OIL AND GAS PRICE ANALYSIS END MAY

INSIGHT BY ANALYSIS AND TRACKING

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Quick Read

- Brent and WTI prices seem to be clear of the Bear Market and are rapidly constructing a new uptrend.
- US oil output is plummeting and now stands at 11.4 million BOPD or 13% less than 77 days ago. This translates to a drop of 22,000 BOPD each calendar day since oil prices dropped below $31 USD/bbl.
- Oil drilling activity in the US has come to a quick stop. Active oil rigs in the US stands at 222 and is the lowest number of active rigs since Baker Hughes began keeping count in 1980.

The Call

- Unforeseen political events aside the next challenge to further moves on Brent price to the upside will be resistance at $41.18 USD/bbl. Reversal to a Bear Market low is now not as likely but events will be closely watched to seek additional confirming data.
- US Oil production will continue to fall, possibly only bottoming in late summer at 10 to 11 million BOPD.

Brent

The bear Market in Brent price can be convincingly be called over and prices are on a strong uptrend, Figure 1.

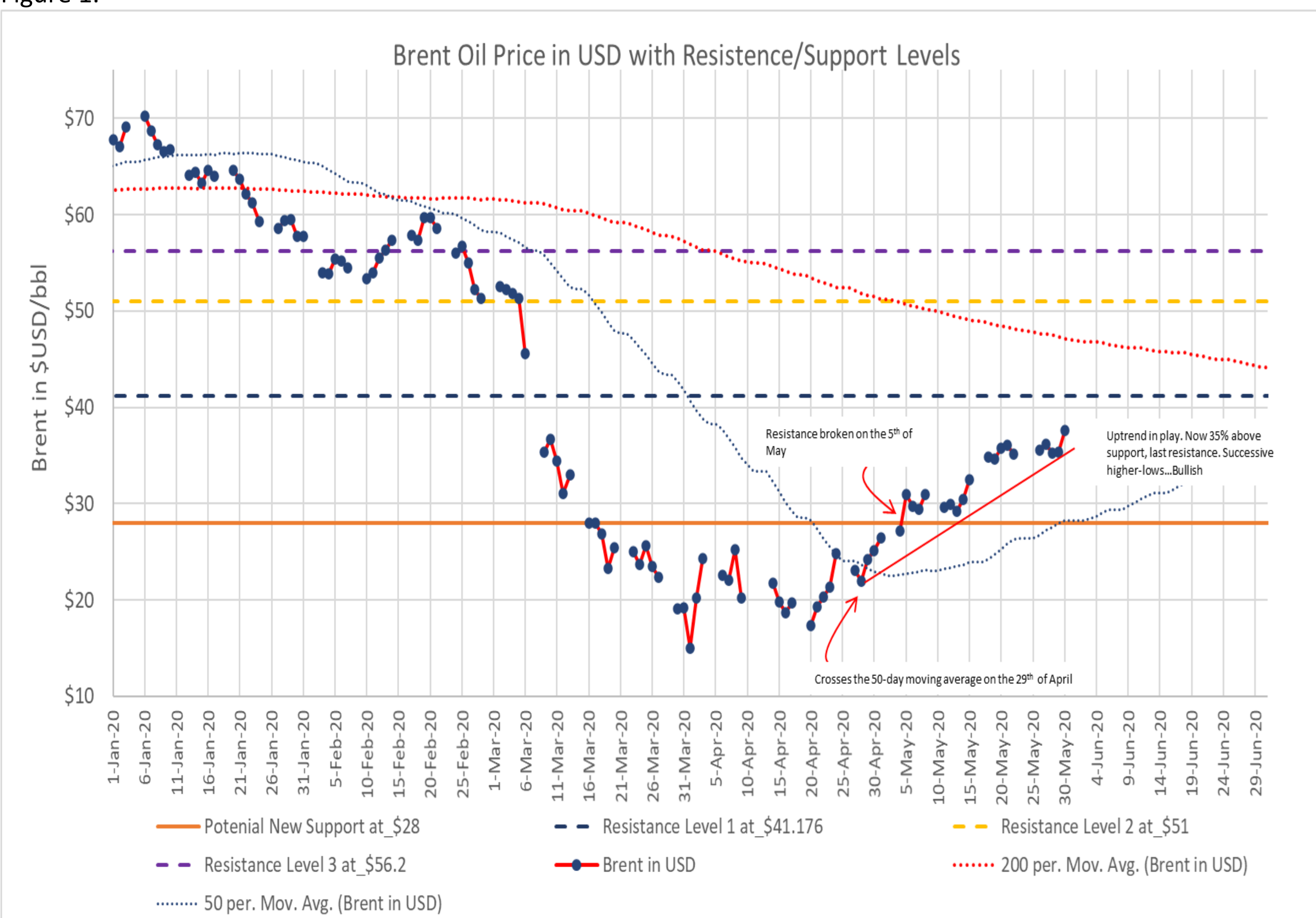

Figure 1: Brent oil price and key levels of price support and resistance.

