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SYNERGY

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Oil Market after Black April

Roughly two weeks ago, most of the analysts and we anticipated another wave of price fluctuations. We called this "the second wave." However, most of the timing was limited between mid-May and mid-June. The rationale was simple. When the storages are full, oil prices will be hit again. As of today, the so-called "second wave" has started earlier than expected. Now, the question remains whether there will be a Third Wave?

The oil market was never precisely a domestic animal. It was a beast under control. As the control gets loose, the chaos triumphs. This chaos hits from micro to macro level. Last week we read news about Norway's Oil Fund manager's expenses as well as Singapore oil trader Hin Leong Trading's hiding of 800million dollars of losses. Surely there will be more scandals to come, but these are backgrounds to the main show.

IEA April report was a big blow to oil markets as Fatih Birol referred to April as Black April. He previously saw Abqaiq attacks as a "heart attack" and the spat between Saudi Arabia and Russia as a "Russian roulette in oil markets." When we look back to the past six months, it is not an exaggeration to claim that the oil markets are in a new kind of chaos. This chaos will not settle soon; that is what everybody is saying. But the main question is whether this new generation of chaos will breed new disturbances. One simple example is probably the delay in the OPEC report last Thursday. It was scheduled for the morning then noon. It was perhaps delayed three times and finally published. I can feel the stress they are under to convey the right message -politically -. OPEC and IEA reports were hugely different in demand predictions Year-on-Year:

- For 2020 (all year), OPEC -6.8 mb/d ; IEA -9.3 mb/d

- For 2020Q2, OPEC: -12mb/d; IEA -23.1 mb/d

- For April 2020, OPEC: ?; IEA -29mb/d

In every energy crisis, same message has prevailed: the importance of data and reporting. Two major organizations are relying on the same data but came up with different results, which is normal. IEA has said to use satellite data for storage numbers. But floating storage numbers are mere predictions. That ambiguity may define the shape of the third Wave.

Fast forwarding a little bit, let's assume that by the end of July, most of the consumer demand is back. Air travel may need more time. The data tells us that from 5 May to mid June there may be wild fluctuations in oil prices due to rolling of contracts and close to full storage levels. Meanwhile markets are reporting an influx of money to June contracts. May-June will be a volatile period, but end of July may most likely be positive.

There is another facade of May-June period. These prices set the oil-linked natural gas prices for the winter. The lowest prices in oil may create another shock for natural gas producers, this will be tested as we move forward.

One important parameter to watch is the result of US elections. If May-June is the first joint in our forecast, second joint should be US elections.

Then we have to create our scenarios for the timeline beyond June. One of the most critical scenarios will be geopolitics, the second will be economics, and probably the third will be "the second wave -in pandemic-".

The geopolitics scenario should capture the disturbances in oil-producing economies and the effect of their lost revenues on other countries.

Economics scenario should be based on whether "new initiatives" or "deals" can push the world forward. The creative destruction takes time, therefore most of the politicians will first try to resurrect the status quo. Then this status quo may move into the new direction.

Second Wave in the Covid19 pandemic is a possibility. The Second Wave of this pandemic may not be as effective. Governments will probably be more informed and ready to act and coordinate. The world will change. This was true before covid19 and it will be true after covid19. If you look at the oil demand graph from the 1960s to present, you may well see two separate trends in oil demand growth. The first one was the stable and high growth up until oil crises 1973-74 and 79-80. The long term growth trend was broken and slowed. When you check the aftermath of Covid19, long term oil demand growth may have been broken once again.

That doesn't mean oil prices will be lower forever. Most probably, the government initiatives and plans will try to stimulate the economy, and the middle class will buy more cars due to avoid public transport. But renewable and tech R&D has earned a valuable break to come up with more market-based solutions. If governments put the money in the right baskets, long term oil demand growth will be broken for the third time.

Barış Sanlı

Crises In The Gulf Never Wanes

If anything, the past couple of months and the upcoming years will be hugely beneficial for future studies concerning oil prices, producers, and economic slowdowns. The price war and the ensuing market share contentions, if examined on its own, could have produced scenarios that could be answered by analyzing precedent events in the markets and politics. The unique mixture of a global economic slowdown and the price crash, however, has created an intricate web of mutual outcomes and disagreements that are evolving daily. In my previous week's article, I went over the dangerously escalating tensions in the Mid. East, especially in the Gulf, and how specific unwanted scenarios could develop while the world's head is turned towards the COVID-19 crisis. This week's article is going to be an addition to that piece with the newly added details and analyses on the subject.

