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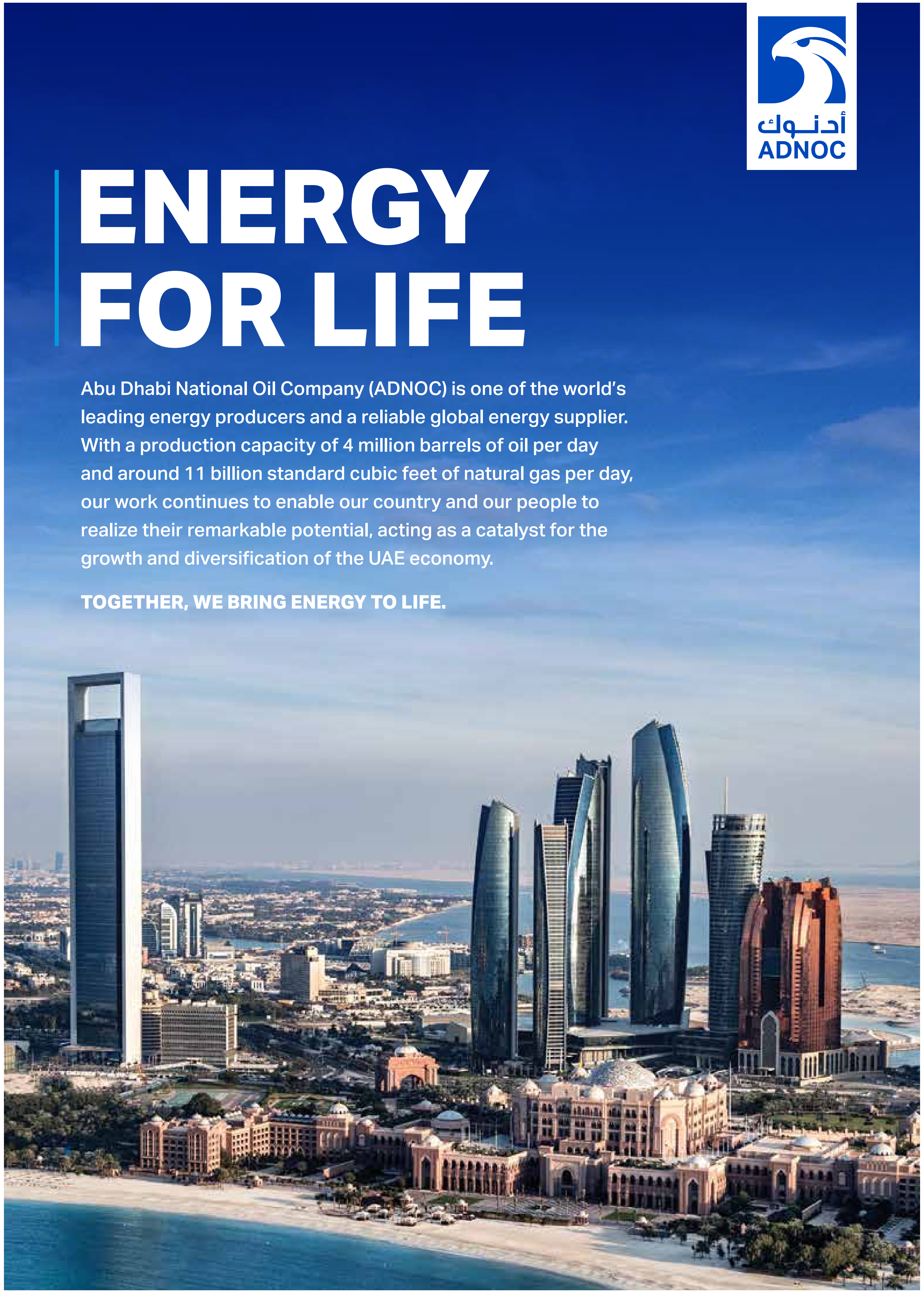
United Arab Emirates

SPECIAL REPORT

ENERGY MARKETS OUTLOOK 2023

Certainty is the Only Cure for Market Volatility



SPECIAL REPORT Oil Market Outlook?

Contents

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Foreword

Waves of turbulence are raising the eyebrows of even the most stoic of oil stakeholders, with intensifying calls to support black gold to help re-stabilize global energy security. There are many different, and some conflicting, drivers. The collapse in global oil inventories, the lack of spare oil production capacity, and limited investment in the oil sector amid a maturing climate agenda are some of the factors pushing oil prices to 8-year highs – knocking on the door of $100/bl.

As world leaders prepare to gather in coming weeks in Egypt for COP27, the world's biggest annual climate event, global oil demand is expected to bounce back above the key level of 100mn b/d – a level last seen before the COVID-19 pandemic.

The Port of Fujairah, with its strategic position outside the Strait of Hormuz, has risen rapidly in the last two decades to become the world's third largest global bunkering port, after Singapore and Rotterdam. At the Fujairah Oil Industry Zone (FOIZ), just north of the main city, the landscape between the rugged mountains and the sea is dominated by rows of tall, cylindrical oil tanks on both sides of the highway. Analysts have forecast that the Emirate is likely to experience another busy year, given incremental crude trade out of the UAE and broader Middle East, with rising production from the Arab Gulf OPEC+ producers.

How can Fujairah take advantage of what might be the foothills of the final boom in oil?

The launch of the ICE Futures Abu Dhabi (IFAD) Murban oil futures contract last year, in partnership with the UAE's state-owned Abu Dhabi National Oil Company (ADNOC), could help build on Fujairah's success to create a major oil trading hub in the East of Suez physical oil market. Energy giant ADNOC has stated that Fujairah is at the center of the national oil company's (NOCs) strategy to go beyond the border of the UAE, saying: "Fujairah is becoming a tipping point between the producers, exporters, and traders." Plus, the oil storage industry is at a crossroads with the energy transition gathering pace and new fuels emerging. In this Special Report, we explore how the Port of Fujairah and the broader region can successfully adapt to this rapidly changing landscape.

Oil: What to Expect in 2023?

Pinning down expectations in a market renowned for its unpredictability is now harder than ever. But the Port of Fujairah's vast infrastructure, evolving relationships, and coveted location make it one of the best-placed hubs worldwide to support stakeholders as the oil supply-demand whirlwind gives them proverbial whiplash.

Geopolitical volatility and soaring momentum behind the energy transition are keeping many investors away from oil. A lack of new supply to the market could last till 2025, with the exception of the US' shale recovery, some stakeholders warn. The implications for global energy security – a system still embedded in the tried-and-tested fossil fuel market – could be dire. This fragility is currently illustrated by how Russia's invasion of Ukraine since February 24 has triggered severe instability across energy markets worldwide. There are some brighter spots emerging, however, including ADNOC's plans to ramp up its oil production capacity by approximately 70% to 5mn b/d by 2025, instead of 2030.[1]

The impact of decisions made by some of the world's biggest economies – including the US, EU, UK, Japan – to put price caps on Russia's oil in coming months have not been sufficiently considered, some stakeholders flag. The knock-on effect on European industries and exporter-importer dynamics, especially in Asia where much of Russia's flow is now expected to go, need more thought. More Russian oil is also expected to go to India – though this will be limited by New Delhi's term contracts with the US and West Africa – and African nations.

Differentiating between short-term and long-term balances in the oil market is vital, i.e., do not sacrifice longer-term growth and stability because today's landscape is so uncertain.

Fujairah pushes ahead

The port achieved record highs in August this year, managing 7mn tons and more than 261 vessels. Such records could continue as the port – home to the largest capacity and flexibility in the region – can increase its volume capacity by up to 15% to further support oil and other energy markets, as per its Master Plan. Plus, the port's sub-10 hour average waiting time for vessels enhances business value in today's strained market, where the cost of a vessel's hour-by-hour operations face extra scrutiny. A global reputation for quality and growth means the port's loyal team of skilled manpower ranks among the best in the global tank storage industry.

How do we get markets to invest in oil? Because oil demand is here to stay.

Advantage of speed

The COVID-19 pandemic was a challenging time for the logistics industry. As soon as the pandemic became a clear concern, the port adapted to the precautions and procedures to control the spread of the virus without interrupting any services – safety and continuity that our stakeholder community deeply valued. Consequently, the port successfully navigated the pandemic and became the first port in the region to resume crew change services, which was a big relief for the maritime industry. Our oil handling volumes actually peaked during the pandemic, while we sustained our world-class level for vessel waiting times (4-7 hours). Most importantly, the port's safety record remained robust; there was no lost time due to injury, impressive for such bustling operations. Ensuring our operations remained streamlined enabled the port to sustain its critical role as a premier hub and trade location between East and West, for local and international goods.

Content harvested from brainstorm session hosted By Port of Fujairah

Oil's Black Hole: What's Next?

Do not expect today's extreme opacity to evaporate by year-end. Disruption will be the norm well into 2023, propelled by unstable geopolitics, notably Russia's invasion of Ukraine and pending sanctions by some of the world's biggest economies. While OPEC+ did a good job balancing supply-demand dynamics as we emerged from the worst of the COVID-19 pandemic, it now faces a far steeper cliff of guesswork. The degree of uncertainty in both supply and demand is not something the market often sees; how oil prices and appetite for much-needed investments in fossil fuels respond remains to be seen.

