

MACROCOSM

No, We Still Don't See \$100 Oil

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And no, it's not "the end of OPEC." It's in Saudi's interest to make it right with UAE.

Despite the failure of the OPEC+ meeting to officially establish higher production levels, we stand by last week's call that crude oil is highly unlikely to see the \$100 "super-cycle" price [some commentators are calling for](#) (see "[\\$100 Oil](#)" May 28, 2021). We had agreed with the consensus going into the meeting, that the cartel would increase production by 500,000 barrels per day for August, but instead, thanks to a very public dissent by the United Arab Emirates, the fourth largest producer, instead there was deadlock. Of course this has triggered the inevitable chorus of [headlines about the death of OPEC](#) – how many of those have we seen over the years? We don't see it that way at all. *OPEC is still very much the swing producer in a world in which post-pandemic oil demand is coming back unpredictably, and US production only recovers gradually.*

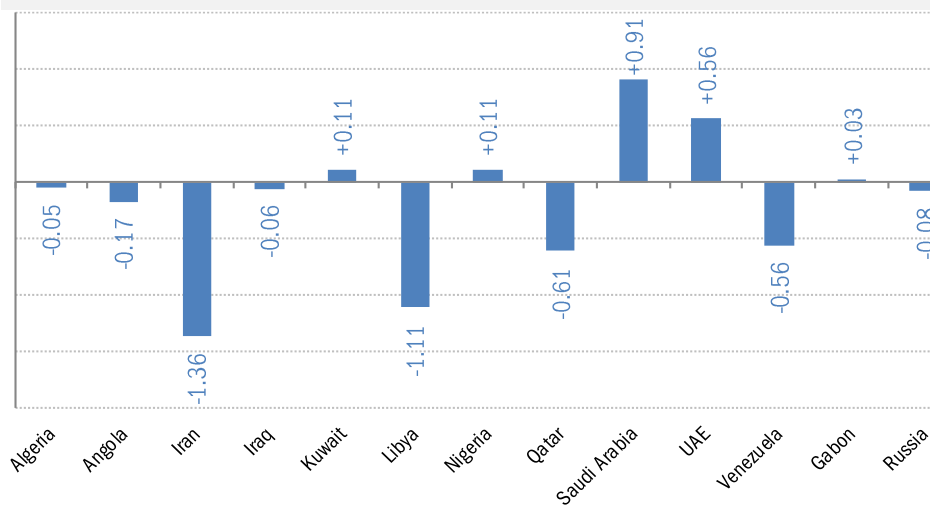
- July's already agreed 500,000 barrels per day production increase is still happening. No change there. That gives OPEC+ time to reach an agreement before August.
- We think the cartel will agree to a 400,000 to 500,000 barrels production increase from August to October – based on the premise that OPEC has been trying to look three months out.
- From November on, it really depends on demand.

Update to strategic view

OIL: The failure of OPEC+ to formally ease production quotas is not what we had expected, but it doesn't pave the way to \$100 oil. A 500,000 barrel increase is already on the books for July. Cartel members almost always cheat anyway. By next month Saudi is likely to find a way to accommodate the UAE's demand for a higher production baseline against which to measure quotas, although by the same logic Saudi would be entitled to the same and more. This will lead to production increases of 400,000 to 500,000 barrels through the end of the year. After that the existing quota system will expire in April 2022 anyway; it is not likely to be extended. With the restart of the Iran nuclear deal becoming less likely, Saudi can afford to make room for a little UAE oil rather than a lot of Iranian oil. Saudi wants to cement OPEC's role as swing producer, and its own reputation and influence in the region, especially versus Iran.

[\[Strategy dashboard\]](#)

Notional increase (decrease) in production baseline by rebasing from Oct 2018 to Apr 2020



Source: Bloomberg, TrendMacro calculations

- *And remember – it's the rule, not the exception, that the cartel members cheat. Production may well grow to meet demand whether or not official quotas do.*
- Most OPEC members do not want to extend production cuts past the current agreement's expiration in April 2022. A new deal with December 2022 as the end date is not going to happen at this time.
- *The UAE in particular wants a higher baseline of production against which quotas are measured – meaning, of course, they want to produce more right here and right now.* Instead of 3.1 million barrels per day, based on the October 2018 production level that all members had agreed to use, the UAE wants the baseline re-set at 3.7 million, where it was producing in 2020 before the pandemic production cuts.
- Using the same logic, Saudi Arabia's baseline would be almost 1 million barrels higher (please see the chart on the previous page). Saudi Arabia has taken the lead in promoting production discipline – so the UAE's logic puts the Kingdom in a difficult position.
- Especially as the restart of the Iran nuclear deal becomes less likely, keeping 1 million-plus barrels per day of Iranian crude off the market for the foreseeable future, *Saudi has more than enough room to make way for a little UAE oil instead of a lot of Iranian oil.*
- It's in Saudi's own interest to complete the agreement in harmony for two reasons. First, it shows that Saudi-led OPEC+ can indeed corral oil producers when needed, cementing the cartel's position as a swing producer. Second, it bolsters Saudi's prestige and position in the region versus Iran. Saudi has been very active diplomatically and commercially, forging new deals with [Iraq](#), [Pakistan](#) and [Qatar](#).

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Bottom line

The failure of OPEC+ to formally ease production quotas is not what we had expected, but it doesn't pave the way to \$100 oil. A 500,000 barrel increase is already on the books for July. Cartel members almost always cheat anyway. By next month Saudi is likely to find a way to accommodate the UAE's demand for a higher production baseline against which to measure quotas, although by the same logic Saudi would be entitled to the same and more. This will lead to production increases of 400,000 to 500,000 barrels through the end of the year. After that, the existing quota system will expire in April 2022 anyway; it is not likely to be extended. With the restart of the Iran nuclear deal becoming less likely, Saudi can afford to make room for a little UAE oil rather than a lot of Iranian oil. Saudi wants to cement OPEC's role as swing producer, and its own reputation and influence in the region, especially versus Iran. ▶