The situation surrounding oil prices (January)

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1. Oil Prices

Oil prices (WTI front month, price per barrel) rose from mid-December 2020 to end the year at just above USD48 as COVID-19 vaccinations started in Europe and the US and expectations of an additional US economic stimulus package increased. At the OPEC+ ministerial meeting held on 4th and 5th January, only Russia and Kazakhstan made a small decrease to the scale of their production cuts and it was decided that the total volume of oil production would increase by 75,000 barrels per day. After the meeting, Saudi Arabia announced it would carry out additional voluntary production cuts of 1 million barrels per day in February and March. As a result, expectations of an improvement in the supply-demand balance rose and oil prices increased further. Currently, oil is trading at between USD50 to USD54 and it remains fixed in the USD50 to USD59 range (Chart 1 upper).

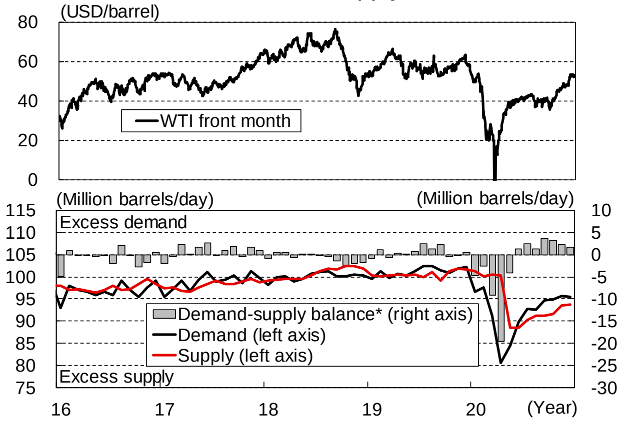
2. Oil Supply and Demand

According to the EIA's Short-Term Energy Outlook published in January, global oil demand in December 2020 was 95.55 million barrels per day and supply was 93.82 million barrels per day, resulting in excess demand for the seventh consecutive month. Nevertheless, it is important to keep an eye on the fact that the volume of supply is drawing closer to the volume of demand, despite the production cuts by OPEC+ (Chart 1 lower).

Another point to bear in mind in particular is the possibility of a future rise in US shale oil. In general, it is said US shale oil companies' breakeven price for new wells is around USD50, yet the number of working US oil rigs has been on an upward trend since October last year – before oil prices recovered to above USD50 – in anticipation of increased demand at the end of the year and a recovery in oil prices (Chart 2 upper). In addition, the number of DUC wells* is falling at present, but this could be a sign that shale oil production will recover due to the progress in well completion (Chart 2 lower). Looking ahead, if shale oil output starts to pick up and the increase in production accelerates further, there may be an unavoidable deterioration in the balance of oil supply and demand. OPEC+ may be able to adjust the supply of oil successfully by increasing the scale of its production cuts, but it is easy to imagine there will be members who protest such action. Although oil prices continue to rise at a relatively fast pace, it will be important to keep an eye on an increase in downward pressure.

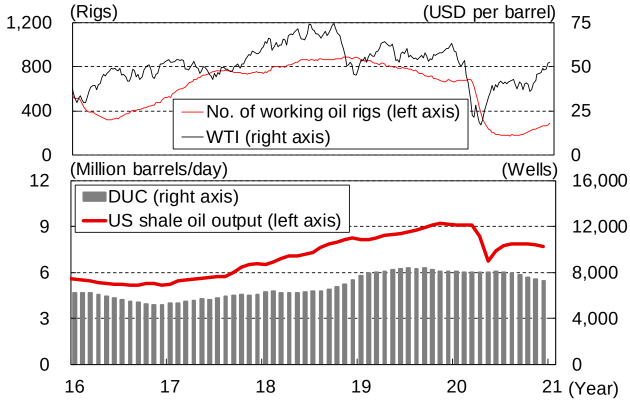
*Drilled but uncompleted wells are those which have been drilled fully but have not yet undergone well completion activities to start producing hydrocarbons.

Chart 1: Oil Prices (Front Month) and the Global Balance of Oil Supply and Demand



Note: *Demand less supply
Source: EIA, Bloomberg, MUFG Bank Economic Research Office

Chart 2: Number of Working Oil Rigs, Oil Prices, Volume of US Shale Oil Output and Number of DUC



Source: Baker Hughes, Bloomberg, EIA, MUFG Bank Economic Research Office

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