The drivers of today's pressure cooker are mounting; the war in Europe, intensifying economic concerns, reduced investment in fossil fuels, an ambitious climate agenda in an extremely squeezed timeframe, to mention a few. This broader picture is unsurprisingly tightening funds; there is no / very little investment appetite in Europe, for example. The finance sector in China was once willing to support an unsecured loan for $50mn. That is no longer the case, in China or elsewhere, with syndicated financings with bigger players becoming the primary route. This restricted access to funds – especially for smaller players unable to compete at the level required for multi-billion syndicated finances – powers more ambiguity.

Amid the nervousness, a few governments and companies' intentions to support oil are clear and bold. For one, ADNOC, which pumps almost all the OPEC member's oil, wants to be able to produce 5mn b/d by 2025 – five years sooner than initially planned. Such momentum is critical to encouraging other governments, state-owned entities, and private companies to come to the fore. The message must be clearly shared: pulling back on oil now will wreak havoc on energy security very quickly. The retraction seen in oil does not generally apply to gas and LNG markets at the moment. In fact, the crises appear to have renewed international oil companies' (IOCs) appetite to invest in these markets.

> We are in a self-feeding cycle. Higher interest rates, more volatility, less liquidity, which feeds more volatility, and less liquidity. How do we end that cycle?

Russia eyes Africa

There is growing fatigue in Europe surrounding the Russia-Ukraine war, especially as the financial strain on those economies increases. This may make it difficult for some countries to find a consensus on what to do next as Russia continues to re-write the diplomatic rulebook. Meanwhile, Moscow has spent a lot of geopolitical effort building links with several African nations, which gives the exporter an advantage as it seeks new homes for its oil.

China and broader Asia can only import so much, especially if the pricing is less attractive, so heading West of Suez may be part of Russia's near-term strategy. Such engagements with some African nations (important to avoid generalizations; there are 54 nations on the continent) can sometimes incur longer-term repayment plans. But Russia will probably be willing to absorb this in return for finding a home for its products.

> The more Putin cuts gas supplies, the greater the chance of oil prices going through the roof.

7

Traders and fund managers have left crude oil markets in recent months, dropping activity to a seven-year low in August.[1]

$90/bl

is where roundtable delegates expect oil prices to hover in the near-term.

Sources: [1] Reuters

2023

The oil industry will start to feel the full implications of the current disruptions to the market in the first quarter of 2023, especially those caused by the Russia-Ukraine war.

2

The ban on Russian crude oil will start in December 2022, followed by another ban on Russian refined products in February 2023.

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Ones to watch

China
For the first time since 2001, the world's biggest oil importing nation is showing negative demand, so expect to see more consequences from this 21-year change in the coming year. Equally, the country's policy for the next 6-18 months is likely to concentrate on infrastructure investments, which means growth could tick higher from March next year.

Russia-Ukraine
How the mechanism for the price caps on oil from Russia, the world's third biggest producer, will be implemented by some of the world's biggest economies later this year remains to be seen. Some stakeholders expect oil prices to remain around $90-$100/bl amid the sustained geopolitical strain.

Beijing's product policy
More clarity is expected on China's policy on product export quotas. Changes could ease inflation on product prices, but as we are seeing with Beijing, the status quo is changing.

Gas flows
Europe's challenging balancing act will likely continue as nations across the continent edit their energy strategies to absorb the volatility driven by Moscow's politics, potentially including some renewable growth plans.

Port of Fujairah's Evolution

3rd
biggest bunkering hub worldwide reflects how the Port of Fujairah has evolved since operations started in 1983.

2024
will see the port's oil storage capacity triple to 12mn cubic meters, as ADNOC and other terminal operators look to expand their facilities.[1]

200,000
of deadweight tonnage (dwt) can be operated at the Port's Oil Terminal (FOTT) via nine main berths, or 14 wing berths.

4
dedicated bunker barge berths for low sulfur fuel oil (LSFO) tankers, all of which comply with the International Maritime Organization's (IMO) 2020 ruling.

1st
Home to the UAE's first jetty for very large crude carriers (VLCCs) on the Indian Ocean; critical for the region's appetite for eastward growth. Infrastructure is in place to add a second VLCC jetty and 12 more main berths should the business need arise.

6.7km
is the total length of the quay today, from just 370 meters when the port opened.

42mn
barrels of crude oil are expected to be stored underground when ADNOC's Fujairah storage caverns open next year.[2]

30%
of the world's total oil consumption passes through the Strait of Hormuz, which lies just 70 nautical miles from the port.[3]

4,808
vessel calls have been made at the port in the last twelve months, an average of thirteen a day.

8
objectives make up the Port of Fujairah's Sustainability Policy, including enhanced monitoring of its environmental impact and training on key issues. The establishment of the policy alone highlights how the port is eager to keep pace with global trends.

14,774
vessels have visited the Fujairah Offshore Anchorage Area (FOAA) over the last year, an average of 40 a day.

123.86mn
tons of cargo have been handled at the port over the last year.

Sources: 1Global Commodity Insight; 2 S&P Global Commodity Insight; 3 The Strauss Centre for International Security and La. Data points without marked sources are all from the Port of Fujairah.

Price Has the Loudest Voice

Dave Ernsberger, Global Head of Commodities Pricing, S&P Global Commodity Insights

Pricing defines competition, first and foremost; we see that play out every day, sometimes brutally. This dynamic is in motion with the rise of much-needed energy infrastructure across the Arabian Gulf and the rim of the Indian Ocean, some of which is being spurred by the mega-investments from China's BRI. Demand for energy will not peak in the Asia-Pacific for another two decades, so investing in strengthening today's insufficient infrastructure East of Suez – which includes one of the BRI's flagship projects, the Port of Gwadar in Pakistan – is key. This will not dent the Middle East's very well-established competitive edge, as long as the focus remains on price and relationships.

> The non-sanctioned barrel is becoming a smaller iceberg, melting in the ocean, which makes it impossible to comply with. So, the idea that sanctions are the answer to everything will prove to be inherently incorrect.

As the Port of Fujairah nears its fortieth anniversary, having officially opened its doors in 1983, the influential role of geopolitics is clearer than ever. Its success is largely dependent on the stability and performance of the Middle East, especially the UAE, the region's second biggest economy. In turn, the UAE's success, on the global energy stage in particular, relies on the performance of the port. This two-way street again illustrates the value of building robust and sustained alliances.

65mn+
barrels of oil storage at the Port of Fujairah.

45mn
barrels of oil product storage at the port.

2017
saw the port start issuing weekly oil product storage figures, boosting communication and transparency.

2021
The port launched monthly bunker sales reporting last year.

Sources for In Numbers: S&P Global Commodity Insights

Beijing may recalculate its reach

China's economic slowdown to normal levels of growth seen in the Organization for Economic Co-operation and Development (OECD) of 3% – versus historical averages nearing 10% – will discourage Beijing from making more vast investments along the BRI. The COVID-19 pandemic has transformed the mentality of global and local markets in ways that has yet to be fully understood; this certainly applies to China, the world's second largest economy, and its BRI plans. The behemoth designed and rolled out the initiative as a projection of economic influence and cultural relevance at a time when its economic growth was in the 8-9% range. Then, its appetite to project was enormous. But as economic growth starts to slow, every country, including China, starts to see a massive redirection of investment towards renewable energy, local infrastructure, debottlenecking the country, and so on. The focus pivots towards strategies that grow the economy quickly. Against this backdrop, it is inevitable that the emotional and patriotic ambition to extend hegemony – especially via an initiative unprecedented in modern times, like the BRI – will dissipate very quickly.

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Risk of suffocation

When you layer more and more sanctions on top of the marketplace, there are more and more rules to follow. Eventually, it becomes very difficult to understand how to comply with them, especially amid the huge uncertainty we see today. Therefore, I question the effectiveness of sanctions. Some of the recent sanctions include those on Russia amid its invasion of Ukraine since February, and long-term sanctions on Iran, a founding member of OPEC, as negotiations for the Joint Comprehensive Plan of Action (JCPOA) labor on.

Even the specialists writing the rules of the price cap for Russian oil do not yet understand how the mechanism will work. So, how can their ideas be enforced and measured? And how is anybody else supposed to align with them? Plus, the more the global energy market is placed under varying kinds of sanctions, the less there is of a market for people to resort to if they want to be compliant. Approximately 17mn b/d of oil is subject to sanctions today, in a world of 100mn b/d of liquids consumption. The non-sanctioned barrel is becoming a smaller iceberg, melting in the ocean.

Leveraging East-West Opportunities

Straddling global East-West trade points gives the Port of Fujairah a tremendous head start, but the port has certainly maximized this potential. Amid its strong infrastructure is the port's position at one end of a 1.5mn b/d crude pipeline that carries Murban grade crude from Habshan in Abu Dhabi to Fujairah. Approximately 42mn barrels of underground storage are also under construction by ADNOC and a 9mn t/yr liquefaction plant is expected to be completed by 2028.

This is only the beginning; the Port of Fujairah has far more opportunities to tap. The Middle East is set to raise its crude distillation capacity by 12% by 2025, with Kuwait's Al Zour refinery (615,000 b/d) and Oman's Duqm refinery (230,000 b/d) among the projects bolstering refined product flows across the region. This swell in refining capacity comes as other countries – including New Zealand, South Africa, Australia, and the Philippines – reduce their refining capacity and will likely need to lean on other regions for support. Furthermore, changing trade flows have seen the US importing fuel oil from Fujairah this year, following the ban by the US on Russian oil imports – another potential growth point for the port.

