

Energy Monitor

Group Economics

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Geopolitical poker games

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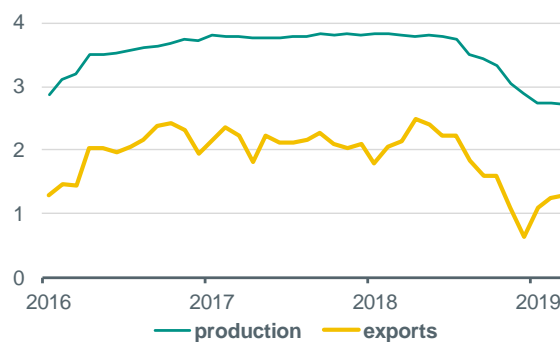
- **US ends waivers on Iran sanctions**
- **Iran crude exports will drop, but not as far as people may fear**
- **Oil prices may gain somewhat, but upside potential is limited**

Iran oil exports to decline as US waivers on sanctions end

The US announced that it will end the waivers on Iranian sanctions. Six months ago the US tightened their sanctions on Iran because it stepped out the nuclear deal. Basically these sanctions form a ban on Iranian access to the US financial system and use of US dollars. But the US gave waivers to eight countries - China, India, Turkey, South Korea, Japan, Greece, Italy and Taiwan - to avoid shortage on the oil market. The last three countries did not use their exemptions. So effectively the waivers allowed the remaining five countries to continue to buy some of its Iranian oil. By ending the waivers Iran is no longer allowed to trade/export oil in US dollars.

Iran crude production / exports

mb/d



Source: Bloomberg

Important data:

25 April	EIA Monthly Energy Review
14 May	OPEC Monthly Oil Market Report
15 May	IEA Oil Market Report
25-26 June	OPEC/non-OPEC meeting

How will China and India respond?

Officials from China and India reacted by saying that this measure is not helping the balance in international oil markets as it will trigger more volatility and increase geopolitical tensions. India indicated that it will stop buying oil from Iran and that will search for alternative supply. China firmly opposed the sanctions. Officially they might want to comply, however, in practice they may find a way around those sanctions. If we look at the previous time that Iran was sanctioned, oil exports and oil production towards countries like China and India continued. In fact, Iranian total oil production was only 400 kb/d lower than it is today (a low of 2.3 mb/d in September 2013 versus current production of 2.7

mb/d). Do note that the production is already curbed by the sanctions which started in November last year (production dropped already rapidly from 3.8 mb/d). Assuming that the Iranian oil production and accordingly the exports could return to a similar situation before the 2015 nuclear deal, there will still be some room for exports. Nevertheless, these exports should be done via non-US-linked financial institutions, via barter trade, or a rise in exports of oil products and/or electricity.

Iran reaction and the limited risk to the oil markets

Iran responded by rejecting the measures taken by the US and threatened that it may close the Strait of Hormuz. This scenario seems unlikely as it would hurt Iran probably even more than it would affect the US or Saudi Arabia. Also it would mean that Oman has to intervene as this would be an intervention in Oman territorial waters. This will unlikely be accepted by the GCC. Iranian officials also indicated that its oil sales will not drop below 1 mb/d. Current oil exports are 1.3 mb/d, which also shows limited risk to oil markets.

What we may see over the coming weeks is an official end to the nuclear deal. Although all the other countries involved (France, UK, China, Russia and Germany) were still in favour of the continuation of the nuclear deal, Iran may pull out now since they are effectively fully sanctioned. Therefore complying to the nuclear deal doesn't make sense. So unless the remaining participants of the deal will step up their support and compensate for it in line with the nuclear deal, it will likely be lifted. Besides this, we don't expect Iran to act in order to safeguard its remaining export facilities. We do expect a continuation of its strong and assertive verbal rejections of the US sanctions.

OPEC crude production



Source: Bloomberg

OPEC meeting in focus

On the 28th of June OPEC and its partners (OPEC+) will meet for its bi-annual meeting in Vienna. Initially, the meeting should have taken place at the end of March. But the meeting was postponed in order to await the Trump Administration reaction regarding the Iran sanctions. Now this decision is taken, the focus shifts towards OPEC+ again. Since the OPEC meeting is still two months ahead, it will create time for the OPEC members to see how the market will respond to this new reality. The question is not only by how much

the Iranian crude production and exports will decline, but also whether other OPEC members are capable and willing to fill the gap.

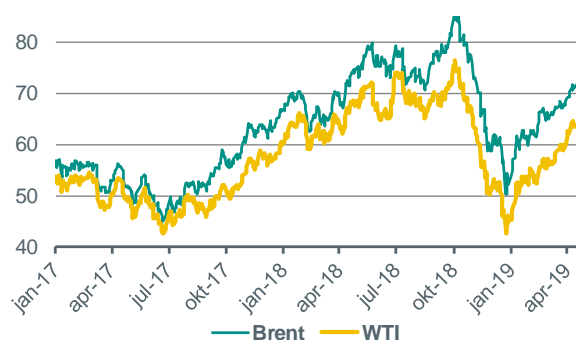
As some OPEC members like Libya and Venezuela are already facing difficulties to keep its production at current levels, this extra production should come mainly from Saudi Arabia. This seems a good strategy for Saudi Arabia as it will be able to maintain its market share without putting pressure on the price. However, at the upcoming OPEC meeting it will be an even bigger than normal challenge to keep all members on board in a) balancing global supply and demand as Iran will not simply accept its market share to be divided between other OPEC members, while b) all – or at least most – members should benefit as much as possible from the market positioning of OPEC.

