Investment Strategy Update

For inquiries related to this article, please contact:

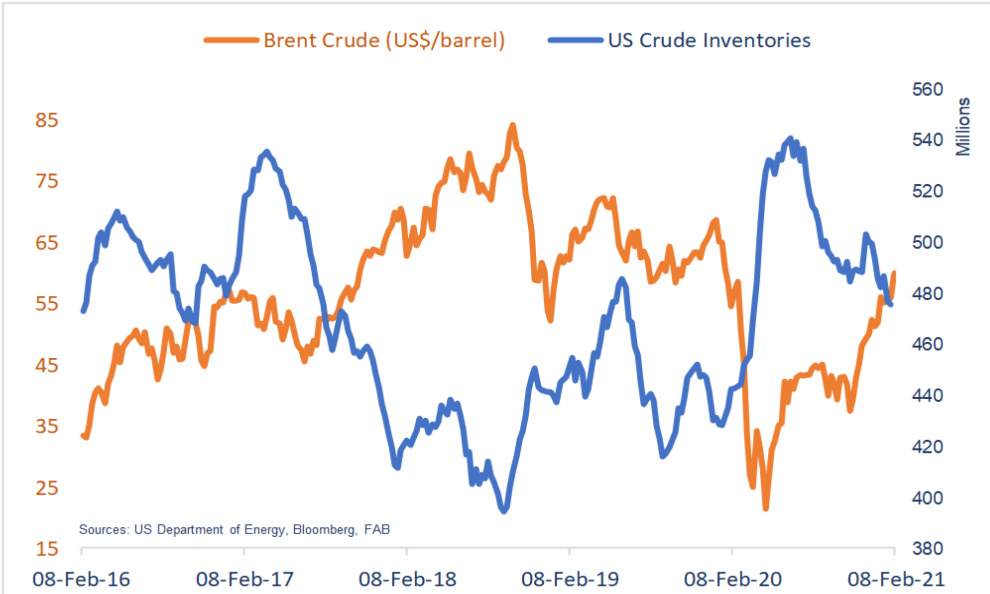
Alain.Marckus@bankfab.com
Christofer.Langner@bankfab.com

بنك أبوظبي الأول
FAB
First Abu Dhabi Bank

8 February, 2021

OPEC+ is winning the oil price war, but its success is a risk

- **Brent crude briefly topped US$60/ barrel today as the reflation trade combined with falling inventories.**
- **The commodity is up 16.1% year-to-date as the oil producing nations have held together in keeping output lower.**
- **The number of active rigs in the US, however, has started to rise, and OPEC+ is reviewing its output targets every month.**
- **The rally may have a limit, but it is in line with FAB's forecast of an average Brent price of US$58/barrel in 2021.**
- **The FAB AAC is overweight in equities, IG and EM bonds, and gold, and is underweight alternatives.**



Brent crude briefly breached US$60/barrel today, a surprise for many economists, who had a more bearish outlook for the commodity in 2021. Year-to-date, Brent prices have rallied 16.1% and are averaging US$55.88/barrel, 29% higher than the full-year average price for the commodity in 2020. FAB has an above-consensus forecast of an average Brent crude price of US$58/barrel this year, much higher compared to Fitch Ratings which expects this number to be US$45/ barrel and S&P Global Ratings, which has it at US$50/barrel.

The move up is due to a confluence of bullish factors. OPEC+ countries, for one, have restrained output, maintaining a supply deficit that is slowly reducing the excess inventories built early last year. That was in evidence last month, as US oil inventories fell by 17.8 million barrels, according to the Department of Energy.

The question going forward is whether OPEC+ members will have the will to keep the current curbs in place. After a key meeting in December, the group agreed to review their curbs every month. The speed of the price rise could easily spur some to call for higher production.

Even if the countries stick to the curbs, the higher prices could prompt more shale oil producers in the US to restart activities. That is already happening, albeit to a small extent. The number of active horizontal rigs in the US, a measure of shale exploration activity, bottomed in the second week of August, at 143. It has risen steadily since, to 240 as of last week, according to Baker Hughes. That is still far short of the 560 active rigs one year ago, but it indicates shale is not dead.

Oil traders seem to be seeing that, too. The futures data of the Commodities and Futures Trading Commission has shown oil traders increasing their short positions even as hedge funds added to their longs.

The OPEC+ output curbs have helped reduce inventories and push crude prices higher

Furthermore, the drawdown in inventories could also slow down going forward. The numbers released by the Department of Energy every week are about a week old. So last week's inventory draw was really related to the end of January. Activity in Europe, in particular, has slowed since then, amid new lockdowns. A testament of that is in China's exports of refined products, which have started to fall.

Even if the upside is capped, OPEC+ has demonstrated its ability to balance the oil market throughout the past year. Furthermore, crude demand has recovered from its lows and the International Energy Agency expects it to end the year at 99 million barrels/day, just 2 million barrels/day short of the record logged in December, 2019.

Investment Strategy Update

بنـك أبـوظبـي الأول
FAB
First Abu Dhabi Bank