

September 2019

MARMORE FIRST TAKE

Crude Awakening

Attack on Saudi Arabia
renew geopolitical risks;
Impact reverberates globally
across asset classes

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HIGHLIGHTS

1. Why did Oil prices rocket over 20 percent?

Drones attacked two of the major oil facilities in Saudi Arabia - Abqaiq processing plant (capacity 7 million barrels per day, mbpd) and Khurais oil field (production capacity of 1.5mbpd), on Saturday (September 14). Subsequently, oil prices rocketed upwards, with Brent, surging as much as 20 percent in the opening trade (Sep 16, 2019) to reach over USD 71 /bbl registering its highest intraday percentage gain since the Gulf War in 1991.

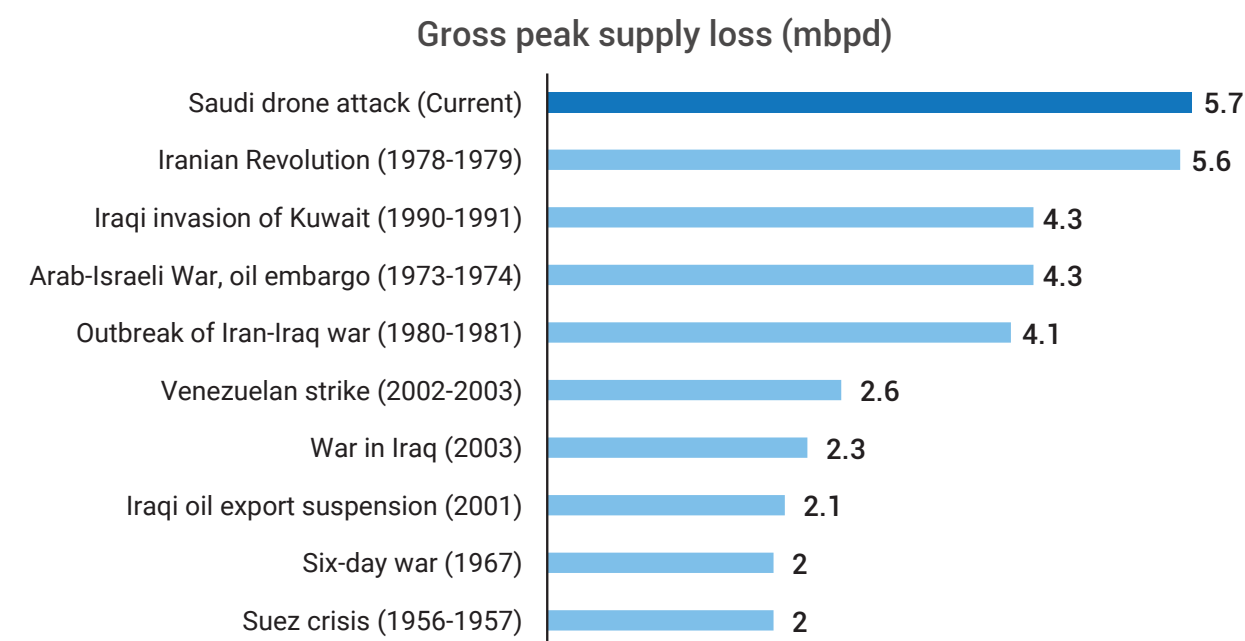
Abqaiq plant is the 'nerve centre' of KSA Oil Industry

Abqaiq processing plant is the largest oil processing facility of Saudi Aramco. The plant is strategically located, through which the country's oil and gas infrastructure flows. Disruption in Abqaiq plant could potentially affect oil exports, domestic refinery and energy needs.

2. How big is the attack in terms of oil supply disruption?

The attack has halted production of almost 5.7million barrels per day (mbpd) or 50 percent of its daily production or 5 percent of global supply. In addition to 2 billion cubic feet per day of natural gas and more than 500,000 barrel per day of Natural Gas Liquids (NGL).

Current attack on Saudi Arabia has led to the biggest supply disruption in history



Source: IEA, Bloomberg

The scale of impact on production and supply is uncertain yet. However, it is widely believed that the stocks from its storage facilities and strategic reserves would help to tide over the situation. Its current inventory stands at 187.9 million barrels. Saudi Arabia has 26 days of crude exports in storage at its main export terminal Ras Tanura. It also has storage facilities in Rotterdam (Netherlands), Okinawa (Japan) and Sidi Kerir (Egypt) that could be tapped, if required.

