

# GLOBAL ECONOMY AND FINANCIAL MARKETS SHORT COMMENTARY



6 August, 2021

## **OPEC+ agree on oil production increase, easing pressure on supplies and prices**

OPEC and its allies had reached a deal on 18 July targeted to increase oil production, the meeting noted that worldwide oil demand showed “clear signs of improvement and OECD stocks falling, as the economic recovery continued in most parts of the world with the help of accelerating vaccination programmes.”

United Arab Emirates had demanded that increasing its own baseline for crude production, which is the maximum volume recognized by OPEC as being able to produce. The baseline determines the size of production cuts and quotas that each country must follow as per the group’s agreed output. Members cut the same percentage from their baseline, a higher baseline means a lower actual cut and a better production quota.

### **The new agreement**

- OPEC originally coordinated to increase the oil supply starting from July but United Arab Emirates rejected the coordinated oil production plan. On the 19<sup>th</sup> July meeting, OPEC+ had made the compromise on the production plan and agreed to adjust upward their oil production every month starting from August 2021 and eventually to phase out the current 5.8 million barrels per day (bpd) of oil production cuts by September 2022.
- The UAE’s baseline for oil production will be raised from 3.16 million bpd to 3.5 million bpd, though short of the 3.8 million it initially requested. In other words, UAE’s production will be increased by 330 thousand bpd.
- OPEC+ agreed new output quotas for several members from May 2022, including the UAE, Saudi Arabia, Russia, Kuwait and Iraq. Saudi and Russia will see their baselines rise to 11.5 million bpd each from the current 11 million. Iraq and Kuwait will see their baselines rise by 150 thousand bpd each.

## Looking forward

The International Energy Agency estimates a 1.5 million bpd shortfall in the second half of this year, indicating a tight market despite OPEC gradually boost supply. By increasing the oil supply by 400 thousand bpd every month starting from Aug 2021, this will add about 2% to the global supply by the end of the year as OPEC+ accounted for around 40% of the world's crude oil supply.

Oil prices have been volatile over the last two weeks while OPEC+ remained in a dispute over adding supplies to the market.



Source: Bloomberg

## Challenges

1. However, the agreement followed by an unprecedented gridlock. Countries around the world are dealing with surges in new cases as the delta variant are high contagious which drove up the infection, for example in Indonesia, the daily cases have surpassed India and Brazil. While the U.K. reported the daily cases reached the highest since January. The spread of the delta variant is stoking a risk-off mood in broader markets and threatening oil demand with fresh mobility restrictions around the world, which slow down the economic activity and postpone the further rebound in oil demand.

The world's two biggest oil consumers, The United States and China, are grappling with rapidly spreading outbreaks of the highly contagious Delta variant that analysts fear will limit fuel demand at a time when it traditionally rises in both countries. Seasonal weakness in economic activity and rising cases of Delta variant continue to weigh on sentiment.

International benchmark Brent crude is up 43% YTD, with many market watchers expected oil trading at \$80 a barrel in the second half of 2021.

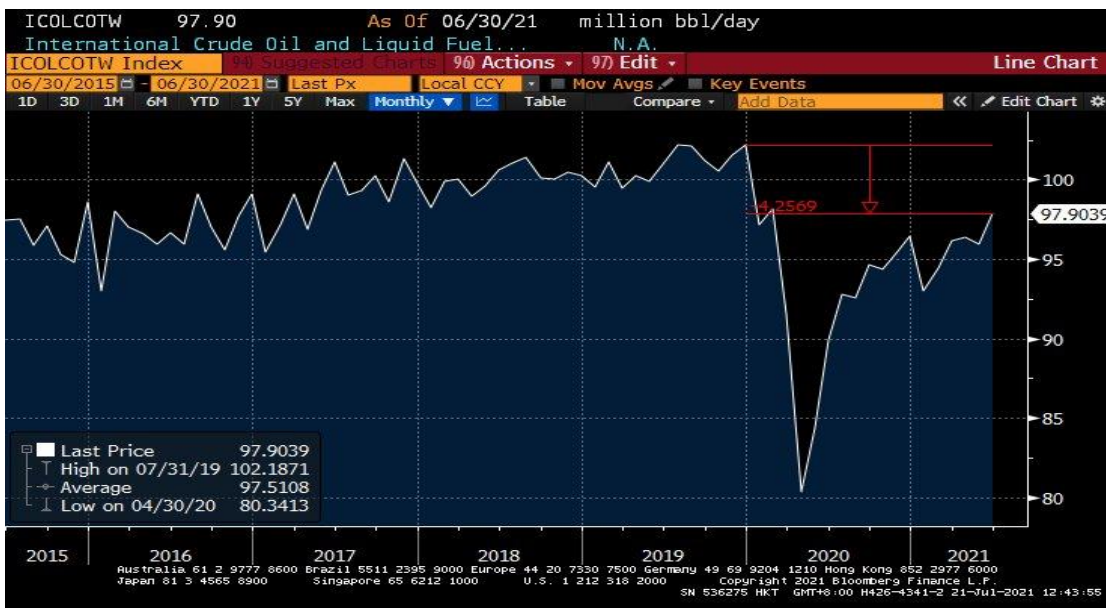


Source: Bloomberg

2. Another concern for is if OPEC+ can remain solid in terms of sacrificing its own benefits but for the group’s best interest. The organization is facing the problem that is not able to reach consensus under difficult circumstances. The dispute with the UAE could be the harbinger of changes that may create rifts between the different members of the group. Each country wants a higher baseline to protect its own interest, therefore apart from UAE, other members are also very likely to request increasing their production baseline.

U.S. oil prices fell for 7.5% on 19 July on mounting concerns that the increasing spread of the Delta variant in top consuming countries will jeopardize the fuel demand recovery.

### Global oil consumption (million barrels per day)



Source: Bloomberg

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