Note that since prices have crossed the 50-day moving average they continue to be in an up-trend of higher lows. In addition, former resistance at $28 which was taken out on May 5th and is now clear support. The next challenge will be to break resistance at $41.18 USD/bbl. Another Bullish indicator that is appearing is the 50-day moving average on price moving upward against the 200-day moving average. As Figure 2 shows when the 50-day average crosses above the 200-day this is a good leading indicator of further moves to the upside.

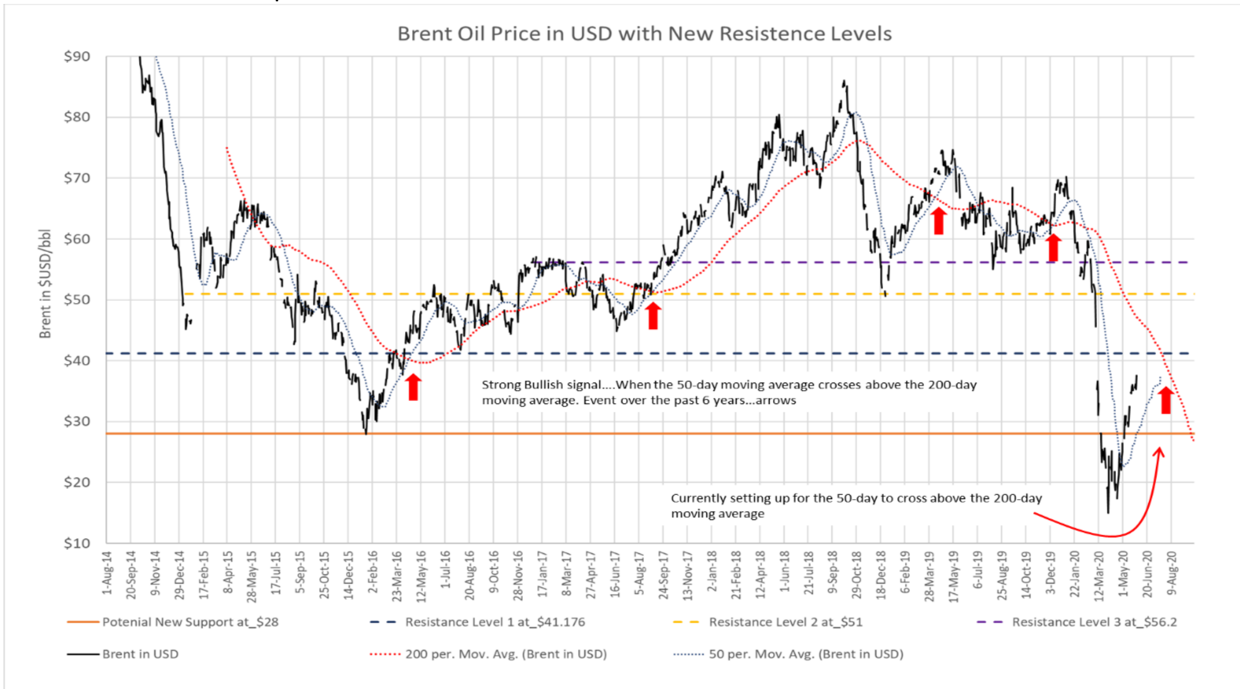

Figure 2: Long term chart of Brent prices showing how the 50-day moving average on price crossing the 200-day average is a leading indicator of continuation of the up-trend.

Tracking the US dollar strength against Brent price reveals another indicator that Brent price should continue to climb. As Figure 3 notes there is a repeat in the pattern from the 2016 oil price collapse and the current crisis.

