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Energy Monitor

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OPEC+ fails to deliver; oil prices under severe pressure

- **OPEC+ failed to reach an agreement to cut production further to balance the market and to support oil prices**
- **Fears about the spreading of the coronavirus are leading to a strong drop in oil demand**
- **ABN AMRO's oil price forecast revised lower**

OPEC and partners failed to reach a new production cut agreement

Russia refused to join the OPEC meeting on reaching an agreement for a bigger production cut. As a result, the current production cut agreement (officially -1.7 mb/d + 0.4 mb/d voluntarily by Saudi Arabia) will continue until the end of March. From 1 April all oil producers are allowed to produce as much as they like, although OPEC's Chairman Barkindo indicated that there will be more informal meetings to follow in the coming days and weeks to find a solution before the end of the month.

OPEC crude production

Source: Bloomberg

Earlier in the week there were already doubts over whether Russia and Saudi Arabia would be willing to compromise. Russia wanted to extend the current agreement until the end of the year, while Saudi Arabia wanted an additional production reduction of 1.5 mb/d on top of the current agreement. On Wednesday, the Joint OPEC/non-OPEC Technical Committee (JTC) failed to produce a strong and aligned proposal, instead advising the conference to come up with a compromise. At the OPEC meeting on Thursday there were signs that an agreement could be reached. The proposal to the conference between OPEC and non-OPEC members on Friday was to extend the current production reduction agreement of 1.7 mb/d until the end of the year. In addition, Saudi Arabia would also continue its voluntary production

reduction of 0.4 mb/d. There was also an agreement to propose an additional production reduction of 1.5 mb/d until June. However, when financial markets reacted negatively (sharply lower oil price) to this news of possible agreement, OPEC then decided on Thursday evening to extend the additional 1.5 mb/d reduction until the end of the year (compared to the earlier proposal of until the end of June). This heaped even more pressure on the Russian delegation.

The Russian Energy Minister Novak indicated that he wanted more time to see the full impact of the coronavirus on global demand, and expects central banks to take the lead in managing the effects of lower economic growth. As a result, Russia was not willing to participate in a bigger production cut at all. The only alternative for Russia was an extension of the existing deal until the next OPEC meeting in June. This suggestion was blocked by OPEC. All ministers left the OPEC building in Vienna, leaving oil prices under severe pressure. Both Brent and WTI dropped by 10%. However, after Saudi Aramco lowered its prices for oil deliveries in April dramatically, oil prices really started to slide lower. On Monday morning, both Brent and WTI traded almost 30% lower.

Although there might be some sort of a deal in the coming days or weeks as informal talks will continue, we believe that market confidence is already badly hurt and oil prices will continue to trade lower for longer.

Brent and WTI oil price developments

Source: Bloomberg

Market share of OPEC remains under pressure

The OPEC market share has been under pressure for several years. For Saudi Arabia, this was the main reason to increase oil production and thereby put oil prices under pressure back in 2014. However, the strategy to regain some market share has failed and has even proven to be counterproductive. Many oil producers were losing money initially, however due to higher production efficiency and production cost declines non-OPEC production increased strongly to levels higher than before. Therefore, the Saudi decision to increase production and to create an oversupply proved a short-lived attempt to halt the slide of the OPEC market share. This week's decision not to lower production again to balance the market and support oil prices will bring back 2015/2016 scenarios. It is quite a challenge to align oil producers as the willingness to compromise is low. Please see our publication on the need for a new OPEC strategy here.

Lower oil demand due to coronavirus impact

Chinese oil demand has dropped significantly since mid January due to the impact of the novel coronavirus. The recent *Oil Market Report* by the International Energy Agency (IEA) already showed expectations for a drop in Chinese demand to 12.6 million barrels per day (mb/d) from 14 mb/d during Q1 2020. In recent weeks, the situation has worsened as the virus continued to spread outside China. Some analysts even expect a total drop in global demand of 4.5 mb/d compared

to December levels. This is around 4.5% of total demand. Although activity in China has partially restarted again, we do see a considerably lower number of flights towards the region. The broader travel and tourism industry also starting to feel the effects

We expect that the negative impact on the economy – and thus on oil demand – will continue and therefore we have downwardly revised most of our growth forecasts for the first and second quarter of this year. We do expect a recovery during the second half of the year. Please see here for more.

