year featured such market tone. In addition, policies and responses of OPEC (Organization of Petroleum Exporting Countries) and other major oil producing countries, the International Energy Agency’s recent decision to release oil reserves, and other various factors have affected the international oil market and prices. We must take note of this fact as well.

How should we anticipate the market in (or after) the second half of this year based on the first-half developments? It may be needless to say that the two biggest market-moving factors in the first half will remain important. Particularly, the conditions of the world economy will be very important for several months to come. As market participants have growingly recognized that the Greek debt problem has become “temporarily stable” with the worst scenario avoided at this moment, crude oil prices have indicated an upward trend since early July. In this sense, future world economy conditions will remain the most important factor for the market. It is difficult to predict the future course of the Middle East and North Africa situation. As far as the current deadlocked situation remains unchanged, its impact on the market may be limited. But no optimism can be warranted for the future of the regional situation. Given that problems that we cannot anticipate now could emerge as new market-moving factors, we should expect the international oil market to remain stormy in the second half as well.

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