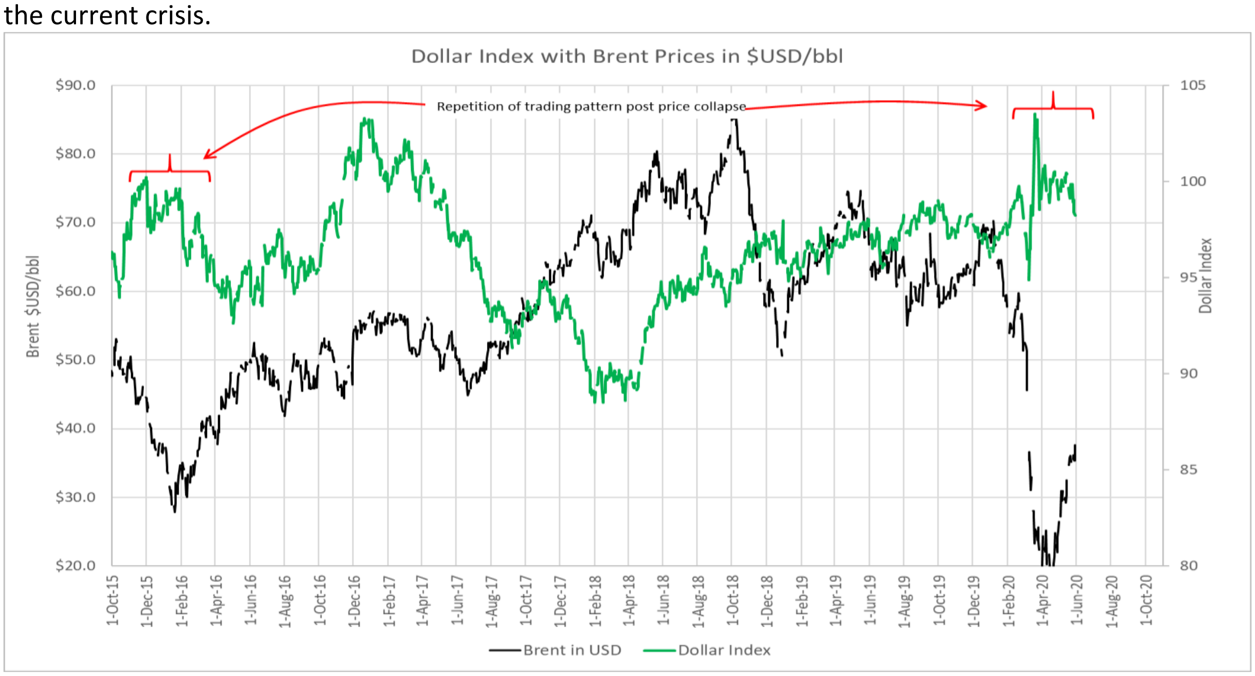

Figure 3: US dollar strength as measured on the dollar index and Brent price.

The pattern that is seen is predictable. As in 2016 the US Federal Reserve lowered interest rates in 2016 which weakened the dollar. This time around the Federal Reserve has injected tremendous amounts of cash by borrowing to stabilize the economy. The end result will be weakening of the US dollar going forward. A weaker US dollar will make purchases of crude cheaper for other currencies and ultimately increase demand and prices.

WTI

The story with WTI is similar to Brent but the return to an improved price pattern is lagging Brent by a couple weeks. As figure 4 shows the price of WTI break old resistance of $26 USD/bbl on May 15th. Similar resistance at $28 USD/bbl was breached to the upside by Brent on the 5th. That delay to recovery by WTI relative to Brent aside, WTI is now clearly in a strong uptrend and the next challenge will be resistance at $46 USD/bbl.

