Investors In The Oil Sector Should Keep One Eye On The U.S. Dollar

The chart and performance data referenced are for illustrative purposes only and not indicative of any actual investment.

View from the Observation Deck

1. This isn’t the first time that the price of crude oil has plunged after trading north of $100 per barrel. It happened back in 2008 (period not captured in chart).
2. Crude oil reached an all-time closing high of $145.29 per barrel on 7/3/08. Roughly 5½ months later the price of a barrel of oil stood at $33.87 (12/19/08), nearly six years ago to the day.
3. The U.S. dollar, as measured by the U.S. Dollar Index (DXY), surged 11.8% in value from 7/3/08 to 12/19/08. The dollar’s strength was a big contributor to the steep decline in the price of oil, in our opinion.
4. The price of crude oil has plunged once again from a 2014 closing high of $107.26 per barrel on 6/20/14 to $55.95 on 12/17/14. Once again, we believe the dollar’s strength is a major contributor to the plunge in the price of oil.
5. As indicated in the chart (data through 11/30/14), world oil demand continues to inch higher. A lack of demand is not behind the slide in the price of oil.
6. In terms of supply, which is not captured in the chart, global oil producers are currently pumping out approximately 2 million barrels more per day than needed to meet demand, according to the International Energy Agency.
7. Historically speaking, OPEC’s (Organization of Petroleum Exporting Countries) spare capacity level alone is considered low when it dips to 2 million barrels per day, so too much supply isn’t a big contributor to the slide in oil.
8. A strengthening U.S. dollar has influenced, if not triggered, the last two major declines in the price of crude oil, in our opinion.
9. Geopolitics can sometimes play a critical role in determining the value of the U.S. dollar. The current trade sanction battle between the U.S./Europe and Russia is a prime example, and one we intend to monitor closely.