The situation surrounding oil prices (October)

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1. Oil Prices

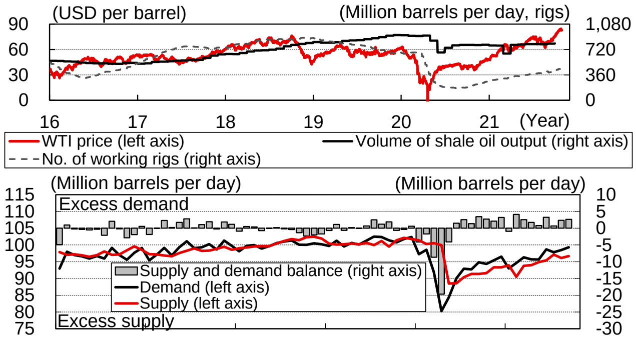
At its Ministerial Meeting on 4th October, OPEC+ decided to maintain its former plan for reducing its oil production cuts (i.e. increase production) that it agreed at its meeting on 18th July and to not increase cuts further, contrary to expectations before the meeting. This, along with the shortage of natural gas in Europe and the coal shortage in China and India resulted in a widespread view that the balance between oil supply and demand will tighten further in the future. As a result, oil prices (WTI front month, price per barrel) rose to above USD 80: the highest level in around seven years (Chart 1, upper).

2. Oil Supply and Demand

According to the Short-Term Energy Outlook published by the EIA, the volume of oil demand in September was 99.29 million barrels per day and the volume of supply was 96.67 million barrels per day, resulting in excess demand of 2.62 million barrels per day (Chart 1, lower). Excess demand has continued almost uninterrupted since June last year, and can be attributed to an increase in demand since the pandemic and the slow pace at which supply is increasing. First, it is important to note that the reduction in oil production cuts by OPEC+ (increase in output) has remained firmly in line with the pace of the increase in demand. Although countries like Nigeria are unable to increase oil production in accordance with the plan agreed by OPEC+ and the actual result for supply is lower than planned, this result can unambiguously be interpreted as Saudi Arabia, which has large spare production capacity, exerting its role as the final coordinator. Furthermore, the production of US shale oil is extremely sluggish in its recovery. The current price of oil is much higher than USD 58 – the upper bound of the average cost of oil field development (according to a survey in March by the Federal Reserve Bank of Dallas) – and the number of working rigs also continues to pick up. However, there has not been a significant push to increase production due to a labour shortage in oil fields and a positive attitude towards the Biden administration's climate change policies (Chart 1, upper).

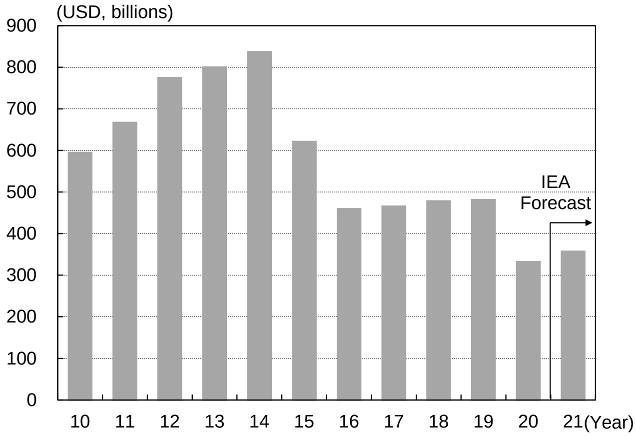
The global trend towards decarbonisation and assumption that the supply of oil will be curbed in the future seems to be suppressing investment in the oil industry in general (Chart 2), and there are concerns at present about the supply of oil in the medium and long term. Added to this the demand for alternative fuels to coal and it appears the upward pressure on oil prices will continue for the time being.

Chart 1: Oil Prices, Volume of US Shale Oil Output, No. of Working Oil Rigs, Global Supply Demand Balance



Note: Volume of shale oil production is monthly data until end September.
Number of working oil rigs is weekly data
Balance of supply and demand = demand less supply
Source, EIA, Bloomberg, MUFG Bank Economic Research Office

Chart 2: Global Investment (Upstream) in Oil and Gas



Source: International Energy Administration,
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