Insights by S&P Global Commodity Insights

We have a Supply Problem, and a Demand Problem!

Majid Shenouda, Deputy CEO and Global Head of Trading, Mercuria Energy

There is only one way to solve the volatility in oil markets and that is to have increased certainty. That's fundamentally the problem. Nobody feels certain about where things are going because you have both a supply problem and a demand problem and that affects how people trade flat price. We've seen volatility almost double today versus historical levels, which results in higher margins. The lack of working capital in the system at the moment is because everything is trapped. To determine what's going to happen in the future, one side of the equation will be to answer whether these problems will drive a recession, and obviously that has one set of impacts. And if you don't have a recession, is there enough supply out there? A lot of the problems that we have in our market are not about true supply and demand. They're actually manmade driven issues. How did we deal with COVID? The Russian Ukraine problem is another – how did governments react to this? Some have basically put caps into the market, while others have issued more paper, more money. So, there's just too much intervention coming from too many different places, which is making it very difficult for anyone to predict what to do. As a result, all it does is drive up the price, which takes away the liquidity, because ultimately every trader has a certain amount they can play with. And today, the tools we have with the prices we have, have been reduced by half.

> It's next winter that's the problem because once we've depleted the gas storage reserves, how do we get them filled again?

What will it take for more CapEx to come back into the upstream sector?

Historically, if you go back 6 to 10 months, anybody who wanted to invest in the oil sector was getting punished in the capital markets. Then, after the war, people started getting rewarded for being long oil and long gas. But the capital markets don't work in three-to-six months cycles - those are five-to-ten years investments in our sector. And, for the last few years, the banks have basically told the investors they will not put money into certain sectors. So, the real champions of developing these kinds of products have been governments and national oil companies. The capital markets have gone completely in the opposite direction. So, for CapEx to come back, the markets have to be told that it's okay to go back to the old economy for a period of time because at the moment, private equity and the banking sector is not open for business for these long-term investments. The other problem is that the 10-year forward curve has deviations in price of about $20/bl. People don't know if it's going to be $80 or $120. The spread where analysts are predicting forward oil prices are just so severe, that it is not conducive to anybody who wants to make an investment. So, ultimately, it's going to come back to governments and NOCs to make those investments - the average capital markets investor is going to find an easier way and lower risk return for their money.

How much more gas to oil switching should we expect to see in Q4?

The difference between oil prices and gas and coal and power are so severe that you if you have the capability, you'd already be switching. Analysts believe that current switching for this winter should be somewhere between 400,000 to 500,000 b/d, which is only 100,000 b/d more than it was last year. Europe has done a very good job in stocking gas, and we should be close to 100% in terms of storage coming into November. Of course, it then depends on how severe the winter is going to be. Governments are already bracing their populations that there may be blackouts, so people are prepared for this winter. It's next winter that's the problem because once we've depleted the gas storage reserves, how do we get them filled again? The Russian gas was coming for a number of months and now it can't come. Whether LNG can replace Russian gas ahead of next summer and winter is going to be the real challenge.

Surfing the Shifting Financial Landscape

Ole Hansen, Head of Commodity Strategy, Saxo Bank

We will hit a peak in central bank hawkishness by year-end, especially in the US. The damaging impact of this strong rally in rising yields is impacting demand and spending worldwide. We are starting to see weakness emerge in parts of the US economy, which might lead to a slight softening of the tone coming from central banks globally. This dynamic has reduced the availability of financing, so positions are being cut. Open interest has come down substantially. Plus, we are very focused on the US dollar as a risk barometer in the global economy. So, if we see oil prices staying high for longer in a slowing economy, the risk is that the central bank could keep their foot on the brake for longer and that will prolong the pain.

Plus, a variety of commodities – from crude oil, to cotton, to copper – are being used by professional financial investors as hedges against a recession that many think is coming. That means we have short positions and the way to squeeze shorts is by creating high levels of backwardation. If you look six months out, we have a backwardation close to 10%. So, the fact that we are getting some of the speculative positions from financial traders who are not involved in the oil market could be just one of the upcoming influences on pricing.

Volatility is Here is to Stay

Christopher Corda, Head of Oil Research,
Energy Aspects

What will the impending embargo on Russian oil by some EU countries mean for oil supply-demand fundamentals in a market roiled by economic worries and geopolitical tensions? This is a tricky question to answer and comes as energy ministers from the OPEC+ group, led by big producers Saudi Arabia and Russia, recently gathered a few thousand miles away in Vienna to discuss cutting output levels.

Apart from the ongoing influence of OPEC+, China is the biggest swing factor on the demand and refining side. There could be 600,000 b/d in 2023 in demand from China, with the extent of product export quotas set to determine the direction of margins over the next six months. Other factors in the supply-demand equation include the possibility of a large-scale resumption of Iranian exports if the long-running negotiations over Tehran's nuclear program could be resolved (unlikely) and the impending end of releases by the US of crude stocks from the SPR. Some in the market assume SPR releases will continue indefinitely.

In these unpredictable circumstances, there is little clarity on how the EU's embargo on Russian seaborne oil imports will affect supply-demand fundamentals. This is especially true as the embargo is reinforced by the G7 countries' planned price cap and measures against the ability of maritime operators to secure insurance for their cargoes. Russia will be able to redirect some, but not all, of the crude and oil products it currently sells to Europe. But there could be scenarios (even if it is a low probability) where the price cap allows more Russian oil to flow to the market.

It is also worth noting that physical trading volumes have shrunk, given the need to hedge, while some smaller proprietary funds have ceased trading altogether, adding to the liquidity void and leading to even sharper price movements. The disconnect between physical and paper markets may well continue, with our price forecast ($123/bl next year) reflected more aptly in the physical market, rather than in futures.

Content harvested from brainstorm session hosted By

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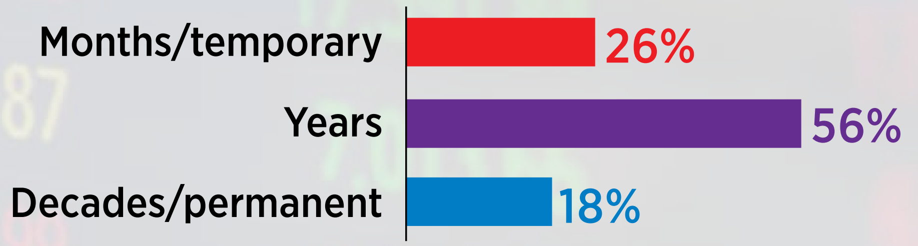
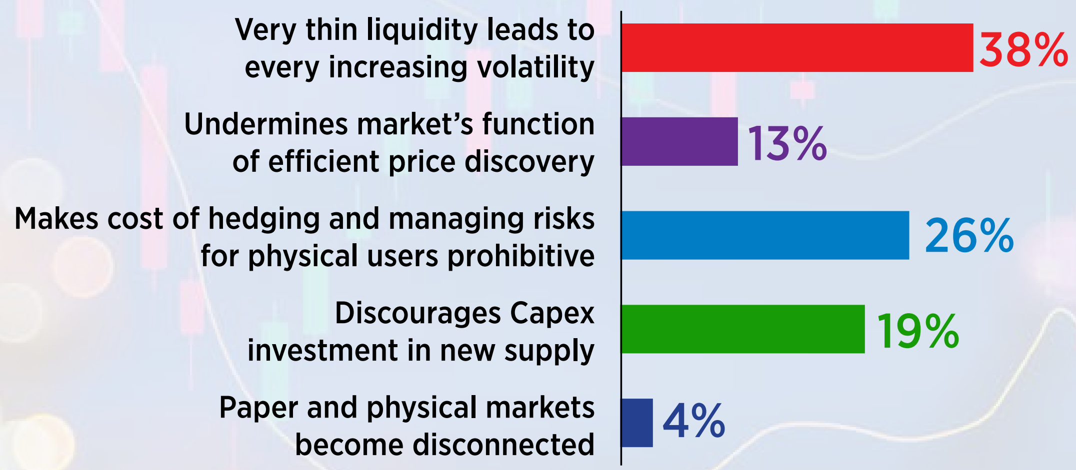
What will be the price for a barrel of Brent crude oil on the last day of 2022?

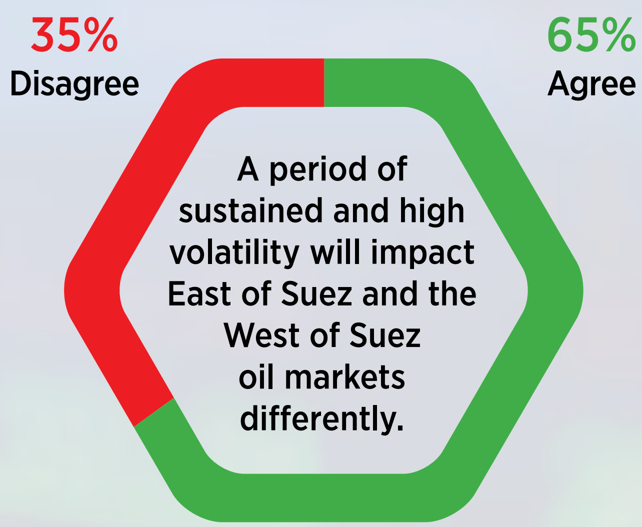
Russian oil is flowing into Asia and the Middle East, while this region's refined fuel goes West. How long will these changes to global trade flows last?

