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2019 January-September Average Brent Price down $8.35/bbl to $64.37/bbl

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The average front-month futures contract price for the benchmark Brent crude oil came to $64.37 per barrel in the first nine months of this year on a daily closing price basis, down $8.35/bbl or 11.5% from $72.72/bbl in the same period of 2018 and up $11.86/bbl or 22.6% from $52.51/bbl in the same period of 2017. The average in the January-September 2019 period thus stood at around the middle between the averages for the same periods of 2017 and 2018. In the January-September 2019 period, the key Brent futures price peaked at $74.57/bbl on April 24 and bottomed at $54.91/bbl on January 2. In a remarkable development on September 16, the price shot up by $8.8/bbl from the previous trading day to $69.02/bbl after Saudi Arabia suffered a crude oil production loss of 5.7 million barrels per day on drone attacks on the oil facilities in the Kingdom.

The average key futures price for the other benchmark crude oil of West Texas Intermediate in the first nine months of this year stood at $57.10/bbl, down $9.69/bbl year on year, peaking at $66.30/bbl on April 23 and bottoming at $46.54/bbl on January 2.

In response to a decision by the Organization of the Petroleum Exporting Countries and some non-OPEC oil-producing countries to jointly reduce production in December 2018, crude oil prices rose in the beginning of 2019 after a plunge late last year. As the United States came up with a full oil embargo on Iran, they increased in anticipation of an Iranian oil export fall and a tighter supply-demand balance, peaking in late April. In May, however, the United States toughened its stance against China again through tariff hikes, leading crude oil prices to enter a downtrend on growing global economic risks through the escalation of the U.S.-China trade war.

Next, geopolitical risks in the Middle East attracted attention from oil market participants. Tensions over Iran grew on attacks on tankers and the shootdown of a U.S. military drone near the Strait of Hormuz in June. Middle Eastern geopolitical risks remained high later on Iran’s seizure of a British tanker and its resumption and enhancement of uranium enrichment. Potential accidental clashes became a matter of concern. Then came the abovementioned drone attacks on the Abqaiq and Khurais oil facilities known as one of the hearts of Saudi Arabia’s oil production, bringing about the oil production loss of 5.7 million bpd and rattling the world. The shocking incident triggered an oil price spike. As Saudi Arabia recovered the destroyed facilities more smoothly than expected and restored its oil production level before the attacks by late September in line with its published schedule, however, crude oil prices regained stability. The Brent futures price closed at $60.78/bbl on September 30, falling back to the level before the attacks.

So far this year, crude oil prices have been susceptible to two major factors -- the U.S.-China trade war and relevant global economic risks, and the destabilization of the Middle East. The two factors move the market in different directions. When the two factors balanced with each other, crude oil prices narrowly fluctuated. When their balance collapsed, however, they moved remarkably. This means that crude oil prices declined when market participants focused their attention on the U.S.-China trade war and rose when the destabilization of the Middle East attracted their attention. As a matter of course, this is an excessively simplified relationship. Other factors attracting attention from market players include U.S. shale oil productions changes, oil supply drops or disruptions in other major oil-producing countries like Venezuela, and OPEC-plus policy trends. Undoubtedly, however, the two abovementioned factors have exerted greater influence on the market.

How the two major factors will develop would remain the most important point for anticipating the international oil market and crude oil prices through the end of this year or 2020. I would like to check oil market supply and demand conditions as the base for considering the influence of the two major factors.

Apart from destabilizing factors such as the two major ones, the international oil market can be expected to see supply growth surpassing demand growth depending on non-OPEC oil production alone. According to the latest monthly oil market report by the International Energy Agency, global oil demand in 2020 is predicted to increase by 1.3 million bpd from the previous year. As the world economy grows at a moderate pace of above 3%, oil demand is expected to increase mainly in Asian emerging countries. At the same time, however, non-OPEC oil production including U.S. output in 2020 is predicted to expand by 2.3 million bpd from the previous year. Non-OPEC oil production growth is thus expected to exceed global demand growth. Therefore, it is important for the OPEC-plus group to continue to adjust supply. Particularly, Saudi Arabia will play a central role in adjusting supply. Saudi Arabia's significance as a suppler adjuster in the international oil market is distinct.

The problem is how the two major factors would be discounted into the market based on such supply and demand conditions. The fate of the U.S.-China trade war remains unpredictable, leading global economic risks to linger. If the situation worsens further with a global economic slowdown realized, downside pressure would grow on crude oil prices. If the U.S.-China trade war follows the worst scenario, global oil demand growth would be 0.67 million bpd (including 0.21 million bpd in China) less than in the reference scenario due to global economic growth deceleration, according to an analysis by the Institute of Energy Economics, Japan. If global oil demand growth is halved from the IEA-projected level, crude oil prices would fall sharply without a substantial additional production cut by the OPEC-plus group. Regarding global economic risks, the fate of the chaotic Brexit problem may also attract attention. From late September to early October, the Brent price declined as U.S. stock prices fell on growing concern about the future course of the U.S. economy. On October 2, Brent slipped below $60/bbl to $57.69/bbl, reflecting global economic risks.

The destabilization of the Middle East is also an unignorable risk. The attacks on Saudi Arabia and subsequent oil supply disruption in September might have ushered in a new stage. Although Saudi Arabia rapidly restored oil production to overcome the disruption, the temporary production loss in Saudi Arabia as the heart of global oil supply shocked oil market players. It is very important how this incident would raise tensions and uncertainties over Iran to bring about relevant geopolitical risks. Given that no one can substitute oil supply from the Middle East or Saudi Arabia over a short term, we must keep various risks in mind and be prepared for "war even in peacetime".

In an analysis published in July, our institute gave a reference outlook indicating that Brent would remain in the lower half of a $60-70/bbl range in 2020. In a higher price case including the destabilization of the Middle East, the price would be $15/bbl higher. In a lower price case including global economic deceleration, the price would be $10/bbl less. We will have to closely watch potential developments and turbulences regarding the two major factors.

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