

Commodity

21 April 2024

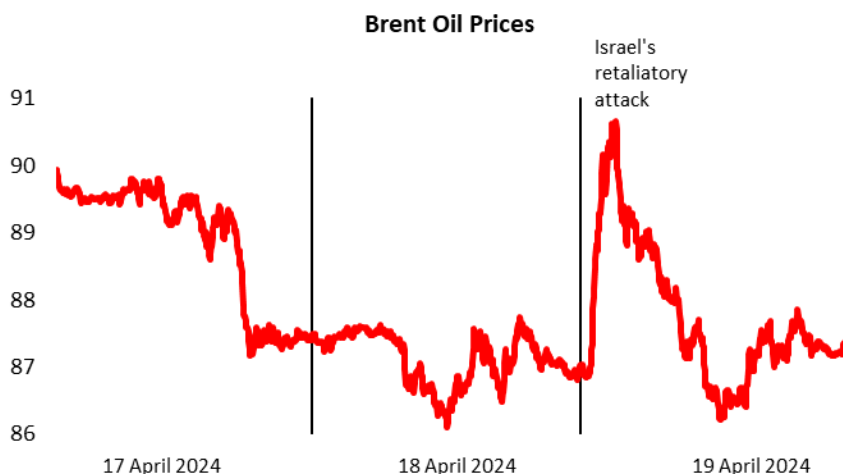
Oil: Skittish On Geopolitics

- Geopolitical tensions have spiked over the past week as risks of widespread conflict across the Middle East intensified.
- We see the risks becoming fairly binary at this point of a de-escalation or escalation in tensions, at least over the coming weeks.
- The situation warrants close monitoring. For now, our baseline forecasts remain for WTI and Brent oil prices to average USD79/bbl and USD85/bbl in 2024.

Geopolitical tensions have spiked over the past week as risks of widespread conflict across the Middle East intensified. Iran and Israel directly attacked each other over the past week, leaving market participants on tenterhooks. As with past episodes of heightened geopolitical tensions, the first point of impact was global oil prices. Crude oil futures saw intraday prices jump more than 4% on 19 April 2024. Gains were, however, pared back after Iran downplayed the attacks by Israel on its soil and announced that it has made “no plan to retaliate immediately”¹.

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Source: Bloomberg, OCBC

To be fair, recent one-on-one attacks between Iran and Israel were telegraphed prior to the event by both sides. Israeli PM Benjamin Netanyahu warned that Israel “reserves the right to defend itself” against Iran over its drone and rocket barrages on 13 April². Prior to which, Iran had publicly stated its intention to seek retribution for the assumed Israeli attack on its embassy in Syria³. The origin of recent heightened tensions can be traced back to October 2023.

¹ Tehran Plays Down Reported Israeli Attacks, Signals No Retaliation, *Reuters*, 20 April 2024.

² Netanyahu Says Israel Reserves the Right to Defend Itself. *Bloomberg*, 17 April 2024.

³ Israel has not officially taken responsibility. However, Iran said it would take revenge on Israel for the airstrike that killed its generals and military advisers at the embassy compound in Syria. Iran Vows Revenge on Israel After Damascus Embassy Attack. *Reuters*, 03 April 2024.

Date	Key Events
07 October 2023	Hamas Attack into Israel
29 October 2023	Israel Ground Invasion into Gaza
19 November 2023	Red Sea Crisis
28 January 2024	Attack on US Forces which Led to Three Servicemen Killed
01 April 2024	Bombing of Iranian Embassy in Damascus, Syria
13 April 2024	Iran Drone and Rocket Attack Into Israel
19 April 2024	Israel Drone Attack into Iran

Source: Bloomberg, Reuters, OCBC

Notwithstanding, tensions are balanced on a knife's edge. We see the risks becoming fairly binary at this point of a de-escalation or escalation in tensions, at least over the coming weeks.

