THE SPECIALIST IN TRADING AND INVESTMENT

Hellerup, 18 June, 2014

Oil markets on edge as Iraq developments dominate agenda

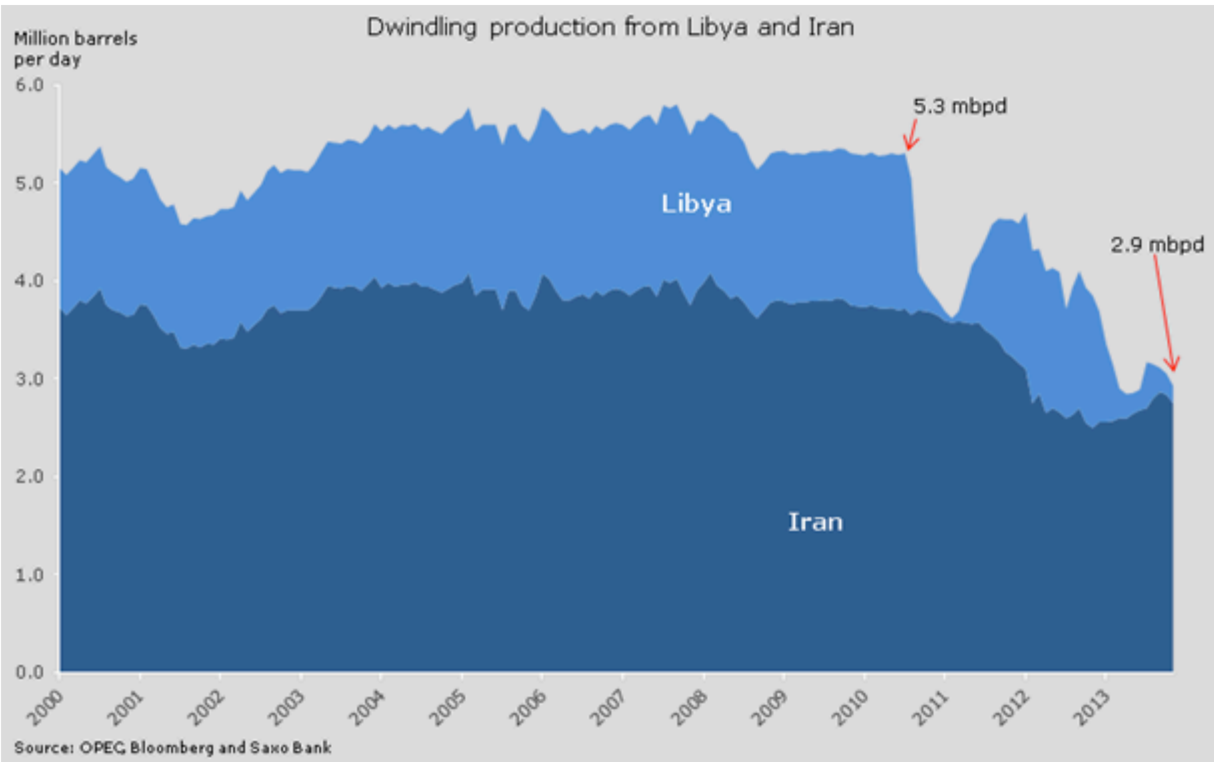
By Ole Sloth Hansen

Crude oil markets have been relatively calm so far this week with Brent crude oil settling into a range following the spike last week. The rally was triggered by renewed worries about stability in Iraq following vicious attacks by Sunni militants to the north and western parts of the country.

Iraq has become a key OPEC producer during the past couple of years, not least considering the sharp drop in exports from Libya. For now the key oil producing regions of the Kurdish controlled north eastern Iraq and the Shiite controlled south remain relative calm and this has helped Brent crude settling into 112 to 114 USD/barrel range but with 3.3 million barrel of daily production at stake the market remain very nervous.

