Special Bulletin

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# Crude Oil Prices Slip Below $30/bbl Briefly

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On January 12, the benchmark West Texas Intermediate crude oil futures temporarily slipped below $30 per barrel to a low of $29.93/bbl on the New York Mercantile Exchange. This level was the lowest in 12 years, since December 2003. The key futures price closed the day at $30.44/bbl, down $0.97/bbl from the previous day, ending lower for the seventh consecutive market day from the beginning of the year. The Brent futures price also fell temporarily below $30 to $29.96/bbl on January 13. It fell further to $29.73/bbl temporarily on January 14. On January 13, the Brent futures ended at $30.31/bbl, closing lower for the eighth straight market day. On January 14, the Brent price rallied to $31.03/bbl on a closing basis. Anyway, the Brent futures briefly slipped below the psychological barrier of $30/bbl, indicating that it could drop below the level on a closing basis in the near future.

Triggering the crude oil price decline were market participants' growing expectations that a decision to lift Western economic sanctions on Iran based on the Iran nuclear agreement would be announced within the week. The expectations exerted downward pressure on the already weak oil market. The underlying oil glut was combined with expectations of Iran's comeback to the oil market to drag crude oil prices down below $30/bbl.

Also contributing to the crude oil price fall were market players' expectations that the severance of relations between Saudi Arabia and Iran earlier this year, which I took up in my previous special bulletin "A Japanese Perspective on the International Energy Landscape (253)," could lead them to intensify their oil market competition.

In addition to these factors, resurging downside risks for the Chinese economy and relevant fears about global economic deceleration have been playing a key role in weakening oil prices since the beginning of the year. On January 4, the first trading day for this year, the Shanghai Stock Exchange Composite Index lost about 7% to 3,296.26, leading the just introduced circuit breaker system to be invoked to suspend trading during market hours. The system was introduced to cool down the market and prevent any excessive rise or decline by suspending trading if the index rises or declines by more than 5%. However, the steep fall and the trading suspension added fuel to market players' fears, inducing selling to trigger more selling. After the circuit breaker system was invoked to halt trading again on January 7, the Chinese government suspended the circuit breaker system itself and vowed to continue restrictions on share sales by large shareholders in listed companies to help stabilize stock prices.

On January 12, however, the Shanghai Stock Exchange Composite Index fell to a low of 2,978.46, slipping below 3,000 for the first time since last September. Although the Chinese government has continued economic measures for soft landing on the "New Normal," market players have focused attention on downside risks in response to deterioration of economic sentiment indicators (including the manufacturing purchasing managers' index) released in the beginning of the year amid lingering fears about deterioration of the real economy. Fears about capital outflow from China have grown since the year's beginning on speculation that the Renminbi will remain weak against the dollar. The weak Chinese currency has prompted the government to carry out dollar-selling intervention in the foreign exchange market, accelerating a substantial decline in foreign exchange reserves. These factors have been feared to worsen the real economy. Various factors have thus been seen behind the Chinese stock market plunge.

The resurgence of downside risks for the Chinese economy has led to a global stock market plunge, as seen last August. The Dow Jones Industrial Average on the New York Stock Exchange fell by about 6% from 17,149 at the beginning of the year to 16,151 on January 13, continuing a downward trend. The trend has spilled over to European markets and Asian markets including Japan. China's economic risks have thus been shaking the whole of the world. Under the circumstances, a risk-off market trend has emerged, prompting money to shift to "safer assets" including the Japanese yen. As a result, the yen has appreciated, leading stock market players to fear the stronger yen's adverse effects on Japanese manufacturers. The fear has dragged down Japan's Nikkei stock average, indicating a complicated cycle where the Chinese economic risks have affected various areas.

The downside risks for the Chinese economy will decelerate the world economy, resulting in slower growth in not only Chinese oil demand but also global demand. Many market players became conscious of this point, leading selling to gain momentum on the crude oil futures market. As noted above, risk-off sentiment has prompted money to flow out of the crude oil futures market as well. In a complicated manner, low crude oil prices are expected to induce a global economic slowdown by deteriorating resource-rich economies and destabilizing emerging economies. Such expectation has led to a vicious circle in which crude oil price drops have triggered further falls in stock markets.

Even after crude oil prices slipped below $30/bbl briefly, the market is still filled with uncertainties and fears. Given the current market environment, crude oil prices may fall below the level on a daily closing basis and test even lower ground. Particularly, unstable Chinese economic trends and their impacts on the world economy will continue to attract much attention for the immediate future. As no optimism can be warranted about the future course of the Chinese economy at present, downward pressure on oil prices is not negligible. Iranian crude oil's comeback to the international market, as taken up above, is also exerting downward pressure on oil prices. Crude oil prices are likely to remain weak even amid further destabilization of the Middle East situation under the heightened tensions between Saudi Arabia and Iran.

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