Energy Monitor September

Hoping for better days

Group Economics
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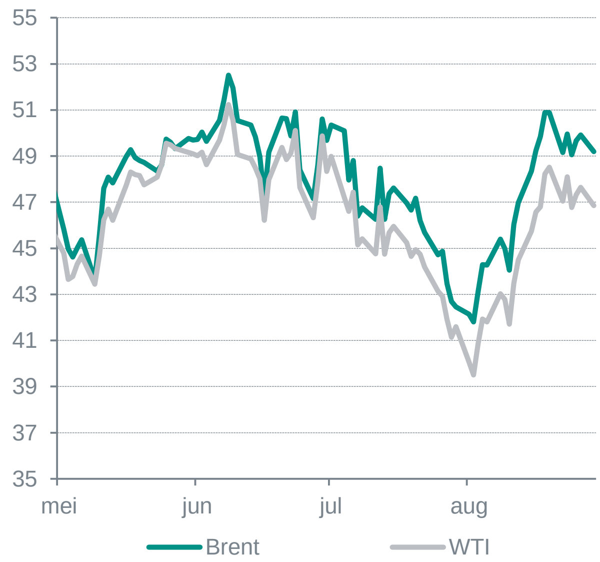
2 September 2016

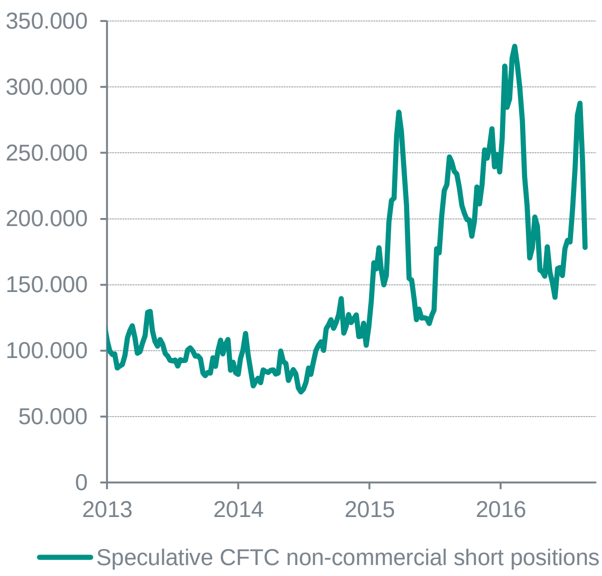
- **Verbal intervention lifts oil price, but genuine action looks a long way off**
- **Speculative positions are main price driver**
- **Gas price falling now that winter stockpiling looks less problematic**

Figure 1: Oil price recovered (x USD/bbl)



Source: Thomson Reuters

Figure 2: Saudi Arabia talks down speculative short positions (x number of contracts)



Source: Thomson Reuters

OPEC talks up oil price

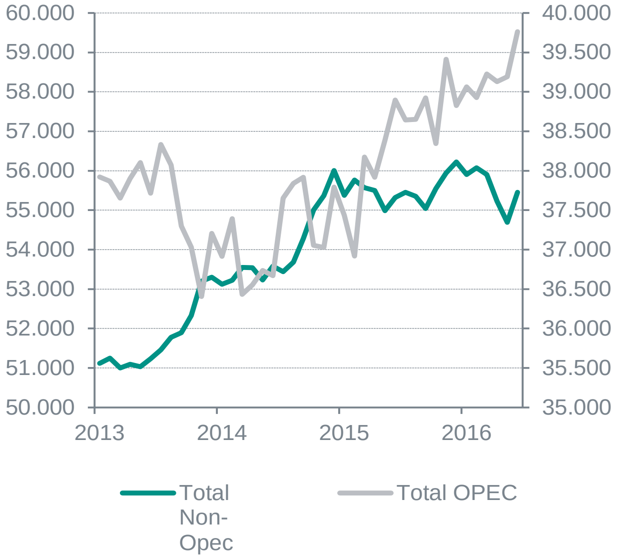
In early August, Brent oil slid back towards USD 40/barrel due to the market's strong focus on oversupply, both in production as well as in crude oil and refined product stocks. Speculation on a further price slump put extra pressure on the oil price. Nevertheless, prices did not fall further during the slacker summer period and the market looked set for a quiet final summer month. Nothing was further from the truth. The Saudi oil minister Khalid al-Fatih announced on 11 August that the OPEC would discuss the market situation together with several non-OPEC members at the next OPEC meeting in Algeria on 26-28 September. He also said that the options for any actions required to stabilise prices would be entirely open at the meeting. One day later came a report from Russia that the country would support a possible freeze in production increases. Finally, the momentum of news was maintained when Iran announced its intention to attend the meeting in Algeria. Iran added, however, that it was prepared to help other oil producers stabilise the global crude market provided that its fellow OPEC members recognised their right to restore their lost market share. In other words: Iran will turn up but will not agree to freeze production growth.