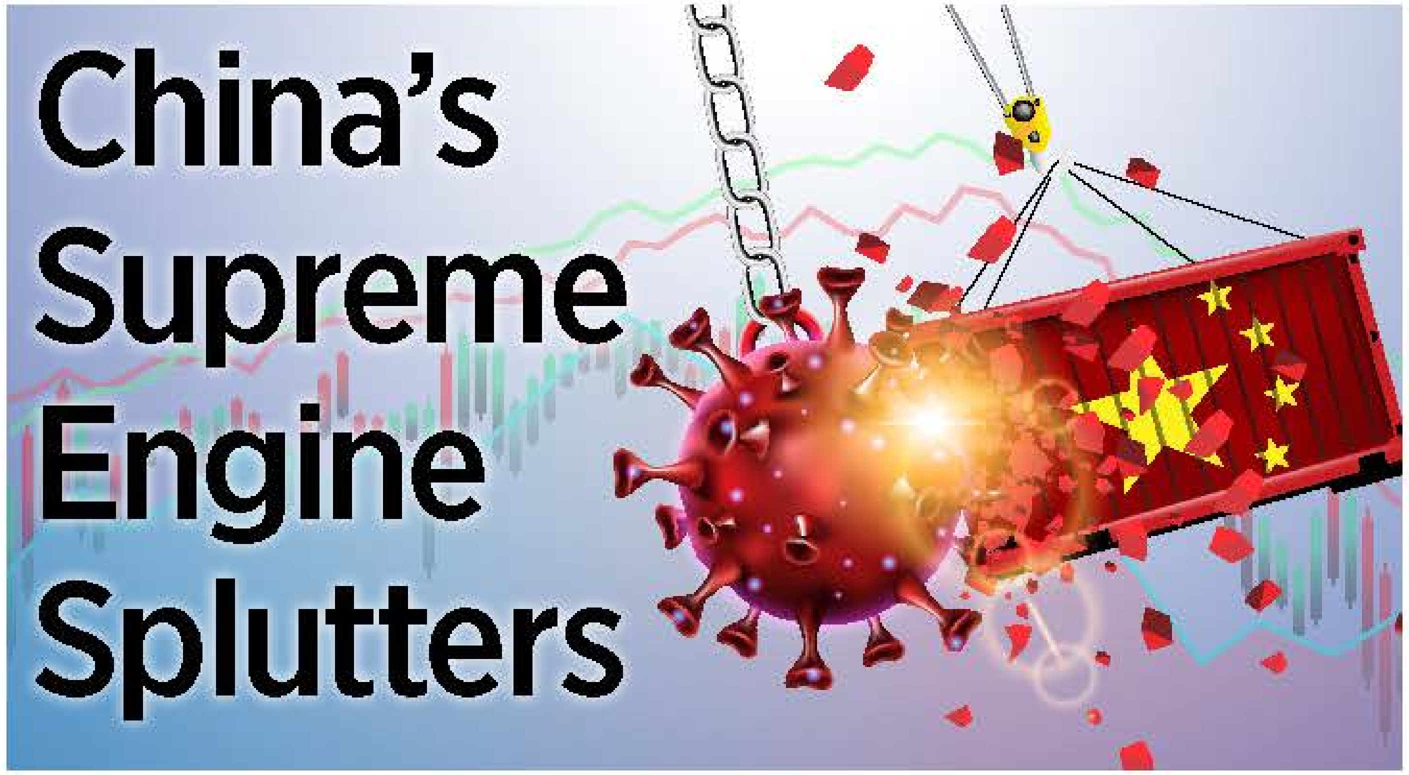


The Arabian Gulf is due to add 1.3mn b/d of new refinery capacity in 2022/23. Where will the majority of that output go amid the European sanctions on Russia amid the war in Ukraine?

What's most at stake the longer the oil markets remain in extreme volatility?







Marc Ostwald, Chief Economist & Global Strategist,
ADM Investor Services International

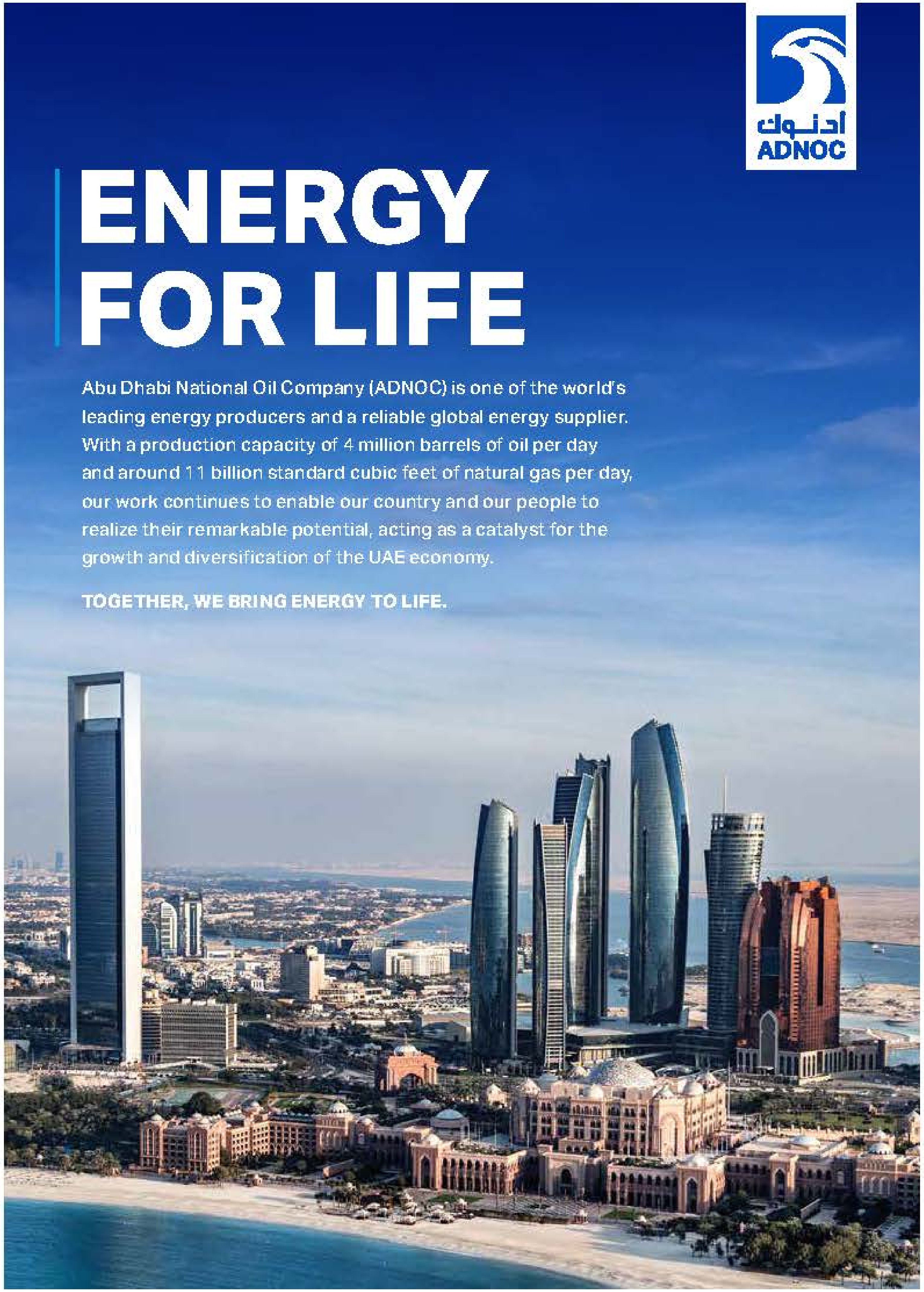
China's economy is clearly at a crossroads. But remember, the spectacular growth of the past 30 years means its regulatory framework all too frequently struggles to keep up. Judgements on the merits or pitfalls of such interventions must take this into account.

While the world's second largest economy initially benefitted from its Zero COVID policy – primarily due to the strength of external demand amid shuttered production worldwide – it has now become a serious impediment to any economic recovery getting real traction. The very low level of core Consumer Price Index (CPI), and the fact that retail sales are running at roughly half their pre-pandemic pace, are testament to this underlying weakness in domestic demand.

#1 challenge

China's key problem is its long-brewing property crisis. For example, in the five years prior to the COVID-19 pandemic, China's overall debt to GDP ratio grew by 45%. Much of that debt went into the property sector, which in turn tends to account for 25% of GDP.

Also noteworthy is China's move to clamp down on debt-fuelled speculative activity, much of which produces little or no economic value. It was hoped that this would redirect money to consumption



and business investment, or so-called 'high quality' growth. But implementing this hand brake turn created a great deal of uncertainty, which induced seizures in credit flows and made the process of balance sheet reconciliation and re-balancing even more challenging. Sadly, it appears that China is now reverting to its prior practice of transferring some of those debts and liabilities onto the already overstretched balance sheets of local governments, rather than balance sheet reconciliation.

Looking ahead

It had been hoped that the recent conclusion of the People's Party Congress would see some easing of China's Zero COVID policy, and measures to alleviate the property sector's woes. But this was not to be. Instead, the already signalled shift to balancing the long-term emphasis on development (i.e., growth) against security concerns, and a clearly more autocratic regime, suggests an overall weaker growth profile, thus impairing demand for commodities. In turn, this will likely heighten tensions with the US and the West and risk policy errors, all at a time when Beijing deals with the escalating challenge of climate change. If economic conditions in regard to the property crisis were to relax somewhat, we could expect to see demand from China rise significantly.