At a time when oil markets have been debating over tepid demand amidst expectations of weak global economic growth, the attack has brought into focus the reliability of oil supply. The risk is exacerbated as Saudi Arabia is one of the largest crude oil exporter.

3. How long could it take for production to resume?

Oil pipelines have been subjected to frequent attacks and are easier to repair; however, processing plants are a different realm and much will depend on the extent of the damage to ascertain its ability to resume production. Based on the commercial satellite imagery released by the U.S. it appears that a number of spheroid domes have been hit. Lack of off-the-shelf replacement components and the need to completely drain, clean and pressure test the systems for safety would take time. Given the complexity of the system, Bernstein research estimates that even a planned maintenance would take up to three months. Though the information and details are still uncertain, media reports that the task will be a complex one and that it would be a lengthy procedure.

4. What it means for the Oil price?

The markets need to price in the current supply loss along with a heightened geopolitics risk premium. A lot will depend on how fast the supply could recover, estimates range from few days to weeks. Supply outage for three to four weeks is expected to increase the oil prices by USD 6-10/bbl or 10 to 16 percent higher from Friday (September 13) closing value of USD 60/bbl. With new information coming forth and assurances by Saudi authorities, that the situation is contained along with the OPEC Secretary General Statement has already pared down the early gains witnessed on Monday (September 16). In the worst case, full-blown crisis due to a war-like situation could push oil prices over USD 100/bbl.

However, a charged political atmosphere with U.S pointing fingers at Iran for the attack and the response by Saudi Arabia would be keenly watched. The event has ratcheted up geopolitical risk in the region; the possibility of escalating tensions leading to future attacks warrants a higher geopolitical risk premium that could support higher oil prices for longer.

5. What would be the impact on Saudi Arabia?

Impact on Oil revenues

As per media estimates, of the 5.7 mbpd loss in production, 4mbpd would take weeks to be restored costing approximately USD 250million per day. Assuming it would take 4 weeks to resume full production, it could result in a revenues loss of over USD 7billion or 4.6 percent of its annual oil revenues.

Saudi Aramco IPO

The stakes are high for Saudi Aramco as it recently accelerated its plans for initial public offering (IPO), the success of which is integral to the ambitious economic reforms envisaged. Attacks on key assets could delay the IPO process. The valuation for Aramco is also bound to be lower as investor would now want to discount the vulnerability of future attacks on its assets.

6. What would be the global implications?

Sustained rise in oil price along with rising geopolitical tensions would be bad news for global economy. Business investment and economic growth globally are already weighed down by policies of central bankers and an unresolved U.S –China trade war. In general, oil price rise driven by increasing demand is construed favourably as it is a sign of healthy economy. On the other hand, oil price rise led by supply disruptions and geopolitical risks have historically been negative for equities.

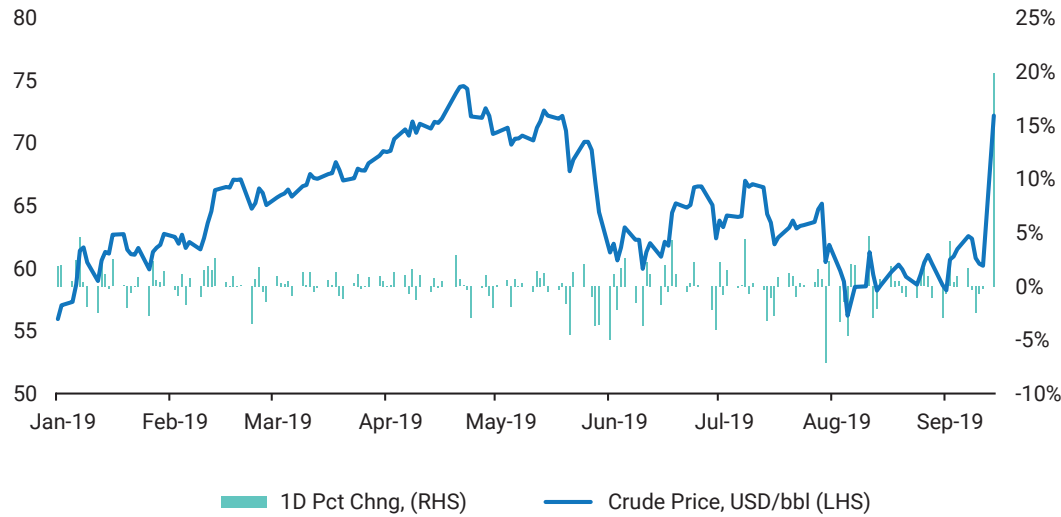
Energy importing countries, mostly those from the Asian region such as China, India and Indonesia could feel the impact through various macro channels such as widening trade balance, higher inflation, and weakening exchange rates.