A newsworthy event that aired on international media outlets this week was the change in the domestic balances in Iran. Recalling the toughened sanctions applied by the U.S. against Iran regarding its oil exports and limitations on engaging in international business endeavors, the applied measures certainly have taken their toll. The economic indicators of Iran were already deteriorating in the late months of 2019, and the widening social unrests were beginning to surface on the international news and social media platforms. The COVID-19 pandemic has undoubtedly made matters worse for all those involved. The authoritarian petrostate regimes across varying regions have been observed in multiple cases to be ensuring the domestic stability in their nations by providing extended incentives and subsidizations. The examples can range from free provision of utilities, subsidized food prices, subsidized fuel costs over to any other method that could positively affect and benefit the lives of its citizens in the absence of democratic and equal rights. The other side of the coin is, however, the extended funding of domestic law enforcement agencies for keeping things under check for any potential unrests/uprisings against the ruling regimes. But what happens when the state does not have the funds to support such programs?

While no single true-across-all answer can be given, we can observe in real-time what is happening in Iran. Such times of economic hardship, bring out the weakest links in the social domains of nations, whether it is social classes, ethnicities, religious sects, or political views. Analysts have viewed the recent(past two weeks) noticeable increase in Iran's aggressive attitude in the Strait through different perspectives. Still, a prominent view is suggesting that the weakening current administration is giving way for regional hardliner groups to take advantage of the forming power vacuum. Such groups are not necessarily standalone political activists but could have its members from different branches of the government and military. Viewing the events of January as a failure of the state, the opposing parties and groups had an advantageous start to begin the current process with. Relying on the government's inability to effectively and timely respond to such power grabs, these groups are likely to hold much more critical in how we view the regional dynamics in the future.

Additionally, being battered by COVID-19 in financial capabilities, not just Iran but all such regional petrostates are going through a rough period of balancing multiple domains. To gain more supporters and gain power room, such hardliner groups will likely pursue the aggressive agenda we can observe now as to put the current administration in a more robust position against the U.S. and in an event where political success can be achieved, it won't be long before we can start hearing the claims for the victories from these groups. How does all of this reflect on the upcoming weeks?

Going back to our High Impact-Low Probability scenario we studied last week where the U.S. pursued a localized military intervention against Iran in the Hormuz Strait, such a situation today will hold a different outcome and impli-

cation for the stakeholders. The current power struggle feeds from the increase in the tensions, and the weighted response might be met with an excessive reaction by Iran, which might spiral out of control in a short moment. While the action might increase the price of oil and aid the shale producers of the States marginally, the adverse effects will likely outweigh this small gain in economic activity.

So how might the scenario develop? The Iranian administration made a call for the International Monetary Fund to forego the pressure of the U.S. is reviewing its funding request, which might be a tough favor to ask for when considering the U.S. holds 16.51% of the total votes in IMF and is in the leading position. It also signals that the U.S. is also trying to block funding for Iran through international organizations as well. But how well of policy is this given the backdrop we are talking on? If all goes well for the U.S. with its current policy, then in an event where the minority hardliners in the decision making bodies of Iran succeed in pursuing an openly aggressive position against the U.S. in the region, then the U.S. will have a new crisis that it has to sort out, besides the COVID-19 pandemic which is wreaking havoc across the real economy. War is known to be an economic magic pill by some when considering the economic activity it creates, but the uniqueness of our current situation kicks in here.

A leading reason for why we are experiencing the current slowdown is because the working population cannot go outside to work, enjoy, or spend. Calling the workers to their offices/factories to kick start the economy would only make the current situation worse by increasing the size of the infected population and immobilize the medical capabilities which the military might need, create disruptions and backlogs across critical sectors such as logistics and create real social unrest where those affected by the lockdowns and quarantines would be brought out of their homes to fight off another crisis, this one being openly and purely initiated by humans. Considering the upcoming elections in the U.S., such a move might not be the wisest policy to follow if the implications it could have been well understood.