Oil price forecasts revised lower

Due to the drop in global oil demand, in combination with the existing and most likely even rising oversupply, oil prices will continue to trade lower, and for longer. In line with our downward revisions of economic growth forecasts, global oil demand will only modestly recover during the second half of 2020. At the same time, global inventories will remain high and with the risk of all oil producers stepping up their production (where possible), the oil glut will remain for longer.

On top of that, it remains uncertain how Libyan exports will develop during the coming months. Due to unrest in Libya, its oil exports have dropped substantially since mid-January. This 1 mb/d drop was not even included in the OPEC+ agreement. If the Libyan crude exports return to their normal levels, it will add another 1mb/d and even further limit upside in oil prices. A balancing factor could come from the US. US shale oil production at current (WTI) oil prices is not economically viable for many producers in the US. This could lead to a stabilisation or even a small drop in US oil production in the coming months.

After the violent selloff, which resulted in a test of the early 2016 lows, we believe that further downside risks may be limited. This dip in oil prices is expected to be temporary and will be corrected by lower production numbers, especially in the US. But, while Russia was ok with an oil price of USD 40/bbl, the current level is hurting the Russian economy as well. The Saudi's have, with their low oil prices for April, signalled to Russia that they are now also in the need of a new production cut agreement.

We expect that there is a good chance that OPEC (with or without their partners) will come to some sort of a deal before the existing agreement expires at the end of this month. For now, we have lowered our Brent oil forecast for the end of this quarter from USD 60/bbl to USD 40/bbl. For the second quarter, we have revised our forecasts from USD 55/bbl to USD 48/bbl with downside risks if a OPEC or OPEC+ deal is not reached in the course of this month. We have lowered the Brent year average forecast for 2020 to USD 49 from USD 58. The forecasts for WTI are revised in a similar way. As a result, the Brent/WTI spread will remain stable at USD 5/bbl. See the table below for our new base case scenario forecasts based on this scenario above.

In our most important risk scenario, if OPEC(+) is not able to reach an agreement after all during the coming weeks, oil prices will remain trading low (USD 30-40 range). A recovery of the oil prices should then come from lower US production. However, it could take several months before the negative impact of the low oil prices start to impact the production numbers. In 2016, US production dropped by maximum 1 mb/d in the months after the steep drop in oil prices. This time, the impact on US production could be bigger due to a weaker financial position of many US shale producers as oil prices were already trading around break-even point levels, which weakened their cashflows and raised their financing needs. If US production would starts to decline, oil prices could find their way up again and recover into the USD 40-50/bbl range.

Forecasts oil and gas prices

End of period		6-mrt	mrt-20	jun-20	sep-20	dec-20	mrt-21	jun-21	sep-21	dec-21	mrt-22	jun-22	sep-22
Brent	USD/bbl	*46,32*	40	45	52	55	60	60	65	65	60	65	65
WTI	USD/bbl	*42,20*	35	40	47	50	55	55	60	60	55	60	60
Natural Gas (HH)	USD/mmBtu	*1,73*	2,00	2,10	2,25	2,75	2,50	2,50	2,50	2,75	2,50	2,50	2,50
TTF	EUR/MWh	*8,70*	13	13	14	15	15	14	15	17	18	17	18
Average		**2019**	**Q1 20**	**Q2 20**	**Q3 20**	**Q4 20**	**2020**	**Q1 21**	**Q2 21**	**Q3 21**	**Q4 21**	**2021**	**2022**
Brent	USD/bbl	64,17	53	43	49	54	49	58	60	63	65	63	65
WTI	USD/bbl	57,00	48	38	44	49	43	53	55	58	60	58	60
Natural Gas (HH)	USD/mmBtu	2,53	2,10	2,10	2,20	2,50	2,30	2,75	2,50	2,50	2,75	2,60	2,60
TTF	EUR/MWh	14,55	12	13	14	15	14	15	15	15	16	15	19

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