PRESS RELEASE

A further tightening of the oil market

Bucharest, April 25th, 2023 – In early April, Saudi Arabia, Iraq, the United Arab Emirates, Kuwait, Kazakhstan, Algeria and Oman announced combined oil output cuts of more than 1.1 million barrels per day (b/d), surprising the markets. This commitment follows a first production cut announced in October 2022 by OPEC+. It comes in addition of Russia's decision to cut output by around 500,000 b/d in reaction to the implementation of a EU ban on seaborne imports of Russian oil and oil products.
In total, the cuts represent about 3.7% of global demand. They reinforce Coface's view that oil market tensions will persist throughout 2023. With the return of actions from producing countries, the long-awaited drop in prices is unlikely to occur despite the uncertainties around global economic growth. Coface thus leaves unchanged its forecast of volatility on the market and a price of $90/barrel in 2023.

An announcement that came as a surprise… but is not without basis

The announcement of the production cut and its magnitude came as a surprise after OPEC+ officials had suggested that no adjustment was necessary. However, there are many reasons for the decision.

- The reduction is "a precautionary measure aimed at supporting the stability of the oil market ". OPEC+ believes that the outlook for oil demand is less robust. The recent turmoil in the banking sector has reminded that the economic environment leaves little room for complacency. Coface shares this point of view and forecasts a slowdown in global GDP growth to 2% in 2023, after 3.1% in 2022.
- Oil prices had fallen significantly. They reached a low point, nearly 48% off the $139 peak reached after the Russian invasion of Ukraine. This move therefore aims at pushing prices higher, while many oil producers are probably uncomfortable with prices below $80.
- This decision is a reminder of the cartel's ability to exercise a pricing power at a time when production growth of U.S. shale oil players is muted. They are indeed affected by the tightening of credit conditions, productivity slowdowns in aging shale basins, as well as some labor shortages.
- Finally, some tensions with Washington over its use of strategic petroleum stocks (SPR) have also arisen. The U.S. administration ordered an unprecedented drawdown of these stocks to contain rising prices after the war in Ukraine and recently indicated that replenishing these stocks would take several years.

The heightened tensions are not without risk to the global economic outlook while they should support the oil industry revenues

The EU's ban on seaborne imports of Russian crude oil had already kept oil markets under pressure despite weak demand. This tension has been exacerbated and Coface expects oil prices to remain volatile, with a trade range of $90-110 in the second half of 2023. The OPEC+ decision should also coincide with a more meaningful economic recovery in China. As China is one of the world's leading oil consuming countries (around 40% of marginal consumption

between 2000 and 2019), a faster and/or stronger rebound in the economy will further tighten the supply-demand balance, pushing prices higher.

At the global level, these upward pressures on oil prices could be a game changer for the inflation outlook. Indeed, while lower energy prices has been one of the main drivers - if not the only one - of lower inflation in advanced economies in recent quarters, the contribution could reverse in the second half of 2023, which would again put pressure on overall inflation rates.

The OPEC+ decision also highlights widening relations between the U.S. and Saudi Arabia. Joe Biden called on the country and other OPEC members to increase production in order to limit Russia's revenues, which are helping to finance the war in Ukraine. The decision to reduce production was thus qualified as "inadvisable" by the White House and marks a new step in the rift between the two countries. Beyond energy policy, the US administration has been watching closely at deepening ties between Saudi Arabia and China, notably illustrated by the Kingdom's agreeing to join the Shanghai Cooperation Council as a "dialogue partner".

However, this announcement is good news for oil and gas companies. Their already strong profitability levels will benefit from higher prices. Western oil & gas companies have reported profits of $219 billion in 2022. With a forecast of $90/barrel, Coface expects their profits to reach around $160 billion in 2023.

COFACE MEDIA RELATIONS
Diana Oros: T +40/374 670 886 - diana.oros@coface.com

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