INDIA

Recovery fuels optimistic outlook

India's economy was hit hard by the pandemic, but its re-opening momentum has been impressive and sustained. This is clearly seen in the upturn in gross value added (GVA), generally a better measure of growth than GDP, and the outperformance relative to China as measured by its composite purchasing managers' index (PMI).

While it will continue to benefit from the pivot away from China as a manufacturing location, a key constituent of India's growth momentum has been the reduction in the banking sector's non-performing loans (NPL). In 2014-2019, there was a very strong headwind to growth, as NPLs ballooned from a high but manageable 4% to more than 11%. But various bankruptcy resolution

and banking sector reforms, including the creation of a national "bad bank", enabled the NPL ratio to fall to below 6.0%, therefore boosting loan growth.

Ramp up reforms

More effort is needed in banking sector reforms to ensure this improvement is sustained. Inflation is a double-edged sword for India. On one hand, if it is driven, as it is at the moment, by rising energy and food prices, it not only hurts businesses and consumers. It also puts pressure on India's current account deficit, which is vulnerable to rising oil prices, as the country imports 90% of its crude. On the other hand, rapid nominal GDP growth gives the government much greater fiscal space to offset the impact of high energy prices by reducing petroleum excise duties, and indeed increase infrastructure investment. In this vein, monthly data on infrastructure industries output is perhaps the most important official data point.

Infrastructure investments are paramount to ensuring that India builds its capacity as an alternative to China and Southeast Asia in manufacturing terms. Within this, it must concentrate on improving energy infrastructure to reduce its chronic dependence on petroleum imports. Plus, if well- planned and delivered, there is plenty of scope to develop untapped domestic energy resources, increase refined product output capacity, and develop alternative energy resources. The biggest risk would be a sharp downturn in the global economy, which would reduce external demand and potentially dent India's flow of foreign direct investment.

Oil: Expect more of the same

The financial paper side of the oil market is going to be squeezed by increasingly high interest rates. People will have to roll over the financing of all these hedges, which are getting more and more expensive because of the unpredictability in the market. Most importantly, if you can earn 4% on US two-year yields, are you going to finance trading positions? And what is going to happen to the trade finance of oil and agricultural commodities? There is going to be an issue. Banks had high liquidity on their books in the first half of this year, but with interest rates at 4%, will they want to take all that risk? That will have an impact on liquidity and in turn, volatility will continue.

Factor in recovery time

No one really understands what COVID-19 did, or is doing in some countries still, to destroy much of the world's production capacity, above all in the energy and industrial sector. We cannot just restart an energy processing plant with the flick of a switch. This squeeze on energy capacity, above all in Europe, does put a floor under all energy prices. Plus, consider that through the recessions the global economy has witnessed over the last four decades, demand may have flattened, but it has rarely turned negative.

Europe's winter jigsaw

Gas demand across industry in Germany, Europe's biggest economy, has fallen by approximately 20-25%, with many companies closing down because of high power prices, which are closely aligned with gas. That is where the hollowing out of demand is happening and why Europe has been able to get to good levels of gas storage. The question is whether we get to a point where we start to see increased gas demand because of weather? The other question is, how do we balance out supply-demand when big petrochemical companies in countries like Germany are reining in production? If we do see demand pick up in China, do we then say that is going to probably be matched by a large drop in industrial demand for energy in Europe? Therein lies the upcoming juggling act.

"How will expansion of China's Belt Road Initiative impact the development of the Midstream energy infrastructure across the Gulf and its near neighbors in Pakistan and East Africa, especially with the change in global energy flows due to Russia's War on Ukraine?"

China's Belt Road Initiative has been bedding in deeper into the Gulf region through major bilateral partnerships, such as the Iran–China 25-year Cooperation Program or Comprehensive Strategic Partnership, and the China-Pakistan Economic Corridor, which has the Port of Gwadar on the Arabian Sea as its flagship project.

According to a report from the Green Finance and Development Center at Fudan University in Shanghai – Chinese engagement through financial investments and contractual cooperation for the first half of 2022 in the 147 countries of the Belt and Road Initiative was about $28.4bn. The focus of BRI in infrastructure, particularly in energy and transport, expanded to about 73% in H1 2022 (up from 63% in 2021). Middle Eastern countries received about 57% of Chinese BRI investments in H1 2022 & increased their share of overall BRI engagement from 8% in H1 2020 to about 32% in H1 2022.

The vision for the China-Pakistan Economic Corridor is one of regional connectivity, with ambitions not only to benefit China and Pakistan, but also to have engagement with Iran, Afghanistan, Central Asian Republics, and the region. Its stated goals are the "enhancement of geographical linkages with improved road, rail and air transportation systems, to facilitate a higher volume flow of trade and businesses, producing and moving energy to have more optimal businesses and enhancement of co-operation by win-win model."

Meanwhile Iran and China signed a 25-year cooperation agreement last year on the further development of Iran–China relations. The final details of the agreement have yet to be officially announced. Under a draft of the 25-year agreement (signed in June 2020 in Beijing) previously obtained by The New York Times, China is to invest $400bn in Iran's economy over that time period in exchange for a steady and heavily-discounted supply of oil from Iran.

Mohsin Ali Mangi, Chief Strategy Officer, Pakistan State Oil Company

China's Belt Road Initiative can be mutually complementary to the Middle East

It will benefit both the Middle East and Central Asia as it will bring in capital efficiencies. We have to compare the relationships of trade between the Middle East, China and Central Asia right now. We need to look at the quantum of the volume of trade existing between the UAE and China and Saudi Arabia and China. The idea of having this one Belt Road Initiative is to link up those economies. You will see the oil surplus flowing in from the Gulf region to the east of China and passing through Pakistan so it will financially and economically justify all those investments. Right now, the Middle East is a physical energy hub, but it has huge potential to also be a financial hub and come up with creative solutions for infrastructure and trade.

Connectivity brings expansion - The region can unlock value if we generate that volume of true connectivity. Right now, Pakistan has been building infrastructure for its power sector as well as developing its road infrastructure. But the idea is to also build pipelines, ports and storage infrastructure that will link up Central Asia and the east of China, where the bulk of the next growth will come from. About 94% of the Chinese population is on the eastern side of the country but that is not in close proximity to Pakistan. The next phase of growth in China has to come from the west side. These energy flows will go from the Gulf region upwards towards that western part of China - that is where the real potential of the Belt Road Initiative will be unlocked.

Dave Ernsberger, Global Head of Commodities Pricing, S&P Global Commodity Insights

Is China's BRI complementary or competitive to the Gulf region?

The infrastructure is 100% complementary. Moreover, competition is decided by price and relationships. There will be competition in the region and we're seeing it now with the shift in flows associated with the war in Ukraine. Infrastructure is necessary for these markets to function in the first place and for competition to truly play out. Fujairah's success depends on the success of the region and the region's success depends on Fujairah being well-run. The idea that storage tanks and pipelines compete with each other, is true to a certain point, but in reality, there still isn't sufficient infrastructure east of Suez for these markets and for what's to come. Demand won't peak in the Asia-Pacific for another 15 to 20 years, which means we need more infrastructure to support all of that.

How effective have sanctions on Russia been?

The more rules you have, the harder it is to follow them and to understand how to comply with them. For example, there's been a huge amount of discussion around the price cap concept and even those who are writing the rules do not understand how it will work. If the sanctions creators don't understand how they're going to be enforced, how can anybody else align with them? So clearly, this is an environment of less compliance. The other point is that the more that you put the global energy markets under varying kinds of sanctions regimes, the less there is of a market for people to resort to if they want to be compliant. Upwards of 15mn b/d of oil is subject to sanctions right now in a world of 100mn b/d of liquids consumption so the competition for what remains is just too high. The idea that sanctions are the answer to everything is going to prove itself to be inherently incorrect.

Saif Al Mazrouei, Head of Ports Cluster, Abu Dhabi Ports

Are growing economies in South Asia and East Africa an opportunity or competition for Abu Dhabi Ports?

Competition makes us grow better and faster and at the same time, we are complementing each other. Competition will make us build hubs for shipping lines for example. Linking Pakistan, Iran and other countries in the region is one of the major roles that we want to play. The center of gravity has moved south, and we want to be the link. Most imports and exports are maritime. The UAE is exporting more than 90% of its products by sea and around 80% of its imports.

Have regional sanctions been an inhibitor to your business as a port operator?

The more rules there are, the more rules there are to break. But sanctions lead to new rules coming in to serve different markets and the route of shipping ports and volumes will change accordingly also. We are well positioned in the middle of all these sanctions and so we will have a role to play.

How does China's economic slowdown impact midstream investment into this region?

Approximately 20 companies have invested in our industrial zone, at a value of above $1.6bn. The purpose of China's Belt Road initiative has been to connect, and we are part of it. Any changes in that due to China's economic slowdown will lead to a requirement to open new markets. It is a shift for China and for us.

