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THE OPEC DEAL: WHY IRAQ'S WORDS MATTER

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By Nick Cunningham

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OPEC could extend its production cuts through the end of 2018 in an effort to rebalance the market, according to comments from Iraqs oil minister.

A few OPEC members even want the cuts to be deepened, Iraqi Oil Minister Jabbar al-Luaibi said at an oil conference in the UAE. Some think that cuts should be extended beyond March, three or four months, or six months, or maybe till the end of 2018, al-Luaibi said. Some, like Ecuador and other countries, even Iraq, think there should be another cut of 1 percent.

OPEC officials have time and again hinted at possible actions as a way of influencing market sentiment. Often, the jawboning works, at least temporarily. Sometimes it can backfire if it raises expectations too much.

The latest iteration of this game of market psychology came a few weeks ago when top OPEC officials suggested they were considering a three-month extension, pushing the deal out through June 2018. It wasnt exactly an overwhelming show of force, and oil prices didnt move all that much on the rumors.

Most oil analysts are of the view that the OPEC cuts are working, but only if they remain in place. There is no shortage of projections from investment banks, energy watchers, and government forecasters that see oil prices crashing if OPEC abandons the cuts at the end of the deal in March 2018. That is why OPEC officials are laying the groundwork for a possible extension.

But the comments from Iraqs oil minister are more significant, for a few reasons.

First, and most obvious, is that he says the group is considering much longer cuts. Extending the

output limitations through 2018 would go a long way to reassuring the market that a return to full production is off the table for now.

Second, he hinted at deeper reductions. That would be a heavier lift for OPEC and the non-OPEC participants and there would certainly be some countries resistant to such an outcome. A few months ago Ecuador decided it could no longer cooperate with the production limits because of the financial burden involved. Asking struggling producers to cut deeper would require a heavy sacrifice. Still, if OPEC pulled it off, it would be a lot more bullish for oil than a simple extension.

A third reason why the latest rumors are more significant than previous comments are because of where they are coming from. Iraq has been one of the laggards to the agreement, failing to fully comply with its promised output cuts for most of this year, so the cooperative tone from Iraqs oil minister carries more weight than if it had come from Saudi Arabia or Kuwait.

In fact, compliance has improved lately, with Iraq in particular carrying out deeper cuts. Iraqs oil minister said his country is now producing less than what is required as part of the deal output stands at 4.32 mb/d, below its ceiling of 4.35 mb/d. That has contributed to more confidence in the OPEC deal, which is putting the oil market on a positive trend, al-Luaibi said.

Others dispute those figures, but whatever the exact production figures are, there is a general sense that Iraq is improving its compliance rate. Nevertheless, Iraqs spotty record warrants some skepticism, analysts say. News that Iraq is giving positive signals about supporting deepening cuts is helping oil prices, Nitesh Shah, commodities director at asset management firm ETF Securities, told the Wall Street Journal. But, Iraq hasnt complied with its portion of the quota since this started so [prices] could come off very quickly, he warned.

The improved compliance rate comes at a time when Saudi Arabia is also specifically trying to target oil exports in order to take more barrels off of the global market. Saudi Arabia said that it will lower its exports by 350,000 bpd in October even though there is plenty of demand for its crude. Despite refiners request for more crude, the decision was made to maintain cuts, an industry source told Reuters earlier this month. That could help improve the oil market outlook in the months ahead.

The expiration date of the current deal is drawing closer, and more importantly, there is one major official OPEC meeting left on the calendar (November 30) before that date arrives. That makes the upcoming meeting in Vienna in two months the crucial deadline for an extension.

Kaynak/Source: