

## Crude oil comment

The logo for SEB (Swedish Export Bank) is displayed in white text on a green square background.

### Longer dated crude oil prices set to move higher

**Brent crude moved to USD 65/bl this morning as more than 4 m bl/d of supply in the US has gone offline due to the winter storms and freezing temperatures all the way down to Texas. The outage will be temporary but it will still help to accelerate US oil inventories down towards the five year average quicker than expected. We think that longer date crude oil prices like the five year Brent contract are in for a hike up towards USD 57-60/bl and higher in periods of overshoot in the front-end contract. The longer the front-end price stays around USD 65/bl the cheaper the longer dated prices will look in the eye of the market. And up they'll go.**

**Brent crude moved above USD 65/bl this morning** with help from a supply loss of some 4 m bl/d in the US due to freezing cold winter storms. Though this loss of supply is likely to be highly temporary, say a week or less, it will still help to drive US crude and product inventories down another 15 to 20 m barrels. This comes on top of the inventory draw data today for last week were partial data from API indicates a net crude and product draw of 5.5 m barrels. As of data published last week US oil stocks were only 21 m barrels higher than one year ago and 57m barrels above the five year average. The outage in Texas of some 4 m bl/d is thus accelerating the drive down towards the five year average in US oil inventories even faster than the recent quite fast pace.

**US shale oil activity still below steady state though activity is picking up.** The US EIA released its monthly Drilling Productivity report on Tuesday and it showed an estimated decline in US production of 77 k bl/d month on month in March. That is less than the estimated decline of 89 k bl/d for February indicating that drilling and completion is picking up though still at a level below what is needed to keep production at a steady state level. For the time being we thus have an ongoing revival in global oil demand while at the same time US production is in general decline with a temporary loss of 4 m bl/d in supply on top.

**Longer dated contracts are in for an upwards hike.** Oil prices are currently in uncharted territory. Never before have we had such a low level in longer dated crude oil prices while at the same time having a Brent front-end price of USD 65/bl. There are of course some good reasons for this being lots of OPEC+ spare capacity on the side-line, Iran getting ready to enter as soon as a new JCPOA nuclear deal is negotiated, reviving US shale oil activity together with an accelerating electrification of transportation on the horizon. So optimism on the longer dated contracts and outlook for oil is and has been extremely low.

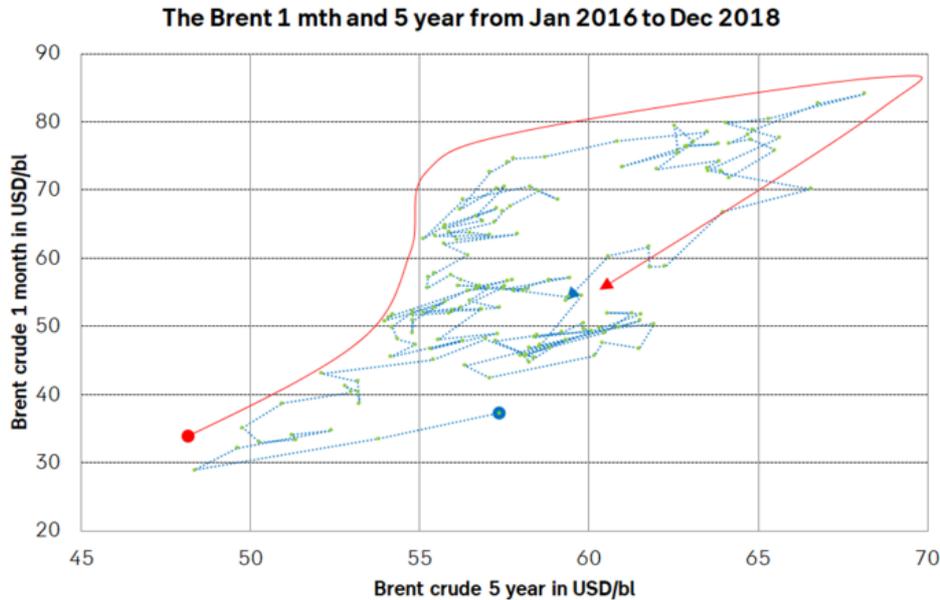
If however we look at the previous oil cycle from 2016 to 2019 we can see a very interesting pattern between the front-end contract and the five year contract. The front-end contract is the first to move higher as the market rebalances, tightens and inventories draws down. The longer dated five year contract however stays at muted levels for quite some time still. But then as the market rebalances further and the front-end price trades in the range of USD 65 – 75/bl for a while then suddenly the longer dated contracts starts to accelerate higher as well.

Maybe it is much about psychology. Seeing spot prices day after day at USD 65/bl or higher unavoidably penetrates the mind of the market: "Wow! Longer dated prices are low!" is the natural instinctive reaction after a while. While longer term fundamentals have not change the mind of the market has and that lifts the longer dated contracts after a while.

There is now a brewing story in the background of a potential global oil supply crunch around 2025 unless investments in new supply accelerates. The longer the front-month Brent contract stays at USD 65/bl level the louder this story will be come and instinctively seeing USD 65/bl printed day after day this story will become more and more believable even though the proof of it has not necessarily become any stronger.