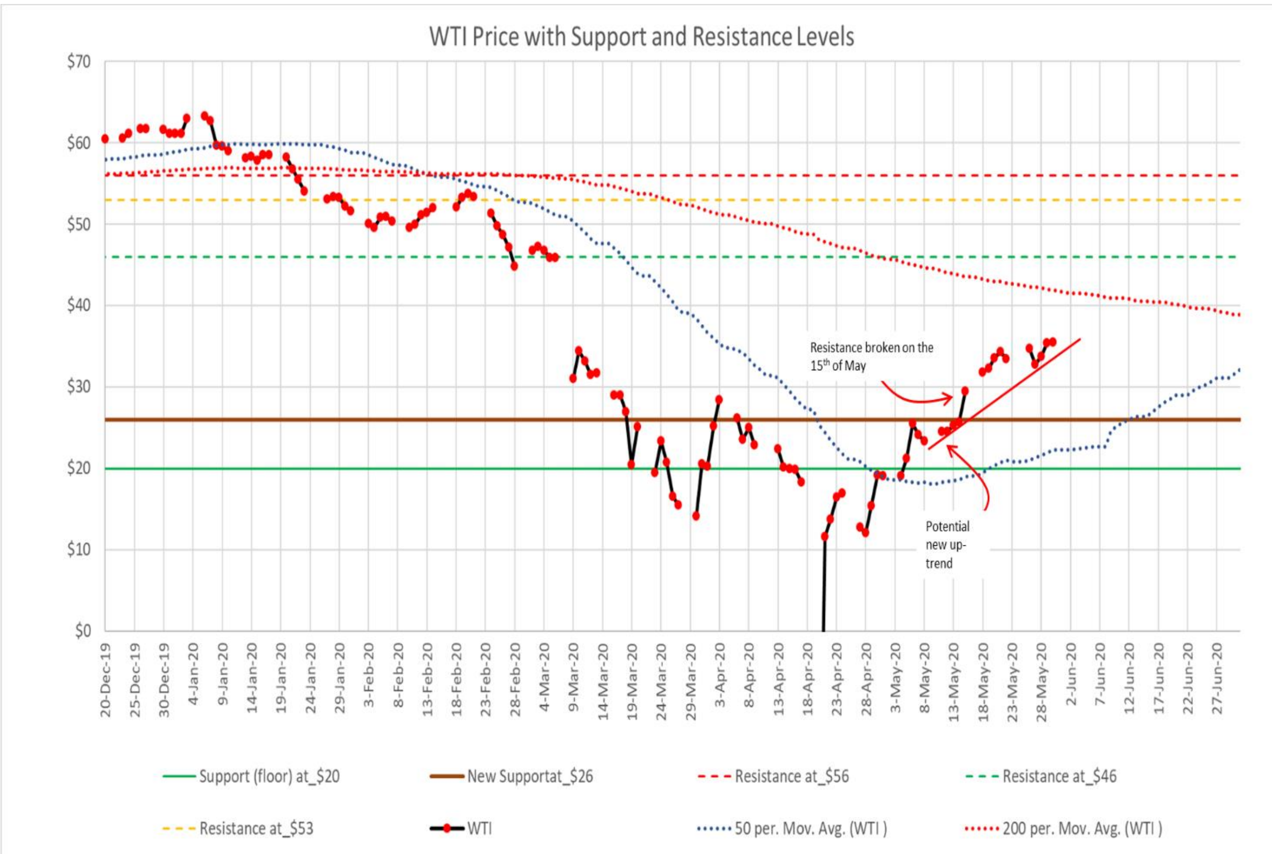

Figure 4: WTI price in USD/bbl and support and resistance levels. WTI is in a clear uptrend, similar to but lagging slightly, the uptrend in Brent.

As with Brent the 50-day moving average on price is making a move up toward the 200-day moving average, Figure 5. This is another confirming indicator that prices should continue on the uptrend.

One thing that does bode well for WTI is the amount of upside to next resistance. It is expected that until prices approach $46 USD/bbl there should be few market-driven impediments to upward rise in prices.

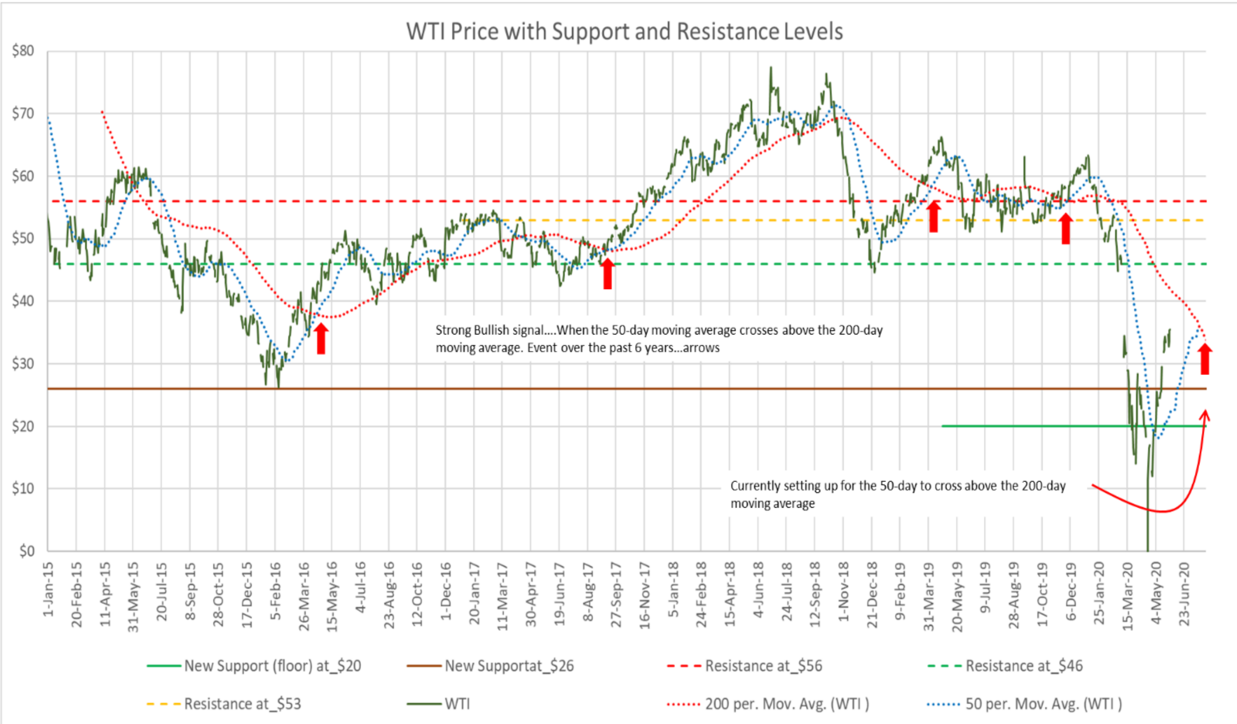

Figure 5: WTI prices and support and resistance levels.

