HEDGEYE ENERGY POLICY
OPEC TRACKER

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OPEC's upcoming November 30 ministerial meeting in Vienna promises to be highly consequential to oil markets. Global oil prices have finally crossed the $60/barrel threshold thanks to a perfect storm of geopolitical risks in Kurdistan/Iraq, Venezuela and Iran as well as consistent inventory draws caused partly by fundamentals (stronger demand/slowing US production), Saudi export cuts to the US and Hurricanes Nate and Harvey. In recent days, Saudi Crown Prince Mohammed bin Salman offered his personal endorsement for a deal extension, and we believe the market now has already priced in a deal extension.

As we enter OPEC month, we expect to see comments from OPEC Ministers and officials regarding potential options for action that the group may take at the November 30 meeting. Already, we have seen several possible scenarios expressed. As a result, we've put together this Hedgeye OPEC Options Tracker to help make sense of the various trial balloons.

BASE CASE: 3-MONTH EXTENSION TO JUNE 30, 2018	We see an 80 percent chance of a deal extension. The only question is how long. Our base case for action at the next OPEC meeting on November 30 is a 3-month extension beyond the current deal's expiration date of March 31, 2018. The 3-month extension would bring the deal to June 30, 2018 --- or just before OPEC's first meeting of 2018 in late May or early June when OPEC will be in position to reassess the situation again at that time. We think this is the base case (minimum action to be taken).
NO ACTION – UNLIKELY OUTCOME	We believe OPEC taking no action at the meeting is highly unlikely since it would be greeted by a negative market reaction. Thanks to OPEC jawboning there are raised expectations of a deal extension. As an added incentive to recalcitrant producers, Russia has announced it will expand production in 2018 if no deal extension is reached.
9-MONTH EXTENSION FOR FULL 2018 CUT	Press reports have detailed, and we have confirmed independently, that Saudi Arabia and Russia prefer to have a 9-month extension of the production cut deal that would translate into cuts for all of 2018. However, there has been so much press coverage and raised expectations regarding a potential 9-month extension that the market may be disappointed by any move short of it. Despite being backed by Saudi Arabia and Russia, a 9-month extension is far from a sure thing. Our feedback is that other OPEC members are cool to the 9-month extension option and reluctant to sign on to a full year of cuts. However, the Saudis continue to hold discussions with other producers to gain support for the 9-month extension, and we expect these consultations will continue right up to the meeting itself. We think the 9-month extension is possible but give it only about a 30 percent chance of success.
DEEPER CUTS	Some analysts believe OPEC needs to make deeper cuts to sustain current prices around $60/barrel. Indeed, Iraq's oil minister Jabbar al-Luabi told reporters at an energy conference in the UAE in September that OPEC was considering both deal extensions and a slight additional cut. "Some, like Ecuador and other countries, even Iraq, think there should be another cut of 1 percent," Luabi said adding there was "no firm decision yet." More cuts of even one percent would be helpful but it seems unlikely that OPEC could get all of its members and the non-OPEC participants to agree to an additional cut when many are already not meeting their cut quota. At the Hedgeye Energy Conference on October 11, former OPEC President and Algerian Energy Minister Chakib Khelil told attendees that "OPEC knows it needs to cut deeper to counter a production surplus early next year but it will be difficult to achieve consensus." We think deeper cuts by OPEC are unlikely with a low probability of 15 percent.

LIFTING LIBYA AND NIGERIA EXEMPTIONS	When the production cut agreement was made, OPEC allowed exemptions for Libya and Nigeria due to conflict-causing disruptions in both countries. But in the months since, both OPEC members have added significant production undermining OPEC's efforts to balance the market and drain the supply glut. In Libya's case, production rose from about 500,000 b/d in October 2016 to about 1 million b/d in October 2017 – an increase of 500,000 b/d. Nigeria's production rose from about 1.4 million b/d in October 2016 to more than 1.75 million b/d in October 2017 – an increase of 350,000 b/d. So combined both OPEC members have undermined the effectiveness of OPEC's production cut deal by about 850,000 b/d. Many OPEC ministers are frustrated about the growing production from both countries and believe both producers need to join the deal. We think there is a 55 percent chance that the Libya/Nigeria exemptions are removed at the November 30 meeting. But don't look for cuts from either country. Instead we think they will agree to production caps at around current production levels. But even caps would be a welcome sign for the market.
CUTTING OR MONITORING EXPORTS	Much of the recent success by OPEC in generating crude inventory draws in the US is the result of Saudi Arabia's concerted effort to cut exports to the US. The Saudis telegraphed this strategy in May after getting frustrated by the market's singular focus on the weekly EIA petroleum reports. So the Saudis adopted a strategy we like to call "working the refs" – they would cut exports to the US in order to cause big draws in EIA data on US crude stocks. Combined with Hurricanes Nate and Harvey, the plan worked pretty well. Adding to the momentum, Saudi Arabia took the unprecedented step of pre-announcing crude export cuts of about 550,000 b/d in November. The Saudis are hoping to push all members and other participants in the deal to focus on exports rather than production. It's a very hard ask but at the very least Saudi Arabia is asking for the Joint Monitoring Committee to monitor exports in addition to production. The monitoring seems doable but it might undermine the compliance picture. Except for Saudi Arabia, limiting exports further would be very difficult and so we expect little cooperation from other producers in the deal.
DELAY OR CANCEL ARAMCO IPO	There has been a great deal of press coverage regarding a delay or even cancellation of the Aramco IPO next year. The continued narrative about a delay was raising market doubts about Saudi Arabia's confidence or commitment to higher oil prices. In response, Minister al-Falih and Aramco's CEO have since both made statements pledging that the 2018 IPO is on track. We believe the Aramco IPO next year is solid. It is the signature initiative of the Crown Prince, and the Kingdom's entire reform plans depend on a successful IPO. In our view, the IPO is a good barometer of the Saudis view of healthy oil prices and is important to watch closely with regard to OPEC actions. OPEC generally takes a cautious approach that responds to market conditions. But with the impending Aramco IPO, the Saudis are pushing for a more proactive and strategic approach. As we have said in previous notes, the Aramco IPO is now driving Saudi oil policy.

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