Economic Monthly
[Oil prices]

The situation surrounding oil prices (December)

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1. Oil Prices

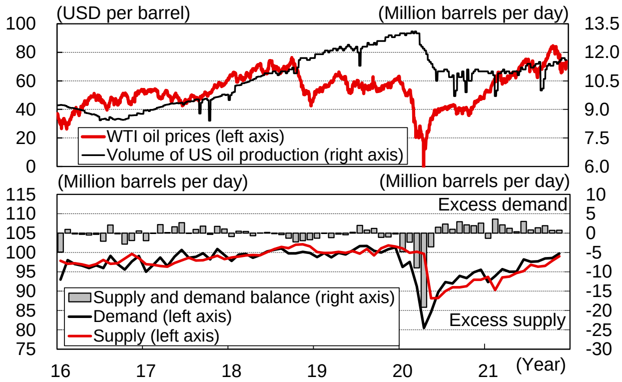
At the end of November 2021, oil prices (WTI front month) fell sharply to around USD 65 per barrel owing to concerns about downward pressure on demand from the spread of the Omicron variant. They then fell further to USD 62 per barrel for a short while after the OPEC and Non-OPEC Ministerial Meeting on 2nd December where members decided to continue to reduce their oil production cuts at the current pace of 400,000 barrels per day from the previous month, thereby not taking action to underpin prices, such as further reducing oil supply. Subsequently, oil prices rose on the back of reports that the Omicron variant was unlikely to present a serious risk, and oil is now trading at just above USD 70 per barrel (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 99.73 million barrels per day and the volume of supply was 99.00 million barrels per day, resulting in excess demand of 720,000 barrels per day (Chart 1, lower). Excess demand has continued almost uninterrupted since June 2020, which can be attributed on the supply side to a controlled increase in output by OPEC+ and a slow recovery of US oil production. The latter is due to cautious behaviour towards new capital expenditure by US shale oil companies, despite the swing to a positive cash flow thanks to the rise in oil prices (Chart 2, upper). The reason for this is assumptions that environmental regulations will become stricter in the future based on the active stance the Biden administration has adopted towards curbing greenhouse gases, as well as a rise in pressure from financial institutions and investors for financial soundness and shareholder returns.

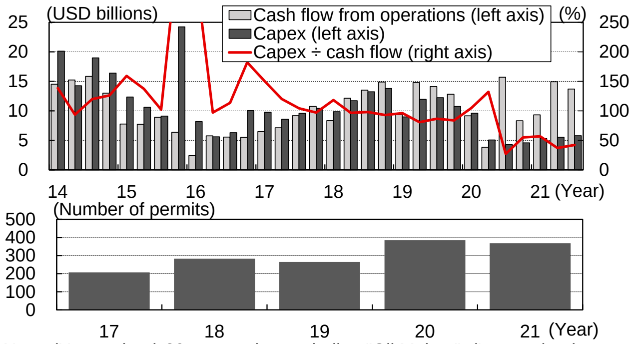
That being said, the Biden administration appears to have shifted away from its position of curbing permissions for resource development recently. This is thought to be partly due to the view that requests to OPEC+ for an increase in production alone will not be enough to address the high oil prices and inflation, about which citizens feel a strong sense of discontent. In November, the US held a large-scale auction of oil and gas drilling leases in the Gulf of Mexico. In addition, the number of oil drilling permits on US federal land issued in 2021 is in line with those issued in 2020, when there was a sharp rise in applications and approvals in anticipation of a change in administration, and exceeds the level of drilling permits issued between 2017 and 2019, during which time the former administration did not place a high priority on tackling climate change (Chart 2, lower). In order to forecast oil prices going forward, it will be important to monitor the situation for comprehensive revisions by the Biden administration to its energy policies in light of the coming mid-term elections as it tries to balance addressing climate change and rising fossil fuel prices.

Chart 1: Oil Prices, Volume of US Oil Production and Global Balance of Oil Supply and Demand



Note: 1. Volume of US oil production uses weekly data
2. Supply and demand balance = demand less supply
Source: EIA, Bloomberg, MUFG Bank Economic Research Office

Chart 2: US Shale Oil Companies' Capital Expenditure and the No. of Oil Drilling Permits on US Federal Land



Note: (Upper chart) 30 companies excluding "Oil Majors". (Lower chart) monthly average from FY2017 to FY2020 (Oct ~ Sep), monthly average of Feb ~ Sep for 2021
Source: Bloomberg, US Department of the Interior - Bureau of Land Management, MUFG Bank Economic Research Office

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