US Activity

Meanwhile is the US oil patch the output, along with everything else oil related, is dropping off a cliff. Figure 6 show how fasr US oil production has fallen. From a peak of 13.1 million BOPD to the current 11.4 million BOPD, a drop of 1.7 million BOPD has taken only 77 calendar days. Or to put it in more perspective, that equates to a drop of 22,000 BOPD every day since the prices in WTI have bottomed, Figure 6.

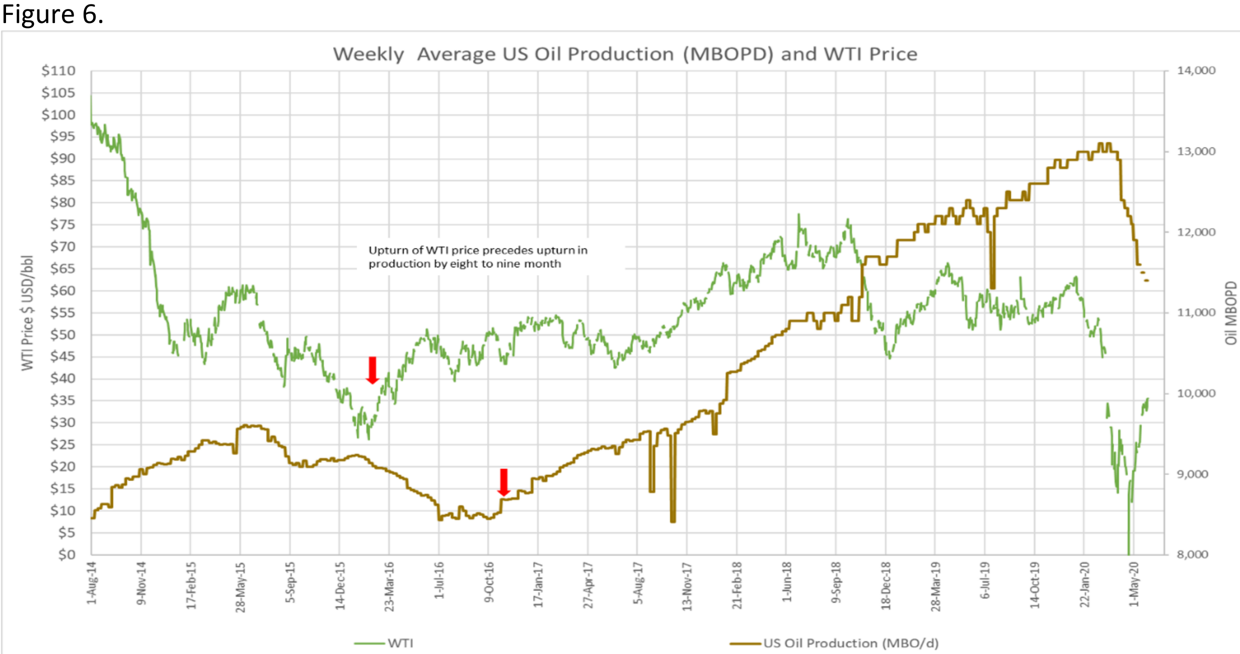

Figure 6: US oil production and WTI price.

Trying to time market reversals is always difficult but using several different indicators can give some clues. In the case of US oil output and WTI price the last pattern seen from the 2016 downturn in price, would seem to suggest that bottoming in US oil production will occur in nine months or March 2021. Best guess on the level of production before any reignition of the Shale oil drilling machine occurs would be around 10 to 11 million BOPD.

As would be expected from an oil price crash the activity levels of oil drillers have come to a quick stop. The US now has the fewest numbers of active oil drilling rigs ever since Baker Hughes has been keeping records. The active rig count stand at 222. This is a 73% drop in active rigs in one year. The impact of fewer drilling rigs is clearly linked to oil production, Figure 7.

