The Commodities Feed: Oil sell-off continues

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Energy

Oil prices continued their decline yesterday. ICE Brent settled more than 6.5% lower on the day, closing below $100/bbl for the first time since late February. The market has fallen by around 28% since trading to an intraday high of US$139.13/bbl back on 7 March. Time spreads have also weakened, with the prompt Brent spread trading at a backwardation of a little over US$2.30/bbl. While this is still a strong backwardation, it is off significantly from the highs seen in early March. Given the weakness that we have seen in the market over the last week, it is clear that there is little risk premium priced into the market, which leaves it vulnerable to upward spikes if there is a deterioration in the Russia-Ukraine war.

For now, the market appears to be focused on two developments. The first is China's Covid situation. While Shenzhen has been in lockdown for a couple of days now, we are starting to see tougher restrictions in other cities. Secondly, it seems as though there could be progress in Iranian nuclear talks. Russia has said it has received US guarantees that sanctions will not affect the supply of Russian fuel to Iran's nuclear plants. This has been one of the sticking points, and if resolved would mean that we are one step closer to a deal, and as a result nearer to Iranian oil supply increasing.

Yesterday, OPEC released its monthly oil market report. The group left its oil demand growth forecasts for 2022 unchanged at 4.15MMbbls/d, although did highlight that there are downside risks to this view given the ongoing Russia-Ukraine war. OPEC also left its forecast for non-OPEC supply growth unchanged at 3.02MMbbls/d for 2022. However, there is clearly also downside risk to these numbers given the self-sanctioning we are seeing with Russian oil. If Russia continues to struggle to ship its crude, it will eventually lead to a reduction in output due to storage constraints. The report also highlighted that OPEC production increased by 440Mbbls/d in February to average 28.47MMbbls/d. Saudi Arabia and Libya led the gains with output increasing by 141Mbbls/d and 105Mbbls/d respectively. All members saw production increasing over the month, except for Nigeria and Equatorial Guinea, where production declined by 10Mbbls/d and 9Mbbls/s respectively.

Finally, there were media reports yesterday that Saudi Arabia is holding discussions with China about pricing some of its oil sales in yuan. There has been talk about this for years, however, nothing has ever materialized. However, with the relationship between the US and Saudi Arabia becoming more strained, it might be worth taking these latest talks more seriously. China is a key buyer of Saudi oil, importing a little more than 25% of total Saudi export supply, whilst Saudi oil makes up around 17% of total Chinese oil imports.

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