Vitol: Global Oil Demand will Peak in the Early 2030s

Chris Bake, Member of the Executive Committee, Vitol & Chairman VTTI

The War in Ukraine is reshaping global energy flows, impacting (along with broader macroeconomic trends) oil, gas and power demand. This reshaping mirrors shifts in international politics and alliances, and a redrawing of spheres of influence. The UAE, with its population of ten million, sits at the geographical epicentre of these energy, trade and financial flows between East and West. Today the Gulf region continues to be shaped by geopolitical events, though this time it feels very much more in control of its destiny. The daily events that have buffeted us of late, stressed the global energy markets, driving European gas prices up tenfold from their five-year average, with echoes of what the Gulf region has seen in the past on its own doorstep. That is an invasion, refinery and power plants being attacked by missiles, and a pipeline being blown up at multiple points at the same time. The difference, this time, is that these stresses are happening in Europe! with the Gulf region feeling the consequences second hand. As with all of us in the oil sector, questions about the future of oil flows have to be asked. In Vitol's view, demand globally will peak in the early 2030s, with demand in Asia peaking in the middle of the next decade and Africa continuing to grow well into the 2040s. This is contingent not only on continued economic growth, which is currently stalling, but also there not being an unforeseen technical revolution. If there is one thing we should remember, it is that the adoption of new technologies and the obsolescence of the old, tends to happen quicker and more completely than the incumbents anticipate. A picture from the US National Archives of 5th Avenue in New York in 1900 shows a street, of horse-pulled vehicles and one car. A picture taken in 1913 shows a street full of cars and only one horse.

Port of Fujairah Makes Big Leaps Forward

I first visited Fujairah in the late 1990's. Standing at the Port yesterday, it does not feel so far away, but so much has changed, as it has in the international energy markets. At the time, the Gulf was short refined products and imported over 1mn t/yr. At that time, the Port of Fujairah was unrecognisable

compared with what exists today. A few product tanks, a legacy of the first Gulf War, and three jetties held the infrastructure available to bunker vessels calling at the anchorage, which was ideally located outside of the straits of Hormuz.

Geopolitical position of Fujairah

It would have been almost impossible to anticipate the huge changes that Fujairah has seen unfold over the last 25 years. Many of these have been driven by the broad economic and geopolitical events, but the local vision and determination of His Highness Sheikh Hamad bin Mohammed Al Sharqi, to facilitate and invest meaningfully in the core infrastructure, have enabled Fujairah to become what it is today – a major energy hub for regional and global energy flows. At the time, each of the decisions taken, seemed bold; the conversion of the original vessel mooring system in the Port to the first three jetties, which are now nine, plus a VLCC jetty, handling hundreds of vessel movements a month, the massive matrix-manifolds, linking the jetties to the independent tank farms, underpinned by extensive land reclamation projects. They have made today's throughput of over 60mn tons of product discharged and reloaded a year possible, enabling Fujairah to carve out a critical role at the heart of the region's energy flows.

In the 1990s the region was a major oil producer, exporting most of its 16mn b/d of production to refineries in Europe, while importing the products its growing economies needed. As China began its rapid economic expansion, the volumes of crude oil flowing east grew and the Gulf region was ideally placed to supply China's expanding refineries. The established Western centric-based pricing mechanisms around diminishing volumes of Dubai crude and growing Oman crude exports, were no longer appropriate and the launch of the DME Oman Export Blend Sour Crude Contract in 2007 marked the beginning of a local futures market, pricing regional sour crude.

Regional product pricing methodologies continue to be challenged and debated, basis on the changes in product flow, the exponential rise in the African gasoil demand this century, the addition of long haul hubs in Dubai, Abu Dhabi and Qatar created new jet fuel sinks, and more recently IMO 2020 has led to a change in the fuel flows where up to 90% of HSFO produced in the Gulf now flows East. Since the early days of this forum, a perennial topic has been pricing. Product markets, with the change in flow, from imports into the Gulf to predominantly exports from the Gulf, shifted from products being priced on a Med or Singapore plus freight basis to a Singapore netback basis. I am sure this will continue to be discussed, with a drive to have more localised price discovery. This continues to be constrained by the lack of a depth in the market, total participants, and development of a fungible, liquid paper market in relation to products being priced.

The launch of the DME crude contract has been followed by the successful launch of IFAD in March 2021, bringing increased transparency and liquidity to the pricing of the benchmark light sweet crude – Murban, and bringing in new financial players that should continue to bring depth (liquidity) to that market.

The energy position of the US has shifted dramatically in the last decade, with a profound change on energy flows, with significant regional geopolitical implications. The growth of US shale oil changed the US from a net importer of over 10mn b/d of crude, a quarter of which came from the Gulf region, to an exporter, accelerating the shift of the region's focus East to the growing economies, and refineries, of Asia. Asian demand has grown by 75% since 2000 from 22mn b/d to 37mn b/d and will continue to drive oil demand growth for the next decade.

And in this past decade, Asia has been reaching West. Seeking to recreate the spirit of the trade routes of old, China's Belt and Road Initiative has 149 countries as signatories and has resulted in tens of billions of investment by the Chinese government and banks, in infrastructure projects across Asia and through to the Middle East and Africa.

Seeking to capture more value from the regional crudes, refining capacity has grown exponentially. A net importer of gasoline in 1999, today the region exports a net 2.5mn b/d of products from its 10mn b/d of refining capacity.

The politics of the region have assisted this growth. UAE's positioning has reflected its regional location and its perceived neutrality has attracted business and barrels. This continues to be the case today as redirected Russian flows find their way to the region and to markets beyond.

Transition story from carbon to green capture

Funding this transition will be more challenging for all of us as the cost of capital rises. The low interest rate environment we have become used to is ending and, coupled with heightened geopolitical risks, this is likely to result in increased investor reticence. In this context, governments have a key role to play leading and shaping change. The UAE was one of the first to implement 10 ppm sulphur gasoline and gasoil for example.

Governments across the region have committed to investing in the energy transition, and with its climate, the region has the great potential to further leverage renewables. What is yet unclear to all of us is the role of trading and trading hubs in a world of renewable energy. It is possible that energy markets fragment and become highly localised. This scenario will favour well developed and diversified economies and the challenge for governments in oil-dependent economies will be to achieve this state before oil related revenues finally diminish.

The UAE has embraced this challenge. It was the first country in the Middle East to ratify the 2016 Paris agreement and, since then, has developed initiatives to capitalise on the evolution of the world's energy needs, through transitional to sustainable solutions. ADNOC's LNG production capacity which will load via Fujairah, will comprise over 9.6mn t/yr, providing additional capacity to facilitate the move to transition fuels.

Longer term, UAE has signaled its intent to be a leader in sustainable energy solutions. The recently announced development of a 200-megawatt green hydrogen facility to support the production of green ammonia which could be traded internationally, or used as a shipping fuel in a key regional bunkering hub, is an exciting indication of how the UAE could leverage its geographical position to carve a sustainable future with sustainable energy flows.

Such a future would be consistent with the great legacy of the late Sheikh Zayed's respect and love for the environment. In these times, it is a legacy we should all be mindful of.

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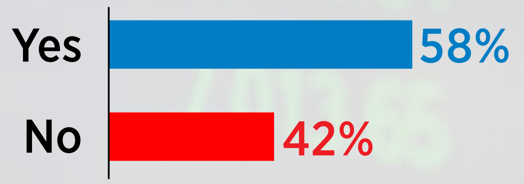
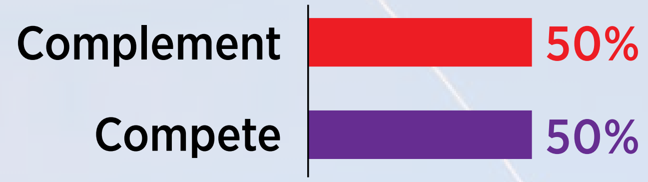
Exclusive results from 200+ senior stakeholders in the Middle Eastern energy market

What impact will changes in global crude oil / product flows have on West of Suez benchmarks going forward?

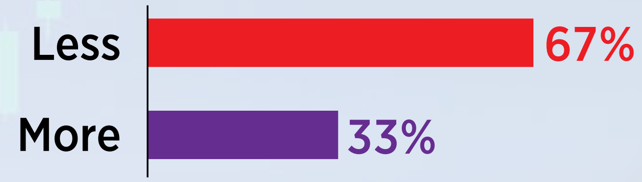
Global investments in the renewable energy sector climbed by 11% to $226bn in the first half of this year. Will this free up more hydrocarbons up to early 2023?



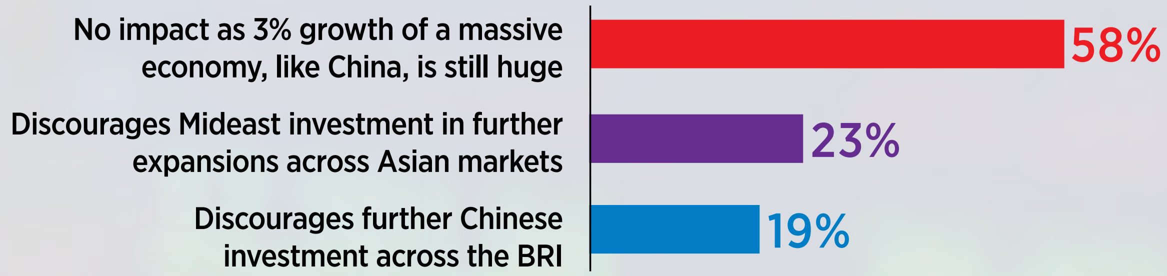
Will projects that form part of China's BRI in the Asia-Arab Gulf region, including the Port of Gwadar on the Arabian Sea, complement or compete with existing midstream energy infrastructure?



