The State of Oil:

# MARKET OBSERVATIONS

*MAY 2020*

## Unprecedented

*Chris Fontenot – May 20, 2020*

"Unprecedented" is a word that has been used frequently in 2020. It could be used once again when on Monday, April 20th, a day before the May futures contract was to expire, WTI oil dropped below zero dollars per barrel for the first time in history. This incredible drop meant that producers were paying their customers to take physical possession of the oil. The presumption is producers could tolerate this for the short term because shutting down production would have cost them more than they would pay their customers to take the excess.

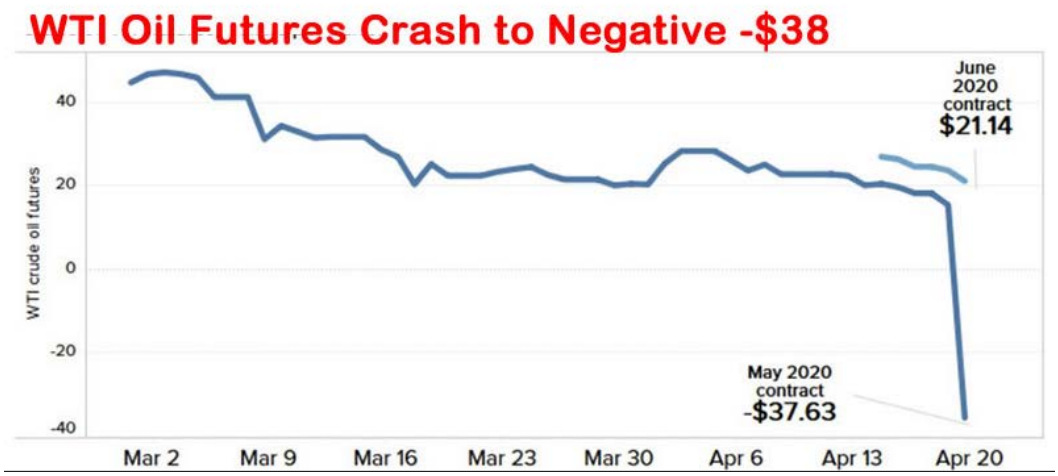


*Image Source: http://marketoracle.co.uk*

The cause of the crash is two-fold, a strong shift in supply, and a simultaneous strong shift in demand. Saudi Arabia and Russia competed for oil market share, seemingly against each other, but the ramifications have been felt worldwide, including and especially US shale. As such, the Saudis ramped up production and oversupply ensued. The shift in demand has perhaps been even more pronounced than that of the supply shift. Likely, 2020 will see the overall crude oil demand drop from 2019. The last time demand dropped from the prior year was in 2009.

As if this doubled-edged sort of supply and demand shift was not enough for the Oil & Gas industry, companies were already feeling the pain of debt burdens before this unexpected crisis emerged. More oil and gas bankruptcies could be on the way as companies such as Chesapeake and California Resources have both issued 'going concern' warnings.[1] A going concern warning implies that there is substantial doubt about a company's ability to continue for the next 12 months. According to Haynes and Boone, around half of the top 60 independent US oil producers are in danger of restructuring and will need to find new ways to boost their cash pile.[2]

1. *marketwatch.com*
2. *reuters.com/article/us-global-oil-usa-restructuring-focus-idUSKCN2250FQ*