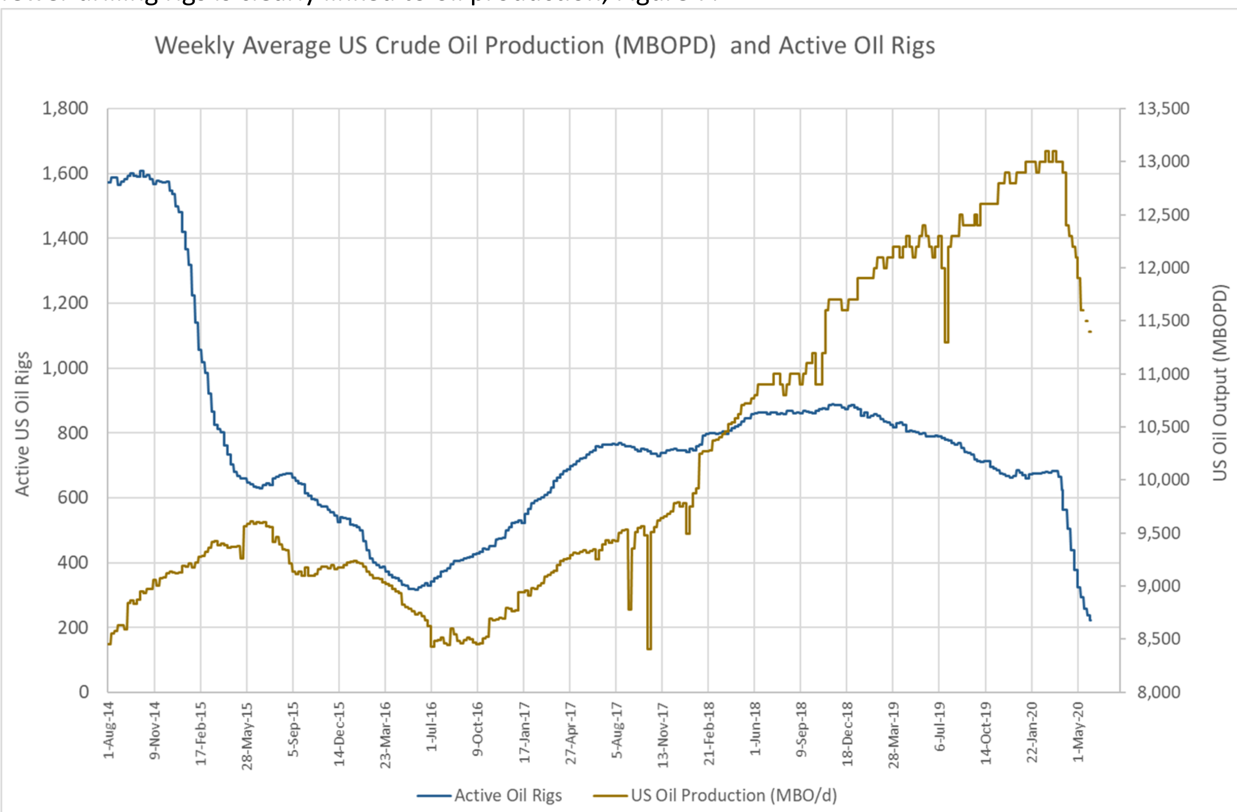

Figure 7: Average weekly US oil output and active oil drilling rigs in the US.

It needs to be pointed out that the total amount of US oil production is difficult to measure on a timely basis. The issue is the segmented marketplace and large numbers of recording districts. It not unlikely that drop in US production could be higher than currently reported. An accounting of barrels exported compared to produced and refinery input has a gap of almost 1 million BOPD. Speculation is that large volumes of crude in storage in the US could be mistakenly estimated as new production.

As US oil production has dropped the differential between Brent and WTI has also decreased. At present WTI sells at only $2-3 USD/bbl less than Brent. Just a couple of month ago this difference was as much as $8 USD/bbl., Figure 8.

