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OPEC: Deal or no deal?

There is growing consensus that OPEC will extend their current output deal when they meet in Vienna this Thursday and we believe it will run through till the end of 2018



Source: Shutterstock

Pre-meeting expectations

There is growing consensus in the market that OPEC will extend their current output deal when they meet in Vienna this Thursday. Market expectations, along with the near record speculative long in ICE Brent has given OPEC and its allies, little choice but to extend the deal. We believe the most likely outcome is that OPEC will agree to extend the deal through until the end of 2018 and this also seems to be what the market is generally expecting.

Most members have come out in support of an extension, and Saudi Arabia has already made it clear that the target to reduce inventories towards the five-year average will not be met by the end of March 2018, which is when the deal is currently scheduled to expire.

It seems the only scenario that would offer significant upside to prices would be if OPEC surprised the market by not only

extending the deal, but making deeper cuts

For the second largest OPEC producer, Iraq, the choice should be easy. Exports from the north of the country have fallen to around 300Mbbls/d, compared to a usual flow of around 600Mbbls/d. This disruption comes following Iraqi forces seizing several oil fields around Kirkuk from Kurdish control. While the Iraqi government has tried to increase exports from the south of the country to compensate, overall exports have still fallen to a 20-month low over the first half of November. Therefore by agreeing to an extension, Iraq can help support prices at a time when its exports are constrained.

Other OPEC members, including Iran, UAE, Kuwait, Qatar and Venezuela have also been largely supportive of the deal. Even Ecuador, which had previously looked for exemption in October, appears to favour an extension. Ally to the deal, Russia, also now appears to support an extension. Previously the Russians were reluctant to extend cuts at this stage, and instead wanted to evaluate the situation closer towards the expiration of the current deal. So with Russia now supposedly on board, it really does seem that there is only one outcome to Thursday's meeting.

Commodity price forecasts

	2017				2018				2019			
	1Q	2Q	3Q	4QF	1QF	2QF	3QF	4QF	1QF	2QF	3QF	4QF
ICE Brent (US$/bbl)	55	51	52	57	50	50	52	52	45	47	50	50
NYMEX WTI (US$/bbl)	52	48	48	52	48	48	50	50	44	46	49	49

Source: Bloomberg, ING estimates

This however does mean there is a significant downside risk for the market if OPEC falls short of market expectations. A deferral in the decision or an extension of less than nine months is likely to be viewed by the market as a disappointing outcome. The speculative net long in ICE Brent remains near record levels, in terms of number of lots, as well as the USD value of the position. Therefore a surprise would likely lead to some heavy liquidation.

It seems that the only scenario that would offer significant upside to prices would be if OPEC surprised the market by not only extending the deal, but making deeper cuts. However we believe that this scenario is highly unlikely, and is something that OPEC and its allies are not considering.

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