Global Oil Market

OPEC+ agrees to cut oil supply and ends price war

Research
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Economics
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The world's largest oil producers reached a historic deal to cut global crude output by as much as nearly 10% in the next two months, putting an end to a devastating price war that started in early-March after Saudi Arabia and Russia failed to agree on a joint production strategy aimed at balancing the global oil market.

Specifically, the OPEC+ alliance, including Russia, agreed to lower their overall oil production by 9.7 million barrels per day (bpd), starting on 1 May 2020, for an initial period of two months ending on 30 June 2020. For the subsequent period of six months (from 1 July 2020 to 31 December 2020), the total agreed adjustment to production will be 7.7 million bpd followed by a 5.8 million bpd reduction for a period of 16 months (from 1 January 2021 to 30 April 2022). OPEC stated that the baseline for the calculation of these adjustments is the oil production of October 2018, except for Saudi Arabia and Russia, with both of these countries having the same baseline level of 11 million bpd. (The oil production targets for each OPEC country in each of the above mentioned periods are detailed in the next page)

On top of this OPEC+ accord, oil producers in the G20 countries will also contribute with their own output reductions. Production from major oil producing countries like the US, Brazil and Canada are expected to decline due to the effects of the current lower oil prices, which could have an additional impact on global oil supply of five million bpd. However, these output reductions could take months, or even more than a year, to materialize, but they will come automatically depending on the future evolution of oil prices. Still, the involvement of the G20 countries, which have sometimes criticized the OPEC, was politically important in the current backdrop for the oil market.

The focus of oil market participants now shifts to whether this output reduction will be sufficient to lessen the massive supply glut that continues to grow as a result of the impact of the coronavirus on global oil demand. Indeed, some estimates suggest that global oil demand has already fallen by 30-35% in recent weeks due to the lockdown of the world economy. This means that these production cuts will have a somewhat limited initial impact on balancing the global market, which is probably why crude prices saw a somewhat muted reaction to the news that a deal had been reached. Nevertheless, the agreement now achieved still represents an important victory for the OPEC+ alliance after only just a few weeks ago it appeared to have been dead. It also (hopefully) ends a turbulent month for Brent crude, as its price plunged to the lowest level in nearly two decades after falling below US$ 30 a barrel in March. Recall that Brent already traded above US$ 70 earlier this year.

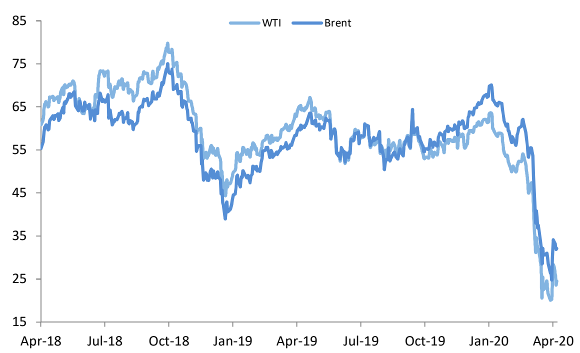
For Angola, this oil production cut agreement means that the country will have to lower its output to 1.179 million bpd in May and June 2020. This represents a drop of almost 350,000 bpd (or -22.8%) from a baseline figure of 1.527 million bpd in October 2018. However, Angola is currently producing much less crude, with the latest data from OPEC showing a supply of 1.390 million bpd in February 2020. This means that the country will have to cut its production by 15% in the first two months of the deal, 10% in the second half of 2020 and 5% until April 2022 (all relatively to the February 2020 figure).

With the absence of a marked recovery in oil prices in the future, this lower production would further depress public receipts over the next two years and make the government's aim of fiscal balance even more challenging. Said differently, the need for Angola to accelerate its current efforts of economic diversification and reduce its dependence on the oil sector has never been more pressing than now.

OPEC TARGETS Thousand Barrels a Day	Baseline	May - June 2020	July-December 2020	January 2021 - April 2022
Algeria	1,057	816	864	912
Angola	1,527	1,179	1,249	1,318
Congo	325	251	266	281
Equitorial Guinea	127	98	104	110
Gabon	187	144	153	161
Iraq	4,653	3,592	3,804	4,016
Kuwait	2,809	2,168	2,296	2,424
Nigeria	1,829	1,412	1,495	1,579
Saudi Arabia	11,000	8,492	8,994	9,495
UAE	3,168	2,446	2,590	2,735
OPEC 10	**26,682**	**20,598**	**21,815**	**23,032**
Production cuts		*-6,084*	*-4,867*	*-3,650*
Russia	11,000	8,492	8,994	9,495
Mexico (1)	1,781	1,681	-	-
Other Non-OPEC	4,417	3,409	3,610	3,812
Non-OPEC	**17,198**	**13,582**	**12,604**	**13,307**
Production cuts		*-3,616*	*-2,813*	*-2,110*
Total OPEC 10 and Non-OPEC	**43,880**	**34,180**	**34,419**	**36,339**
Production cuts		*-9,700*	*-7,680*	*-5,760*

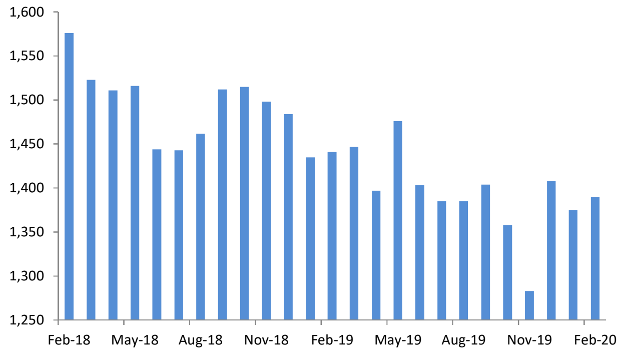
(1) Mexico only agreed to production cuts in the first stage. Source: OPEC.

BRENT AND WTI CRUDE PRICES (US$ PER BARREL)



Source: Bloomberg.

ANGOLA OIL PRODUCTION (THOUSAND BARRELS/DAY)



Source: OPEC.

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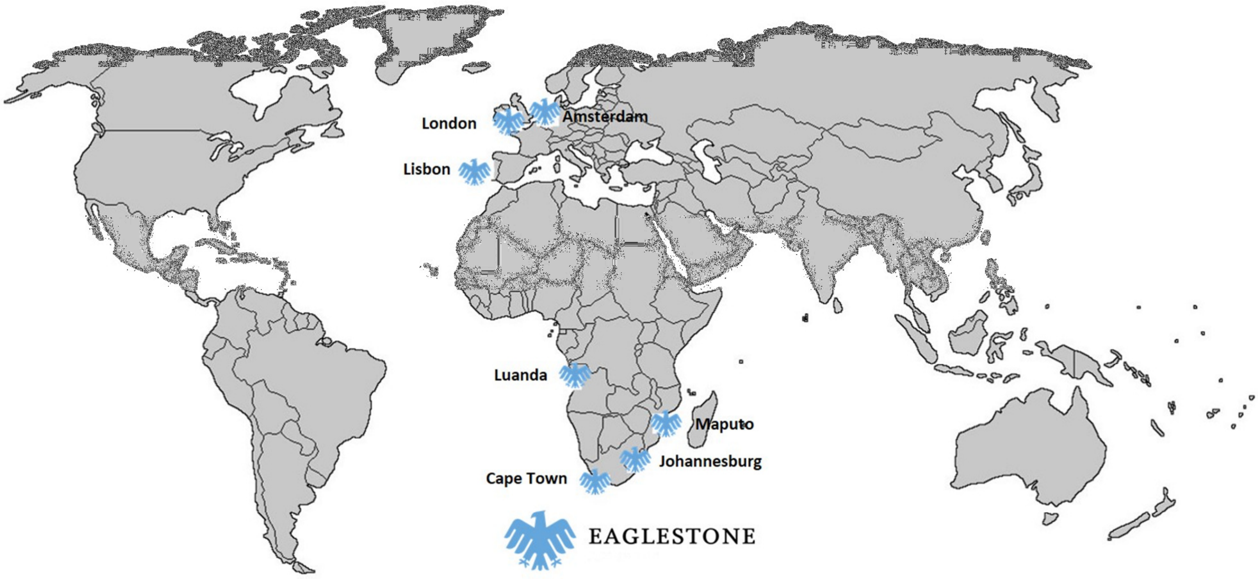

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