In the other scenario where the U.S. chooses to cooperate on funding terms for Iran, which it morally should base on the current humanitarian medical crisis, then the current Iranian administration might gain breathing room and could potentially provide the much-needed services its citizens need and indirectly thwart the potential power grab by the opposing groups whom could cause much havoc in the region. Interestingly enough, it would be a win-win for the U.S. and Iran when you consider the alternative scenario which both powers are more than likely aware of. A critical question to ask at this point is, how soon will these countries come to terms considering the regional and the global crises?

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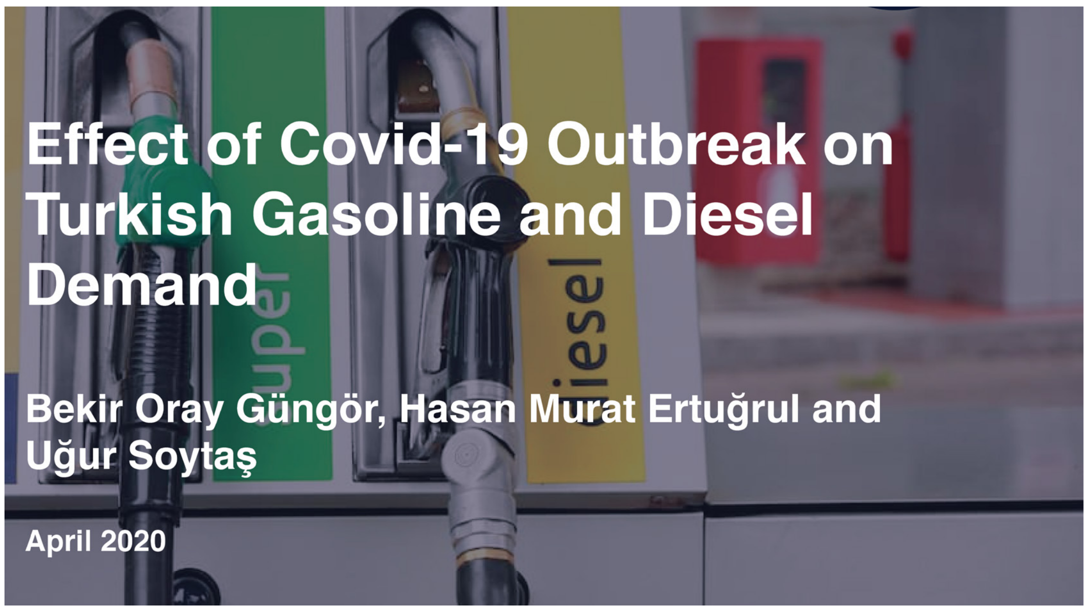
News From Bilkent EPRC



During the Coronavirus pandemic, the Bilkent Energy Policy Research Center continues to produce valuable content for the energy sector and other related areas by inviting international guests through online events. Up to now, we have made three open lectures and six YouTube videos.

Our last event was about the financialization of the energy markets, and we discussed the role of speculations on energy prices. All of our content is available online.

This week at our Center, we will have a busy week. On Tuesday morning, we will share the new video of Synergy Gündemi, where we discuss the current situation in the oil market. Bahattin Büyükşahin and Sohbet Karbuz will be joining us.

On Tuesday evening we will have another live event for the Energy Crisis and World of Energy course.

The CEO of Rapidan Energy and the author of the Crude Volatility, Robert McNally, will join us to discuss the recent events on the oil market and whether there are similarities with the COVID crisis and previous crisis. In the lecture, we will also discuss the future of the post-Corona world in terms of energy.

In his book, McNally discusses the development of the oil sector under two parts. In the first part, he focuses on the history of oil in the United States and how Texas become the power of controlling oil supply until the 1960s.

In the second part, McNally discusses the development of OPEC countries and how they become the global oil cartel throughout the years.

Finally, this week we will also publish a new Bilkent Energy Note, which is #27. Bekir Onay Güngör, Hasan Murat Ertuğrul, and Uğur Soytaş investigate the effect of COVID-19 Outbreak on Turkish Gasoline and Diesel Demand by using the data from Energy Market Regulatory Authority of Turkey.

The report will be published in English initially, and the Turkish translation will be posted in the upcoming days.

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