Opec+ oil production boost to reassure market investors: EIU

The 1mn barrels per day production boost by Opec and its allies will help to reassure market investors and prevent a spike in oil prices in the near term, Economist Intelligence Unit (EIU) has said in a report.

This would be equivalent to about 1% of global supply, EIU noted. Nonetheless, EIU said a “number of geopolitical risks remain”, including the potential for further output declines from Iran and Venezuela, which will push oil prices gradually higher over the remainder of 2018.

“The fundamental problem facing Opec at its ministerial meeting in Vienna on June 22 was that some of its members do not have the capacity to rapidly increase output even if quota caps are relaxed, given problems related to under- investment and politics,” EIU said. “This means that they would suff er revenue hit from lower prices without a counterbalanc- ing increase in volume,” EIU said. Venezuela’s output in May was just 1.4mn bpd, its lowest in 30 years, as domestic political and economic turmoil has undermined the oil sector.

This, EIU said was down from 2.1mn bpd in October 2016, making the reduction more than seven times greater than its obligation under the Opec deal, which is also described as more than 700% “compliance” with its cut target. Angola, meanwhile, has strug- gled owing to underinvest- ment since the collapse in oil prices in 2015, meaning that it produced just 1.5mn bpd in May, equivalent to a 290% compliance rate. “Despite the diff erences in pro- duction capacity, all members do fundamentally benefit from an environment in which prices are more stable and avoid an- other dramatic crash driven by a shale boom. As a result, they were able to achieve an agree- ment, firstly among the Opec countries and then on June 23 with their non-Opec partners," EIU said.

In November 2016 Opec and major non-Opec exporters, particularly Russia made a decision to cut nearly 1.8mn barrels per day (bpd) from sup- ply. This had a dramatic impact on the oil market, particularly from mid 2017 after compli- ance began to improve, and the deal was twice extended, first until March 2018 and then until December. A pick-up in the global econ- omy, boosting demand, and problems with some produc- ers, notably Venezuela, which saw them producing below their Opec quota, added to the upward pressure on oil prices, which rallied by more than 50%, hitting a four year high of $79/barrel in May, a level which had seemed almost incon- ceivable back in 2016, when prices averaged just $44/b.

"However, the success of the deal in bolstering prices stoked complaints from oil consum- ers – notably the US president, Donald Trump – and added to worries of a repeat of the previous crash, as high prices motivate investment in new capacity outside the exporter bloc, particularly in US shale. "This all led to a growing consensus that the exporters need to release more oil to put a ceiling on prices," EIU said.