Oil Market Report: April 2020

Putting the Oil Market Report together can sometimes be a difficult task, particularly in those months where nothing actually of interest happens on the oil markets. April 2020 certainly wasn't one of those months! In fact, this Oil Market Report could probably have been written based on events on any single day in April – such was the turmoil and volatility over the last 30 days.

At the beginning of the month, prices were already languishing below $30 per barrel, as the devastating combination of an OPEC price war and the coronavirus each took their grip. Having declared on April 1st that low oil prices were a welcome tax cut for US consumers, President Trump took a sharp change of direction 1 day later, when Senators from Texas, Pennsylvania and Ohio (all key states in Trump's re-election bid) reminded the President that about 1m oil workers were about to lose their jobs. Trump's response was to make one of his unilateral "truths" - shot from the hip and aiming for maximum impact.

"Will be an oil deal between Saudi and Russia. Production cuts of 15m barrels per day", declared Trump on Twitter on the 2nd April. The fact that no-such deal had been agreed between Saudi Arabia and Russia and further, that neither country were (at that stage) even in talks, was initially of no import - such is the febrile nature of the current oil market. In the space of 1 hour, oil prices rose by an unprecedented $8 per barrel (that's about 5 pence per litre), but within the space of the next hour, they had fallen by about $5 per barrel. This, as the market digested the actual reality of the so-called "deal", ie, there was none...

To be fair however, the President probably does know more about oil, than medically appropriate cleaning fluids. So no doubt he was banking on the fact that the continued drops in the oil price would indeed force OPEC members and Russia back to the table. In February, a production cut of only 2m barrels per day (bpd) had caused such disagreement within OPEC, that a total breakdown of the cartel had resulted. But now only 2 months later, oil prices had dropped so vertiginously, that the very existence of the global oil industry was under threat. So over the Easter Weekend, OPEC+ oil ministers got together via Zoom (what else!?) and a 10m bpd production cut was agreed. Furthermore, there was also to be a "commitment" from G20 Countries (spearheaded by the International Energy Agency) that they would seek to cut their production by a further 4m bpd.

This is a time of unprecedented events, so perhaps it was not too surprising that OPEC agreed to cut so much production and for so long (basically until 2022, although the level of cuts do steadily diminish over the 2 year period). All the same, there is a certain schadenfreude around the fact that having fallen out so spectacularly over a 2m bpd cut back in February, OPEC and Russia managed over a video conference, to accommodate a production cut five times as large! But that wasn't all. It was also unprecedented that G20 countries were now effectively signing up to join the world's largest oil cartel, and within that, the USA – who only last year were pushing to have the NOPEC congressional bill reinstated – were now pushing for "gas"(oline) prices at the pump to rise! Strange times indeed...

Yet in the second half of April oil prices still tanked, culminating in the futures price for WTI hitting the absurd level of minus $37 per barrel on 20th April (listen to our BBC Radio interview on 21st April for an explanation of this; https://stabilityfromvolatility.co.uk/media/). The first obvious reason for the continued drops in price was that the new production cuts would not come into force until May 1st, meaning that the April surplus continued throughout the month. In fact, there was good evidence to suggest that the situation was exacerbated by oil producers desperately trying to maximise production before the quotas hit.

Secondly, whilst OPEC members may have the tools to limit production (because their oil companies are state owned), the idea that independent commercial operators within G20 nations could be reined in overnight, was fanciful to say the least. Business owners and shareholders might have something to say on that matter! However, easily the biggest reason that prices kept falling was because demand had been so totally and utterly obliterated. It is estimated that consumption of oil in April fell by a whopping 30m bpd (down 30%) and May is likely to look much the same. In that light, no amount of production cuts will stop oil prices falling and only the recovery of demand will put an end to the price rout. When that will be, is dependent on when the effects of Covid-19 dissipate and at what point the world economy can start to revert to normal.