PORTLAND MARKET REPORT

"A RECIPE FOR DROOPING OIL PRICES"

February update

A new year in a new decade and time for some oily predictions from Portland Towers! Last year when we wrote our start of year report, oil prices were at $50 per barrel and we predicted that as long as President Trump didn't do anything too crazy, prices in 2019 would increase to a range of $65 - $75 per barrel. Well, there was certainly plenty of craziness from the orange-faced one, but prices did indeed sit in our predicted range for much of the year. The average for the 12 months was actually $64.23 (largely the result of the low starting price in January), with prices peaking at $75 per barrel in May. In the second half of the year, prices did steady and start to fall, so that by December, the oil price stood at $67 per barrel. 98 working days in 2019 saw a price between $65 to $75 and 178 working days (70% of the year) experienced prices somewhere between $60 - $70. So, if anything, we were a tad bullish in our range prediction (to the tune of around $5/barrel), but as predictions go, we think we didn't do too badly…

What does stand out from 2019, is how significant levels of tension in the Middle East had so little impact on oil prices. In any year up to the present day, missile attacks on Saudi oil facilities, the seizure of oil tankers in the Straits of Hormuz and targeted killings of Iranian officials by American forces, would have sent prices sky rocketing. Not so in 2019, and whilst these events did have immediate effects (the Abqaiq-Khurais Saudi drone attack pushed prices up $5 a barrel overnight), price movements were short-lived and oil prices soon settled back to "normal" levels. Which mainly tells us that the underlying oil market is a bearish one and Portland sees this bearish trend as one that will continue throughout 2020.

The main reason behind this view is that most economists seem to agree that some form of economic slowdown is inevitable in 2020 and this will bring a slowing down of demand (a trend already evidenced in Q4 of 2019). It is also difficult to see how any thawing of US-China trade relations will sufficiently lift the economy to accelerate oil demand growth back to the levels of 2016-18. On the production side, the US shale oil industry is pumping more and more oil (up 10% on 2018 volumes), making the US now easily the biggest oil producer in the world (a whopping 13m bpd versus 10m bpd for Saudi Arabia and Russia). With export facilities in the Gulf of Mexico finally coming into play, that excess oil is now finding its way to global markets, just as demand looks to be tailing off. Put the two together and you have a recipe for drooping oil prices.

"SOME FORM OF ECONOMIC SLOWDOWN IS INEVITABLE IN 2020'

Such a scenario puts very significant pressure on our friends at OPEC, as they rein in their own production, and try and drive prices back up. For the last three years, they have shown uncharacteristic discipline in maintaining agreed production cuts and indeed, in December of last year, further production cuts were signed off. But it is beginning to feel now that OPEC is swimming against the tide, with more and more of their Member states (and "guest" nation Russia) bitterly complaining about production caps, as they see shale oil simply gobbling up the market gaps that appear when OPEC pulls back. It is also worth pointing out that the production cap regime introduced by OPEC at the end of 2016 was supposed to be a temporary 6-month measure (to "support the market"), but has now gone on for more than three years…

So, we have a global economy possibly heading for skid row, the US shale oil industry going absolutely fracking crazy and the operational unity of OPEC beginning to crack – prices are only going one way surely? That would certainly seem to be the logical conclusion, but each one of the aforementioned bearish factors can easily be deconstructed. Number one; a concerted effort by Trump and Xi Jinpeng could easily set the global economy back into a mega growth phase. And remember, neither of these two Presidents play by any rules, other than their own. Two; the Saudis have just started the process of floating their most precious asset (Saudi Aramco) and a prolonged drop in prices would be disastrous for long-term Saudi prosperity. So, expect them to do whatever it takes to maintain OPEC unity and continue to drive for production cuts. Finally, factor number three; it's not even a well-kept secret, that most US shale oilers are not only massively in debt, but they haven't made any money for the last three years. A drop in price will scatter investors and send them in search of considerably safer bets than shale oil. In turn, this will put most of the smaller, marginal producers out of business and the whole sector could easily wrap-down, just as quickly as it racked-up in the last decade.

Those are three entirely credible scenarios, which can be layered on top any number of bullish scenarios around tension in the Middle East, regime change in Venezuela and the rapid decline of conventional (non-shale) oil exploration projects. Which means that whilst a bearish year is the most likely outcome for 2020 (with prices slowly ticking down), we also fully expect to see some major price spikes in the 12 months ahead, as geopolitics and economics frequently boil over. Depending on when those spikes occur, the price of oil this time next year could easily be back up to the $80 mark - but for the average of the year, we expect a price of around $55 - $60 per barrel.

For more pricing information, see page 22

Portland Fuel Price Protection
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