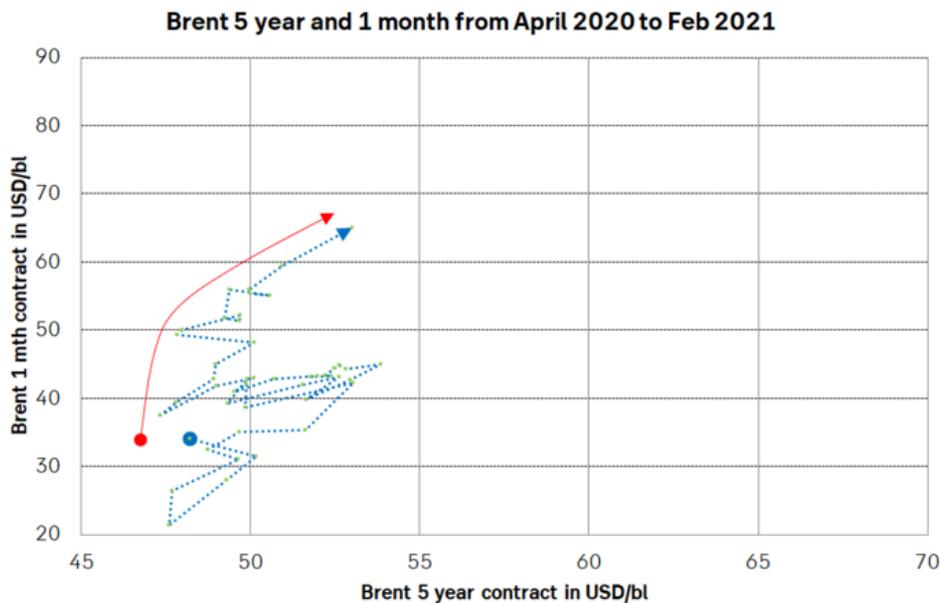
We think that OPEC+ will stay coordinated and restrained but also that it will add more supply to meet rising demand. Thus we might not see all that much higher spot prices than we have now except for periods of overshoot. **The longer dated contracts are however unavoidably going to rise steadily higher and up towards USD 57 – 60/bl or potentially even higher during spot price overshoot.**

The previous oil price cycle from Jan 2016 to Dec 2018. During the first initial revival we saw that the 5 year contract (x-axis) moved up to USD 55 - 57/bl and stayed close to that level for quite some time while the front-end contract (y-axis) rose higher. Then as the front-end price reached USD 70/bl the longer dated 5 year contract started to accelerate higher and moved all the way to USD 68/bl as the front-end price spiked to USD 86/bl. The scatter plot is weekly data.



Source: SEB, Bloomberg

In the current oil cycle we have for quite some time now moved higher in the front-end contract while the 5 year contract has been almost fixed at around USD 50/bl. Lately however it has started to move higher along with the front-end price. We think that the longer dated contracts have more to go. Especially during overshoots in the front-end price. But even if the front-end price just stays at USD 65/bl we are likely to see the longer dated prices drift higher from there and up towards USD 57 - 60/bl

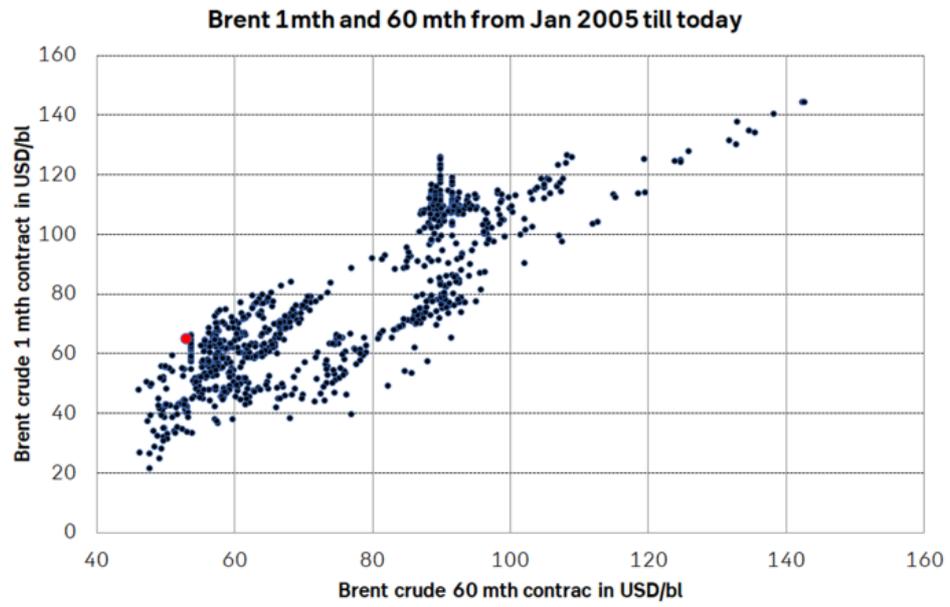


Source: SEB, Bloomberg

Brent crude oil prices are in uncharted territory. This is on the extreme in terms of longer dated prices at USD 53/bl versus a front-end price of USD 65/bl. From here either the front-end will come lower or the longer dated prices will move higher. Most likely we are going to see the front-end to move around the USD

65/bl while the longer dated prices tick higher and higher.

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Source: SEB, Bloomberg

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