Are oil prices ready to rise?

Despite tensions in the Middle East and Ukraine, oil prices have yet to soar. Other factors are influencing the crude oil market. Alessandro Gelli, analyst at Diapason Commodities Management in Lausanne, explains.

SWISSQUOTE MAGAZINE ▸ **Why didn't the price of oil spike this summer with all the geopolitical tension?**

ALESSANDRO GELLI ▸ The market is under less pressure than expected. The economic slowdown in Europe and weaker industrial growth in China have resulted in lower demand. Despite the turmoil in the country, crude exports from Iraq have remained stable. Furthermore, Libya has increased its oil output despite the conflict currently ravaging the nation. This situation forced Saudi Arabia to cut its oil output in August, a period when production is usually ramped up.

Has output in the United States reduced the geopolitical risk?

The Americans are reducing foreign crude imports as a result of the exploding production of shale gas in the United States. Given the ban on US crude exports, there is even a risk of surplus in the short term, as refineries are not equipped to handle all the light oil being produced in the country. However, the boom will not drive oil prices down in the medium term, as a high price structure is needed to make shale gas drilling and production economically viable.

What other factors are influencing the market?

Economic growth remains a dominant factor. And the rise in the dollar has also played a key role, making oil more expensive in other currencies. However, output has increased very little outside the United States and Canada.

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What are your forecasts?

Even if overall market sentiment is negative, we're more optimistic than others about the future of demand. For instance, we expect the Chinese economy to pick up and the European situation to stabilise.

What should our position be?

It's a very complex market, but exposure to the Brent can poise investors to benefit from a global economic recovery. The Brent is currently the most accurate reflection of the international landscape, while the WTI is "stuck" in the United States. With the increase in its domestic production, the United States no longer sets the global price. We therefore expect the WTI to remain at a discount to the Brent.

What are the risks to beware of?

The geopolitical factors – for now lurking in the background – could come back in full force if the economy recovers, as the market will be under higher pressure. The price will climb with each barrel produced and fears will intensify. The reserves in OECD countries have dropped close to levels seen before the 2008-2009 economic crisis, while global demand has increased nearly 6% since 2008. The available production capacity in Saudi Arabia is also relatively low. All these factors could amplify market tension and drive up prices. ◢

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