RESEARCH AND
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Oil market rebalancing remains a challenge

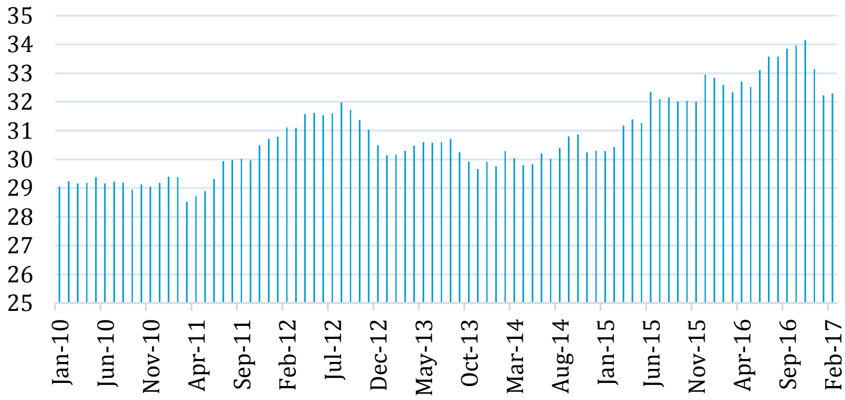
In August 2017, the monthly average Brent spot price rose by USD2.5pb MoM to USD51.9pb, recovering after prices fell below USD50pb in June-July. This happened on the back of falling US crude oil inventories for eight consecutive weeks, and slowdown of the pace at which producers have been adding drilling rigs. Although on the surface this may look bullish for oil, the decline happened because the US significantly increased oil exports.

There are still no substantial fundamental drivers for a rally in the oil market. OPEC's cuts do not take much out of the market, as raising prices in turn incentivize higher levels of shale supply. Moreover, it will be harder for the producers to sustain discipline in adherence to their pledge with the course of time. OPEC supply continues to matter, but more in terms of supply disruptions caused by possible tensions in the Middle East, turmoil in Venezuela and instability in Libya. Future rise in oil prices is expected to remain curbed by still high level of stocks and economic viability of a large volume of US shale oil. **As such, we maintain our average Brent price forecast for the rest of 2017 at USD50-52pb.**

Geopolitical factors in OPEC have major impacts on the oil market

In July 2017, OPEC crude production climbed to 32.8mln bpd, 230,000 bpd MoM higher based on secondary sources. This was due to the increase of supplies by Saudi Arabia, Libya and UAE. The IEA estimates OPEC's compliance at 75%. OPEC supply continues to matter, but more in terms of supply disruptions than supply management. OPEC and other non-OPEC producers by cutting oil production has led to raising prices and in turn incentivizing higher levels of shale supply. However, geopolitical factors within the cartel continued to have major impacts on the oil market, i.e. the return of disrupted supply to market from Libya and Nigeria.

OPEC oil supply, mln bpd (Jan 2010 - Jul 2017)



Source: Bloomberg, Samruk-Kazyna

Saudi Arabia to cut crude oil shipments in August

Saudi Arabia's oil production in July rose to 10.05mln bpd, slightly above its OPEC target, mainly due to an increase in domestic crude burning for power during summer. Saudi Arabia planned to cut crude oil shipments to its customers in August by more than 600,000 bpd to balance the rise in domestic consumption during the summer, while staying within its OPEC production commitment. Crude exports for August are expected to fall to their lowest level this year at around 6.6mln bpd. Crude exports to Asia for August will be reduced by about 200,000bpd to 3.5mln bpd, while exports to Europe will be down by around 70,000bpd at 520,000bpd. Exports to the US will be below 800,000bpd in August.

Iran's output reaches 8-year maximum

In July 2017, Iran produced 3.8mln bpd, 0.3% and 4.9% higher than MoM and YoY. This is the highest level of output since 2009. Iran crude oil supplies to India amounted to 502,000bpd, which was significant larger than 83,000bpd in June 2017. Oil supplies to Europe and Asia stood at 2.2mln bpd.

Libya's crude oil output nears 4-year high

Libya's crude oil output rose to 1.02mln bpd, 21% higher than MoM. The production was near a four-year high. Participants of an OPEC and non-OPEC monitoring committee meeting held on July 24 decided to allow Libya to increase production as high as 1.25mln bpd. The production has risen 60% since January 2017. Libya can ramp up production by 22% from current levels.