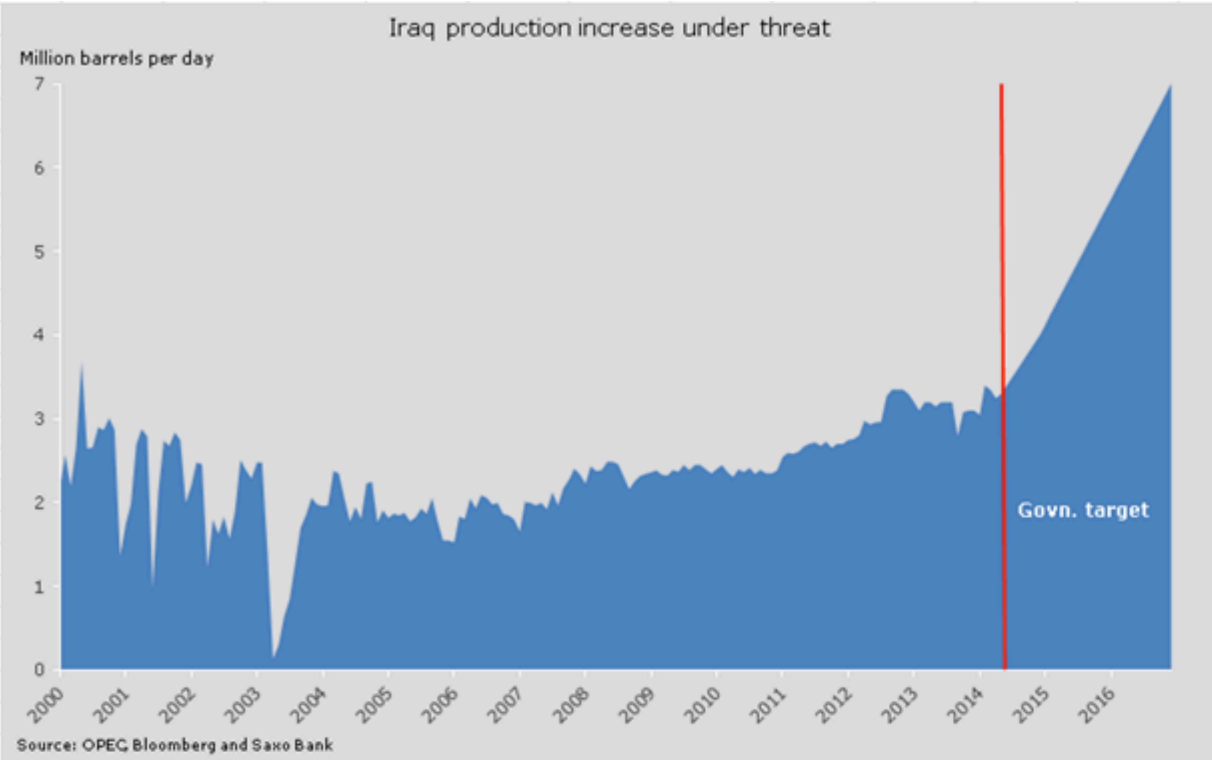
So far the militants have managed to break into Iraq's largest refinery Baija and some damage has been reported but international exports though Turkey to the North and Basra to the south remain unaffected which helps to explain the current calm in the market.

Iraq has risen to become OPEC's second biggest producer during the past couple of years during which time supply disruptions from Libya and the embargo against Iran has seen the combined production from these two countries drop by around 2.4 million barrel per day since the Arab Spring began in late 2010.



During the same time, Iraqi oil production has risen by almost one million barrels per day and up until now the government has been very bullish on the prospect for an even higher production. From current levels around 3.3 million barrels per day they been looking for an increase towards 4 million by the end of year rising to 7 million by the end of 2016.

These targets are now looking unreachable which raises even further the pressure on Saudi Arabia to increased production to avoid oil markets becoming too tight, especially during the next quarter which is a period of peak demand. Saudi Arabia just recently said they preferred a price of a barrel of oil in the 95 to 110 USD/barrel range, somewhat below current levels.

