

# UAE to more than double LNG export capacity with Fujairah plant



Bloomberg / Dubai

Abu Dhabi National Oil Co plans to build a new liquefied natural gas plant as the world's producers race to expand their exports amid surging demand.

The LNG facility, to be built at Fujairah on the United Arab Emirates' coast outside the Arabian Gulf, will be able to produce as much as 9.6mn tonnes a year. The UAE currently has three liquefaction trains with a combined capacity of 5.8 mtpa at Das Island, which is located inside the Gulf.

Adnoc has appointed McDermott International Ltd as design contractor and intends to award a contract for the construction of the plant in 2023, said the oil company in a statement on its LinkedIn page. The plant will use new technologies and "clean power" to reduce the carbon intensity of the LNG it produces, according to the statement.

Appetite for LNG among energy consumers has grown since

Russia's invasion of Ukraine, particularly in Europe, reinforcing a global market for the fuel that was already strengthened by rising demand in Asia last winter. While prices have eased slightly over the past month "higher prices and more volatility" are expected because of Europe's switch to LNG, Biraj Borkhataria, associate director of European research at RBC Europe Limited, said in a note.

A pipeline will be constructed linking Abu Dhabi's Habshan gas production facilities to Fujairah and the liquefaction plant is scheduled to start in 2027, according to two people familiar with the matter. A spokesperson for the company declined to comment on the matter.

A government official previously said the UAE was considering building an LNG plant at Fujairah to facilitate the extra exports and state producer Adnoc last month agreed to buy two LNG carriers from a Chinese shipyard.

The UAE was the world's 12th-largest LNG producer last year, making it a relatively small global player. However, a \$20bn push to develop more of its natural gas resources means it will be able to produce much more from about 2025 and the country aims to become self-sufficient by 2030.

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## **Saudi expects 13mn bpd oil capacity by 2027: Minister**



Saudi Arabia expects to ramp up its daily oil production capacity by more than 1mn barrels to exceed 13mn barrels by early 2027, the kingdom's energy minister announced Monday.

"Most likely it will be 13.2 to 13.4 (million barrels per day), but that would be (reached) at the end of 2026, beginning 2027," Prince Abdulaziz bin Salman told an energy conference in Bahrain.

Production at that level would be maintained "if the market allows it", he said.

Energy giant Saudi Aramco announced in March 2020 it had been directed by the energy ministry to increase its maximum sustainable capacity from 12mn bpd to 13mn bpd.

No timeline was given then for the new target.

Monday's announcement came one day after Saudi energy giant Aramco posted an 82% jump in first quarter profits, buoyed by a global surge in oil prices stemming from the Ukraine war.

Those results helped Aramco dethrone Apple last week as the world's most valuable company by market capitalisation.

They continued a string of positive economic news for Saudi Arabia, which in early May reported that growth in the first quarter had risen 9.6% over the same period in 2021.

Yet Aramco has faced security challenges stemming from the war pitting a Saudi-led military coalition against Yemen's Houthi

rebels who have repeatedly targeted the kingdom, including Aramco sites.

Saudi Arabia, the world's biggest oil exporter, has resisted US entreaties to raise output in an attempt to rein in prices that have spiked since the Ukraine war broke out on February 24.

As the war got underway, Saudi Arabia and the United Arab Emirates stressed their commitment to the Opec+ oil alliance, which Riyadh and Moscow lead.

Last year, ahead of the COP26 climate-change summit, Saudi Arabia pledged to achieve net zero carbon emissions by 2060, sparking scepticism from environmental campaign group Greenpeace.

With increasing global urgency to limit global warming, experts warn of the urgent need to reduce fossil fuel use.

But Saudi officials' stated targets indicate "they still believe in oil as a source of energy for the coming decade", Mazen Alsudairi, head of research for Al Rajhi Capital, a financial services firm in Riyadh, told AFP. "They are not following the global trend by reducing exposure to hydrocarbons."

Also at Monday's conference in Bahrain, Iraqi Oil Minister Ihsan Abdul-Jabbar Ismail said his country was accelerating its production capacity goals, targeting 6mn bpd in 2027 and 8mn bpd in 2029.

Iraq's current daily production is just under 3.5mn.

It reported \$11bn in oil revenues in March, Iraq's highest in half a century.

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## **Record fuel costs driven by**

# refining crunch, says Saudi energy minister



Bloomberg / Riyadh

Saudi Arabia's top oil official said that a refining crunch – rather than any shortage of crude – is driving the surge in fuel costs to unprecedented levels.

