Oil prices in review

THE SENSATIONAL AND UNPRECEDENTED NEGATIVE PRICE FOR MAY WTI FUTURES WAS AN ANOMALY DUE TO US PRODUCTION AND US STORAGE ISSUES BUT IT IT WILL HAVE WIDER IMPACTS FOR AS LONG AS THEY CONTINUE AND WAS ALSO A SYMPTOM OF UNDERLYING ISSUES THAT THE INDUSTRY MUST ADDRESS. WE LOOK AT THE WIDER PRICING PICTURE.

A rebalancing of supply and demand

Ian Moore, director of the Oil Market Journal, gives some insight; "Oil prices are in free fall as the market tries to force a rebalancing of supply and demand. The storage crisis which is now being played out was inevitable after the combined effects of the failure of OPEC and Russia to agree cuts on 6th March as well as widespread COVID lockdowns taking effect resulting in oil demand down to about 70m bpd from 100m bpd. The cuts from 1st May agreed over the Easter weekend, will shift things in the right direction but still leave a Q2 2020 oversupply of around 20m bpd.

"The latest data (15th April) indicates "US Total Oil Demand" down around 6,000 million bpd (-30%) from before the COVID crisis spread to the US. And the fall in demand in the US is replicated across the world.

Even late March, the OMJ daily report was already anticipating the current issues stating: 'In the near term we expect things to get rather messy in April and May as storage fills. Oil analysts continue to warn that global oil storage tanks will be full by mid-May.'

And by early April: 'Our expected scenario is full global oil tanks in late April and into May which would result in a very "hard landing for oil."' A forecast which certainly played out in the spectacular and historic lows seen at time of writing

Asked about the likely outlook Ian replied, "We expect demand to rebound in late May and June as the lockdown is lifted across the US and Europe. However, demand during the summer will likely level off much lower than normal.

"Global oil stocks will remain high through 2020 and it is likely crude prices will remain below $45 during 2020 and well into 2021. We also expect some important demand sectors such as aviation to take years to recover resulting in low cost heating oil for UK and Ireland consumers over the next few years. "

Aberdeen-based Derek Leith, EY's global lead for oil and gas tax, comments; "The West Texas Intermediate (WTI) price drop is not reflective of the oil and gas industry worldwide but is very specifically driven by the production and demand imbalance in the US. The headline-grabbing negative oil price was driven by a relatively small number of May contracts held by financial traders having to be sold before they expired, and the sellers finding there were absolutely no buyers.

"While WTI prices won't directly impact on the UKCS, this is a stark reminder of oil price volatility, and that smaller UKCS producers may find it very hard to sell their crude at the prevailing market rate. There is likely to be a renewed focus and rigour on decreasing operational costs, particularly for smaller players. The companies which respond quickly, are agile and carefully strategic are likely to emerge in a better position in the medium and long-term."

An unprecedented oil market

"We are faced with an unprecedented oil market where the factors affecting price are beyond anyone's control," comments Basil Shrourou, founder of Fuel Prices Online. "What began as a three-way output spat between Russia, Saudi and the shale oil producers in US was quickly overshadowed by the catastrophic impact on demand of the coronavirus resulting in a price in freefall and cargoes reportedly almost 'given away' as storage reached capacity and no-one was inclined to buy"

Asked about the likely future direction Basil stressed that there is very little action anyone can take with future pricing dependent on the containment of Covid-19 as the first OPEC+ cut seems to have had very little impact on the market. "Based purely on previous experience, if we don't hear some good news on the virus and economy soon, we will see international facilities shutting down and cessation of imports. With a reported 75% drop in forecourt sales as a result of the lockdown, there is no point producing some product that cannot be sold or stored."

However, Basil is hopeful that we are approaching the bottom. "Once there is positive news, we will see demand begin to lift again. With kerosene at approximately 9ppl (Platts calculated PPL) at time of writing and the spot real time, as I am looking at my FPO App, it is trading even lower than the 8ppl level we saw in 96/97 when the Pound £ exchange rate was at approximately $2 US Dollars. This is creating a real dilemma for distributors considering buying long term but concerned about storage"

With UK 'heating oil' prices down more than 57%, is it time to fill the tank?

While the UK and the rest of the world get their benchmark from Brent Crude Oil this is also down to less than $21 per barrel. At its highest point in 2020, it was trading at $71.25.

For people on oil-fired heating, this is already having a massive effect on their prices but more could follow. OGUK boss Deirdre Michie commented; "The dynamics of this US market are different from those directly driving UK produced Brent, but we will not escape the impact.

"Although production levels have been reduced drastically, it is still not enough to offset the fall in demand, which is at the lowest levels in 25 years. A recent report from The IEA warned markets to brace for an unprecedented lack in demand, that will reach levels not experienced since 1995.

While there is still the potential for the price to decrease some countries are starting to relax lockdown measures, this could lead to an uptake in demand and cause oil markets to begin to recover.

