PORTLAND MARKET REPORT

"A CHAOTIC AND LARGELY DIRECTIONLESS MARKET"

November update

As we hit the final quarter of the year, it's fair to say that pricing volatility and uncertainty have, to date, been the oil market watch words of 2015.

After the massive downward price trend in Q4 2014, we have seen for most of the year a chaotic and largely directionless market, but that nonetheless, has generated significant price volatility on a daily basis. Such price movements – up one minute and then down the next – are very different to what was experienced in 2014. That was a price crash, characterised by big movements in price, but always in the same direction. Planning and decision making in such a bearish environment actually becomes easier, because the market signals are so strong. Absolute price volatility on the other hand – large price movements but in neither direction over any period of time – makes life extremely difficult for both buyers and sellers of oil, as there are simply no clear or visible trends to aid decision making.

"NOBODY KNOWS EXACTLY WHERE PRICES ARE GOING"

That prices have been so volatile in 2015 is illustrated by the graph on page 4. On the surface, this simple bar chart doesn't seem particularly spectacular. But it's actually quite remarkable that 2015 has so far been the 3rd most volatile year for oil prices over the last 10 years – only surpassed by 2008 and 2011, which experienced the financial and Eurozone crises respectively. To think that price movements in 2015 have been greater than last year (with all the movements in price that we experienced in 2014) and yet the price today ($50ish per barrel), is not much different to the price at the start of the year, only highlights just how much absolute volatility we have experienced over the last 9 months.

The uncertain outlook for oil prices

It also shows just how uncertain the outlook is for oil prices going forward and it's probably worth considering why oil is seemingly at such a crossroads. In the red corner we have a formidable array of factors that seem likely to push prices down further. First up we have China's economic slow-down which is clearly having a significant downward impact on all commodity prices around the world (oil, coal, metals and agri products). Put simply, China is not buying as much and building even less. Also in the red corner is the ongoing death struggle between the frackers and the sheiks – neither willing to cut production and both seemingly with large appetites for sustaining financial losses in order to maintain market share. Adding their bit to this part of the narrative are the bankrupt petrostates like Venezuela and Iran, releasing more and more oil onto the markets (because they have little choice but to keep up revenue streams) and in doing so are further compounding the supply glut. Finally in the red corner we have two political factors that are currently weighing heavy on oil prices. Firstly, with all of Europe's political, social and humanitarian woes, who would confidently bet against another recession in the Eurozone? And more pressing than this, is the almost certain, imminent rise in US interest rates. This will considerably strengthen the value of the $, which for those who have to convert their local currency into $ to buy oil, (ie, the rest of the world) means that they can afford less and will thus buy less.

Wow – so far, so bearish! Surely all of the above means that prices can only keep falling? Well, don't get carried away just yet, because in the blue (bullish) corner, we have arguably the most powerful price driver of all – the fear factor! Talk to anybody in the street and they will confidently tell you that oil prices are going to rebound upwards and that it is just a matter of time. Take a look at any global population forecasts (7bn to 10bn over the next 20 years) and try and argue convincingly that oil consumption will not continue to rise. Then listen to the radio or watch TV and declare with confidence that social and political instability in the Middle East will no longer affect oil prices. Even the Chinese economic slow-down has an angle that doesn't point to a drop in demand. Yes, a slow-down means slower growth, but that is not the same as a reduction in oil consumption. A China showing 4% GDP growth (rather than 10%) is still consuming more oil than last year, or the year before, or the year before that. Plus let's face it, if the Chinese economy can suddenly slow down, then so it can just as easily be ramped back up by a state controlled economic system that sees much geo-political value in keeping ahead of the rapidly recovering US economy. Lastly, turning to the supply side of the argument, don't forget that conventional oil production continues to fall each year and supply levels are only being propped up by unconventional sources (eg, fracking). What happens when the fracking boom ends, as some commentators are predicting, either because of reducing production yields (due to geological limitations) or lack of funds (due to the low oil price)?

The world's worst oil price predictors

Nobody knows exactly where oil prices are going and if anybody does – or claims to – they tend to try and keep quiet about that fact. Unless you're Goldman Sachs of course – the world's worst oil price predictors – who have declared that $20 per barrel is now a possibility and is probably the best reason to think that prices will rise! But, Portland has no right to be smug when it comes to price predictions (as regular readers of this report may remember), so the only thing we will predict with confidence is continued volatility and more uncertainty.

For more pricing information, see page 26

Portland Fuel Price Protection
www.portland-fuel-price-protection.com