40 Bank Street, Canary Wharf, London E14 5NR
E-mail: enquiries@lbc-energy.com

# Two weeks on from the OPEC Meeting on 22 June 2018

## In the wake of a potential US-China trade war


***Source: BBC News, Business Briefing, Friday, 22 June 2018 – BBC's interview with LBC Energy's Dana Novakovic ahead of the OPEC Meeting in Vienna***

HE Ahmed Zaki Yamani, Saudi Arabian Minister of Oil and Mineral Resources from 1962 to 1986, and a Minister in the Organization of the Petroleum Exporting Countries (OPEC) for 25 years, famously said "The Stone Age didn't end because we ran out of stones". This was said as far back as 1973, and OPEC's official decision two weeks ago echoes similar logic:

*"Recalling the 171st OPEC Conference resolution reached on 30 November 2016 for a production adjustment of 1.2 m b/d. Noting that OPEC Countries have exceeded the required level of conformity that had reached 152% in May 2018. Accordingly, the Conference hereby decided that countries will strive to adhere to the overall conformity level of OPEC-12, down to 100%, as of 1 July 2018 for the remaining duration of the above-mentioned resolution and for the JMMC to monitor and report back to the President... The Conference also acknowledged the crucial role played by participating non-OPEC nations in the 'Declaration of Cooperation', and stressed the importance of the 4th OPEC and non-OPEC Ministerial Meeting to take place tomorrow (23.06.18) at the OPEC Secretariat."*

However wise, the 1973 logic no longer suffices. In LBC Energy's interview given to BBC's Business Briefing in the morning of 22 June, we correctly predicted that OPEC+ meetings, "*will result in a modest and gradual reversal of the 2016 cuts*", but only as a prelude for far more exciting developments to unfold during the second half of 2018 and into 2019. Two weeks on, we are facing strong reactions from oil producers and buyers alike, and a potential US-China trade war, started at 12:01 on Friday, 6 July, when USA imposed tariffs on $34 billion worth of Chinese goods.

40 Bank Street, Canary Wharf, London E14 5NR
E-mail: enquiries@lbc-energy.com

Shortly after our interview in the morning of 22 June, President Donald Trump tweeted: *"Hope OPEC will increase output substantially. Need to keep prices down!"* - 7:10 am, 22 Jun 2018

Indeed, last week Riyadh briefed energy analysts that the Kingdom's domestic output could be increased from nearly 10 million b/d in May to 10.6 million b/d in July and hit record levels of about 12 million b/d later this year, far higher than agreed at the OPEC meeting last month. Quite a few more tweets followed.

*The OPEC+ meeting held in Vienna on Saturday, 23 June 2018, under the Co-Chairmanship of OPEC's President, HE Suhail Mohamed Al Mazrouei, Minister of Energy & Industry of the UAE and Head of its Delegation, and HE Alexander Novak, Minister of Energy of the Russian Federation, decided:*

*"Recalling the 171st OPEC Conference Resolution reached on 30 November 2016 for a production adjustment of 1.2 million barrels a day (mb/d) for OPEC Member Countries, with the understanding reached with key non-OPEC participating countries, including The Russian Federation, to contribute a production adjustment of 0.6 m b/d.*

*Recalling the DOC reached on 10 December 2016; and noting that countries participating in the DOC have exceeded the required level of conformity that had reached 147% in May 2018.*

*Accordingly, the 4th OPEC and non-OPEC Ministerial Meeting hereby decided that countries will strive to adhere to the overall conformity level, voluntarily adjusted to 100%, as of 1 July 2018 for the remaining duration of the DOC and for the JMMC to monitor the overall conformity level and report back to the OPEC and non-OPEC Ministerial Meeting."*

Saudi Arabia has the world's largest spare capacity of ca. 2 million b/d. Amin Nasser, CEO of Saudi Aramco, stated that the company could increase production to 12 million b/d by the end of 2018.


*Source: BBC News, Business Briefing, Friday, 22 June 2018*

*Our view on any oil price movements in reaction to the oil production increase decided in the OPEC meeting itself remains conservative in July. On a purely technical level, Saudi Aramco's expected increase in production is offset by oil production decline in Iraq, Libya, Mexico, Angola, and, especially, Venezuela - a cumulative decline of ca. 2.8 million b/d in less than 6 months.*

40 Bank Street, Canary Wharf, London E14 5NR
E-mail: enquiries@lbc-energy.com

Nonetheless, whilst technical factors will merit a balanced view on oil prices in July, geo-political uncertainties will lead to more pronounced and exacerbated oil price volatility for the rest of 2018.

US sanctions on Iran call on buyers to discontinue purchases from Iran of ca. 2.5 million b/d by 4 November 2018, two days before the US mid-term elections to be held on 6 November 2018. A 2.5 million b/d cut in oil supply should give a marked rise to oil prices before the US mid-term elections in November.


*Source: BBC News, Business Briefing, Friday, 22 June 2018*

However, any cuts in Iranian production can be quickly replaced by production from Kuwait and Saudi Arabia. Furthermore, the impact of sanctions on Iran may be muted, as Iranian production numbers tend to be opaque and potentially larger than reported. Iran may also seek to barter crude oil for goods, as it did in the previous round of sanctions between 2012 and 2016. The matter of Chine imports from Iran remains an open question, too, in particular in the light of the weakening Yuan versus USD, making oil more expensive for Chinese importers. In Yuan terms, Brent price increased by 20% in the past three months, while the Chinese diesel prices increased by only 12%.


*Source: BBC News, Business Briefing, Friday, 22 June 2018*

Production cuts by Iran due to US sanctions leave room for Saudi Arabia to increase proprietary production at a minimal impact on the oil price ahead of the US mid-term elections, with ca. $70-80/bbl sufficient to achieve $1.5 trillion in valuation for Saudi Aramco's IPO at elevated production levels.

40 Bank Street, Canary Wharf, London E14 5NR
E-mail: enquiries@lbc-energy.com

The two supposed conceptual conflicts at play: 1) the US electorate's wish for a low oil price at oil pumps, versus Saudi Aramco's need for a higher oil price ahead of the IPO, and 2) Saudi Arabia alone wishing both a high price and high production for the IPO at the same time - are mitigated and alleviated by the interplay between technical factors and geo-political tools.

Ergo, our final conclusion in the morning ahead of the OPEC meeting remains. Beyond the technical decline in oil production in countries such as Iraq, Libya, Angola and Venezuela on the supply side, and IMF's forecast 3.9 % in global GDP growth this year on the demand side, there remain at least three key spheres to unfold and observe over the next 6-12 months:

**- Will Chinese participation in Saudi Aramco's planned IPO help sway the Saudi towards accepting Yuan, used in only ca. 2% of global payments?**
**- Could paying in Yuan for oil become part of President Xi Jinping's "One Belt, One Road" initiative across Eurasia, including the Middle East?**
**- Will US Strategic Petroleum Reserve have to be used? Or, will Saudi Aramco increase production to aid US mid-term elections, before focusing on its desired valuation at the IPO?**

Beyond the price of oil, will China-US trade actions started on Friday, 6 July, exactly two weeks on following the OPEC meeting in Vienna on 22 June 2018, escalate to an actual trade war? Will it carry a major risk of lower investment, depressed spending, unsettled financial markets and slower global economy – to result in a potentially significant effect on oil prices, as well?

**For an expanded report containing answers to the above questions please contact:**

**emily.wong@lbc-energy.com**
LBC Energy Advisory Limited
40 Bank Street
Canary Wharf
London E14 5NR
Telephone: +44 20 7164 6127
Facsimile: +44 20 8043 1636
**www.lbc-energy.com**