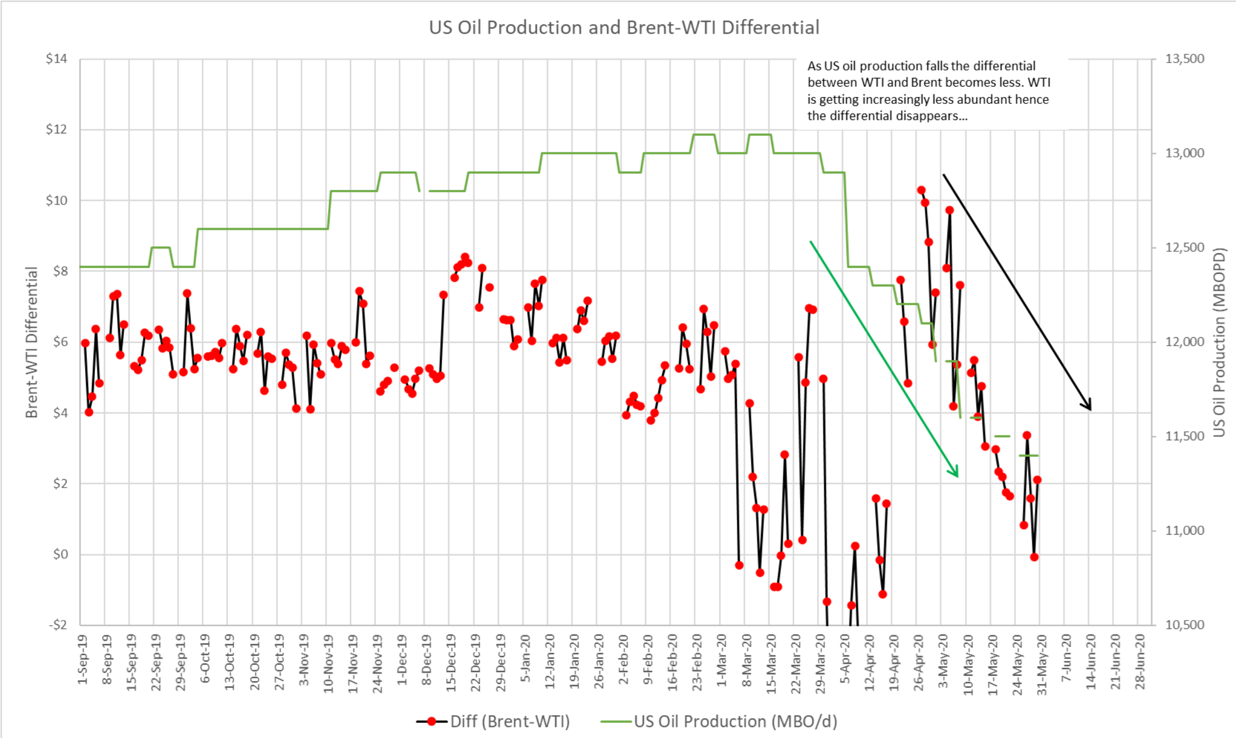

Figure 8: US oil output and WTI to Brent differential.

When WTI is in over-supply it is priced less than Brent. With the current drop in US output traders are betting that WTI and Brent will soon trade near parity once the low in US output is reached. As Figure 9 shows parity or near parity in price between WTI and Brent may be a leading indicator of the coming low in US output as was the case in 2016.