“The bottleneck has now to do with refining,” Saudi Energy Minister Prince Abdulaziz bin Salman said in an interview. “I did warn this was coming back in October. Many refineries in the world, especially in Europe and the US, have closed over the last few years. The world is running out of energy capacity at all levels.”

The processing crunch – previously outlined by the Prince at the CERAWEEK conference in India last October – is buoying prices above \$100 a barrel even as markets are well-supplied with crude, he added.

Tumult across fuel markets is widely evident. Gasoline futures climbed to a record of 389.98 cents a gallon on Friday, with prices at the pump already at unprecedented levels, while diesel still commands a premium after spiking in recent

months. The surge is compounding inflationary pressures that threaten the economy recovery and worsening the cost-of-living crisis suffered by consumers. Nonetheless, the Organisation of Petroleum Exporting Countries (Opec) and its partners has stuck to schedule of modest supply increases, rubber-stamping another small increment last week, even as flows from coalition member Russia are disrupted by an international boycott.

Their intransigence has caught the attention of US lawmakers. Last week, the Senate Judiciary Committee approved legislation known as NOPEC that, if passed, would subject the group to antitrust laws. The bill has been introduced several times in previous years but never made it into law.

Yet Riyadh and its allies remain adamant that the market still isn't facing a deficit of crude barrels. United Arab Emirates Energy Minister Suhail al-Mazrouei expressed similar views at a conference on Wednesday, saying that high taxes in consuming nations are responsible for surging costs.

Their perspective is gaining support elsewhere.

The International Energy Agency – which advises consuming nations and has called on Opec+ to raise production faster – shifted its focus to products markets in a report on Thursday. While an “acute supply deficit” of oil isn't on the horizon, consumers do face more strain from limited fuel supplies. The lack of refining capacity is being aggravated by the disruption in flows from Russia, which used to send significant quantities of diesel fuel to Europe, the IEA said. Shipments of diesel-type fuel out of Russia's Baltic and Black sea ports were about half-a-million tonnes, or 14%, lower last month than in February, according to data from Vortexa Ltd.

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# Gasoline, diesel, jet fuel refining capacity too low in US to meet demand



Bloomberg / New York

From record gasoline prices to higher airfares to fears of diesel rationing ahead, America's runaway energy market is disquieting both US travellers and the wider economy. But the chief driver isn't high crude prices or even the rebound in demand: It's simply too few refineries turning oil into usable fuels.

More than 1mn barrels a day of the country's oil refining capacity – or about 5% overall – has shut since the beginning of the pandemic. Elsewhere in the world, capacity has shrunk by 2.13mn additional barrels a day, energy consultancy Turner, Mason & Co estimates. And with no plans to bring new US plants online, even though refiners are reaping record profits, the

supply squeeze is only going to get worse.

"We are on the razor's edge," said John Auers, executive vice president at Turner, Mason & Co in Dallas. "We're ripe for a potential supply crisis."

The dearth of refining capacity has dire implications for both US consumers and global markets. At home, retail gasoline prices continue hitting new records, exacerbating some of the worst inflation American households have ever seen.

Meanwhile, the East Coast is on the brink of a diesel shortage that risks crippling already strained supply chains that have disrupted the flow of everything from grocery staples to construction supplies in the last two years. The factors fuelling the refining shortage won't surprise anyone: With demand for gasoline and jet fuel practically vanishing during the height of the pandemic, companies closed some of their least profitable crude-processing plants permanently.

Some of those plants had been affected by fires, explosions and hurricanes and were just too expensive to fix, especially because an eventual transition toward cleaner energy makes their long-term business model unprofitable and makes them less likely to attract buyers. By the end of 2023, as much as 1.69mn barrels of US capacity is targeted for closure compared to 2019 levels, according to Turner, Mason & Co.

At the same time American refining shrinks, the war in Ukraine has made the global divergence between supply and demand even more acute. With many countries shunning Russian fuel exports in the wake of the war, the US is now supplying more of the world's fuel with an ever-shrinking fleet of plants. Europe has been seeking alternatives to Russian diesel since the war began, while fuel demand in Latin America, the largest buyer of US refined products, is strong and growing. Meanwhile, the US is itself gearing up for a spike in consumption this summer.

That's setting up refiners to reap record profits this year. Valero Energy Corp is seen generating the most cash from operations since its stock started trading in 1997, while top refiner Marathon Petroleum Corp. is expected to post its



highest margins in a decade. The two companies are the second and 10th best performers, respectively, in the S&P 500 index this year as of Friday morning.

Retail prices for both gasoline and diesel climbed to fresh records of \$4.432 and \$5.56 a gallon respectively, AAA data showed on Friday. US gasoline futures also rose to a new high. In other kinds of markets, a surge of demand and shortage of supply would trigger more investment, especially with such swelling cash hordes. But the longer-term transition away from fossil fuels dims the outlook for demand, making companies unwilling to put up the billions of dollars needed to build new plants.

Even resurrecting idled plants can be prohibitively costly at a time when construction and labour costs in the US are booming. With California unveiling this week a roadmap to slash oil use by 91% from 2022 levels by 2045 and other places moving to limit fossil-fuel use in the decades ahead, refining companies and their investors can see the writing on the wall. "Nothing about the current environment is promoting investments in fossil fuels," said Bloomberg Intelligence analyst Fernando Valle. "It's a 15 to 20 year payback on most of these investments."

Phillips 66, for example, would have to spend more than \$1bn to restart its Alliance refinery in Louisiana that was shut after damage from Hurricane Ida, Bloomberg Intelligence estimates. LyondellBasell Industries NV has opted to shut its Houston Refinery no later than the end of 2023 over cost concerns related to keeping the 104-year-old facility running. A portion of shuttered plants are now being converted into smaller renewable-diesel facilities, including Phillips 66's refinery in Rodeo, California, which was confirmed this week. As for selling those assets to someone who could ramp up production, no one's buying – even as industry players are sitting on massive piles of cash. "We feel we've got higher returns, better uses for the capital to employ than buying a refinery that's on the market at this point in time," Valero chief executive officer Joe Gorder said in a conference call

with analysts in late April.

To be sure, there could be some small-scale relief ahead. US refiners ran at 90% last week, and that percentage will increase as seasonal maintenance wraps up this month. Some units can then even run 10% or 20% beyond their nameplate capacity to maximise production in the short term.

But that's a rate that can't be sustained without risking damage. A few refineries are also focusing on debottlenecking or even adding new units inside existing facilities to boost capacity, though it's a drop in the bucket volumewise compared to the total already lost – and it won't come until 2023 or 2024. In short, “too much refining capacity was closed during the pandemic,” Bloomberg Intelligence's Valle said. “Diesel shortages and the price surge are likely here to stay.”

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## **U.S. diesel shortages lift refining margins to a record**



LONDON, May 10 (Reuters) – Global stocks of refined petroleum products have fallen to critically low levels as refineries prove unable to keep up with surging demand especially for the diesel-like fuels used in manufacturing and freight transportation.

The result has been a surge in prices refiners receive for selling fuels compared with prices they pay for buying crude and other feedstocks, boosting their profitability significantly.

In the United States, refiners currently receive roughly an average of more than \$150 per barrel from the sale of gasoline and diesel at wholesale prices, while paying only around \$100 to purchase crude.

The indicative 3-2-1 margin of \$50 per barrel is based on the assumption a refinery produces two barrels of gasoline and one barrel of diesel from refining three barrels of crude.

The margin is meant to be representative for an “average”

refinery and is a gross figure out of which refiners have to pay for labour, electricity, gas, hydrogen, catalysts, pipeline transport and the cost of capital.

Net margins are narrower and refinery costs have been rising rapidly as result of widespread inflation ripping through the economy following the coronavirus pandemic.

Nonetheless, even allowing for rising input costs, gross margins have more than doubled from \$20 at the end of 2021, ensuring refiners have a strong financial incentive to maximise crude processing and fuel production.

## **DISTILLATE FOCUS**

Gross margins are currently higher for making diesel (almost \$60 per barrel) than for gasoline (\$45 per barrel) reflecting the relative shortage of middle distillates.

(Chartbook: <https://tmsnrt.rs/3PdSJdC>)

U.S. distillate fuel oil stocks are 31 million barrels (23%) below the pre-pandemic five-year average compared with a deficit of only 6 million barrels (3%) in gasoline.

The squeeze on fuel inventories and refinery capacity is compounding already high prices for crude caused by sanctions on Russia and output restraint by OPEC+ and U.S. shale producers.

The resumption of international passenger aviation as quarantine restrictions are lifted is tightening the fuel market even further because jet fuel is broadly similar to diesel and gas oil.

The effective wholesale price of diesel has climbed to over \$160 per barrel while gasoline is trading at over \$150, based on futures for delivery in New York Harbor.

