# Spring forward, fall back?

*As 2011 draws to a close, UX Energy Services' consultant Dr. Craig Lowrey looks back on another volatile 12 months for oil prices, as well as considering what 2012 could hold for consumers….*

**International factors**

With approximately 90 % of the change in the price of heating oil determined by movements in the global price for crude oil, international factors have continued to dominate the market in 2011. Since 2008, economics and geopolitical factors have been the main drivers and look set to remain so into 2012 and beyond.

At the start of 2011, the crude price had been drifting upwards from the level of around $90 per barrel seen in December 2010. At the end of January, prices climbed above $100 per barrel as the Arab Spring emerged across the Middle East. From this point on, the price of a barrel of oil remained above $100 almost exclusively throughout 2011 and – at the time of writing – has only fallen below this level on a very small number of occasions.

As far as availability is concerned, loss of supply from Libya has been the main issue in the crude oil market. Flows fell from around 1.6 million barrels per day at the start of the year to effectively zero in early February as the conflict escalated. This contributed to the crude price climbing towards $125 per barrel – a level seen by the International Energy Agency (IEA) as putting the world at a greater risk of recession. (For a large part of the year, the price has been around $110 per barrel.)

Of course, this is below figures seen in mid-2008 when the market was around $150 per barrel. At that time the sterling-US dollar exchange rate was approximately $2 to the pound – implying a UK price of around $75 per barrel. This year, exchange has been closer to $1.60 to the pound, meaning that (assuming a figure of $110 per barrel) a price of oil to UK consumers of around $69 per barrel has not fallen by as much as the price of the underlying fuel itself.

**Crisis in the financial markets and OFT investigations**

As well as the situation in the Middle East, the other main driver for oil prices has been crisis in the financial markets. The evolving situation in the Eurozone and its implications for world economy have never been far from the headlines or the thoughts of traders in the crude markets. As such, the price of oil has ebbed and flowed in line with economic expectations – albeit remaining firmly above the aforementioned level of $100 per barrel.

One major development was the investigation by the Office of Fair Trading (OFT) into the off-grid energy market. While this probe did not focus exclusively on heating oil, it did form a very large part of the findings published in October.

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The OFT found no evidence of price fixing or any other form of collusion, and that competition had been a limiting factor on prices with suppliers not achieving what it viewed as excessive profit margins. However, a number of companies were criticised for the way in which heating oil prices were presented – an issue addressed through the organisation's enforcement powers under competition law. One aspect of the investigation is still ongoing, namely that some suppliers have been charging a different price at delivery to that quoted when ordered.

***The 2011 Annual Energy Statement*** presented by the Department of Energy and Climate Change did not see any mention of heating oil, despite the 1.6 million domestic users in the UK. Although, in his statement to the Commons, energy secretary, Chris Huhne, did highlight energy efficiency and insulation as a means by which customers could keep spending on fuel down. However, with the government reiterating its view that the long-term objective was to move away from "an excessive reliance on fossil fuels", what this goal means for the heating oil sector remains unclear.

**The outlook**

As the year drew to a close, the IEA published its ***2011 World Energy Outlook***, in which the Asia-Pacific region's crucial role in determining the future of oil prices was again highlighted. In the short term, the restart of Libyan output is bolstering supply with the country's state-owned oil company expecting production will be back at pre-conflict levels by the end of 2012. Crucially for the short to medium-term, the IEA stated that the period to 2015 will be pivotal in terms of investment in new fields and infrastructure. If the actual figure is a third less than this amount, then oil price increases to $175 per barrel ($150 per barrel in real terms) are a possibility it warns.

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Looking to 2012, whilst, in the OFT's eyes, there is a "fair" heating oil market across the UK, international factors will dominate. Although the continuing increase in production from Libya will help bolster supplies, this may prove to have little in the way of an impact on prices should the crisis in the Eurozone not be resolved. Indeed, with growth forecasts for the EU and US in question and fears over the rate of expansion of China's manufacturing sector, the main issue may in fact not be one of ensuring adequate supplies but rather ascertaining where oil demand will come from in a potentially stagnating global economy.