Brent Crude Oil

Introduction

Crude oil Trading

Crude oil, also known as petroleum, is the most actively traded commodity in the world. Leading marketplaces are Geneva, London, New York, Chicago and Singapore. Because crude oil serves various production needs as the primary raw material and energy source, it is often referred to as “the black gold”. There are several grades of crude oil with respect to the gravity/density and sulphur content. These are the three primary benchmark grades:

- West Texas Intermediate (“WTI”), also known as “Texas Light Sweet”;
- Brent Crude, which is sourced from the North Sea; and
- Dubai Crude, extracted from the United Arab Emirates.

Other well-known blends/grades include the OPEC basket (weight average made up of many blends), Malaysian Crude (known as “Tapis Crude”) and Nigerian Crude (known as “Bonny light”). Brent Crude (also known as Brent Blend, London Brent, and Brent petroleum) is recognized as a high grade crude oil sourced from the North Sea (the region between the British Isles, mainland Europe, and Scandinavia). It is generally classified as a light, sweet crude blend, thereby making it easy to refine. It is however, not as light as the WTI. It is also considered worldwide (alongside with WTI) as a benchmark for oil pricing. Oil price is usually quoted per barrel (around 160 liters). The price of oil, as quoted in the news, generally refers to the spot price per barrel of either WTI or Brent. The price of a barrel of oil is highly dependent on both its grade and its location. Brent crude oil futures contracts are traded on the Intercontinental Exchange (ICE) as well as other exchanges across the world and are delivered in every month of the year. Every product traded on the ICE conforms to strict specifications described below.

ICE Brent crude oil futures contract specifications

Contract symbol: B
Contract size: 1’000 barrels
Currency: US Dollars and cents
Underlying product: Brent crude oil
Recent price history

In October 2007 crude oil rose above USD 80 for the first time. This price was a reflection of rising tension in Eastern Turkey and the decline in strength of the USD. Oil broke again through USD 110 in April 2008; in the same year it continued its rise, passing USD 135 in June and USD 145 in July. On the 03rd of July 2008, oil prices rose to an all-time high of USD 146.08 following concerns over Iranian missile tests being carried out at the time. On the 14th of July 2008, US President Elect George W. Bush lifted the order banning offshore drilling that had been implemented by former US presidents. As a direct consequence, oil prices declined very quickly in the following days by more than USD 20 to reach USD 125. By October 2008 it had dropped further to USD 60, finally culminating in December 2008 when the price of a barrel of oil attained USD 36.61, around ¼ of the price reached six months earlier. In March 2009 oil rose again and broke through USD 125 in April 2011. Since then, oil prices range while slightly declining to below USD 110 in July 2013.

Which factors can affect oil prices?

The price history of oil shows that demand and supply can be impacted by various different factors such as:

- Politics
- Social factors
- Environmental factors (such as natural disasters)
- Macroeconomics
- Speculation
- Technological advancements (such as with alternative energies)
- Global economic conditions
- Emerging economies and markets
Due in part to its presence in numerous markets, oil price is subject to various external forces as well as other markets' conditions. Changes in the industries that use oil in their products can have a significant impact on the oil industry itself. Moreover, the usage of oil may be significantly impacted by global economic conditions and by the development of emerging economies. It is important to note that currency trading is also directly affected by oil prices. For example, the US dollar may cause the rise or fall of the price of oil, and vice-versa. Due to this fact, the US dollar is known as a commodity currency. Other commodity currencies are the NOK, CAD, AUD and NZD.

**Who uses the oil market?**

The oil marketplace comprises of a large array of participants, including:

- Commercial enterprises with a direct stake in the price of oil: the contract can be a valuable hedging instrument. As a safeguard against falling cash market prices, producers and traders can sell oil futures to lock in prices for future delivery, protecting the value of future oil sales.
- Other oil industry participants: such as refiners.
- Professional energy traders.
- Investors and speculators: with no intention of buying or selling actual physical commodities, are simply trying to make money by trading its value.