Once distributors' and retailers' margins and taxes are included, the average price at the pump paid by motorists has climbed to \$236 per barrel for diesel and \$186 per barrel for gasoline.

The refining margins and fuel prices cited in this column are all for the United States but the same shortage of refining capacity and fuel inventories is boosting diesel prices in Europe, and dragging up gasoline prices with them.

## **SLOWDOWN AHEAD**

There is scope for refiners to increase fuel production by postponing non-essential maintenance and running refineries flat out into the early autumn.

And some room to adjust the output mix by switching from maximum gasoline to maximum diesel mode in downstream processing units.

But any increase in diesel production is unlikely to be able to reverse the depletion of inventories fully and return them to pre-pandemic levels.

Prices will therefore have to continue rising until they begin to restrain consumption or the economy enters a cyclical downturn.

Consumers can reduce fuel use in the short term by consolidating freight loads (fewer voyages, flights and deliveries), reducing speeds (slower voyaging, flying and driving) and eliminating engine idling.

But the fuel savings are relatively modest and tend to degrade service levels, reduce capacity and increase capital costs.

By contrast, a slowdown in the business cycle delivers large simultaneous reductions in diesel use – absolutely or relative to trend – by freight firms, manufacturers, miners and

construction firms.

Business cycle slowdowns have therefore tended to be the main path by which the distillate market and other fuel markets have rebalanced in the past.

The adjustment process is probably underway in 2022. The cyclical slowdown and reduced fuel demand could occur in one, two or all three of the major consuming regions.

Parts of China's economy appear to be in recession already as coronavirus lockdowns paralyse factories and transport systems and depress consumer spending.

Europe's economy is on the verge of recession as Russia's invasion of Ukraine, the sanctions imposed in response, soaring energy prices and rampant inflation disrupt manufacturing and depress household spending.

The only major economy with significant momentum is the United States, but there, too, the rate of expansion is slowing, which will likely result in slower growth in distillate consumption later in the year.

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## **Big Oil Spends on Investors, Not Output, Prolonging Crude Crunch**



*By  
Kevin Crowley and Laura Hurst*

May 7, 2022, 10:30 AM GMT+3

Big Oil is raking in historic amounts of cash, but the windfall isn't being invested in new production to help displace Russian oil and gas. Instead, executives are rewarding shareholders – setting the world up for an even tighter energy market in the years ahead.

The West's five biggest oil companies together earned \$36.6 billion over and above their spending in the first quarter, or about \$400 million in spare cash a day. It was the second-highest quarterly free cash flow on record and enough to relegate billions of dollars of Russia-related writedowns to mere footnotes in their recent earnings reports.

Oil booms typically spark a chase for higher production – but not this time. All five supermajors have kept their capital expenditure budgets firmly in check and pledged that this discipline will hold in future years – even as oil prices have

closed above \$100 a barrel on all but five days since Russia invaded Ukraine in February. With wells naturally declining in production every year and large projects taking half a decade or more to come online, any expansion lag happening now will push the possibility of new production even further into the future.

“In prior cycles of high oil prices, the majors would be investing heavily in long-cycle deepwater projects that wouldn’t see production for many years,” said Noah Barrett, lead energy analyst at Janus Henderson, which manages \$361 billion. “Those type of projects are just off the table right now.”

In short, if consumers are looking for Big Oil to replace Russian production with any urgency, they better look elsewhere.

The last time crude was consistently over \$100 a barrel in 2013, Big Oil’s combined capital expenditure was \$158.7 billion, almost double what the companies are currently spending, according to data compiled by Bloomberg. The group includes Shell Plc, TotalEnergies SE, BP Plc, Exxon Mobil Corp. and Chevron Corp.

“Discipline is the order of the day,” BP Chief Executive Officer Bernard Looney told analysts Tuesday. The London-based major isn’t budging on its \$14 billion to \$15 billion spending plans for the year, with its mid-term guidance creeping up to a maximum of \$16 billion despite 10% cost inflation in some parts of its business.

Shell, which posted record profits that exceeded even the highest analyst estimate, was equally clear. In her first set of results as chief financial officer, Sinead Gorman repeated time and time again that Shell would keep within its \$23 billion to \$27 billion range. “Nothing has changed in terms of our capital allocation framework,” she said.



Instead of spending on new projects, companies are opting to reward shareholders after years of poor returns. Exxon, BP and TotalEnergies increased share buybacks while Chevron is already repurchasing record amounts of stock.

