PORTLAND MARKET REPORT

JANUARY IN VIEW

PREDICTING THE PRICE OF OIL THROUGH 2022

Although sensible people try to avoid making oil price predictions, we like to put our head 'above the parapet', at the beginning of each year, with a projection of where we see prices over the next 12 months. Before doing that, we're happy to point out that, in 2021, we got our price predictions pretty much bang on, meaning that, for 9 out of the last 10 years (the exception being 2014), we have got our annual forecasts broadly correct. We won't labour the point as no-one likes a smart-a*se and the reality is that 2021 was a fairly easy year to call after the carnage of 2020. Prices were low, investment in new oil and gas projects was non-existent and the economic impact of covid (i.e., lockdowns) was steadily diminishing. It didn't take a genius, therefore, to conclude that prices would rise in 2021.

'THE SUPPLY-DEMAND SITUATION REMAINS CRITCAL'

And so, it came to pass, with the price of crude starting the year at $55 per barrel (Jan 21) and finishing 2021 at $77, having hit a peak 2 months earlier at $86 per barrel in October. The narrative behind these price movements was pretty much as we wrote last year; "we predict that prices will go up in 2021 and even see the possibility of a major price spike, as the gap between supply and demand becomes critical". Now that we are turning our attentions to 2022, we can say that the supply-demand situation remains critical and, in fact, the danger of a major price spike looks more likely this year than it did in 2021. Ongoing factors around declining investment in oil and gas coupled with buoyant demand growth are still at play, but the joker that has now been added to the pack is the extraordinary situation regarding global gas prices.

We covered this in detail in November but, when the price of any commodity octuples (natural gas has risen by over 800%!), buyers naturally start to look for alternative sources of supply. Crude (or refined crude) is one of those alternatives, and power stations, heavy industry, fertiliser manufacturers and a legion of other gas users are all now switching to oil. Anecdotally, only last week Portland was approached by a food processor who wanted to switch to oil because the gas price made their operations commercially unviable. And, whilst the general public may consider oil prices already to be too high, they are still nothing like as high as gas! The collateral damage from the high gas price can be seen everywhere and oil isn't the only commodity being leaned on as a result. Coal too has seen an incredible recovery over the last 12 months, with demand rising by over 10% and global coal powered electricity in 2021 hitting all-time record highs. Even more concerning is the International Energy Agency's prediction that these figures will be exceeded in 2022.

The current situation should also be a surefire opportunity for renewables to fill the gap created by exorbitant prices and subsequent abandonment of gas. To a certain extent this is true in Europe and North America, where renewables are well developed and already plugged into the energy grid. However, where there are the greatest energy requirements (China, India, South-East Asia), green energy simply cannot keep up with the rapid growth in electricity demand that comes with post-pandemic economic recovery. This is a subject that Portland has returned to many times and is the reason why gas exploration (if not oil) must continue, because the alternative is a world where coal usage rockets every time gas prices become too high. Only a regular supply of new gas over the next 10 years will stop these price spikes taking place.

Let's go back to oil though and where all of this leaves the price in 2022. The likely development is that oil prices will significantly increase in the first 6 months of this year, with supply continuing to be starved, whilst rebounding economies and hitherto users of gas, put significant pressure on oil demand. Hopefully the gas crisis will have dissipated somewhat by Q3, as the American fracking industry responds to clamouring demand, which in turn should bring more crude to the market, as fracked gas goes hand in hand with fracked oil. This should see prices ease by Q4, although they will still end the year higher than they are today.

'WE SHOULD BE HOPING FOR THE LESSER OF THE 2 EVILS'

In numerical terms, we easily see oil topping $100 per barrel in the next 6 months, before settling at the $80 to $90 per barrel band by December. Only one thing can realistically stop this happening and that of course is Covid. You only have to see the impact of the Omicron strain in December (21) to see the profound impact covid continues to have on oil markets. In the run-up to Christmas, oil prices fell by an incredible $10 per barrel, as traders and analysts suddenly panicked about the possibility of further covid-related lockdowns. In 2022, any new strain of the virus, a growing inefficacy of the vaccines available or a sudden increase in hospital patients (at a national level) could all bring about new lockdowns and, if the last 2 years have taught us anything, it is that lockdowns bring oil prices crashing down. Overall though, such an outcome is beginning to feel less likely and, furthermore, we should probably now be hoping for the lesser of the 2 evils. If we accept that the weakening impact of covid will mean fewer global lockdowns, then we also will have to accept the inevitable and unwelcome increase in the price of oil.

For more pricing information, see page 26

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