**What are the underlying risks of oil trading?**

The risk of loss in trading oil or other commodities can be substantial. You should, therefore, carefully consider whether such trading is suitable for you in light of your financial condition.

*Brent crude oil trading is speculative and influenced by many factors*

Oil trading can be very volatile and involves a high degree of risk. The low margin deposit required permits an extremely high degree of leverage. Accordingly, a relatively small price movement in an oil contract may result in immediate and substantial loss or gain to the trader.

Price movements are influenced by among other things; changing supply and demand relationships, economic events, trade, fiscal, political, monetary and exchange policies of governments, weather (climate conditions), and emotions of the market place. Foreign policy of certain countries can have a big impact on oil prices, and investors can do very little about this aspect of oil trading.

As an example OPEC is a huge driving factor in the price of oil. While OPEC carefully regulates oil production to keep the oil market steady, fluctuations in the market can cause drastic changes in the price of oil, therefore making oil trading extremely risky. War or civil unrest can decrease oil production, increasing demand and sending prices skyrocketing, however producing too much oil can lead to a drop in oil prices, resulting in a big loss for oil traders.

None of these factors can be controlled and no assurance can be given that the trading activity will result in profitable trades and not in substantial losses.
Demand for oil can be extremely difficult to predict

Analysts generally predict the demand for oil to go up, and therefore the price to increase.

Oil has many applications and the oil demand is worldwide. As this demand increases, prices should also be expected to rise. However, oil demand is a tricky thing to predict! As the price of oil increases, this places greater pressure on consumers’ consumption. For example, should oil prices increase at a time when the economy is worsening; this will more than certainly result in the drop in demand from consumers. Less demand means a decrease in oil price, with oil traders ultimately losing money.

Trade leverage

Depending on your experience level, trade leverage can be a powerful tool to help maximize returns, or alternatively it can cause significant loss. Due to its complexity, trade leverage must not be taken lightly and it is recommended that you refrain from trading until you have read and fully understood the mechanism described in the eForex contract, in the Account opening documentation and on Swissquote’s websites.

In addition, oil trading with leverage may not be suitable for all investors as it carries a high degree of risk. As you could lose your initial deposit, you should ensure that you fully understand all the risks. These risks are also intensively described in the eForex contract, in the Account opening documentation and on Swissquote’s websites.

Failure of Electronic Trading System

Electronic trading systems are susceptible to temporary breakdown. In the event of system or component failure, it is possible that (for a certain period of time), you may not be able to enter new orders, execute existing orders, modify, or cancel orders that were previously entered. In such circumstances, you shall directly contact a sales representative or the dealing desk in order to check and monitor your open positions.
Brent crude oil Trading

Swissquote aims to facilitate to its clients the access to online Brent crude oil trading, as well as to provide an alternative to current solutions offered by other online brokerage platforms (namely futures).

We aim to propose an Brent crude oil trading alternative with the same trading features that are currently applied to currencies, precious metals and energy on all of our eForex platforms such as;

- Real time trading
- Deep liquidity
- Low cost trading
- Leverage use
- Automatic closing out
- Automatic rollover of open positions
- No physical delivery

A Brent crude oil transaction executed through Swissquote is made against USD (LCO/USD).

What does Swissquote propose?

Through its Brent crude oil contract, Swissquote proposes a combination between:

- OTC trading (with no physical delivery); and
- Derivative products (which imply automatic management of expiration dates).

The Brent crude oil transaction is a computation derived from the ICE Brent crude oil Future contracts (hereafter "ICE Brent crude oil Futures") traded and quoted at the Intercontinental Exchange (Symbol: B).

ICE Brent crude oil Futures are organized through a specific calendar and only standardized contract months are available in the marketplace (for example: January 2013, February 2013, March 2013, etc.). On the other hand, ICE Brent crude oil Futures have the benefit of a high liquidity.

Price generation

The Brent crude oil contract is constructed through the combination of two ICE Brent crude oil Futures contracts with different maturities.