There are clear reasons why Big Oil is choosing not to spend more. Chief among them are climate concerns and uncertainty over the future direction of oil demand. Years of pressure from investors, politicians and climate activists came to a head in the past two years, when all the oil majors pledged some form of net zero target by mid-century. BP and Shell actively positioned themselves to move away from oil and gas over the long-term. All are under added pressure to improve returns that dwindled over the past decade due to cost blowouts and low prices.

“Any decision to increase, support or add-in new fossil projects today could see returns risk within a few years,” said Banco Santander SA analyst Jason Kenney. Climate change, technology developments like electric cars and rapidly evolving government policy on emissions are major risks today when deciding whether to invest billions in a new project, he said.

Against that backdrop, investment in the upstream oil and gas sector slumped 30% in 2020, while last year’s spend of \$341 billion was 23% below pre-pandemic levels, the International Energy Forum wrote in a report.

“Two years in a row of large and abrupt underinvestment in oil and gas development is a recipe for higher prices and volatility later this decade,” warned Joseph McMonigle, Secretary General of the IEF.

That message has not gone down well with consumers around the globe. From Pakistan to Paris, billions of people are suffering a cost-of-living crisis fueled in large part by high energy costs. In the U.S., President Joe Biden has implored

oil companies to reinvest profits from surging oil prices into more production to help ease the shortages caused by Russia's war against Ukraine. Some U.S. and European politicians have called for a windfall tax on companies' profits to help ease the burden on consumers.

To be fair, that doesn't mean companies aren't investing in growth at all. But they will "focus only on low risk, high return assets" such as shale or expanding offshore fields near existing operations, according to Kenney.

Exxon and Chevron, for instance, are spending aggressively to grow production in the U.S.'s Permian Basin, the world largest shale oil region, with planned growth rates of 25% and 15%, respectively. BP is boosting investment in U.S. shale, but the company won't be able to ramp up Permian production until it finishes building two large gathering systems at the end of the year.

However, most Permian growth will largely offset declines from elsewhere in the U.S. supermajors' global portfolio, rather than adding to total barrels. Exxon's first quarter production of 3.7 million barrels per day was the lowest since its merger with Mobil in the late 1990s. Together Exxon and Chevron plan to spend more on buybacks and dividends this year than they do on production.

"For so long the industry has been told by investors and politicians we need less oil and executives remember that," said Barrett of Janus Henderson. "If the world needs an extra million barrels a day to ease prices, I'm not sure where it will come from."

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# Iraq may make decision on Halliburton gas deal in May



(Bloomberg) – Iraq’s cabinet may reactivate a deal with Halliburton Co. to drill wells in a western gas field in Akkas next month, Oil Minister Ihsan Abdul Jabbar told local media.

An agreement with Halliburton would enable the oil ministry to get clear data on the production capacity of the Akkas field and it may reach a decision after the Islamic holy month of Ramadan, which ends in early May, the minister said.

If the government decides to develop the field, which has been idle since Baghdad retook it from Islamic State militants in late 2017, it would have to pick a production company for the project.

Officials have been in talks with Chevron Corp. and Saudi Aramco about investment in the region. That “will depend on the data we get from the exploration and well-drilling operations,” Abdul Jabbar said in an interview on Al-Forat channel.

## **Kurdistan Talks**

Abdul Jabbar said 80% of the contracts that the Kurdistan Regional Government signed with oil companies are correct and the rest need to be reviewed. The KRG has no problem with half the solutions the federal government offered to resolve the oil issues in Kurdistan.

The Kurdish region exports 430,000 barrels of oil per day, Abdul Jabbar said.

Baghdad has long sought to bring Kurdish production under its control in exchange for funds from the national budget. A February ruling in Iraq's top court asserted the central government's right to the semi-autonomous region's hydrocarbons. The KRG has said its rights to control the region's oil and gas are enshrined in the Iraqi constitution.