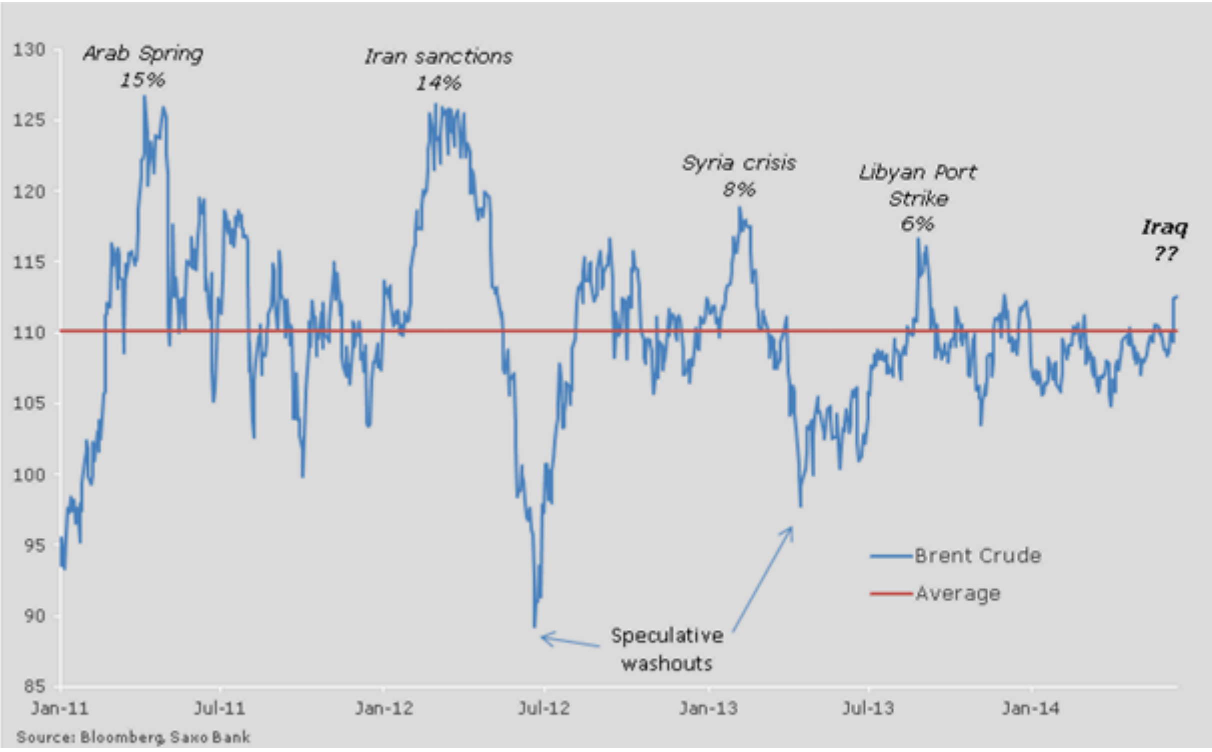


Despite the current worries the world has recently been witnessing less volatility in oil prices than during any time in recent history. The sharp increase in non-OPEC production, especially in the US has helped remove some of the worries of Middle East and North African supply disruptions. We have witnessed several geopolitical scares since 2011 but as the chart below shows, the impact of these have resulted in ever smaller price reactions.

WWW.SAXOBANK.COM SAXO BANK A/S Philip Heymans Allé 15 2900 Hellerup Denmark
Telephone: +45 3977 4000 Telefax: +45 3977 4200 Reuters Dealing Code: SAXO Cvr. nr. 15 73 12 49 info@saxobank.com

THE SPECIALIST IN TRADING AND INVESTMENT

If the current crisis is being maintained at current levels we should probably not look for Brent crude much higher than USD 115 while any realised threat to supplies could see a return to the 2011 and 2012 peaks and possibly beyond. Nothing ever goes just one way and with the hedge fund community once again holding a record net-long exposure in the market any move towards solving the issue could result in the price fall by 5 to 10 USD/barrel. This would remove some of the geopolitical risk premium but not all as we still have Libya producing less than 15 percent of capacity.



For more information

Ole Sloth Hansen, Head of Commodity Strategy, Saxo Bank A/S
Email: olh@saxobank.com
Phone: +45 3977 4810

Ole Sloth Hansen is a specialist in all traded Futures, with over 20 years' experience both on the buy and sell side. Hansen joined Saxo Bank in 2008 and is today Head of Commodity Strategy focusing on a diversified range of products from fixed income to commodities. He previously worked for 15 years in London, most recently for a multi-asset Futures and Forex Hedge fund, where he was in charge of the trade execution team. He is available for comments on most commodities, especially energies and precious metals.