As in January, the speculative short positions had risen sharply since the beginning of June and were well on their way to reaching new record levels. The Saudi oil minister's verbal intervention was an indirect but unequivocal signal to hedge funds that further speculation on falling prices would not be appreciated. And this signal was received loud and clear. Positions were partly closed out and the oil price found fresh support. Brent oil rebounded to USD 51/barrel, while WTI stopped just short of USD 49/barrel, where the recovery stalled due to profit-taking and a shift in market focus. The reason was that, one week into the revival, traders suddenly realised that prices over USD 50/barrel could boost (shale) production in the US. And this, in turn, would keep the oversupply intact. Although we do not see US output accelerating as quickly as the market fears, this was perceived as sufficient reason to call the price recovery to a halt.

All eyes on the meeting in late September

The market is now oscillating between two possibilities: oversupply and disappointing demand on the one hand and a freeze in production growth on the other. Accordingly, increased volatility is a near certainty in the weeks leading up to the end of September. The focus surrounding the weekly publication of the US inventory data (API on Tuesdays and EIA on Wednesdays) is invariably on oversupply. Usually, a confirmation of higher-than-expected inventories puts more pressure on the oil price. When inventories decrease, the data have less impact on the oil price. At the moment, comments and speeches of oil ministers who will attend

Figure 3: Development crude production OPEC vs Non-OPEC (x kb/d)



Source: Energy Intelligence

Figure 4: TTF price dropped, while US Henry Hub remained stable (TTF x EUR/MWh, HH in USD/mmBtu)

Source: Thomson Reuters

Table 1: Oil and gas price forecasts ABN AMRO (oil prices in USD/barrel, HH in USD/mmBtu, TTF in EUR/MWh)

Price	Q3 2016	Q4 2016	Q1 2017	2016*	2017*
Brent	50	65	65	50	70
WTI	50	65	65	50	65
HH **	2,25	2,25	2,50	2,10	2,60
TTF ***	14,00	14,00	13,00	13,50	12,75

Source: ABN AMRO Group Economics

* Annual average ** Henry Hub *** Title Transfer Facility

the meeting in Algeria are also being scrutinised to see whether they can provide some direction to the expectations. The likeliest scenario, however, is that there will be no freeze in production growth whatsoever. The market, after all, is already moving towards a better supply-demand balance as a result of the verbal intervention. In addition, such a decision would be in direct contrast to the OPEC's actions so far. Regaining market share was the primary objective. And increasing the oil price by simultaneously reducing production could actually have a detrimental impact on OPEC's market share. A likelier outcome is that the oil-producing countries will continue monitoring the market closely for the time being, but will consider it too early to freeze production growth at this stage. If necessary, they can still agree on production restrictions at the official OPEC meeting on 30 November in Vienna.

Oil price neutral to positive

The oil price will remain volatile over the coming weeks. We do not expect the market to settle on a clear direction. Our projection for the end of the third quarter remains USD 50/barrel for both Brent and WTI. We see more upward potential for oil prices in the fourth quarter and 2017. Sustained growth in demand for oil (albeit lower than previously assumed) combined with stagnating global production (notably non-OPEC and non-shale oil) will lead to a better supply-demand balance. The first clear signal appeared last week when a report suggested that 2015 oil discoveries dropped to a 70-year low. This suggests that the risk of a supply shortfall clearly increased. Any anticipation in the market of a structural decrease in the current oversupply – or even a shortfall – will provide support for the oil price. It is impossible to provide an exact timeline, but we do expect the oil price to rise towards USD 65-75/barrel by 2017.

Gas prices are cooling, TTF down by 30%

Gas prices soared in the second quarter, mainly because of a gas storage problem in the United Kingdom. An outage at the *Rough* gas storage facility led to the loss of 70% of the storage capacity, raising the threat of shortages during the coming winter season. However, when it transpired in early August that, as from November, the gas storage capacity would probably be greater than previously expected – 20 of the 30 storage units – prices rapidly fell again. The price of Transfer Title Facility (TTF) plunged by about 30%. At the same time, demand for gas is expected to pick up. LNG supply to Europe is projected to rise now that demand from the Middle East and North-East Asia is set to slow as the cooling season (high demand for electricity for air conditioners) draws to a close. Uncertainty about the gas stocks for the coming winter could cause heightened gas price volatility. The recent strong price fall has gone a little too far in our view, so a recovery of the TTF gas price looks like a plausible scenario to us. Almost the reverse applies in the US, where the price of Henry Hub gas remains high (> USD 2.80/mmBtu). We expect demand for gas to slacken as soon as temperatures fall, probably leading to more price pressure in the fourth quarter.

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