## **High Oil Prices**

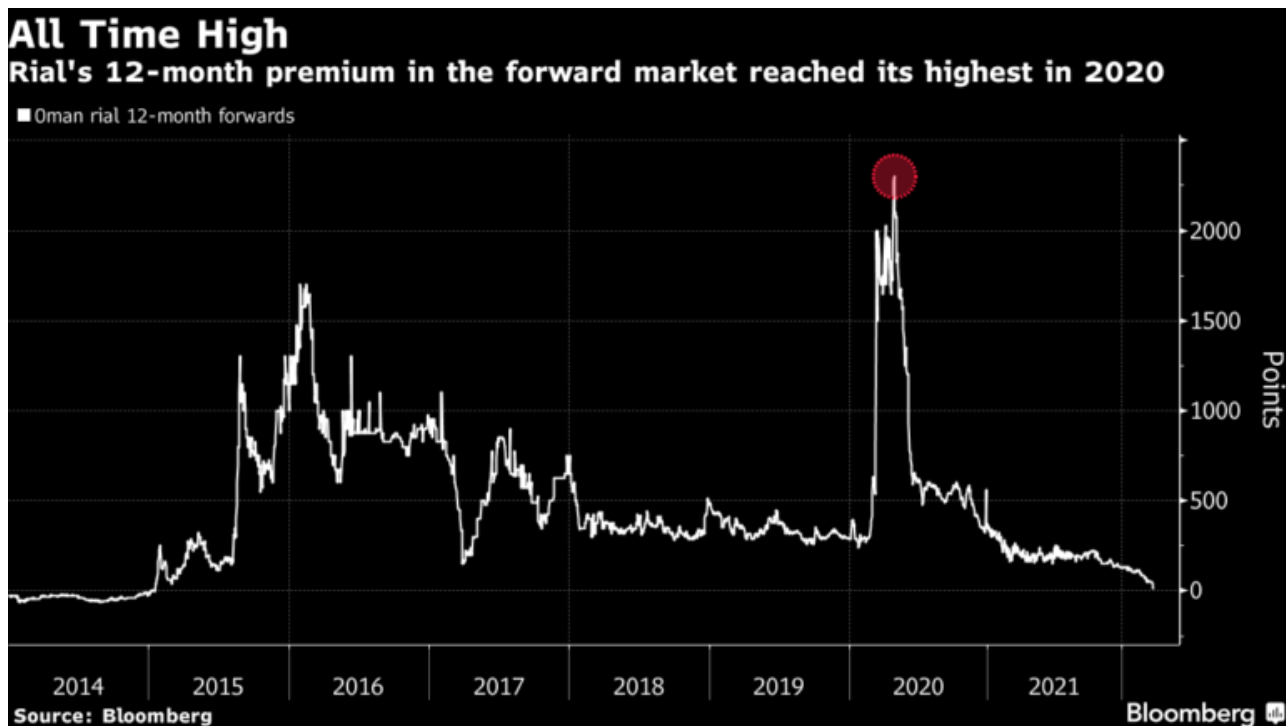
Iraq will probably sell its oil for an average of \$106-\$107 a barrel this month if prices remain at current levels, the minister added.

The oil ministry is providing 30 million liters of gasoline a day for local consumption, which Abdul Jabbar called a "big" number. Work on a new refinery in Karbala has been delayed by Covid-19 but the facility is expected to enter service in the first quarter of 2023, he added. The country will continue to import gasoline until 2024.

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# **Why Gulf Dollar Pegs Survive**

# Through Wars, Oil Shocks



Gulf Arab nations have pegged their currencies to the dollar for decades. There's a reason for that: they reduce foreign-exchange risk for states in the region because so much of their revenue comes from oil, which is priced internationally in the U.S. currency. Periodically the mechanisms are tested, as they were in 2020 when a price war sent crude plummeting below \$20 a barrel. With oil back around \$100 in 2022, they appear to be in good shape, despite questions about the dollar's role in the global economy.

## 1. Who has currency pegs and why?

The six members of the Gulf Cooperation Council – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates – have been running currency pegs or managed foreign-exchange regimes since the 1970s and 1980s. Kuwait's dinar tracks the value of a basket of currencies believed to be dominated by the dollar, while others are linked solely to the greenback. The pegs have helped to shield the region's economies from the volatility of energy markets and allowed central banks to accumulate reserves in the good times. Those reserves, along

with foreign assets held by the region's sovereign wealth funds, are used in turn to defend the pegs.

## 2. What could put the pegs under stress?

Fixed exchange-rate regimes in Asia were swept away during the currency crisis of the late 1990s, when speculators forced the likes of Thailand and South Korea to abandon their links with the dollar. They're now largely confined to the major oil producers in the Middle East along with Hong Kong, whose dollar has been pegged to the U.S. currency since 1983. The Gulf pegs mean local central banks often take a cue on monetary policy from the U.S. Federal Reserve, which creates the risk of policy misalignment when business cycles are out of step. Today, the Gulf region is grappling with heightened inflation and the prospect of global interest-rate increases led by the Fed. There is disquiet about global dollar dominance, and the U.S.'s willingness to use the dollar as a weapon in sanctions to punish Russia for its invasion of Ukraine.

