



Weekly round up (Week 11)

The conflict in the Middle East continued to dominate the news this week, with price movements and market sentiment closely tracking fluctuations in oil prices. Oil itself faced a thankless task, absorbing a relentless wave of volatility fueled by breaking news amid an extremely volatile media environment. The result was an intraday price swing of \$35 per barrel—the largest single-day nominal swing ever recorded since Bloomberg began tracking intraday data on oil futures in the 1980s.

The importance of oil prices to the global economy cannot be overstated, as virtually everything depends on energy to function. A broadly neutral price range, between \$50 and \$70 per barrel, tends to keep the economic impact at a moderate level. However, when prices exceed this range, energy acts as an economic brake: the cost of business rises, consumers' real income falls, inflation expectations rise, and central banks tend to tighten financial conditions. Conversely, when prices fall below the lower threshold of this range, cheaper oil acts as an economic accelerator, reducing costs across the board and increasing purchasing power. For example, if the price of oil rises by 66% (from \$60 to \$100 per barrel), the Federal Reserve's DSGE (Dynamic Stochastic General Equilibrium) model on oil shocks estimates that headline inflation would rise by about 1% over twelve months, while the negative impact on growth would be approximately -0.5% over the following 12 to 24 months.

Yet, despite oil's enormous economic importance, forecasting price movements is notoriously difficult. As John Kenneth Galbraith once quipped: *"The sole function of economic forecasting is to make astrology respectable."* Nowhere is this truer than in commodity markets—and particularly in the oil market. Prices there are at the mercy of unpredictable supply shocks, demand fluctuations that are difficult to measure, and speculation that is poorly understood. Oil sits at the intersection of geology, geopolitics, economics, and human psychology: an unruly mix that makes reliable forecasting extremely difficult.

Thus, for investors, the key questions today are: what is the scale of the energy supply shock, what can be done to minimize the shortfall, and what are the extreme risks weighing on the consensus?

The United States and Israel have clear military superiority, while Iran's advantages lie in its endurance and geography. The Strait of Hormuz is the crucial energy chokepoint now at the heart of the conflict. In February, oil exports transiting the strait from Iran, Iraq, Kuwait, Saudi Arabia, and the United Arab Emirates totaled 18.53 million barrels per day, excluding refined products. More recent real-time estimates, based on the number of reported vessels, show that flows have fallen from 19.4 million barrels per day to just 0.6 million on a four-day moving average. This compares to the widely cited consensus estimate of approximately 20 million barrels per day of petroleum liquids transiting the strait.



According to our analysis, the first potential lever for relief is to redirect supply from maritime transport to pipelines. Saudi Arabia could theoretically redirect an additional 6 million barrels per day via pipeline, while the United Arab Emirates has additional capacity of approximately 0.7 million barrels per day.

The second safety valve lies in strategic reserves. The International Energy Agency (IEA) stated that its 32 members hold more than 1.2 billion barrels in their emergency stocks, and G7 countries as well as IEA member countries have indicated that they will organize the release of up to 400 million barrels from emergency reserves in the coming days. The critical variable, however, is the rate of release. Historically, the highest sustained release rate has been around 1.4 mb/d³, but given the magnitude of the potential supply shock facing energy markets, we assume it rises to 2 mb/d.

The third source of relief, and the most speculative, is what is known as the “ghost fleet.” Following the tightening of sanctions on Russian oil between August and September 2025, a significant volume of crude became stranded at sea as tankers struggled to find buyers compliant with the sanctions. Estimates suggest that approximately 200 million barrels of excess floating inventory could return to the market relatively quickly if sanctions were eased. Again, the speed at which this would hit the market is uncertain, but we assume that around 2 million barrels per day could realistically be released.

Finally, and perhaps most controversially, Iranian exports would likely continue, albeit at a level probably lower than before the conflict. We are revising downward the 2.2 mb/d exported in February to 1.5 mb/d.

Thus, in total, the emergency measure would still result in a net supply shock of approximately 7.2 mb/d on energy markets.

The next challenge is to estimate how long this supply shock will last. When examining prediction markets, the oil futures curve, and options markets to arrive at a consensus estimate, the picture is consistent: markets do not expect the disruption to last more than three months. The probability that a ceasefire will be announced before June 30 stands at 61%. The oil futures curve shows significant backwardation, with prices below \$100 per barrel starting in the second month, falling to \$75 in twelve months. Options markets assign only an 8% probability that the price of oil will exceed \$100 by the end of May.

According to our previous econometric analysis, a 1 mb/d change in the four-quarter moving average of inventories corresponds to a roughly \$12 change in oil prices. Consequently, a 1 mb/d disruption over a quarter would equate to a price change of about \$3. In summary, investors are currently anticipating a bearish scenario for oil: they are either pessimistic about the extent of the supply shortage or about the duration of the shock. Note that for the pessimistic scenario, we reduce pipeline supply from the theoretical maximum to known capacity, slow the rate of withdrawals from strategic reserves to bring it back to historical norms, and assume a complete halt to Iranian exports. The base price for Brent corresponds to the level at the end of 2025.



A rational explanation for the fact that oil recorded its largest daily price swing this week, and that volatility remains high in the coming days, is that extreme risks are significantly amplified in both directions. The downside risk (left tail) primarily concerns the duration of the conflict and, more broadly, the risk of damage to energy infrastructure and production shutdowns in the Middle East, as well as growing difficulties in reopening the Strait of Hormuz, particularly the threat of sea mines and drone attacks. Our most pessimistic scenario suggests that Brent crude could reach \$136 per barrel; with a succession of negative developments, it would be reasonable to anticipate a test of the \$150 level.

Conversely, for the positive scenario, everything depends on the speed of the response. The IEA has stated that it would be theoretically possible to release up to 12 mb/d from collective strategic reserves; even half that amount would significantly mitigate the supply shock. Furthermore, with the exception of Iran and perhaps Russia, nearly all stakeholders have an interest in seeing this conflict end quickly. The U.S. administration also faces midterm elections in November, and prediction markets have put the probability that Democrats will control both the House of Representatives and the Senate at 48%, up 10 points since late February. The president, who has often used financial markets as a barometer of his policy's success, will likely be very disappointed with the markets' reaction so far.

The positive scenario also depends on the United States' ability to partially reopen the Strait of Hormuz. It was announced that the insurer Chubb would be the lead insurer for a U.S. government program aimed at providing coverage for ships transiting the strait. Meanwhile, Energy Secretary Chris Wright stated that the U.S. Navy would begin escorting oil tankers through the Strait by the end of the month. To give a sense of scale, a VLCC (Very Large Crude Carrier) carries approximately 2 million barrels, while a Suezmax carries about 1 million. Thus, even a few successful escorts per day could significantly restore supply flows.

If any of these positive risks materialize, the oil futures curve offers a clue: Brent is currently priced at \$75 in twelve months and \$72 in twenty-four months. Against a backdrop of successive good news, it would be reasonable to imagine a test of the \$70-per-barrel level.



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