Due to the global rise in oil demand – mainly driven by India and China – there was already room for a smaller production cut than the existing 1.2 mb/d production cut as we indicated in our previous Energy Monitor. We thought at that time that financial markets may not like such a decision. However, with Iran crude production and -exports under pressure the need for the production cut agreement diminished even more.

We have seen in recent months that the OPEC spare capacity recovered, suggesting that there is indeed room for more production. However, this spare capacity also includes the potential production from Venezuela, Libya and Iran. Capacity of which we know that it will not be brought into production in the near term and should thus not be accounted as spare capacity. Nevertheless, recent production data shows that Saudi Arabia is able to stretch production from the current 9.8 mb/d to levels above 11mb/d. The question remains how long they are able to sustain such a production rate per day while keeping an eye on the expected rise in domestic seasonal demand, and whether there is still room to increase production again in case of new calamities. We believe that there are no supply issues in the near term, but this does form a risk in the longer run.

Brent and WTI oil prices

USD/bbl



Source: Bloomberg

Oil prices: comfortable within the forecasted price range

Oil prices gained after the US announcement to end the waivers for Iran oil consumers. Brent reached the highest level in six months' time (> USD 75/bbl) and also WTI traded higher and reached levels above USD 66/bbl. The question is if there is much further

upside in prices. There are reasons for higher oil prices in the near-term. For a start, there are fears that the balance in the oil market will now turn into a supply shortage because of the US sanctions and production declines in Libya and Venezuela. Second, from a technical analysis point of view, the recent break above the 200-day moving average suggest that there is further upside potential for oil prices. Finally, there is enough room for market speculators to increase their bets on further price gains as the market is only marginally long compared to the positions seen in Q3 2018.

However, we think that oil prices are toppish around current levels. For a start, there is enough supply growth potential in for instance Saudi Arabia and Russia to meet the drop in Iranian oil supply. This will be at the expense of the spare capacity though. Moreover, slower economic growth could translate into lower oil demand. In addition, there is still a risk of a failure of the US/China trade talks which would be a negative driver (not our base view). China is however strongly opposing the US sanctions against Iran.

Even more importantly is the fact that US gasoline prices near the USD 3/gallon mark again. This is a psychological level at which US consumers tend to start complaining because prices of gasoline start to bite into the disposable income. Especially ahead of the US driving season (unofficially at Memorial Day, end of May), the risk is high that that US president Trump will increase the pressure on OPEC to lower oil prices again. In recent months, the oil market has often reacted strongly to such calls.

To sum up: Although there is some more room for further upside in oil prices in the very near term, we remain cautious and warn for possible price declines if the market a) decides to take profit on recent price gains, and b) start to price in higher production to cap oil prices (read US gasoline prices).

Our current (Brent) price forecasts contains a USD 60-80/bbl price range, with an 2019 average of USD 70/bbl. We remain confident with our price forecast as:

- Higher prices will trigger a vocal reaction by president Trump and action by OPEC+ to prevent a further jump in prices
- Prices below USD 60/bbl are not sustainable as it would directly cap the rise in US crude production

The key risks to the main scenario are:

- A shortage in investments in the heavy sour types of oil given that the rise in US light sweet oil will not fully make up for this. This could translate in higher oil prices in the long run.
- Another risk is still that the ongoing rise in US shale oil biting into OPEC – mainly Saudi Arabia – market share which could trigger a reaction. However, with Iran giving in market share at the benefit of Saudi Arabia, this risks seems to have declined somewhat for the moment..
- The US sanctions on Iran could jeopardise the possible trade-deal between the US and China. No trade deal could result in considerable price weakness in oil process because of change in overall investor sentiment.

Table 1: Oil and gas price forecasts ABN AMRO

End of period		25-apr	jun-19	sep-19	dec-19	mrt-20	jun-20	sep-20	dec-20	mrt-21	jun-21	sep-21	dec-21
Brent	USD/bbl	75,38	70	70	70	75	75	75	80	80	80	85	85
WTI	USD/bbl	66,15	60	60	60	65	65	65	65	70	70	70	75
Natural Gas (HH)	USD/mmBtu	2,47	3,25	3,00	4,00	3,25	3,00	3,25	3,75	3,25	3,00	3,00	3,50
TTF	EUR/MWh	14,45	18	20	24	26	21	23	26	28	23	24	26
Average		Q2 19	Q3 19	Q4 19	2019	Q1 20	Q2 20	Q3 20	Q4 20	2020	Q1 21	Q2 21	2021
Brent	USD/bbl	70	70	70	70	73	75	75	78	76	80	80	83
WTI	USD/bbl	60	60	60	60	63	65	65	65	65	68	70	71
Natural Gas (HH)	USD/mmBtu	3,75	3,25	3,50	3,50	3,75	3,25	3,25	3,50	3,25	3,50	3,25	3,25
TTF	EUR/MWh	18	19	22	20	25	24	22	25	24	27	26	25

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