US senators are trying to compel the administration to use secondary sanctions on international banks to strengthen G7 countries' planned price cap on Russian oil. Will this result in more or less compliance in the East of Suez markets?



How will China's economic slowdown to normal OECD growth levels of 3% impact energy demand and investment in midstream infrastructure needs across the BRI?



Decarbonization: Policies to Thrive?

Timely, transparent, proactive, and ambitious. These cornerstones of decarbonization policies are non-negotiable for the UAE and others striving for Net Zero by 2050; a very short 28 years away. The OPEC member has already made huge progress, including global firsts in green energy and environmental protection and management. But the world recorded more climate-related disasters than ever in 2021. Clearly, national policies in the UAE and the wider Middle East's energy sector must work far harder and far quicker.

The complex and delicate dynamic between juggling energy security and climate targets is being highlighted more starkly than ever before, especially amid the domino effect of Russia's invasion of Ukraine on global supply markets. These growing intricacies, propelled by clashing needs and capabilities, mean decarbonization is a multifaceted marathon, not a sprint – and policies must be far fitter to effectively drive and guide change.

As policies evolve in a world of globalization 4.0, we must avoid generalizing regions, especially when referring to developing countries; there are 21 nations in MENA, while Africa and Asia are comprised of 54 and 48 countries, respectively, for example. Clearly, decarbonization journeys will vary for different places and different people, which good policies will acknowledge and cater to. Of course, some very broad policies and frameworks will help establish a global baseline of best standards and knowledge, as illustrated by the United Nations Framework Convention on Climate Change (UNFCCC). Then, countries must design tailored policies to address their specific needs. In an ideal setting, this creates a holistic yet nuanced approach, which is best to meet the Paris Agreement's target to limit global warming to well below 2°C by 2050, preferably to 1.5°C. As it stands, we are far off track.

> Imagine a carriage being pulled in lots of directions at the same time; it never actually moves forward. This is what the world's decarbonization journey could become unless we have clear, firm, and realistic policies.

Ten blind gentlemen and an elephant

Take a moment to consider ten blind gentlemen who are each drawing parts of an elephant they have touched different parts of, but never seen. Once finished, all the gentlemen describe the elephant very differently; we must avoid this sort of fragmentation with the global energy transition. The journey to Net Zero is extremely new to all stakeholders and there are far, far more questions than answers. Each stakeholder has their own perspective of this uncharted territory, so ensuring upmost visibility and communication via clear and relevant policies must be the collective starting point. This is especially pertinent as many developing economies have long felt their concerns are being lost in the winds of political rhetoric. It remains to be seen if COP27 in Egypt this November – heralded as 'Africa's COP' – or COP278 in Dubai next year marks a change of pace. The fact that it is the first time two consecutive COPs have been held in the MENA region in the gathering's 27-run has some hopes tentatively building.

The Trickiness of Sanctions

Hatem Al-Mosa, CEO, Sharjah National Oil Corporation (SNOC)

A strong level of buy-in from affected countries is critical for sanctions to succeed – and the sanctions on oil from Russia, the world's third biggest producer, are no different. Right now, compliance on the sanctions against Russia is not as widespread as it is with the sanctions on Iran, for example. The robustness of sanctions partly depends on the price versus the penalty. If you are getting Russian crude at a 30-50% discount, the loss from the sanctions imposed by the US or Europe may no longer be financially effective. Plus, when there are many sanctions – Russia, Iran, Venezuela – it generates a big draw for buyers to seek those discounts.

> If you are getting Russian crude at a 30-50% discount, the loss from the sanctions imposed by the US or Europe may no longer be financially effective.

OPEC's move?

The global macroeconomic situation means it does not make sense to cut production right now. If production is cut, I would expect it to be 100,000-200,000 b/d from Saudi Arabia and the UAE and maybe one or two other countries, not the whole 2mn b/d. Many members are still producing significantly lower than their quotas, including Russia, the organization's second-biggest member. Competition will intensify in the downstream and refined product markets and it tends to be more regional than global. Still, China is expanding significantly on that front, with investments in infrastructure in Pakistan and South Asia, including the Gwadar Sea Port in Pakistan, one of its flagship projects in its BRI. If completed, these investments in infrastructure could compete with the downstream markets from the UAE, for example, but that also depends on the strength of recovery in demand for oil.

** Paraphrased comments from a public plenary session, which was not held under the Chatham House Rule.*

30%

reduction on the 2019 level of energy-related emissions globally is needed by 2030, followed by a 75% decline by 2040, in order to reach Net Zero worldwide by 2050.

2030

This reduction in emissions implies a 3.2% reduction each year over the next eight years and a swift reversal of recent trends: emissions rose 0.9% a year from 2015 to 2020.

12

Diversity and equality, climate change, and safety and standards are the three top priorities linked to Environment, Social, and Governance (ESG) for businesses in the Middle East surveyed by PwC over the next twelve months.

60%

More than half of respondents from businesses in the Middle East have become more eco-friendly in the last six months, as sustainability becomes a strategic decision.

Source: Bloomberg New Energy Finance, PwC, ESG, Middle East Report 2022, PwC, Global Consumer Index Survey

Swinging pendulum

Amid today's fast-changing energy landscape, appetite for investing in fossil fuels regularly changes and growth forecasts for new types of energy, like green hydrogen, vary wildly. This makes it very tricky for investors; the "frozen carriage" hinders the flow of funds that are urgently needed to tackle decarbonization in the Middle East and beyond. Russia's invasion of Ukraine has exacerbated this dynamic, sparking deep concerns over energy security and seen Europe, the matriarch of green energy production, increase coal imports. Comparatively, the Middle East's approach – openly stating it will continue to support both fossil fuels and renewables to underpin energy security – is something regional stakeholders and investors should find reassuring. Plus, to help relieve this 'perfect storm' in regard to supply, far more focus must be given to reducing energy consumption. Part of this means continually reducing energy subsidies; a process that is ongoing in the Middle East, but far from complete.

Focus on Scope 1

Expecting all oil and gas companies to complete Scope 1, 2, and 3 in the short and medium-term is unrealistic. Companies must first master Scope 1. The industry has not yet clearly defined whose responsibility it is to spearhead Scope 1 progress, the source of additional funding, decisions over stranded assets versus upgrading infrastructure, and many other points. Confusion is growing in an industry already grappling with great change related to decarbonization, which risks slowing overall progress in 2023. Amid the uncertainty, one roundtable participant shared a welcomed rallying cry: "We are all living in very exciting times. We are coming together to solve something hugely complex – there is great value in that. Let's figure this out!"

Content harvested from brainstorm session hosted By

مؤسسة نفط الشارقة الوطنية SNOC

Spotting Trends, Tackling Challenges?

A kaleidoscope of changes are reshaping the face of the oil market in the Middle East. From underinvestment to geopolitical volatility, from rising demand to near-term peak oil, from very ambitious climate targets to juggling the risk of stranded assets, and so much more – all while competitively trying to sustain energy security. Plus, the coming thirteen months will see COP27 and COP28 held in the MENA – the first two consecutive events in the region in the gathering's 27-year run. As the world's historical epicenter of fossil fuels explores how to master this uncharted territory, we ask: what's next?

Decarbonizing the energy industry remains a crucial priority, but escalating concerns over security mean it is likely to take a back / side seat while supply chains are stabilized in the short and near-term. The biggest focus over the coming quarter will be how the invasion of Ukraine by Russia – the world's third biggest oil producer and second biggest gas producer – will impact critical supply chains worldwide. Energy stakeholders' attention is also focused on how OPEC+ responds in this fast-changing landscape. The organization is in a unique position. No stranger to mitigating instability, it has typically reacted to signals from customers, but now some customers, like China and India, are adopting a more hawkish stance, and an increasingly complex US-Saudi Arabia relationship must be factored in.

> Oil is approximately a 150-year-old market that has dramatically elevated global growth. Renewables are still closer to the starting line, comparatively. Clearly, it will take time to diversify the energy basket. Equally, the pressure is rightly on the oil industry to bolster energy efficiency and environmentally friendly practices, especially across its vast aging portfolio.

Rethinking Russia

Oil accounts for 40% of Russia's income, so the world's largest economies' plan to restrict its activities amid the Russia-Ukraine war is capturing the Kremlin's attention. Even with restrictions, Russia would likely still be able to export 4mn b/d to the East, as ally Iran exports 1.2mn b/d – 1.5mn b/d under its sanctions. A price cap just above Russia's cost of production would dissuade Chinese and Indian buyers. This could erode Russia's income, which the world's biggest exporter of oil to global markets may respond to by shutting in 1-2mn b/d of supply, thus potentially sparking price movements. It is important to note that these are speculative comments and speak to the guesswork occurring throughout geopolitical and energy circles, as stakeholders seek snippets of clarity. Another point to consider is that approximately 90% of the insurers for the world's maritime industry are based in Europe, which raises the question of how Russia would affordably insure its oil cargoes as they head East?

99.7mn b/d
is the anticipated global demand for oil in 2022, rising to 101.3mn b/d in 2023.

2022
has seen Russian oil exports fall to 7.4mn b/d in July, from 8mn b/d at the start of the year.

5
destinations have seen crude and product flows slump since the outbreak of the Russia-Ukraine war: the US, UK, EU, Japan, and Korea. Approximately 66% of this flow was sent to other markets.