OPEC members oil output in June - July 2017, mln bpd

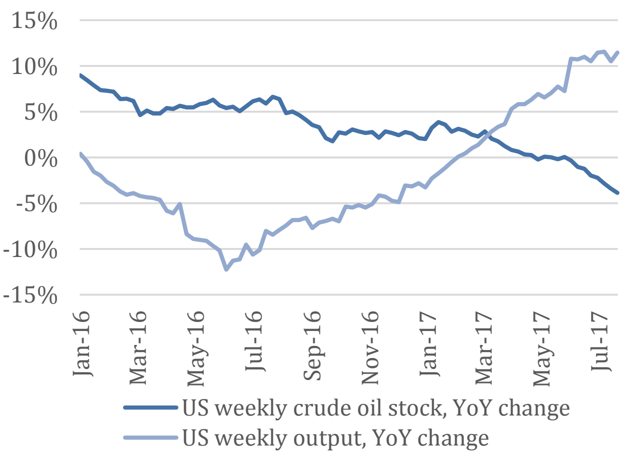
Country	Jul-17	Jun-17	Agreed cut
Saudi Arabia	10.05	10.02	-0.49
Iran	3.75	3.76	0.09
Iraq	4.48	4.48	-0.21
Kuwait	2.7	2.71	-0.13
UAE	2.93	2.9	-0.14
Qatar	0.61	0.62	-0.03
Algeria	1.06	1.06	-0.05
Libya	1.02	0.84	N/A
Nigeria	1.75	1.75	N/A
Angola	1.64	1.67	-0.08
Gabon	0.22	0.2	-0.01
Venezuela	1.97	1.97	-0.1
Ecuador	0.54	0.53	-0.03
OPEC	32.87	32.66	-1.17

Source: Bloomberg, Samruk-Kazyna

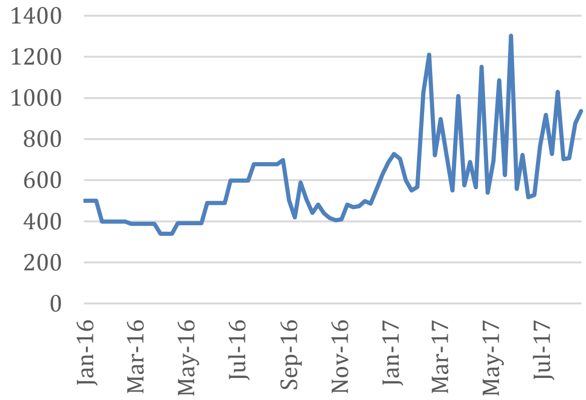
Competitive advantage of US producers is flexibility

US crude oil production increased by 1.25% MoM and 11.5% YoY to 9.5mln bpd in the week ending 18 August. US crude inventories continue their downward trend dropping by 3.3mln barrels during the week ending 18 August. This was for the eighth straight week. The pace at which producers have been adding drilling rigs also slowed down, falling to 763. Declining oil inventories may look bullish for oil; however this decline happened because the US significantly increased oil exports.

US weekly oil output and stock, YoY growth (Jan 2016- Aug 2017)



US weekly crude oil exports, '000 bpd (Jan 2016- Aug 2017)



Source: EIA, Samruk-Kazyna

The latest trade figures reveal that exports for the first eight months of 2017 averaged 0.8mln bpd up 59% from an annual average of 0.5mln bpd in 2016. It is estimated that about one-third of US exports in 2017 has flowed to Asia compared with just 10% in 2016. China accounts for 20% of US exports. Europe has emerged as the second key export market for US crude exports, accounting for 23% market share for the YtD.

Flooding caused by Tropical Storm Harvey resulted in investors' worries about negative implications of disruptions to refineries on demand for crude oil. Hurricane Harvey led oil majors Royal Dutch Shell, Anadarko Petroleum and ExxonMobil to evacuate staff and curb some oil and gas output at platforms in the Gulf. Approximately 25% of US Gulf of Mexico oil production is offline now.

One of the biggest advantages of the US oil industry is that it is extremely flexible. American drillers adapted to lower oil prices by reducing drilling costs and increasing production efficiency. US producers are enjoying the higher prices for future delivery, which they managed to lock in during the temporary price boost caused by OPEC.

Oil price trend and outlook

Average oil crude price stood at USD52.92pb in Jan-Aug 2017. In August 2017, the monthly average Brent spot price rose by USD2.5pb MoM to USD51.9pb, recovering after prices fell below USD50pb in June-July. This happened on the back of falling US crude oil inventories for eight consecutive weeks, and slowdown of the pace at which producers have been adding drilling rigs. Although on the surface this may look bullish for oil, the decline happened because the US significantly increased oil exports. Recent volatility in oil prices was caused by disruptions to refineries due to hurricane in Texas.

Brent price trend, USD pb (Jan 2016 – Aug 2017)

Source: Bloomberg, Samruk-Kazyna

There are still no substantial fundamental drivers for a rally in the oil market. OPEC's cuts do not take much out of the market, as raising prices in turn incentivize higher levels of shale supply. Moreover, it will be harder for the producers to sustain discipline in adherence to their pledge with the course of time. OPEC supply continues to matter, but more in terms of supply disruptions caused by possible tensions in the Middle East, turmoil in Venezuela and instability in Libya. Chinese demand, one of the world's main oil refiners, looks subdued, as the state refinery, Sinopec, has been reducing its oil refining output by around 240,000bpd between June and August due to weaker fuel demand.

Future rise in oil prices is expected to remain curbed by still high level of stocks and economic viability of a large volume of US shale oil. We expect volatility in oil prices to remain high for the remainder of 2017. As a result, we are maintaining our 2017 average forecast of USD50-52pb for Brent.

Oil price projections 2016-2017, USD pb

Price	2016 average	Average YTD, as at 28 August 2017	2017f average
Brent	48.69	52.92	**50-52^**

Source: Bloomberg, Samruk-Kazyna

^ represents in-house projection by Samruk-Kazyna, average price expected for 2017

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