

Daily Energy Markets

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Why are we seeing a divergence between equities and energy prices?

There is a key number which sums up the surprise of equity markets quite well. In December 2020, the Fed's forecast of the inflation rate for 2021 was 1.2%. A week ago, that number came in at 7.2%. That's a gross mis projection and consequently the pivot which the Fed had to do was quite dramatic and came unexpected to markets. If inflation is persistent, we will see two things. A need for more rate rises, possibly for more time and we will see more disappointment and volatility in the markets even if the consensus among policymakers will be that an inflation rate of 3% or 4% is not too bad. Meanwhile, the oil price has gone up so smoothly and fast because of a political decision to cut supplies. There is no reason to expect equity markets and all markets to move in tandem. The key question on oil today is that OPEC is running up against its normal capacity of two million barrels. That should happen this year and will indicate when and to what extent supply will come online from outside OPEC plus.

Is the Russia Ukraine situation a big problem for the energy market?

We have is an almost intractable situation which is very likely to lead to a military escalation, probably not in the form of a full-scale invasion of the Ukraine because that would be costly. Russia does not want a thriving and prosperous Ukrainian democracy on its eastern border which could be attractive enough to attract the attention of other countries in that region. Russia wants Ukraine in its orbit as a subservient state with a nonfunctioning government which acts as a buffer of strength. The weakness in the Western response – to prefer peace at all costs and preserving gas deliveries – means that this is a situation which we will find ourselves in again after this crisis has been settled. This is a much more consequential crisis than most of us are expecting.

Immediate outlook for oil fundamentals?

Global demand is key. Secondly, if US sanctions on Russia were to happen, the maximum it would mean would be no Nord Stream two and cutting off Russian financial institutions from the swift system. I can't see this happening, but if it did, energy markets would be in complete turmoil. It would be very hard for consumers of Russian oil to pay for these exports and very hard for the US and the Europeans to maintain a united front in the face of rising oil and gas prices. ■

**Paraphrased comments*

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