Impact on stock market

In the short-term, shares of energy companies could increase while those that are dependent on oil and petrochemical derivatives for raw materials such as airlines, paints and packaging materials could decrease. Following the attacks on Saturday, Saudi Arabian main index -Tadawul opened on Sunday (September 15) with a loss of 2.4 percent. However, over due course it pared down the losses and closed with a loss of 1.0 percent. While an increase in oil price is normally market positive, in this case it can be market negative due to geopolitical fears.

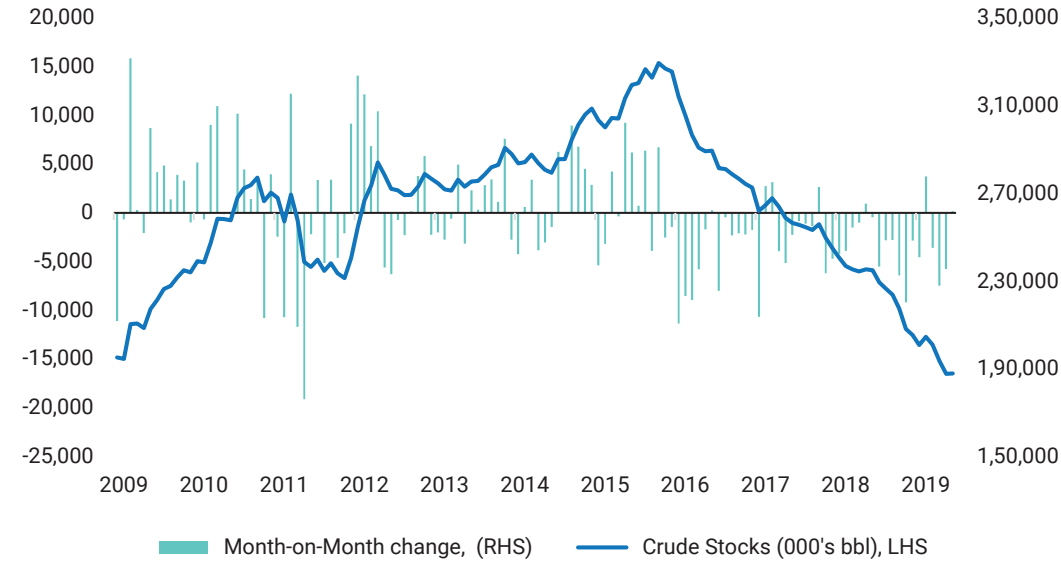
Appendix

Brent crude prices registered its biggest opening since Gulf war in 1991



Source: Reuters; September 16 (2019) opening price is considered

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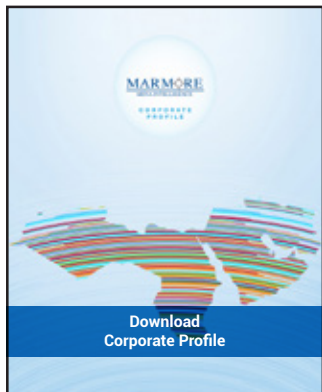


Source: Reuters; Data as of June 2019

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Marmore MENA Intelligence provides research-based consulting solutions to help understand current market conditions, identify growth opportunities, assess supply/demand dynamics, and make informed business decisions.

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- » Deep understanding of MENA market and access to wide-ranging database
- » Delivers high quality, client specific, insightful research reports; highlighting key client issues and uncovering key answers/opportunities for the clients.

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