2
years of reduced demand growth worldwide are now anticipated; 1.9mn b/d in 2022 and 1.7mn b/d next year, down by 60,000 b/d and 470,000 b/d respectively.

10%
fall in Russia's export revenues, with $21bn in June sliding to $19bn in July amid reduced volumes and lower oil prices.

900,000 b/d
is the anticipated build in global inventories for the rest of this year, with 500,000 b/d in H1 2023.

Source: International Energy Agency (IEA)

Iran's next move?

Greater complexity now surrounds the Joint Comprehensive Plan of Action (JCPOA) between Iran and several world leaders, notably spurred by Russia's invasion of Ukraine and its domino effect on geopolitical alliances and supply chains. The deal between world leaders and Iran was about to be concluded, after many twists and turns, before the invasion on February 24 this year. Broadly speaking, restrictions on Russia could see the oil giant pivot to make Iran a new hub of oil exports and financial transfers. Equally, more than $7bn of frozen assets in South Korea could soon be released in what may be a clear nod from the US administration to Tehran that they are still open to reviving the deal. Meanwhile, Iran's position is further complicated by significant civil protests over human rights, which includes workers from the oil sector.[1]

Source: [1] New York Times

Staying safe

The security of oil infrastructure and operations needs greater attention, especially following alleged attacks on the Nord Stream gas pipelines and unapproved drones at oil installations in the North Sea. Plus, ADNOC faced a missile attack in February this year[1] and a drone-enabled missile attacked major Saudi oil infrastructure in 2019.[2]

The US' physical presence, or reduced thereof, in the Middle East will probably not affect the security of the region's oil infrastructure either way, due to the continued influence of the behemoth's "almighty dollar, powerful regardless of where the country plants its military," a delegate said. Some operators in the region also have indirect security as their spare capacity makes an attack on key oil infrastructure less disruptive to regional and international supply-demand dynamics – the opposite of what attackers desire. Still, consider that the UAE and Saudi Arabia's spare capacity did not make them immune to attacks, just maybe less attractive than others. Therein lies the need for all stakeholders to be on higher alert.

Physical attacks are just one part of the threat; ransomware attacks worldwide have risen by 150% over the last year.[3] The disruptive impact of this threat was illustrated when an attack on the Colonial Pipeline in the US, the world's biggest oil producer, triggered the shutdown of 5,500 miles of pipelines, carrying around 45% of fuel supplies on the country's East Coast,[4] home to nearly 120mn people.[5]

Sources: [1] CNBC; [2] Al Jazeera; [3] World Economic Forum (WEF); [4] Bloomberg; [5] World Population Review

Content harvested from brainstorm session hosted By S&P Global Commodity Insights

ESG: Finding its Feet in Trade Finance

Financing norms for the region's vast and established energy sector are rapidly changing as investors try to balance supporting fossil fuels and renewable energy amid strict climate targets and escalating unease over energy security. Simultaneously, global eyes are on MENA as two COPs – the world's biggest annual climate gathering – are held in Egypt and the UAE, respectively, over the next thirteen months. Amid these paradigm shifts lies an opportunity for trade financiers to thread Environment, Social, and Governance (ESG) – what some stakeholders argue is the future of climate, social, and operational finance – into their toolkits.

Cutting risk, boosting reputational value, enhancing sustainable profitability, and enabling new partnerships are some of the key benefits of integrating ESG into trade finance in the Middle East's energy market. Appetite is undoubtedly swelling for this historically niche space; the world's sustainable finance market reached $1.6trn in 2021.[1]

ESG is one of the main spokes in the wheel of decarbonization, but it is still finding its feet in some financial-energy circles. This is primarily because designing and implementing ESG criteria is not always quick, simple, or easy. Establishing scoring, tracking, and accountability can be very complex and implementation takes multi-stakeholder buy-in, for example. This can be tricky amid a lack of regional or global standardized policies, best practices, or legal obligations.

However, the effort is worth it. First movers in this fast-growing market are already benefiting from a direct link between their proactivity and being able to harness large, competitively priced financings (while supporting climate and social targets, particularly important for NOCs). This increased ease for pro-ESG players has not faltered amid the current concerns over global economic growth, for it is seen as an inevitable market of the future; one of the safest growth bets in a space riddled with uncertainties. Plus, the benefits are far-reaching. Companies' forward-thinking makes them more alluring to new partners, especially outside the Middle East, and top talent, particularly the younger generation – human capital increasingly coveted in fossil fuel markets worldwide.

Momentum amongst the region's major energy players is clearly building. Companies are increasingly looking at sharing progress reports on their sustainability drives, and more are sharing reports or information on ESG specifically. ADNOC Distribution released an ESG 2021 report, ADNOC has a Sustainability Strategy, and Dubai's state-owned ENOC conducts Sustainability Performance Reporting. To the west, Saudi Aramco, the world's most profitable company and biggest oil exporter, has a Sustainability report and a website page dedicated to ESG.

Source: [1] PwC

6%
of global GDP is attributable to trade finance.

75%
Trade finance facilitates global supply chains, which in turn account for approximately 75% of the world's CO_2 footprint.

$5.2trn
is the size of the global trade finance market.

2030
An improved global trade finance system could add 600mn of the new jobs needed worldwide by 2030, supporting ESG strategies. It is particularly meaningful for the Middle East, home to one of the highest rates of youth unemployment worldwide.

43%
growth in ESG is anticipated between 2018-2036, reaching global assets of $160trn.

80%
The one-year growth rate of ESG fund launches in the US is more than twice that of funds without ESG (80% versus 34%).

$125trn
is one estimate of how much it will cost to tackle climate change by mid-century, with ESG and trade finance playing a central role in how this will be achieved.

Sources: McKinsey, Roundtable Participant, McKinsey, McKinsey, International Institute for Sustainable Development, Deloitte, Institute of Economics and Peace.

Plugging gaps

Comprehensive and transparent benchmarks lie at the core of building much-needed and robust regulations for ESG. The regulatory landscape is more advanced in Europe and the US, providing valuable templates that stakeholders in the Middle East can echo. Of course, countries and regions' nuanced needs mean one size will not fit all, but it is a good starting point – very valuable for stakeholders overwhelmed by the breadth and depth of ESG.

ESG reports are meant to be transparent and proactive statements on a company's evolution. But first, greater clarity over the E, the S, and the G is needed to boost stakeholders' understanding and confidence. In this vein, there must be greater dialogue between financiers with governments, the private sector, academia, technology companies, cross-border alliances, and more, to craft knowledge and data banks. Pinning down common parameters is key.

This is particularly the case when companies have to benchmark EGS criteria / scoring principles that are not quantifiable, such as employee wellbeing (which lies within 'Social'). Employee surveys can develop trackable metrics gauging

> A need for rigorous benchmarks lies at the heart of ESG and trade finance.

employees' status, but this transitory approach can lack depth. Other areas are far easier to track, such as Governance, which includes the creation, implementation, training, and tracking of policies on Anti-corruption, Anti-bribery, board representation, and Modern Slavery Statements, to name a few.

Applying ESG to the Middle East's world-leading fossil fuel market is critical to reducing the oil and gas industry's high CO_2 footprint – which accounts for 42% of indirect and direct emissions worldwide – as well as reducing the risk of stranded assets and buoying energy security. Equally stakeholders often think investing in fossil fuels eradicates ESG value. That is not always the case. One part of ESG promotes renewable and efficient energy, but that is only part of the broader criteria. There is also a focus on waste, waste, transport, and CO_2 emissions management under the Environment umbrella, for example, not to mention the many non-energy advancements that need attention under Social and Governance.

The two Vs

The importance of verifiability and visibility as stakeholders reshape the energy market cannot be underestimated. ESG ratings are not coordinated globally, which is hindering growth, but blockchain could change that. Using this evolving technology to track ESG-related collateral helps companies build new partnerships, avoid greenwashing, triggers greater buy-in from management and supply chains, and more. Full transparency from point A to point B legitimizes this growing market, bolstering stakeholders' confidence and appetite.

-10%

of the capability of technology in driving sustainability, including ESG, has been tapped.[1]

Source: [1] Roundtable delegate

Power of practicality

More systemic thinking is critical to help stakeholders advance their ESG journey, as too much idealism around decarbonization carries its own risks. One view is that the biggest risk of the climate crisis today is not actually climate change. Instead, it is how the focus on climate issues is retracting stakeholders' support of fossil fuels, currently a cornerstone of our energy system. One cannot be traded for the other and many believe ESG is the largely untapped common ground: meet climate targets without sacrificing commercial success.

> Seeing ESG as a quick fix or a side-effort will lead to failure. The greatest challenge of ESG is also its greatest asset; it is a comprehensive, company-wide operational and cultural rethink that prepares energy companies to walk tall in this new chapter of trade finance. It will take time and effort.

Will India step forward?

India is a strong candidate to spearhead developing countries' ESG evolution. The nation of 1.4bn with a Net Zero target by 2070 has the global gravitas and ambition needed to represent the myriad of developing nations in the energy-finance-climate nexus, especially as many developing nations have long complained that their plights are overshadowed by the political spotlight of developed nations. Ensuring the foundation of ESG is a level playing field across developed and developing nations (within reason) will strengthen its credibility and attractiveness for investors, i.e., regulations for supply chain management in India would be the same as those in the US, and so on.

$15bn

is what Africa, the world's poorest continent, can currently lose per year to climate change. This could reach $50bn in eight years.[2]

Source: [2] African Development Bank (ADB)

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