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2019 First Half Average Brent Price Down $5 to $66.14

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Brent crude futures prices (the front-month contract's daily closing prices) averaged $66.14 per barrel in the first half of 2019, down about $5/bbl from the same period of last year. The highest level in the six-month period was at $74.57/bbl on April 24 and the lowest at $54.91/bbl on January 2. For the other benchmark crude oil brand of West Texas Intermediate, the average futures price came to $57.45/bbl, down about $8/bbl. The highest level in the period was at $66.30/bbl on April 23 and the lowest at $46.54/bbl on January 2. The following reviews crude oil price trends in the first half and analyze future trends:

As indicated by the low for Brent in the six-month period, the year 2019 began after Brent fell close to $50/bbl on growing concerns about oversupply and global economic deceleration in December 2018. Fearing crude oil prices' further fall, the Organization of the Petroleum Exporting Countries and some of the non-OPEC oil-producing countries decided to jointly cut their oil production by 1.2 million barrels per day from the beginning of 2019 and implemented the decision. In response, the oil supply-demand balance tightened gradually from the beginning of the year, paving the way for crude oil prices to enter an uptrend. The slow, steady uptrend lasted until April, allowing Brent to rise back above $70/bbl for the first time in five months, since November 2018.

Accelerating the uptrend was the United States' announcement of a policy seeking to impose a full oil embargo on Iran. While withdrawing from the Iran nuclear deal in May 2018, the United States granted a 180-day waiver from November 2018 on an Iran oil embargo for eight countries including Japan. In late April 2019, however, Washington vowed to repeal the waiver and impose the full Iran oil embargo from May. Amid concerns about a substantial fall in Iranian crude oil exports and growing tensions over Iran, crude oil prices rose further. Brent hit the first half's high of $74.57/bbl on April 24. Some market participants then expected to see Brent topping $80/bbl and rising further.

In fact, however, crude oil prices turned down in May, entering a downtrend. The biggest factor behind the downturn was the resurgence of the U.S.-China trade war. Although some deal between the United States and China had been expected in late April, the U.S. President raised an additional tariff from 10% to 25% on $200 billion worth of Chinese products in May. Furthermore, Washington started preparations for imposing a 25% additional tariff on about $300 billion worth of Chinese goods. In response, China raised tariffs to counter the U.S. action, adopting a confrontational approach. While some deal was expected at U.S.-China trade talks, Washington found China retreating from its earlier indication of concessions, concluded that China's concessions would not be enough and decided to raise tariffs to increase pressure on China. This is the reason China adopted the confrontational approach. The clash between the world's first and second largest economies led to the resurgence of concerns about global economic deceleration risks, prompting crude oil prices to decline. Substantial growth in U.S. shale oil production might have also exerted downward pressure on crude oil prices.

The downtrend was reversed again by growing tensions over Iran. After Brent slipped below $60/bbl on June 12, two tankers, including a Japanese one, were attacked in the Gulf of Oman near the Strait of Hormuz, leading crude oil prices to shoot up. Although the attacks caused no disruption to oil supply, the oil market reacted to the risk event regarding safe passage through the strait known as the key artery for oil transportation. Furthermore, the Iranian Revolutionary Guard shot down a U.S. military reconnaissance drone. Tehran claimed that the drone intruded into Iranian airspace, while Washington flatly denied the intrusion. Thus, tensions between the United States and Iran grew steeply. Later, President Trump said that he had given a go-ahead to a retaliation for the drone shootdown and canceled the retaliation 10 minutes before the planned implementation time. He thus indicated a volatile situation shaking the world. Amid the growingly tense Iranian situation and rising geopolitical risks including a potential military clash, Brent has remained around $65/bbl. As for the U.S.-China trade war, the two countries held a summit on the occasion of the Group of 20 Osaka Summit in late June and agreed to resume trade talks. Washington then decided to shelve the plan to impose a 25% tariff on $300 billion worth of Chinese goods. The market was relieved to see the avoidance of a breakoff at the bilateral summit. Given that the U.S.-China dispute is deep-rooted, however, no optimism can be warranted about future bilateral trade talks.

In this situation, it may be significant to set branching points and develop scenarios from the branching points in analyzing the international oil market and crude oil prices in the immediate future. Given the growing geopolitical risks, the first branching point is whether a military clash would occur regarding the Iranian situation. The second branching point is what the clash would be like.

In a scenario free from any military clash, oil supply and demand factors and global economic risks would exert dominant influences on the market and crude oil prices, though with U.S.-Iran tensions remaining. If oil demand increased steadily in the absence of global economic risks, crude oil prices would remain around the current levels, with oil supply meeting demand. Although non-OPEC oil production would increase faster than global oil demand, the OPEC-plus group would continue supply and demand adjustment. If the global economy decelerated on the intensification of the U.S.-China trade war, however, crude oil prices and their fluctuation range would come under heavy downward pressure and fall by some $10/bbl or more.

If a military clash occurred and ended up as a temporary, limited one, crude oil prices and their fluctuation range would rise over a short term. Such clash would come in an unforeseen circumstance and parties to the clash would exercise restraint. With efforts to avoid any expansion of the clash gaining momentum, the clash would end up as a temporary, limited one. Even in this case, however, safe passage through the Strait of Hormuz would be affected, causing disruptions to oil supply temporarily. After a short-term spike, crude oil prices' fluctuation range would rise by $10-20/bbl (or more depending on the seriousness of supply disruptions). If the situation were stabilized later, with any additional clash continuing to be avoided, developments would be close to those in the abovementioned scenario free from any military clash.

If a military clash occurred and lasted for a certain prolonged period and became a full-blown one, crude oil prices would spike substantially, with the international supply-demand balance tightening. Such military clash would occur in an unforeseen circumstance, leading to a repetition of retaliatory attacks. The clash would expand geographically and spatially, instead of being resolved in a short span. This would be the worst scenario where safe passage through the Strait of Hormuz would remain difficult during or beyond the duration of the clash, with oil supply disruptions growing serious. Furthermore, the geographical, spatial expansion of the clash would lead oil production in other Middle Eastern countries to decline on foreign companies' withdrawal and damage to infrastructure, making oil supply disruptions even more serious. Crude oil prices then could rise beyond $100/bbl or shoot up further depending on the greater seriousness and longer duration of supply disruptions.

The above analysis on future possibilities focuses on geopolitical risks. Factors exerting influence on the international oil market and crude oil prices are extremely uncertain. They are difficult to predict. Japan, which depends heavily on oil among energy sources, on oil imports and on the Middle East, must closely watch the future oil situation and prepare a strategy to flexibly, timely and adequately respond to any relevant development.

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