Our View: Crude Oil Prices Are Going Nowhere

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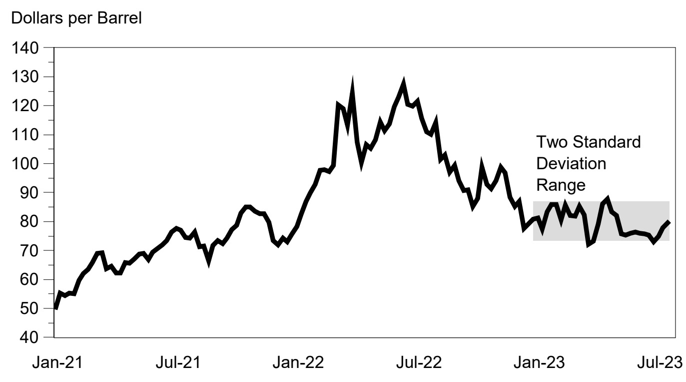
Reporters and consultants who follow oil seem certain that the production cuts announced by Saudi Arabia and Russia will push prices higher. Twenty-five years of market history and data contradict their view.

The data indicate that oil prices will go nowhere. The key information behind this conclusion is excess returns to storage. PKVerleger LLC has been publishing excess returns data for more than thirty years. Our friends keep asking why? They (and others) raise a good point. To date, we have never offered a strong reason for paying attention to these returns.

As the data show, returns to storage today are barely positive and well above returns observed in 2022. These data indicate that markets are not as tight today as in the previous year. Buyers now are not as concerned about their inventories—whatever they may be—as they were in 2022. This is a point we have repeatedly tried to get across, with little success it seems.

One can conclude that firms buying and selling oil feel sanguine about the current market conditions. Their nonchalant view contrasts sharply with that of barrel counters. Grant Smith, Bloomberg's chief counter, reported in his July 13 review of the OPEC and IEA forecasts that "OPEC predicted an even tighter global oil market next year, as the group anticipates a much bigger demand increase than other major forecasters."[1] More recently, he wrote an article headlined "Oil Surge to $80 Shows Long-Awaited market Tighteing is Here."[2]

Figure 1
Dated Brent Prices, 2021 to 2023, and the Two Standard Deviation Price Range Generated from Excess Returns to Storage



Source: Platts; PKVerleger LLC.

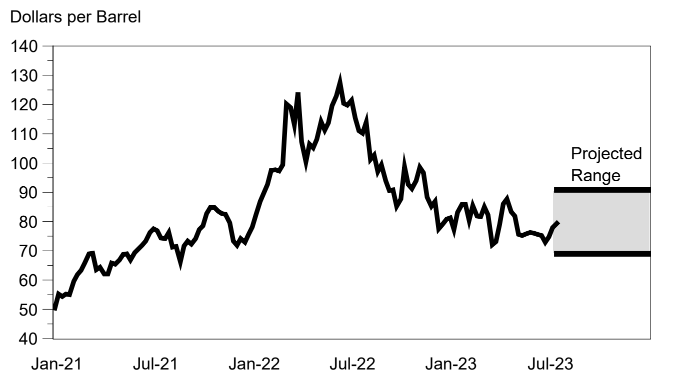
The data do not support Smith's view. Excess returns to storage indicate that Dated Brent prices could climb as high as $90 per barrel or fall as low as $70 in December. These numbers mark the high and low points of the two standard deviation price forecast range we generated from excess for the last two years for mid-July. Figure 1 shows the forecasted range (shaded area) for Brent during the first half of 2023 generated using mid-December 2023 excess returns to storage along with the actual Brent prices.

Looking forward, data on excess returns to storage for the October Brent futures contract at the end of the first week of July point to a

[1] Grant Smith, "OPEC Sees Even Tighter Market in 2024 as Demand Climbs," Bloomberg, July 13, 2023 [https://tinyurl.com/3kd4n92f].
[2] Grant Smith "Oil Surge to $80 Shows Long-Awaited Market Tightening Is Here," Bloomberg, July 16, 2023 [https://tinyurl.com/mj8dn9zd].

constrained future for oil prices for the rest of the year. Based on our analysis, crude prices will continue to fluctuate between $90 and $70 per barrel. Figure 2 shows the estimated price range (shaded area) for July through December.

Figure 2
Dated Brent Prices, 2021 to 2023, and the Two Standard Deviation Price Range through December Generated from Excess Returns to Storage



Source: Platts; PKVerleger LLC.