RESEARCH INSIGHTS

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The Oil Patch
What's the catch?

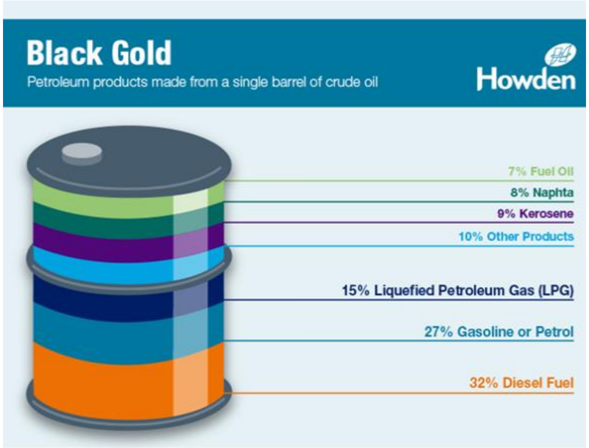
Amidst the new wave of COVID-19 cases around the globe and especially the new Omicron variant, we take a closer look into the oil market in a bid to answer a curiosity; what's so important about the oil prices in the economy?

At a Glance

Before diving in on the oil prices in the economy, let us delve into why Oil is vital to the world economy.

Oil is one of the world's most important raw source of energy we have on Earth. Its products underpin modern society, mainly supplying energy to the power industry, heat homes and provide fuel for vehicles and aeroplanes to carry goods and people all over the globe. But where does oil come from?

Oil or most specifically Crude Oil is a naturally occurring fossil fuel which is made up of a mixture of hydrocarbons. It is often interchangeably referred to as petroleum includes both the unrefined crude oil as well as refined petroleum products. It gets it nickname "Black Gold" from the monumental number of products that can be processed from unrefined crude oil, namely Diesel Fuel and Gasoline.



Products made from a barrel of crude oil
image retrieved from Howden

Asia's Undisputed Oil Hub

In Singapore, it is described as "The Undisputed Oil Hub in Asia" as it leads the way in the Oil and Gas industry, reigning supreme as the world's top shipping centre for the sixth year running (beating the likes of Hong Kong, London, and Dubai). Singapore is also one of the world's top three export refining centers. Singapore has maintained its reputation as a market leader for floating production, storage, and offloading (FPSOs) conversions and offshore jack-up rigs and operates some of the world's largest and most innovative oil refinery project. But what makes Singapore undisputed from the rest of Asia?

Singapore boasts many amazing and ground-breaking projects in the recent years. One of them being the building of the world's largest semi-submersible crane vessel named the "Sleipner", built in 2019 by Sembcorp Marine (Singapore's leading marine and offshore engineering company).

Sleipner
Named after the Norse God Odin's eight-legged stallion
Image retrieved from Sembcorp

Demand and Supply for Crude Oil

Crude Oil prices are determined by global supply and demand. Economic growth is one of the largest factors affecting petroleum product and therefore leads to increase demand for crude oil. Growing economies increase demand for energy, especially for transporting goods and materials from producers such as diesel fuel and gasoline. Many countries worldwide also heavily rely on petroleum fuels for cooking, heating as well as generating electricity, to name a few. These petroleum products are produced by crude oil and other hydrocarbon liquids account for about one-third of the total world energy consumption.

OPEC's Influence

Many of the largest oil-producing countries in the world are part of cartel, known as The Organization of the Petroleum Exporting Countries (OPEC), who have a significant influence on oil prices by setting production targets for its members. OPEC include countries of the world's largest oil reserves namely Iran, Iraq, and Saudi Arabia. The cartel's goal is to exert control over the price of crude oil. In 2016, OEC allied with other top non-OPEC oil-exporting nations to form an even larger and more powerful entity named OPEC+ or OPEC Plus. OPEC+ controls over 50% of the global oil supplies and about 90% of proven oil reserves. This dominant position ensures that the coalition has a significant influence on the price of oil in the short term. Over the long term, its ability to manipulate the price of oil is diluted, mainly due to individual nations having different incentives than OPEC+ as a whole. Frighteningly, OPEC+ member countries agree on how much oil to produce which directly affects the ready supply of crude oil in the global market at any given time.

