While oil prices look set to remain volatile amid low liquidity in holiday trading, CIO expects Brent to trend higher in 2024. (UBS

Crude rally should gain momentum in 2024

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The price of oil continued its recent rebound yesterday, with Brent crude now up more than 4% so far this week and trading close to USD 80 a barrel amid mounting concerns that the cost of shipping fuel could rise due to disruptions in the Red Sea.

Brent has now gained around 9% since hitting a six-month low only last week. Technical factors may also have helped push prices higher, with speculative traders forced to cover short positions.

With more Russian oil being transported via the Red Sea and Suez Canal to Asia, around 8.2 million barrels of oil each day had been relying on the Red Sea route recently, according to analytics firm Vortexa. But more ships are now avoiding the region, preferring alternative routes via South Africa, resulting in a longer journey and higher costs, despite plans by the US and other nations to strengthen security in these trade routes over the coming weeks.

But despite the extent of recent gains and worries over slowing economic growth, we believe the oil price will continue to move higher into 2024.

Demand for oil looks set to remain healthy next year, especially due to rising consumption in key emerging markets. Much of the recent concerns over the outlook for oil consumption has revolved around slowing economic growth in the US and Europe. Investors will continue to closely monitor consumption in these regions. However, developed nations have not been the main drivers of rising oil demand in recent years. Instead, much of the impetus has come from emerging nations, a trend we expect to continue.

Rising jet fuel use is also likely to remain a driver of demand growth. While jet fuel consumption in the US has already returned to levels prior to the pandemic, usage in Europe and China is still lower, with room to recover further. In addition, several emerging markets, including India, plan to buy more aircraft, which should further boost jet fuel demand over the coming years. More broadly, the International Air Transport Association (IATA) expects that 2024 will see 4.7 billion global travelers, 4% higher than the 4.5 billion before COVID-19 in 2019. We also expect rising structural fuel demand in India.

On the supply side, we expect the recent acceleration in non-OPEC+ production to subside, while OPEC+ remains disciplined on output. Rising production from the US and Brazil has boosted global output in 2023. But following a recent fall in drilling activity, we expect US supply growth to slow in 2024.

And while oil prices were dented by the outcome of the most recent meeting of OPEC+ nations in late November, OPEC + crude production is likely to fall from January, with several countries within the alliance implementing cuts. We believe the group will seek to guard against a further weakening of oil prices.

Geopolitical tensions should also provide support for crude into the new year. Our base case remains that the war between Israel and Hamas does not lead to a significant disruption in oil supplies, despite recent concerns over shipping lanes. However, events remain fluid, and the risk of an escalation looks likely to contribute to hedging demand for oil. In addition, pressure has been building for tighter sanctions on Russian output. This week. the US Treasury announced fresh measures targeting companies shipping Russian oil and changed the process of how companies need to attest that the oil transported on tankers relying on Western services was sold below the price cap. Earlier in December, the US imposed restrictions on three shipping companies for breaching the USD 60 a barrel price cap on Russian oil.

So, while oil prices look set to remain volatile amid low liquidity in holiday trading, we expect Brent to trend higher in 2024. Our base case is for Brent to recover from current levels over the coming months. Risk-tolerant investors can consider adding exposure to oil via longer-dated Brent crude contracts, or selling the risk of prices falling.

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