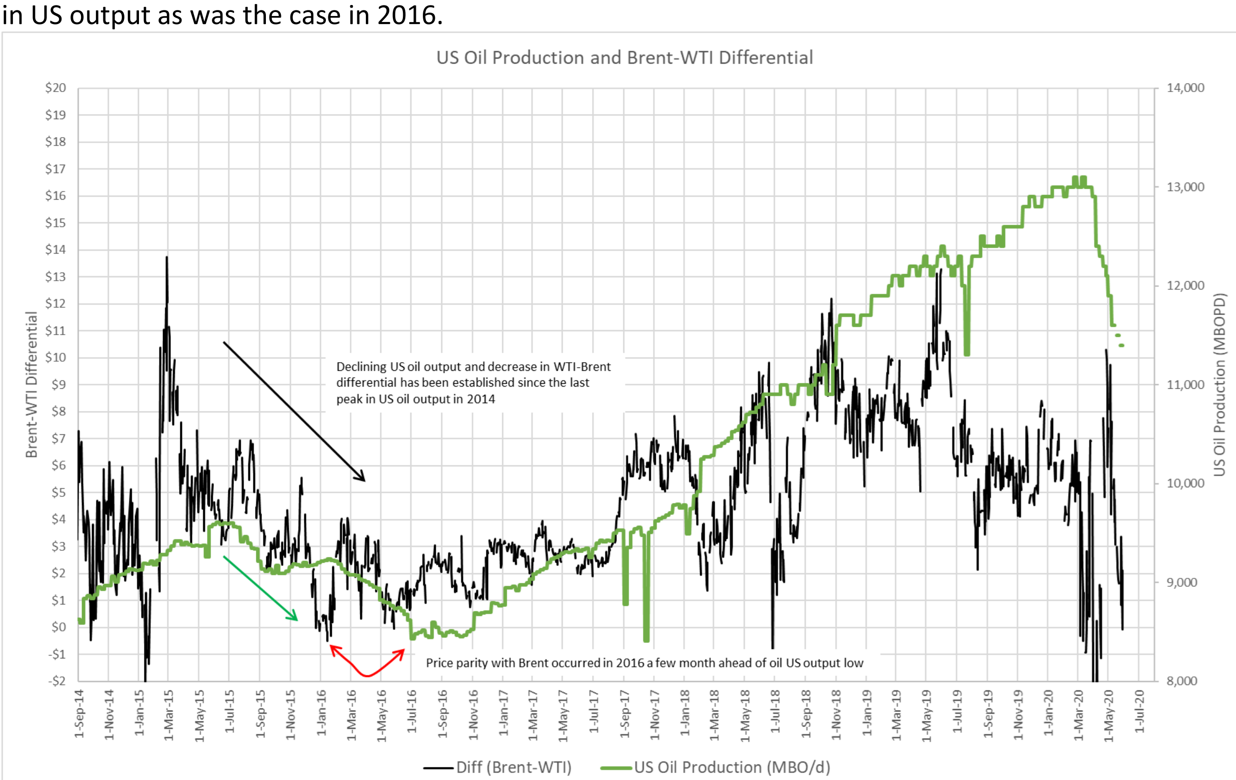

Figure 9: Differential between WTI (cheaper) and Brent. When US oil output drops WTI begins to price more closely to Brent prices.

Finally, some observations on trading pattern comparison between this Bear Market and the Bear Market in 2016. Looking at the pattern reveals that we are probably clear of any Bear Market and that a new uptrend is in play, Figure 10. Technical analysis supports the call that the chances of a Ber Market trap is low. Not likely the previous lows of March and April will be re-visited.
What is worth pointing out in support of the call to an end of the Bear Market is the pattern comparison on price per calendar day of the two Bear Markets, Figure 10. Although the current Bear Market was faster to fall and cut deeper, the time at bottom was the same as 2016. In addition, just like 2016 there was a bottom and a re-test about a month later that actually was lower. But after that second re-test the move was clearly to the upside.

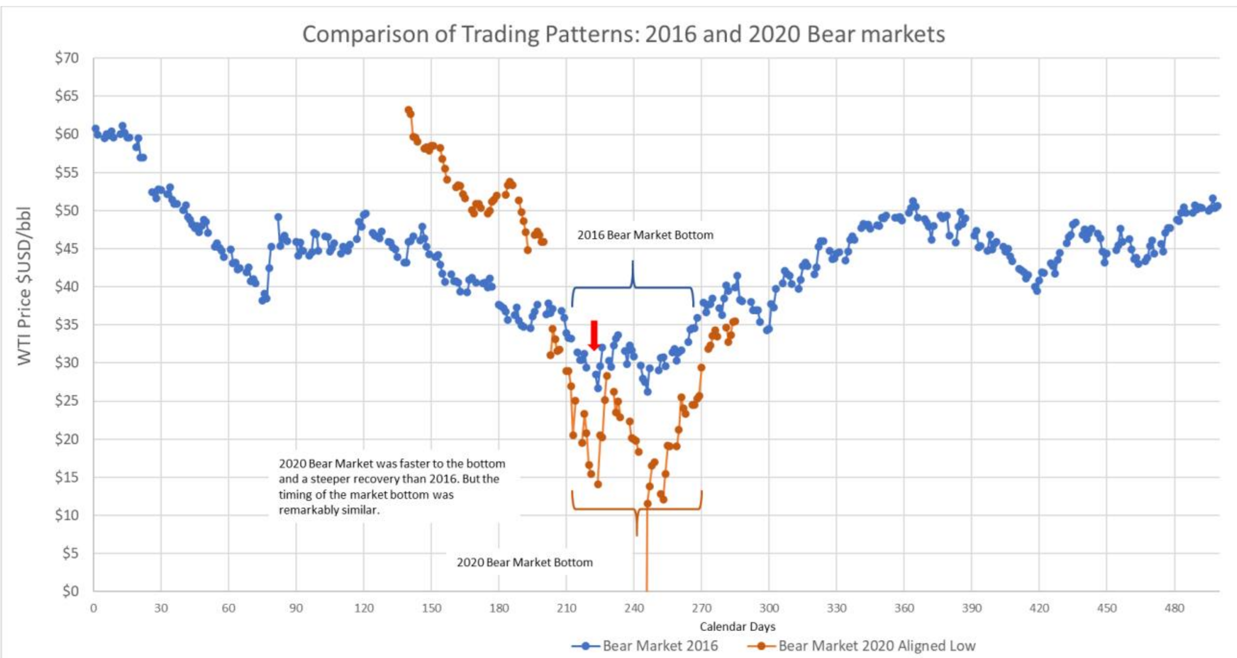

Figure 10: Trading pattern comparison of WTI prices during the 2016 and current price collapse. Alignment of patterns is based on the first low of each pattern, arrow.