Lesser Supply, Higher Oil Prices
Image retrieved from Scoopnest

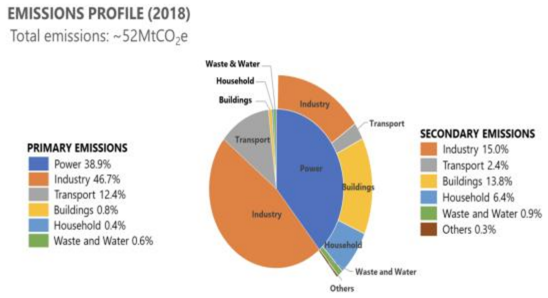
However, if OPEC+ countries are unsatisfied with the price of oil, it would be in their favor to cut the supply of oil, so prices rise. Then again, no individual country wants to reduce supply as that would result to reduced revenue.

Singapore's Emission Profile

Singapore also owes much of its success in the Oil Industry to the plant on Bukom Island, which is a part of massive refining and petrochemical industry built largely on reclaimed islands just off the city-state. In-tandem with the cargo vessels they fueled, the refineries helped drive Singapore's economic success after independence, attracting billions in investment and spawning businesses from plastics to rig construction and finance.

Bukom Island
Image retrieved from Shell Singapore

However, based on Singapore's Emission Profile itself, Singapore has contributed to around 0.1% of global emission. Historically, Singapore's strategic position along the East-West trade routes has made Singapore a natural location for oil storage and refining facilities serving the region. Building on a position as a vital regional port, the refining and petrochemical plants help create synergies as it plays a crucial role as part of a business supply network in Southeast Asia, the Western Pacific, South Asian and Australasia. Despite the refining and petrochemical sector being a large source of carbon emission, improvements on energy efficiency will remain a vital strategy to lower the industry's sector's emissions.



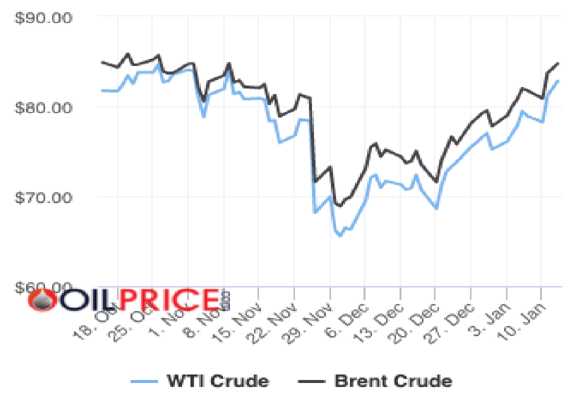
Singapore's Emission Profile
Image retrieved from NCCS

Omi-gone?

What begs the question is, does the new coronavirus variant affect oil prices? In fact, oil prices hit a two-month high on Wednesday, 12 January, on tight supply as crude inventories in the United States, the world's top consumer, fell to their lowest since 2018. Accompanied with the fact that as the dollar weakened, worries eased about the Omicron coronavirus variant.

Brent crude gained US$2.85, or 3.5%, to US$83.72 a barrel which was its highest settlement since early November, whereas the global benchmark dropped 1% on Monday according to The Straits Times.

US West Texas Intermediate (WTI) rose US$2.99, or 3.8%, to end at US$81.22, also its highest price since mid-November as it shows the despite the new variant, oil prices remain strong.



Increasing Oil Prices
Image retrieved from OilPrice

"Omicron has yet to wreak the havoc of the Delta variant and may never do so, keeping the global recovery on track."

- Jeffrey Halley, analyst at brokerage Oanda.

"Demand is going to be stronger than anticipated and that OPEC's supply may not grow as fast as the demand – is why prices are climbing."

- Phil Flynn, senior analyst at Price Futures Group.

Despite the speculations of Omicron impacting oil prices, it was not severe enough to derail a global demand recovery. In fact, oil prices spiked more than 50% in 2021 and even some analysts expect the rally to continue, predicting that scant production capacity and limited investment could lift crude to $90 or $125 a barrel this year according to JP Morgan.

Outrage in Libya

Libya is the 16th largest country in the world in terms of land mass with its economy depending primarily on the oil sector. Moreover, the oil and gas sector account for about 60% of total GPP. Apart from petroleum, Libya's other natural resources are natural gas and gypsum. However, Libya's oil industry has suffered for years through a civil war, political uncertainty, and a lack of investments.

