



Where Next for Oil?

Description

Since hitting a low of \$27 per barrel a year ago, the price of oil has more than doubled. Much of this gain has come in recent weeks, with OPEC's decision to cut production having a positive impact on the price of black gold. However, that production cut will only last until May and so the outlook for oil remains uncertain. Can it keep rising? Or is it now due a significant fall?

Demand and supply

OPEC's cut in production was followed by an agreement by non-OPEC states such as Russia to do likewise. This means that the imbalance between demand and supply which has been a feature of the oil industry in recent years has been reduced somewhat. Although an oil surplus still exists, this is expected to recede within a matter of months so that in the first half of 2017 there is an oil deficit.

This would be good news for the price of oil, since a reversal of the supply glut would mean a higher price could be justified. However, the danger is that demand growth remains sluggish and fails to catch up with supply as quickly as expected. This is particularly relevant given that OPEC's production cut only lasts until the end of May. Therefore, even if the oil price rises between now and then on lower supply, there is a good chance that it will fall thereafter unless OPEC extends its reduced production level.

An uncertain outlook

Last year, it seemed likely that demand for oil in the developed world would gradually fall as cleaner forms of energy become more popular. However, with Trump as President of the US, this process may proceed at a much slower pace. That's because he has questioned the validity of climate change and this means he may be more sympathetic to the fossil fuel sector than his predecessor. This may take the form of more relaxed regulations and fewer incentives for clean energy.

This would be good news for the oil price and traders could begin to price this in over the coming months. Alongside this, demand for oil from China and the developing world is likely to increase rapidly in future years. It will remain the dominant fuel in transportation and across other sectors. This should

mean that even if oil dips this year, it has a bright long term future.

A volatile year

2017 looks set to be another volatile year for the oil price. Uncertainty surrounding supply and demand looks likely to remain, although its long term future remains upbeat due to a new US President and continued rising demand from the developing world. As such, investing now for the long term seems to be a sound move, with a number of Oil & Gas sector companies trading on relatively low valuations. They may lack consistency or stability this year, but they may prove to be highly profitable investments over the medium term.

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