Indeed, the Brent crude oil contract price is based on the 1st Maturity Future (B1) and adjusted by the Spread between the front contract (B1) price and the next available Future (B2) price; the spread itself adjusted by a Delta Factor and a Time Factor.

**Spread** = B2 – B1 (eq to. Price difference between 2nd & 1st Maturity Future contract)

B1: the 1st Maturity Future

B2: the 2nd Maturity Future

**Delta Factor** = Price adjustment computed once a month to avoid a price gap at the Future contract switch.

**Time Factor** = ratio combining the remaining days before B1 expiration and the total number of day between the last and the next expiration.

**Leverage**

During the week, you will enjoy a maximum leverage of 30:1. Actually, this leverage is only available between 11:00 pm CET on Sunday and 09:00 pm CET on Friday. On weekends (between 09:00 pm CET on Friday and 11:00 pm CET on Sunday), the maximum leverage is 15:1. Regardless of which platform you choose, a 30:1 leverage with a capital outlay of USD 1,000 will allow you to invest USD 30,000 in the market.

**Automatic closing out**

You are fully responsible for monitoring the activity on your account. However to ensure that your losses do not exceed your entire equity, Swissquote operates a system which ensures the automatic closing out of all open positions as soon as the margin threshold is breached, at the next available market price for the corresponding execution size. For additional information, please refer to the Forex contract, the Account opening documentation and Swissquote’s websites.

**Rollover/overnight fee**

It is not possible to physically deliver the aluminium traded on our platform. The aluminium contract is purely speculative by nature. To prevent the delivery, the open aluminium positions are automatically renewed for the following maturity date. To smooth out the price difference between the two Futures contracts (B2 & B1), which basically represent the monthly rollover cost, we would apply this difference on a daily basis, as a rollover fee. With such a fee actualized on a daily basis, the client does not suffer from the switch from one contract to another.

**Daily Rollover cost** = ( ( [ B2 – B1 ] - Delta Factor ) / Y) ± SQ Markup

Y = total number of days between the last and the next expiration (B1 & B2).

This rollover mechanism is applied on daily basis and therefore has consequences on your account. An amount is credited or debited to your trading account and is related to the renewal of your position: this being the price difference between the next available ICE Brent crude oil Future maturity (B1) and the subsequent available ICE Brent crude oil Future maturity (B2). The rollover process takes place automatically between 11:00 p.m. and 11:15 p.m. The debit or credit is then booked to your account on the following day.
Practical examples of Overnight Rollover

Example 1

Date of transaction: 24 January 2011

Available ICE Brent crude oil Futures contracts:

<table>
<thead>
<tr>
<th></th>
<th>Price</th>
<th>Roll date</th>
</tr>
</thead>
<tbody>
<tr>
<td>B1 maturity</td>
<td>80.39</td>
<td>13.02.2011</td>
</tr>
<tr>
<td>B2</td>
<td>80.82</td>
<td></td>
</tr>
</tbody>
</table>

Delta Factor = 0  

Time factor = 0.57  

Spread = 80.82 – 80.39 = 0.43

$LCO/USD Price = 80.39 - ((0.43 - (0)) * 0.57) + mark-up = 80.15 + mark-up$

Roll over fee: 0.01265 + mark-up

Example 2

Date of transaction: 30 March 2011

Available ICE Brent crude oil Futures contracts:

<table>
<thead>
<tr>
<th></th>
<th>Price</th>
<th>Roll date</th>
</tr>
</thead>
<tbody>
<tr>
<td>B1 maturity</td>
<td>81.25</td>
<td>10.04.2011</td>
</tr>
<tr>
<td>B2</td>
<td>81.64</td>
<td></td>
</tr>
</tbody>
</table>

Delta Factor = -0.01  

Time factor = 0.39  

Spread = 81.64 – 81.25 = 0.39

$LCO/USD Price = 81.25 - ((0.39 - (-0.01)) * 0.39) + mark-up = 81.09 + mark-up$

Roll over fee: 0.01357 + mark-up.
Help

If you require help or further information, please do not hesitate to contact our FX sales team +41 44 825 87 77.

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