Special Bulletin

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January-February Average Brent Price Rose Close to $60/bbl

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The average daily closing price of the front-month Brent oil futures contract in January and February 2021 rose by about $15 per barrel or 36% from the 2020 average of $43.21/bbl to $58.78/bbl. That of the front-month West Texas Intermediate contract in the period also increased by about $16/bbl or 41% from the 2020 average to $55.58/bbl. Brent closed at $60.56/bbl on February 8 and WTI finished at $60.05/bbl. They rose back above $60/bbl for the first time in 13 months from January 2020.

Both Brent and WTI have crept up since the beginning of this year. WTI stood at around $47/bbl in the beginning of the year and rose above $50/bbl on January 6. It took some one month to go up above $55/bbl on February 3 and it topped $60 on February 16. Its peak in the first two months of the year was $63.53/bbl on February 25. In fact, the uptrend since the turn of the year started in the second half of last November. Until then, WTI remained around $40/bbl for about five months from last July. In this way, WTI entered an uptrend last November and has recently topped $60/bbl. Its peak of $63.53/bbl was the highest in 22 months from late April 2019.

Under the COVID-19 disaster, WTI slackened throughout 2020, plunging to the unprecedented low of minus $37/bbl. Its rise to the present levels has been supported by a complex combination of some key factors.

The first important factor is COVID-19 vaccination that has brought about hopes of an end to the COVID-19 pandemic and global economic recovery. The current uptrend started last November when COVID-19 vaccination began with vaccines approved in the world. Since then, vaccination has made progress mainly in Western advanced economies. Israel has completed first vaccine doses for more than 50% of its population. The vaccination's effects including those against variant COVID-19 viruses, as well as adverse events related to the vaccination, have still remained uncertain, but progress in vaccination has led hopes to grow on the effects. In reality, the pandemic is still expanding, infecting more than 110 million people and killing more than 2.5 million in the world. However, it is increasingly expected and hoped that the pandemic would come to an end as vaccination makes further progress.

In such situation, hopes of global economic recovery are growing. The latest world economic outlook by the International Monetary Fund, released in January, forecasts that global GDP would grow 5.5% in 2021 after contracting 3.5% in 2020. In all countries including such advanced economies as the United States, European countries, and Japan, GDP contracted substantially in 2020 and is expected to grow steeply in 2021. While it is still uncertain whether the global economy would achieve a smooth V-shaped recovery, hopes of the pandemic's end and economic recovery are undoubtedly growing.

Mirroring the growing hopes of economic recovery has been the stock market. The Dow

Jones industrial average on the New York stock exchange entered an uptrend along with crude oil prices around last November and topped 30,000 in December for the first time. Hopes placed on the incoming Biden administration were combined with expectations on an end to the pandemic. The average topped 31,000 in January and sustained an uptrend until February 24 when it hit an all-time high of 31,962. In Japan where the stock market has retained an uptrend, the 225-issue Nikkei average on the Tokyo Stock Exchange rose back above 30,000 on February 15 for the first time in 30 and a half years.

Such stock market upsurge has led to hopes of real economic improvements and rising demand for energy including oil. Hopes of an end to the pandemic also lead to those of rising transportation demand that would trigger a full-blown pickup in oil demand. Market players have grown conscious of such hopes. Even more important for the oil price uptrend than such oil demand-boosting effects have been financial factors such as excessive liquidity and a subsequent rise in appetite for risk assets, which have underlain the stock market upsurge.

As the COVID-19 disaster plunged the global economy into the worst situation since the Great Depression, countries stepped up fiscal expansion and monetary easing on an unprecedented scale to support and boost their economies. The powerful monetary easing has not only supported economic activities but also brought about remarkable interest rate drops and excessive liquidity or money supply. Surplus money has gone into the stock market to support the abovementioned stock price upsurge. At the same time, surplus money has apparently flown into other risk asset markets including the oil futures market. Attention should be paid to such financial factors that have boosted stock and oil prices.

The second important factor behind the oil price uptrend is joint oil production cuts by the Organization of the Petroleum Exporting Countries and some of the non-OPEC oil-producing countries including Russia. In response to “oil demand evaporation” under the COVID-19 pandemic in 2020, the OPEC-plus group has implemented record production cuts. Since the second half of 2020, the group has gradually narrowed the cuts in view of oil market supply and demand, but the joint production cuts have functioned well. At the group’s meeting early this year, Saudi Arabia made a surprise offer to unilaterally reduce its oil production by 1 million barrels per day, which has also supported oil prices. As hopes of global economic and oil demand recovery have grown, the OPEC-plus group’s joint production cuts and Saudi Arabia’s additional cut have successfully supported the oil price uptrend.

In the future, however, the oil price uptrend cannot necessarily be expected to continue. This is because the factors supporting the uptrend have some uncertainties. While hopes of an end to the pandemic are high and are expected to come true, there are uncertainties about when or how fast the pandemic would go in the direction of the end. Even in advanced economies where vaccination is making progress, carelessness could make it difficult to control infections again. Hopes of economic recovery are high, as reflected in the stock market upsurge. However, financial factors have contributed much to the stock and oil price upsurge. We must watch how firmly the global economy would actually recover. Regarding oil supply, crude oil prices’ rise above $60/bbl is encouraging U.S. shale oil production to increase. The International Energy Agency in its February oil market report revised its U.S. oil production projection in 2021 up by 0.31 million bpd from the previous report to 16.55 million bpd, close to the 2020 level. Given crude oil price hikes in the second half of February, the projection may be raised further. On the other hand, the OPEC-plus group could narrow its production cuts in response to crude oil prices’ rise above $60/bbl. While the OPEC-plus group continues to adjust production to maintain an appropriate supply-demand balance, oil price hikes could lead some group members to be tempted to increase production. Towards the second half of this year, we see numerous destabilization factors including the possibility of Iran's comeback to the international oil market. Crude oil prices have risen faster than assumed in the higher price scenario in an IEEJ outlook released late last year, but we will have to pay attention to their future trend.

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