## 3. What might the Gulf states do next?

None of the region's governments have suggested they might abandon the pegs and let markets decide the value of their currencies. However, Saudi Arabia, the biggest economy in the region, is said to be considering accepting yuan payments for its oil exports to China. If the kingdom does take that step, the petrodollar system would be tested, especially if neighbors follow suit, with China accounting for over 20% of the bloc's total oil shipments. Currency strategists said Saudi Arabia appeared to be sending a political message to the U.S. with the yuan reports, amid strained relations with Washington, and played down the likelihood of any immediate action.

## 4. What stresses have there been in the past?

The system has survived stern tests, including successive

years of low oil prices in the 1990s, a period of dollar weakness before the financial crisis in 2008 and an oil-price crash in 2014. Speculators jumped in at that point in a failed effort to challenge the Saudi peg, boosting the price of 12-month forward contracts used by investors to bet on the peg breaking or to hedge in case it does.

#### 5. How did Saudi Arabia react?

Instead of choosing to devalue the riyal, the kingdom cut spending and subsidies and turned to debt markets to fund its budget deficit. Its neighbors have adopted similar strategies. The Saudi forward contract jumped again in 2020 amid the double-hit of weaker crude prices and the pandemic. Oman's rial forwards reached a record high that year, before edging lower.

#### 6. What happens to Gulf economies if the U.S. hikes rates?

The risk is that, to maintain their pegs, the region's governments are forced to follow the Fed with a succession of interest rate rises that end up hammering their own economies. If they do, there's still a way for them to avoid recessions: Oil prices are riding high, leaving them with plenty of ready cash to boost state spending and support growth.

#### 7. Which pegs appear most vulnerable to speculators?

The weakest economies in the region have for long been Oman and Bahrain, with the latter being the only nation in the region needing oil above \$100 a barrel to balance its budget, according to the International Monetary Fund. The two countries have fared better recently, with S&P Global Ratings raising Oman's credit ratings in April. The oil rally has eased concerns about the sultanate's ability to keep the rial pegged, prompting traders to slash bets on a devaluation. Saudi Arabia, the UAE, Kuwait and Qatar have for the most part always had firepower in the form of sizable currency reserves to defend their pegs.

## 8. What if dollar pegs were abandoned?

While the pegs give the region's governments less freedom to pursue policy goals like reviving growth or creating jobs, they provide more predictability for investors and foreign residents. The dollar's status as a global reserve currency would be undermined if GCC countries dismantled the pegs. Middle East countries account for between 10% and 15% of global foreign exchange reserves outside of China, according to Goldman Sachs. Saudi Arabia alone makes up around 5%. If Saudi Arabia accepted yuan for oil, it would accumulate big yuan reserves that it would then need to allocate, Goldman pointed out in a research note in March. This could pose challenges of its own, given the size of China's bond market.

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# Germany faces \$240bn hit if Russian energy cut off

Bloomberg / Berlin

Germany was warned it could face a €220bn (\$240bn) hit to output over the next two years in the event of an immediate interruption in Russian energy supplies over the war in Ukraine.

Economic institutes advising the government in Berlin said on Wednesday in a joint forecast that a full halt in Russian natural gas imports would result in a "sharp recession."

"The decision to become independent from Russian supplies of raw materials is likely to remain valid even when the military



and political situation calms down again," the report said. "That means part of the energy supply and energy-intensive industry must realign itself."

While the €220bn estimate is the equivalent of 6.5% of annual output, it's nowhere near the almost €890bn in borrowing Germany carried out in 2020 and 2021 to shield the economy from the fallout of the pandemic.

Amid mounting casualties and reports of brutal atrocities, Germany has been under increasing pressure to justify its resistance to an embargo on Russian gas – widely seen as the ultimate leverage against President Vladimir Putin.

Ukraine snubbed a request by Frank-Walter Steinmeier, Germany's president, to visit Kyiv this week following criticism for his past support for the Nord Stream 2 gas pipeline from Russia to Germany and for his role when foreign minister in encouraging reconciliation and dialogue with the Kremlin.

Finance Minister Christian Lindner highlighted the huge challenges facing Germany as it tries to wean itself off Russian energy as quickly as possible while also pursuing a goal of climate neutrality by 2045.