"We have many oil and gas discoveries that can be developed, and it is possible to open the door to foreign investments."

- Mohammed Oun, minister for oil and gas in Libya

Despite optimism from Libya's minister, uncertainty still looms across Libya, with political-military instability from the civil war leaving Libya's inability to tap into its fullest potential, who is thought to hold 48 billion barrels of crude, making it the world's ninth-largest oil nation, as well as 52 trillion cubic feet of natural gas.

Halt in oil production
Image retrieved from Anadolu Agency

Libya has repeatedly faced problems with its oil output, as a disagreement between Petroleum Facilities Guards (PFG) and the National Oil Company. Weak infrastructure and the volatile relationship between the government and the PFG results to the country's oil output being uncertain as the week goes by. Issues as such that has repeatedly hindered Libya's foreign investment prospects despite Libya's oil industry potential being significant.

In a move to better it's oil production, it must invest in its ageing infrastructure to ensure it can handle greater oil output. Additionally, ongoing political unrest could further hinder the country's output, ultimately deterring international oil firms from investing. However, if the presidential elections go ahead and the country were to achieve a relative level of political stability, it could garner greater foreign investments and develop its energy sector to its fullest potential and achieve greater of heights.

Oil Benchmarks

Open a newspaper, surf the web and there's a high chance you will find a news story about oil prices fluctuating. To an average consumer, it is easy to comprehend that there is a singular worldwide market for this crucial energy source.

There are dozens of different oil benchmarks, with each one representing crude oil from a particular part of the world. However, the price of most of them are pegged to one of the following three primary benchmarks:

Brent Crude

Around two-thirds of all crude contracts around the world reference Brent Crude, making it the most widely used marker of all. Nowadays, 'Brent' refers to oil from four different fields in the North Sea, Forties, Oseberg and Ekofisk.

West Texas Intermediate (WTI)

WTI refers to oil extracted from wells in the U.S. and sent via pipeline to Cushing, Oklahoma. The fact that supplies are land-locked is one of the drawbacks to West Texas crude as it's apparently expensive to ship to certain areas of the world.

Dubai/Oman

This Middle Eastern crude is a vital reference for oil of a slightly lower grade than WTI or Brent. A "basket" product consisting of crude from Dubai, Oman, or Abu Dhabi, it is somewhat heavier and has higher sulfur content, placing it in the "sour" category.

The Bottom Line

This market for crude is incredibly diverse, with the quality and original location of the oil making a major impact on the price. Because they are relatively stable, most crude oil prices worldwide are pegged to the Brent, WTI or

Writer's Opinions

Oil will never be replaced (for the time-being)

Despite many oil conglomerates pledging to go green in the near future, there is still no consensus what a future with less oil would look like for companies like Exxon Mobil, Total and Shell that have been greatly enriched by fossil fuels steering climate change. Yet regardless of the amount committed to clean energy, most companies are still pumping in more money toward oil and gas based investments, a sign hinting that a revolution would not occur overnight. Now let's take a pessimistic view and assume that by 2030, the majority of vehicles sold are electric and by 2040, gas cars are no longer mass produced.

TESLA Model X
Image retrieved from TESLA

Even in this almost impossible scenario, there will always be a market for people that are more inclined toward gas cars, it would still take decades before gas automobiles were to completely off the road. With all these assumptions in mind, the global use of automobile gasoline would likely peak until the shift towards electronic cars outpace overall use of automobiles. Another very important consideration is that the masses that predict that oil will become replaced will essentially fall prey to their own argument. A shift towards electronic vehicles would only occur if it was more economical, which would assume that oil would have to become expensive. If the market shift towards electronic vehicles was so significant, it would lead to a lower price oil, which in itself would retard the growth of the electronic vehicle market. In order for electronic vehicles to beat out oil-advantage of electricity in market share, there would need to be a long term cost advantage of electricity over oil. Lastly, I believe that we will continue to discover more reserves of oil as right now, we have only scratched the surface. Would that being said, this would keep the price of oil low, preventing it from hitting peak oil prices.

Global oil reserves will only continue to rise over the next few years and it will most likely continue to increase beyond the amount oil that is consumed annually. Oil and natural gas are necessary resources to every country. A lack of oil and natural gas would have or any other country grinding to a halt.

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