"It would be advisable for people with oil central heating to at least consider filling the tank while prices are still low."

Sustained increase in orders

Through this period of 'change and turmoil', Rob Maynard, CFO Boilerjuice, has also seen significant impacts on the heating oil supply chain.

"There has been a significant and sustained increase in people searching online for heating oil since the middle of March, with an initial period of slightly panicky buying as people spent more time at home followed by customers stocking up at the lowest prices seen for a very long time.

"We've experienced a record number of online quotes and orders through the

BoilerJuice platform, peaking at around 6million litres a day. During this time, our priority has been working with our amazing suppliers to manage customers' expectations while the supply chain was stretched and prioritising deliveries for vulnerable customers. Our suppliers have been resolute throughout, working around the clock to manage huge order volumes (approx. 3x higher than we would expect at this time of year).

Rob also comments on the appeal of stocking up at current prices; "Prices continued to fall through April as global oil prices fell to record lows and many of our customers have enjoyed significant savings, with average prices dropping to pretty much half of what they were 12 months ago. Demand remains very high with customers sensibly stocking up at exceptionally low prices."

Free oil? Not today

Mark Waddington, Channoil Consulting, addresses the impact on fuel prices in the UK of WTI Futures trading at negative prices.

"The WTI futures contract is an important global crude oil benchmark but its price is based on market value for delivery at an inland terminal at Cushing, Oklahoma, USA, one of the main storage hubs in US crude oil export. The recent demand collapse has left it practically full but that alone is not enough to explain why the benchmark price went negative.

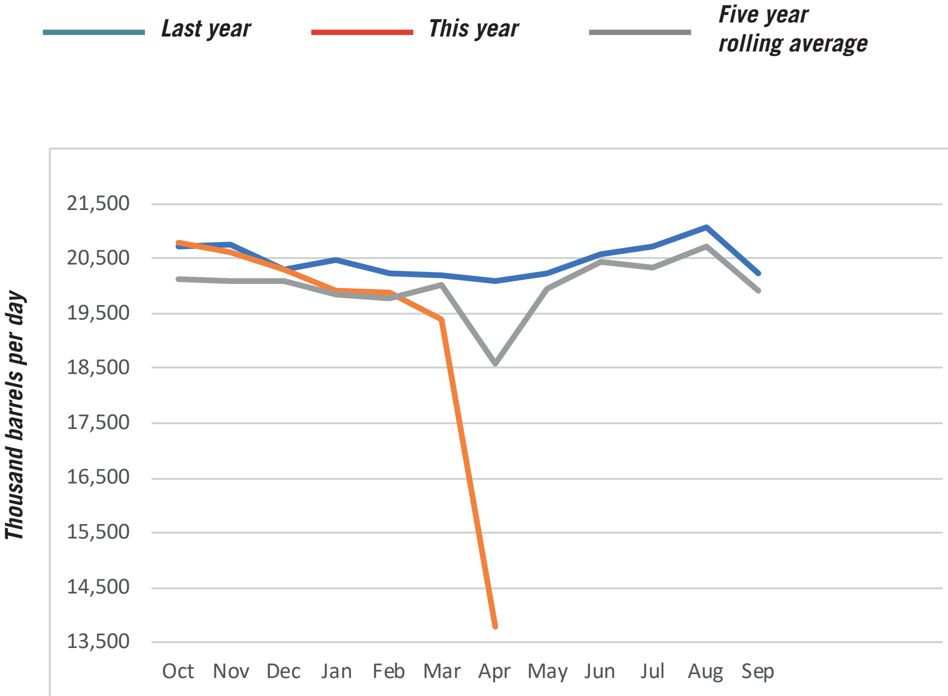
"It is also important to understand who uses oil futures contracts. These are oil producers who sell forward on futures market to secure a selling price for their oil production, consumers of oil, such as refiners, airlines, trucking companies, and others, who buy ahead on futures markets to guarantee the price of the oil they are buying; and finally, investment funds and speculators in the financial sector, who want to invest in a commodity asset class.

Mark goes on to explain the negative price; "It is largely a technical thing: speculators who bought futures contracts for delivery in May found themselves holding something that no-one wanted and were then looking to close out their financial exposure by selling them back. Since there were no buyers for these long positions the speculators were at a disadvantage and had to sell at a huge loss. The parties on the other side of the deal are most likely to be crude oil producers who had sold forward.

"It is unlikely that any oil has changed hands at negative prices. If anything, the oil producers will have taken extra profit from their hedging. None of these extremes has any real bearing on the pump price or the delivered price of fuel, even though those prices are much lower today because of the general collapse in oil prices."

As Mark concludes; "It would be unwise for customers to expect suppliers to deliver free of charge at any point soon."

U.S. product supplied of crude oil and petroleum products thousand barrels per day



Source: U.S. Energy Information Administration and OMJ