(A) Under a scenario of de-escalation, global diplomatic efforts will take hold. Direct Iran-Israel attacks will be contained but tensions in Gaza may continue. The geopolitical risk premium that has been priced into Brent oil prices over the last two weeks would likely start to unwind as the threat of broader regional conflict de-escalates. This outcome is similar to our base case under which we forecast Brent oil prices falling back USD90/bbl by end-June 2024. That said, we would expect Brent oil prices to remain elevated around USD86/bbl in 2Q24.

(B) Under the alternative scenario of an escalation to a broader regional conflict, we do not rule out a series of tit-for-tat attacks between Israel-Iran. Brent oil prices could top USD100/barrel, touching USD120/barrel, reflecting fragile risk sentiment and market edginess of every incident sparking a wider escalation.

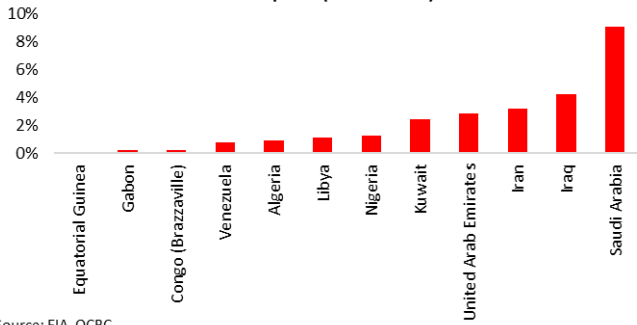
Under these circumstances, further sanctions on Iran and trade routes blockages in the Strait of Hormuz (SOH) cannot be ruled out. The US, which has already issued new sanctions on Iran on 18 April and 21 April⁴, will issue further sanctions to constrain the government. The lowest hanging fruit would be Iranian oil exports being curtailed. Iran's crude oil output in March 2024 was 3.3mbpd and its share within the OPEC-12 was 12%. Iran's crude oil output relative to global oil consumption was ~3% in March⁵.

Retaliatory action could include closing of the SOH, which is a critical transit route for oil from the Middle East to the rest of the global oil market. An average of 20 mbpd of oil (~30% of global seaborne oil trade) passed through the route between January-October 2023, according to the International Energy Agency (IEA). Any disruption to oil flow in this node will have severe implications to the global oil market.

⁴ The sanctions on 18 April targeted 16 people and two entities linked to the production of Iranian unmanned aerial vehicles (UAV), or drones. The US also sanctioned five companies that provide materials for steel production to Iran. US and Britain Announce New Iran Sanction After Missile and Drone Strike on Israel. *Reuters*, 19 April 2024. The House passed further sanctions on Iran on 21 April to include foreign ports, vessels and refineries that knowingly process Iranian crude in violation of existing sanctions. The bill extends sanctions to cover all transactions between sanctioned Iranian banks and Chinese financial institutions used to purchase petroleum and oil-derived products.

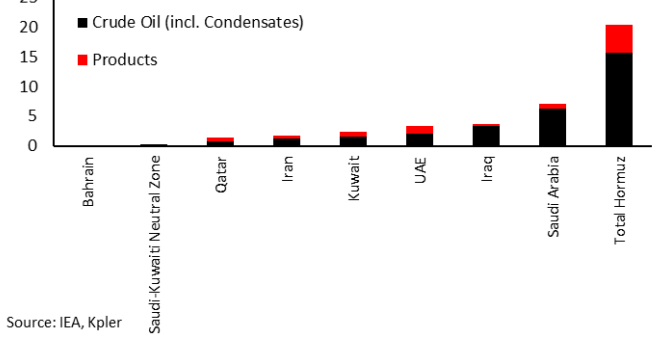
⁵ US Energy Information Administration, *Short-Term Energy Outlook*.

OPEC-12: Crude Oil Production Relative to Global Oil Consumption (March 2024)



Source: EIA, OCBC

Oil Exports Through Strait of Hormuz Between January-October 2023



Source: IEA, Kpler

The situation remains fluid and we will continue monitoring implications closely. From a macroeconomic standpoint, we will closely monitor whether oil prices will rise beyond USD100/bbl and importantly persist at those levels. For now, our baseline forecasts remain for WTI and Brent oil prices to average USD79/bbl and USD85/bbl in 2024.

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