

Middle East escalation pushes energy prices higher

Oil and gas prices have moved higher following an Iranian missile attack on Israel. Markets are waiting to see how Israel responds. Escalation in the region is putting energy supply at greater risk



Bushehr nuclear power plant in Iran

The impact of losing Iranian oil supply

Oil prices briefly broke above \$80/bbl as the market waits to see how Israel responds to Iran's latest missile attack. Clearly, growing tensions have seen the market price in a greater war risk premium. However, where prices go from here will depend on how Israel responds. A similar response to Iran's April attack would likely see the risk premium eventually start to erode, with fundamentals once again coming to the forefront. And with the global market set to be in surplus through 2025, this means that oil prices will likely weaken. We are forecasting that ICE Brent will average \$72/bbl over 2025.

However, Israel may decide on a more aggressive response. There have been suggestions that Israel could target Iranian energy infrastructure. The key question would then be whether Israel hits downstream assets or mid/upstream assets. Hitting downstream oil assets, such as refiners, would likely increase oil supply for the global market as Iran would be unable to process this oil and so would have a larger exportable surplus. In theory, this should be bearish for prices.

However, given it would be seen as an escalation, oil prices would still likely move higher, at least initially. A more serious impact for the global oil market would be if Israel targeted mid and upstream oil assets, which would affect Iran's ability to export crude oil. This would put as much as 1.7m b/d of supply at risk, which could see oil prices trading above \$90/bbl in 2025.

This kind of response would only escalate the situation further and take the market a step closer to a more extreme scenario, which for now we still think is unlikely. There is the potential in a worst-case scenario that Iran attempts to disrupt Persian Gulf oil flows through the Strait of Hormuz. Almost a third of global oil flows through the Strait of Hormuz and any significant disruption to these flows could very well see oil trading to new record highs, exceeding the record price of almost \$150/bbl in 2008. Unfortunately, given that the bulk of OPEC capacity sits in the Persian Gulf, this spare capacity would be of little help if Iran was successful in significantly disrupting oil flows through the strait.

Persian Gulf LNG flows disrupted under worst-case scenario

European natural gas prices have also rallied on the back of Middle East developments. TTF once again broke briefly above EUR40/MWh. While the European market is well supplied with storage close to 95% full and likely to be close to 100% full ahead of the 2024/25 heating season, it is still vulnerable to supply disruptions.

We believe that European natural gas prices should fall through 2025. However, much will depend on how the weather develops over the winter. Europe has had two mild winters and we cannot assume a third. Even assuming a normal winter, as well as the loss of Russian pipeline flows through Ukraine from 1 January 2025 following the expiry of Gazprom's transit deal with Ukraine, we still expect Europe to exit the 2024/25 heating season with storage more than 40% full. The starting and ramping up of several US LNG export facilities should help to offset potential Russian supply losses via Ukraine.

However, a growing concern for gas markets related to Middle East escalation is the potential for disruption to Persian Gulf LNG supplies moving through the Strait of Hormuz. While it is an extreme scenario, the potential impact of these supplies being disrupted is significant. Qatar exports a little more than 100bcm of LNG annually and makes up around 20% of global LNG trade. Losing a large share of this trade would leave the global LNG market in deficit, pushing up prices. The ramping up of new LNG export capacity elsewhere will take time, so any potential disruptions to flows from the Persian Gulf would be difficult to offset through the 2024/25 winter.

Author

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial

instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.