"Our world will not be the same again as it once was," Lindner, who's chairman of the pro-business Free Democrats, wrote in a guest article for the Handelsblatt newspaper published on Wednesday.

"We need new business models, new ideas, new supply chains and new trade relationships," he said. "We have to reduce one-sided dependencies, be it when it comes to importing energy from Russia or exporting to China."

Berlin-based DIW, one of the institutes involved in the estimate, said on Friday that Germany could be in position to survive without Russian gas, which currently accounts for two-fifths of its gas deliveries. The group said a combination of high storage, bolstering other energy supplies and implementing programmes to lower demand could offset Russia as soon as this winter.

That's not a view that's generally shared by the business

community, with industry leaders including Deutsche Bank AG Chief Executive Officer Christian Sewing warning of dire economic consequences if Russian supplies are severed.

Even absent a cutoff, Wednesday's report pared the outlook for Germany's economy, predicting growth this year of 2.7% and 3.1% in 2023. Those numbers compare with previous projections for expansion of 4.8% and 1.9%. Inflation will average 6.1% in 2022 – the most in 40 years.

“The shock waves from the war in Ukraine are weighing on economic activity on both the supply side and the demand side,” said Stefan Kooths, vice president of the Kiel Institute for the World Economy. “Increasing prices of critical energy commodities following the Russian invasion further fuel the upward pressure on prices.”

Germany's industry-heavy economy faces considerable hurdles after the war sent energy prices higher while disrupting supply chains that had already been suffering from pandemic-related snarls. Inflation reached 7.6% in the first full month of the war – the highest level since records began after reunification in the early 1990s.

Companies are seen as particularly vulnerable because of Germany's reliance on Russian gas. The ruling coalition last week agreed on an aid package for suffering businesses that includes loans, loan guarantees and capital injections, and is meant to help energy firms in particular.

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## **IEA cuts oil demand forecast as China reimposes lockdowns**



Bloomberg / London

The International Energy Agency cut its forecast for global oil demand this year after China reimposed lockdowns to contain the spread of a resurgent coronavirus.

With the weaker demand outlook and the massive release of emergency oil reserves by IEA members, the agency now sees global markets in balance for much of the year. Crude prices have already lost most of their gains since Russia's attack on Ukraine, to trade near \$100 a barrel in New York on Wednesday.

"We're seeing now that economic forecasters are continuing to downgrade their outlook for the world economy, and obviously this will have an impact on oil demand," Toril Bosoni, head of the IEA's markets and industry division, said in a Bloomberg Television interview. "The market does look more balanced."

The Paris-based agency, which advises most major economies, lowered projections for world fuel consumption this year by 260,000 barrels a day, with a particularly steep reduction of 925,000 a day for China in April. Still, global demand remains on track to increase this year.

The IEA also dialled back estimates for the loss of Russian supplies from an international boycott over its military aggression. Production in April may be 1.5mn barrels a day

lower than the prior month – roughly half the drop that was previously expected. Those losses may still double in May, the IEA said.

Oil surged well above \$100 a barrel following Russia's attack on its neighbour. While prices have eased, they are still high enough to stoke inflationary pressures and exacerbate a cost-of-living crisis for millions of consumers. To counter this, IEA members announced last week that they will deploy 240mn barrels from emergency reserves, the biggest stockpile release in the agency's history.

"Prices are now back to near pre-invasion levels, but remain troublingly high and are a serious threat for the global economic outlook," the IEA said.

World oil consumption will expand by 1.9mn barrels a day to average 99.4mn a day this year, according to the IEA.

"Oil demand is still recovering from Covid," said Bosoni. "The aviation sector is recovering, there's pent-up demand, so we are expecting growth. But obviously downside risk if the economic outlook deteriorates."

China's fierce zero-Covid policy has diminished demand growth, as millions are locked down in their homes, imports drop and business activity slows in the world's second-biggest economy. The IEA noted that Saudi Arabia and other members of the Organization of Petroleum Exporting Countries have refused to open the taps faster, partly from a belief that markets didn't face a genuine shortage, and partly to preserve the Opec+ coalition they lead with Russia.

Opec+ members managed to provide just 10% of the supply increase scheduled for March, according to the IEA. The 19 coalition members, which have been engaged in a pact to stabilise markets since the start of the pandemic, added a mere 40,000 barrels a day as diminished investment erodes production capacity across the group.

The clash over policy between Opec+ and the IEA – which has openly expressed disappointment with the group's inaction – came to a head last month with Opec abandoning the agency as one of its data sources.