Oil Prices Continue Uptrend amid Expectation on Oil Producers’ Meeting
-- Brent Rises Close to $50/bbl --

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On August 16, crude oil futures prices rose further. The front-month contract closed at $49.23 per barrel for Brent and at $46.58/bbl for West Texas Intermediate. These price levels were the highest since early July. The Brent price rose close to the psychologically important level of $50/bbl. Both crude oil futures prices increased for the fifth straight market day.

A major factor behind the uptrend was a growing expectation that the Organization of the Petroleum Exporting Countries and non-OPEC oil producing countries could meet to hold down the oil oversupply in the international market when OPEC holds an unofficial meeting on the occasion of the 15th International Energy Forum to be held September 26-28 in Algeria. Triggering the expectation was a remark by OPEC President and Qatari Energy and Industry Minister Mohammed Bin Saleh Al-Sada revealing the unofficial OPEC meeting plan.

Crude oil prices gradually recovered from lows (including the WTI level below $27/bbl) in the beginning of the year and topped $50/bbl in June. Since then, they have seesawed without continuing to rise. Behind such top-heavy trend of crude oil prices, there has been concern on global economic fears including the impact of the United Kingdom’s planned exit from the European Union and downside risks for the Chinese economy. Moreover, OPEC production has remained high, with crude oil prices’ rally above $50/bbl expected to bring about a stop to the U.S. shale oil production fall.

From mid-July to early August, crude oil prices came under downward pressure as market participants expected oversupply in the international oil market to be prolonged in consideration of high oil inventory levels, a record OPEC production in July (33.39 million barrels per day for the 14 OPEC members according to the International Energy Agency) and the seventh consecutive weekly rise in the number of U.S. oil-drilling rigs in operation since late June, which indicated a halt to the U.S. crude oil production decline.

In fact, crude oil prices fell from a $45-50/bbl range in the first half of July to a $40-45/bbl
range in the second half. On August 2, the key WTI futures contract fell to $39.51/bbl, slipping below $40/bbl for the first time since April 18. In a sense, the price drop might have led OPEC to plan the unofficial meeting to address the oil oversupply.

Most oil market participants have shared a view that moderate oil demand growth and slack non-OPEC oil production under low prices are leading the market to go in the direction of rebalancing in which the oil oversupply will be eliminated. However, the speed and scale of the rebalancing have been uncertain. Until early August, market participants had expected to take more time than earlier predicted to eliminate the oversupply.

For example, the IEA’s monthly report in August changed its oil supply and demand outlook. Its July report indicated that given the current OPEC production level, excess demand would arise in the international oil market in the third quarter of this year and continue to exist before becoming substantial in the second half of 2017. In its August report, however, the IEA hinted that given the current OPEC production level, small excess supply would continue to exist until the first half of 2017 before large excess demand arises in the second half of the same year.

In the face of concern about prolonged oversupply and lower crude oil prices under such oversupply, OPEC sent a message to the market indicating that some measures would be taken, if necessary. In response, Khalid Al-Falih, energy minister of OPEC leader Saudi Arabia, made a positive remark on the unofficial meeting and oil producing countries’ cooperation in rebalancing the market, the Financial Times reported, supporting crude oil prices in the market.

Conversely, however, market participants may believe that it is difficult or time-consuming to eliminate oversupply without oil producing countries’ cooperation in making some response. In this sense, the market has just responded to the news of the unofficial meeting and will shift its focus of attention to the implementation and results of the meeting. No optimism can be justified about cooperation between oil producing countries.

In the run-up to the coming unofficial meeting, oil ministers from Saudi Arabia, Russia, Venezuela and Qatar announced their agreement to freeze any increase in oil production on February 16. This action responded to a severe situation in which the WTI sank below $27/bbl on February 11. As is well known, however, this “freeze” agreement has yet to be realized, with oil producing countries divided on the freeze.

In response to a new market environment where the elimination of oil oversupply could be delayed as mentioned above, the idea of oil producing countries’ unofficial meeting and cooperation has emerged again, attracting market attention. Regarding cooperation between oil producing countries, however, relations between key stakeholders including Saudi Arabia, Iran and Russia are
complicated. In addition, they have various problems beyond the oil market logic. As a matter of fact, we see a new development where Iran’s oil production has recovered a level before Western countries imposed economic sanctions on Iran over its nuclear development program. This development could be taken into account when oil producing countries consider their cooperation. This possibility is interesting. For the immediate future, we may have to pay attention to the possibility and fate of cooperation between oil producing countries as a key point for analyzing crude oil prices.

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