December 08, 2018

Better Than Expected OPEC Outcome

After two days of negotiations, OPEC and it's non-OPEC allies reached an agreement to cut crude oil production by 1.2 mmb/d. While the announcement was taken positively by markets, the extended timeline of negotiations has hurt market confidence in OPEC's ability to follow-through on the production cuts come January 2019. Despite these reservations, prices will definitely be supported through the end of the year. Brent is likely to exit the year near $65/bbl while WTI exits around $55/bbl.

Prices ended the week up approximately 4% and after-market trading has been steady. While doubts will always persist about whether any cut is enough, the announcement was about as firm as could be expected. The volumes cut were near the high end of estimates, there was clear and substantial buy-in from Russia, the Organization outlined a clear baseline level – all positive indicators about how serious OPEC is about committing to the deal. While the Organization did not specify a full roster of country level quotas, it did share some interesting details. Saudi Arabia will be aiming for approximately 10.2 mmb/d in January while Russia is targeting 11.2 mmb/d. Essentially, OPEC members are committing to a 2.5% production cut from October 2018 levels while non-OPEC members are committing to a 2% reduction.

This time around, only Libya, Venezuela, and Iran received exemptions. Given on-the-ground problems, Venezuelan production is virtually guaranteed to continue declining in 2019, while Iran will be constrained by US sanctions. This makes Libya the most likely upside surprise risk, with volumes dependent on maintaining political stability. When it comes to Iran, the last-minute waivers granted by the Trump Administration were one of the variables leading to recent price weakness. The exact timeline and requirements for extending those waivers has not been made clear, and may not even be officially established yet. In light of OPEC's, and more specifically Saudi Arabia's, decision to cut production the White House may take a much less charitable stance when issuing waiver extensions in an effort to force/tempt OPEC+ not to adhere to production cuts.

The table below calculates approximate production targets based on the IEA's latest report of October 2018 production. However, these numbers are merely a guide, as Saudi Arabia indicated during the press conference that it would likely be shouldering a larger share of the cuts.

OPEC	Oct 2018 Baseline	2.5% Share	New Production
Algeria	1.07	0.03	1.04
Angola	1.5	0.04	1.46
Congo	0.33	0.01	0.32
Ecuador	0.52	0.01	0.51
Equatorial Guinea	0.11	0.00	0.11
Gabon	0.19	0.00	0.19
Iraq	4.65	0.12	4.53
Kuwait	2.76	0.07	2.69
Nigeria	1.67	0.04	1.63
Qatar	0.61	0.02	0.59
Saudi Arabia	10.65	0.27	10.38
UAE	3.21	0.08	3.13
Iran	3.34	Exempt	3.34
Libya	1.12	Exempt	1.12
Venezuela	1.26	Exempt	1.26
Non-OPEC	**Oct 2018 Baseline**	**2.5% Share**	**New Production**
Azerbaijan	0.78	0.02	0.76
Kazakhstan	1.86	0.04	1.82
Mexico	2.05	0.04	2.01
Oman	0.98	0.02	0.96
Russia	11.79	0.24	11.55
Others	1.18	0.02	1.16

All volumes mmb/d