MarketWatch

FUTURES MOVERS

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Oil notches highest close in over 2 years

Gasoline also higher, but natural gas sinks after recent gains

By Myra P. Saefong and Claudia Assis, MarketWatch

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SAN FRANCISCO (MarketWatch) — Oil prices climbed nearly 3% Tuesday as violence in Libya and the potential spread of the turmoil in the Middle East and North Africa continued to feed concerns over global oil supplies, prompting futures prices to mark the highest closing level in over two years.

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>
> *Usha Haley, Massey University*

Traders are "recognizing what the Middle East turmoil might do to prices" or oil consumers are "being overly cautious to be sure they have plenty of oil supplies on the way," said Charles Perry, president of the energy consulting firm Perry Management.

But, either way, fundamentals — inventories and consumption — "have not changed enough to see these type of price rises," Perry said.

Light sweet crude for April delivery (NEW:CLJ11) rose $2.66, or 2.7%, to close at $99.63 a barrel on the New York Mercantile Exchange. That's the strongest closing level for a most active contract since September 2008.

"The struggle in the [oil] market currently divides at those who see the uprising in and about the oil-producing regions as epochal, which will bring far-reaching changes to the production and distribution of oil, and those who are more concerned with the feeble recovery and intransigent debt problems in the consuming countries," said Mike Fitzpatrick, editor of Kilduff Report's Energy Overview.

"We hardly have the answers to these weighty issues, but certainly there is little doubt the recovery is feeble, at best, and spontaneous uprisings like these are hard to suppress. For this reason alone, lean marginally long, until a resolution appears reachable," he said in a note to clients.

Crude prices gained as the international community called for the embattled Libyan leader Col. Moammar Gadhafi to step down, and the United Nations imposed sanctions on the country. Government forces reportedly regained control of a key oil-terminal town east of the capital Tripoli.

"It is clear that Saudi Arabia has enough spare capacity to make up for the current estimated (800,000 barrels a day) shortfall from the disruptions in Libya — as well as any further reductions," analysts at J. P. Morgan said in a note to clients Tuesday. "As Saudi Arabia was already in the process of raising output ahead of the disruption, the process of restarting capacity may take less time."

In addition, reports emerged that some oil continues to flow in Libya, much of the world is in refinery maintenance season, Saudi Arabian output is running as high as 9 million barrels a day, further dimming the impact of the loss of Libyan supplies, the analysts said.

Saudi pressure

But some traders and analysts were concerned about the likelihood of cuts to Saudi Arabia's spare capacity.

Saudi Arabia has stepped up production to counter the Libyan outages, Tim Evans, energy analyst at Citigroup's Citi Futures Perspective, said in a note, but "multiple problems would soak up additional capacity, reducing the remaining cushion."

And fears of contagion to other North African and Middle Eastern countries continued. Read about Tuesday's developments in the Middle East.

"As the violence rages on in Libya and overall uncertainty grows, there are mounting fears that other producers in the immediate vicinity will suffer similar outages due to political unrest," analysts at Barclays Capital said.

“Though Algeria is an immediate concern for the market, we would view Iraq as a larger threat to the oil market, especially if the unrest continues to spread in the country,” the Barclays Capital analysts added.

In Saudi Arabia, concerns over the spread of unrest were particularly prevalent.

“King Abdullah’s ‘royal gift’ last week of $35 billion to go towards social causes and housing benefits has not assuaged the unrest,” said Usha Haley, an expert on emerging markets at Massey University in New Zealand, and “rumors point to massive planned demonstrations around March 20th or 21st.”

“This matters because Saudi Arabia unlike Libya, Egypt and Tunisia is the largest exporter of oil in the world,” she said. “Simply put, the unfettered supply of oil matters for every aspect of global welfare.”

Brent oil futures advanced on Tuesday, adding $3.62, or 3.2%, to close at $115.42 a barrel on ICE Futures in London.

Energy products in New York tracked oil higher, with gasoline for April delivery (NEW:RBJ11) up 9 cents, or 3.1%, to end at $2.983 per gallon. April heating oil (NEW:HOJ11) added 8 cents, or 2.9%, to close at $3.024 a gallon.

April natural gas (NEW:NGJ11) , however, lost 16 cents, or 4.1%, to finish at $3.873 per million British thermal units, pulling back from recent gains.

Energy traders also digested news that Noble Energy Inc. (NYSE:NBL) had received a permit to resume drilling at the Santiago prospect in the deepwater Gulf of Mexico. The permit is the first deepwater permit issued in the Gulf since the BP oil spill last year.

Well operations at the Santiago prospect had been suspended in June of last year as a result of the drilling moratorium in the deepwater Gulf of Mexico, Noble said.

“We will wait for additional permits before adjusting our expectation for activity to gradually resume in [the second half of 2011] for halted projects and [first half of 2012] for new drills,” analysts at Canaccord Genuity said in a note to clients.

“Gulf of Mexico output should decline 0.3 [million barrels of oil per day] this year, partly offsetting the 0.5 [million barrels of oil per day] expected gain in U.S. onshore supply,” they said.