Special Bulletin

A Japanese Perspective on the International Energy Landscape (578) April 1, 2022

1Q Brent Average Up 60% to $97.90/bbl

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Crude oil prices shot up year on year in the first quarter of 2022. The average daily closing price of the front-month futures contract in the quarter came to $97.90 per barrel for Brent, up $36.60/bbl or 60% from a year earlier, and to $95.01/bbl for West Texas Intermediate, up $36.87/bbl or 63%. Quarterly average crude oil prices thus rose close to $100/bbl for the first time since the third quarter of 2014. In the first quarter this year, crude oil prices featured not only substantial year-on-year hikes but also wild fluctuations. Brent ranged from $78.98/bbl on January 3 to $127.98/bbl on March 8, indicating a fluctuation of as much as $50/bbl. WTI ranged from $76.08/bbl to $123.70, posting a fluctuation close to $50/bbl. These fluctuations are of daily closing prices. Temporarily, Brent soared above $139/bbl on March 7. While gaps between the lowest and highest prices were wide, daily closing price changes exceeded $5/bbl on 11 market days in March As daily changes sharpened from late February. On more than a half of market days in March, prices posted extremely sharp changes. Price volatility was unprecedentedly high.

As a matter of course, the biggest factor behind the wild oil price fluctuations was the impact of the Ukraine crisis on the international oil market. Following oil prices' uptrend from the second half of 2021, prices accelerated their rise on speculation that the crisis could affect oil and gas exports from Russia, which accounts for 11% of global oil exports and 25% of global gas exports in 2020. Particularly, news about the United States' embargo on Russian oil exports exerted a great impact on the market. As U.S. Secretary of State Antony Blinken indicated a potential embargo on March 6, oil price hikes gained momentum. On March 7, oil prices temporarily topped $130/bbl to the highest levels since the global financial crisis. On March 8 when oil prices posted the highest closing levels in the January-March quarter, the United States announced the embargo, with President Joe Biden signing an executive order to this effect. After launching a military invasion into Ukraine on February 24, Russia has attacked major Ukrainian cities including the capital city of Kyiv. As Ukrainian forces have fought against Russian forces, the Ukraine war has lasted for more than one month. Civilian deaths have been massive, while millions of refugees have fled to neighboring countries in a serious humanitarian crisis. In response, the international community, including Western countries, has urged Russia to immediately stop the invasion and withdraw its troops from Ukraine. Western countries have also imposed unconventionally tough economic sanctions on Russia. Under growing tensions, market players have been concerned that Russian energy exports and supply could be disrupted. Such concern has triggered crude oil and natural gas price spikes.

On the day after hitting the highest level on March 8, the benchmark oil price posted a sharp decline of nearly $17/bbl to $117.14/bbl. Even after the rapid drop, the price was still high above $110/bbl. Behind the sharp downturn, market players seemingly acknowledged that the U.S. oil embargo joined by U.K. and Canadian embargoes would not have serious direct impacts on Russian crude oil supply because of the three countries' light dependence on Russian oil. They also understood that Germany and other major European countries that depend on Russian oil refrained from imposing an embargo on Russian oil. Given these points, the risk premium that pushed up oil prices disappeared, leading oil prices to fall back.

Even amid oil price hikes, other various factors exerted influence on oil prices. For instance, the United Arab Emirates' reported indication of a positive attitude towards expanding oil production in response to price hikes led to a sharp oil price fall. Later, oil prices rose back on speculation that the UAE would give priority to its cooperation with the other members of the OPEC-plus group of oil-producing countries. Oil prices came under upward pressure when market players speculated that Saudi Arabia, which holds the key to increasing OPEC-plus production, remained cautious of accepting U.S. and European requests for an increase in oil production partly because of reported complication and difficulties in U.S.-Saudi relations. Regarding the Middle East situation, the Iran nuclear talks might have some impacts on oil prices. When market participants speculated that the talks made progress towards agreement, oil prices came under downward pressure despite the possibility that Iran's comeback to the international oil market may come later in the second half of this year even if a nuclear deal is cut soon. When media reports stated that it would be difficult for the Iran nuclear talks to produce any agreement due to a new Russian request, upward pressure was exerted on oil prices. The situation of Middle Eastern oil-producing countries has thus had some impacts on crude oil prices in the first quarter of this year.

On the other hand, developments in oil-consuming countries have also shaken crude oil prices. First, the spread of COVID-19 infections in China known for its zero corona policy has exerted a major impact on crude oil prices. As a lockdown began on the COVID-19 spread in Shanghai, crude oil prices came under downward pressure in late March on growing speculation that oil demand and imports in the world's largest oil-importing country would be affected. Future economic trends and oil demand in China have potential to push up or down crude oil prices. Second, news about a U.S. plan to release strategic petroleum reserves again has had a great impact on crude oil prices. On March 31, the United States announced that it would release 1 million barrels per day or up to 180 million barrels toward the second half of this year. This is a record SPR release. The United States plans to promote cooperation with its allies to expand the global reserve release to lower crude oil and gasoline prices. The U.S. announcement led the WTI price to plunge by more than $7/bbl from the previous day. Thus various factors have had great impacts on the oil market.

This is because no new major developments have recently come in regard to the direct impacts on oil market due to the Ukraine crisis and concern on future Russian energy supply. However, we must pay attention to the Ukraine crisis and potential disruptions to oil supply as the most influential factors for crude oil prices. I here would like to boldly provide three potential scenarios. In the first scenario, the military invasion and economic sanctions will continue, with geopolitical risks remaining high, in the absence of major energy supply disruptions. In this case, crude oil prices will fluctuate in a core range between $100/bbl and $110/bbl and deviate by up to $20/bbl from the core under pressure from geopolitical risks and other influential factors. In the second scenario, serious oil supply disruptions will trigger crude oil prices' upsurge to record-high levels. In response, Middle Eastern oil-producing countries will increase production, with oil-consuming countries releasing oil reserves further, exerting downward pressure on oil prices. Basically, however, oil prices will be far higher and more volatile than at present. In the third scenario, a cease-fire agreement will be achieved to gradually stabilize the Ukraine situation. Crude oil prices will then fall to a core range between $70/bbl and $80/bbl. This range, seen in the second half of last year, is not necessarily low.

Great uncertainties exist about future crude oil prices. With various potential oil market developments in mind, we will have to keep close watch on the Ukraine crisis and the international oil situation.

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