POTEN TANKER OPINION

The Haves And The Have Nots

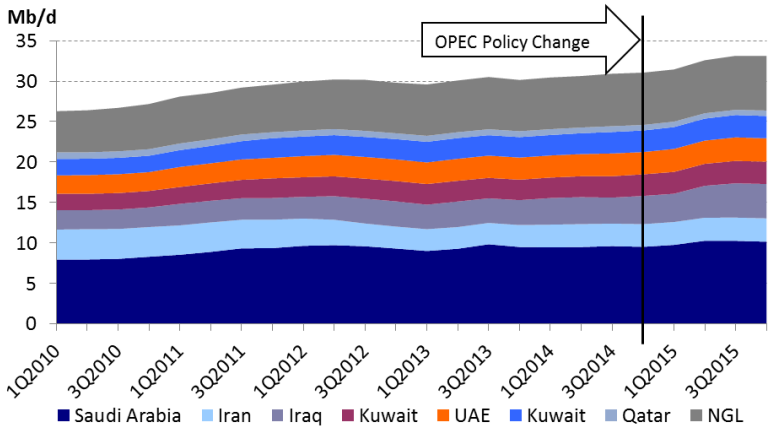
Not all OPEC producers are created equal

During their meeting on 27 November 2014, the members of the Organization of the Petroleum Exporting Countries ("OPEC") decided not to cut production to arrest a slide in global oil prices. The next day Brent oil fell more than $6 to $71.25, a price decline described at the time as "sending benchmark crude plunging to a fresh four-year low". Ah, the good ol' days ... Yesterday, the price for Brent crude fell as low as $29.92 per barrel and some analysts think it can go much lower. In the early years of the oil industry, John D. Rockefeller's Standard Oil would sometimes flood the market with crude, pushing the price of oil down to put pressure on his competitors. This strategy was sometimes referred to as a "good sweating". It has been speculated that OPEC is implementing its version of this strategy in an attempt to squeeze out some of the higher cost non-OPEC production like U.S. shale and Canadian oil sands. Whether it is a deliberate strategy or not, it is important to point out that the 13 OPEC member countries are very different based on their capacity to increase production and their ability to withstand low oil prices. For this discussion I would like to split OPEC into two groups: the 'Haves' and the 'Have-nots'.

The Haves are the OPEC members that have the capacity to increase production and have done so since 2014. The producers in this group include Saudi Arabia, Iraq, Iran and some of the other Middle Eastern producers. Combined, these countries have ramped up production by almost 2 million barrels per day (excluding a reduction in the Neutral Zone and including NGLs) when comparing fourth quarter averages for 2015 with the same period of 2014. The biggest increases came from Iraq (+750,000 b/d) and Saudi Arabia (+630,000 b/d). Smaller growth came from the UAE, Kuwait and Iran. For 2016, Iraq's output is expected to increase further, while Iran has ambitious plans to increase production and exports following the lifting of the sanctions related to their nuclear program. Iranian output could increase by as much as 700,000 b/d this year. While by no means compensating for the significant drop in oil prices, higher production does cushion the blow somewhat in these countries.

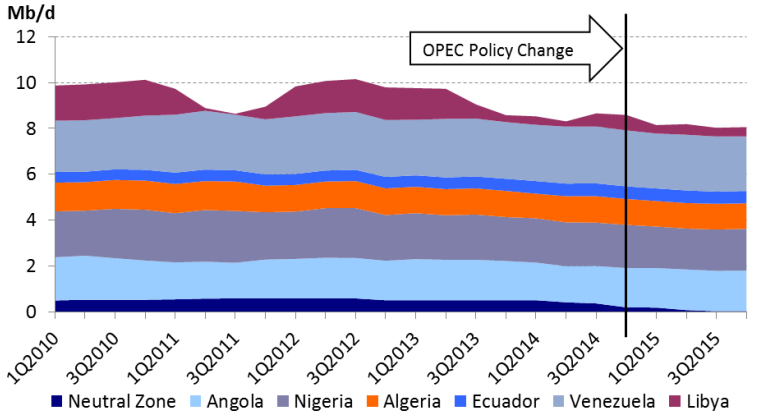
The Have-nots are the OPEC members that do not have the capacity to raise production or – even worse – are faced with declining output. Countries that are facing particular challenges include Nigeria, Libya and Venezuela. Nigerian production has been around 1.8 – 1.9 mb/d in recent years, well below the 2.25 million b/d level reached in 2011. Libya's challenges have been well documented. Before the Arab Spring revolution that removed Muammar Gaddafi from

Fig. 1: 6 OPEC Countries with Expanding Production



Source: IEA

Fig 2: OPEC Countries with Stable or Declining Production



Source: IEA

power in 2011, Libya produced more than 1.5 million b/d. Since then, the conflict between rival factions has brought the oil industry of the country to a near standstill. The IEA estimates that Libya only produces 380,000 b/d at the moment. The third country in this group is Venezuela. Low oil prices have wreaked havoc on the Venezuelan economy, which depends on crude oil exports for 96% of its export earnings. Venezuela is the country with the largest proven oil reserves in the world (estimated at 298 billion barrels at the end of 2014 according to the BP Statistical Review of World Energy), but at the same time state owned oil company Petroleos de Venezuela S.A. is struggling to maintain production at around 2.4 million b/d.

While the oil industry is suffering from this "good sweating", the tanker market has benefited from the abundance of crude produced and exported by OPEC, especially the countries in the Middle East. Long-haul exports originating from the Arabian Gulf provide an important multiplier effect on tanker demand, while some of the countries that are struggling, like Libya and Venezuela, have a customer base that is, at least partially, closer to home. The larger crude carriers, in particular the VLCCs, are therefore the main beneficiaries of OPEC's largesse. Aframaxes, which rely more on short-haul crude movements, have been less impacted by the changes OPEC output.