



بنك الإمارات دبي الوطني
Emirates NBD

Commodities

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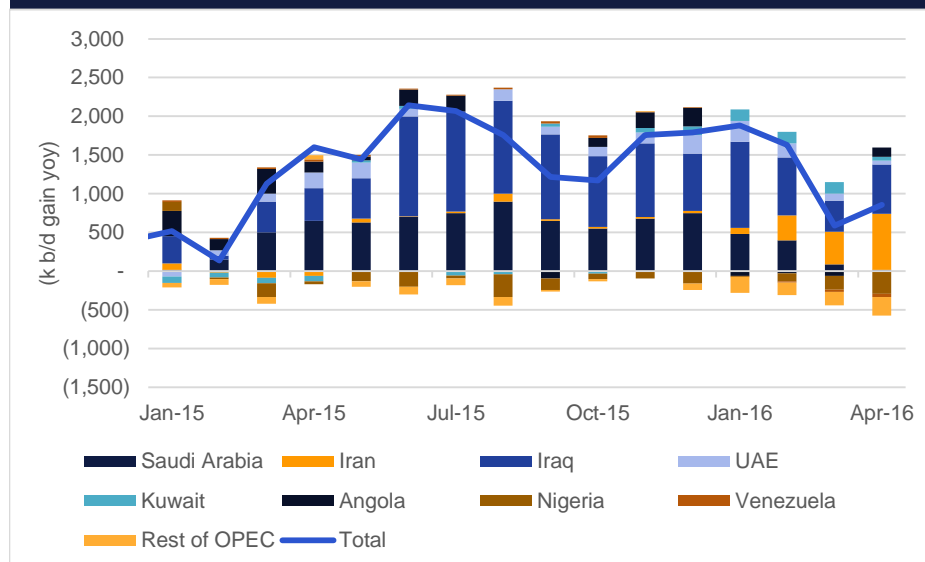
Crude oil update

OPEC meets amid potential for higher output

OPEC holds its semi-annual meeting on June 2nd with all the evidence that the strategy to target market share is working. Oil prices have recovered strongly from multi-year lows and are now hovering close to USD 50/b while production and investment plans across the oil and gas industry are in decline. Despite the improvement in market conditions and the pressure on some of OPEC's more strained economies we do not expect the producer's bloc to announce a change in policy in the form of a production cut or freeze. Rather, we anticipate that flows from OPEC producers will continue to move higher despite the risks that may pose to the sustainability of the oil rally.

Total OPEC production has increased substantially on year ago levels, up over 850k b/d as of the end of April. In the short-term, volumes from Saudi Arabia are likely to pick up on higher seasonal domestic demand for crude needed in power facilities. Elsewhere in the Gulf we expect volumes to gradually edge higher as the economies target higher output by the end of the decade.

Despite disruptions, OPEC output has pushed higher



Source: Bloomberg, Emirates NBD Research.

However, in terms of structural shifts to markets we are concerned that a significant amount of OPEC production could re-enter the markets over the next 18 months, threatening the potential for oil prices to rise much beyond current levels. We estimate, at a minimum, around 1.7m b/d of OPEC production is being held off markets owing to political/security disruptions. Nigeria, Libya and Iran represent the current major disruptions to OPEC supply. How quickly they can move closer to recent maximum production levels is country-specific and prone to some delay but we do not expect much more downward slippage.

Nigeria's production has fallen 229k b/d since the end of 2015 as militant attacks on oil infrastructure have forced oil companies to declare force majeure and interrupted cargoes. However, we do not view this as a permanent risk to Nigeria's production as the government takes a two track approach in dealing with militants: stepping up military activity in the affected region and extending dialogue (and potentially amnesties) to moderate militant figures as they have done in the past. There is no clear timeline for how quickly Nigeria's output could recover and in the short-term a major recovery in output looks off the cards. That said, extending attacks to offshore facilities and interrupting further supplies of Nigerian output may be beyond the reach of the militants.

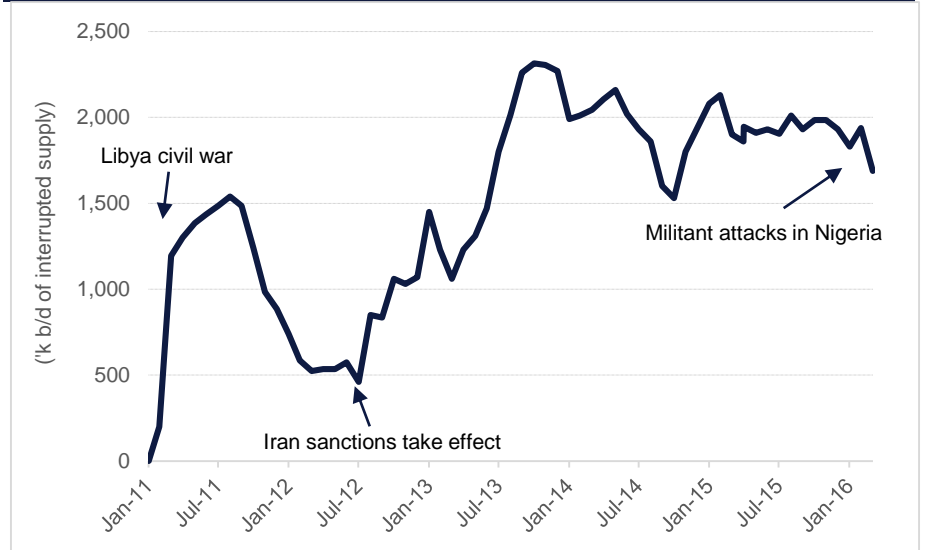
Libya's output present a major wild card in terms of contributions to OPEC supply growth. Current output of around 300k b/d is more than 1m b/d lower than Libya's pre-civil war levels but if the recovery timeline for Nigeria's production is unclear, Libya's outlook is even more opaque. Progress is being made on unifying oil policy at the least and exports of crude are now leaving the country, albeit at levels far below pre-civil war levels.

Edward Bell
Commodity Analyst
+971 4 230 7701
edwardpb@emiratesnbd.com

www.emiratesnbdresearch.com

Iran has quickly raised production as sanctions have been lifted, adding 700k b/d as of the end of April. The country is still somewhat short of its pre-sanctions level of around 3.8m b/d but the pace of its gains have been surprisingly strong. How much more Iran can add to markets without international oil company investment is unclear.

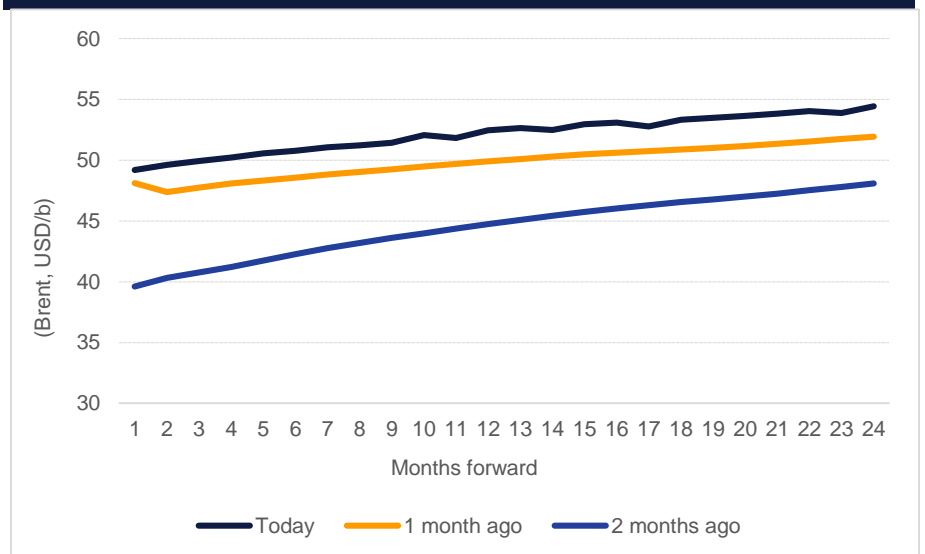
Potential for large volumes of OPEC oil to re-enter markets



Source: Bloomberg, Emirates NBD Research.

The potential for these volumes of OPEC oil to return to markets (along with a recovery in Canadian output) is keeping pressure on the back end of the Brent futures curve. The forward curve has flattened considerably from where it was ahead of the Doha meeting in mid-April and there has been active producer hedging in both Brent and WTI futures as the price rally will encourage some higher cost producers back into the market.

Oil markets not pricing in much more gains



Source: Bloomberg, Emirates NBD Research.

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Emirates NBD Research & Treasury Contact List

Emirates NBD Head Office
12th Floor
Baniyas Road, Deira
P.O.Box 777
Dubai

Aazar Ali Khwaja
Group Treasurer & EVP Global Markets &
Treasury
+971 4 609 3000
aazark@emiratesnbd.com

Tim Fox
Head of Research &
Chief Economist
+9714 230 7800
timothyf@emiratesnbd.com

Research

Khatija Haque
Head of MENA Research
+9714 230 7803
khatijah@emiratesnbd.com

Jean Paul Pigat
Senior Economist
+9714 230 7807
jeanp@emiratesnbd.com

Aditya Pugalia
Analyst
+9714 230 7802
adityap@emiratesnbd.com

Anita Yadav
Head of Fixed Income Research
+9714 230 7630
anitay@emiratesnbd.com

Athanasios Tsetsonis
Sector Economist
+9714 230 7629
athanasiost@emiratesnbd.com

Edward Bell
Commodity Analyst
+9714 230 7701
edwardpb@emiratesnbd.com

Mohammed Al-Tajir
Analyst
+9714 609 3005
mohammedtaj@emiratesnbd.com

Shady Shafer Elborno
Head of Macro Strategy
+9714 2012300
shadyb@emiratesnbd.com

Sales & Structuring

Group Head – Treasury Sales
Tariq Chaudhary
+971 4 230 7777
tariqmc@emiratesnbd.com

Saudi Arabia Sales
Numair Attiyah
+966 11 282 5656
numaira@emiratesnbd.com

Singapore Sales
Supriyakumar Sakhalkar
+65 65785 627
supriyakumars@emiratesnbd.com

London Sales
James Symington
+44 (0) 20 7838 2240
jamess@emiratesnbd.com

Egypt
Gary Boon
+20 22 726 5040
garyboon@emiratesnbd.com

Group Corporate Affairs

Ibrahim Sowaidan
+9714 609 4113
ibrahims@emiratesnbd.com

Claire Andrea
+9714 609 4143
clairea@emiratesnbd.com

Investor Relations

Patrick Clerkin
+9714 230 7805
patricke@emiratesnbd.com