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## TD Economics

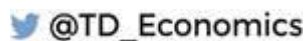
### Data Release: OPEC agrees to production cut

- OPEC surprised markets yesterday by announcing that the cartel has agreed to collectively cut production to a target range between 32.5 and 33.0 million barrels per day. This would translate into a 240-740k barrel per day decline from OPEC's estimated August output of 33.24 million barrels per day.
- To put this move into some perspective, the low end of the target range would amount to the production level recorded in the first quarter of this year, which was widely-considered to be elevated.
- Aside from the production targets, not many details are available. The organization did not specify targets for each member country. Rather, they agreed to form a committee to study and recommend the implementation of the production levels across the members of the cartel.
- While not included in the official OPEC statement, there has been some indication that Libya, Nigeria and Iran would be exempt from the production cuts, which puts some upside risk to these targets as any increases from these countries would have to be offset elsewhere.
- The cartel also did not indicate when the production quota will come into force, suggesting that it won't be before the next scheduled meeting on November 30<sup>th</sup>, at which time we expect to have these details ironed out.

### Key Implications

- Yesterday's agreement sparked a 5% jump in oil prices to US\$47 per barrel, but the rally has been more muted this morning. Markets have had time to digest the news and realize there is still a great deal of uncertainty around the deal.
- The fact that OPEC is willing to cut production signals that there is some increased flexibility around the hard stance that the cartel – and Saudi Arabia in particular – has been showing since November 2014 when it vowed to fight for market share. This is positive for the market. However, the lack of detail suggests that there are still a lot to work through before any action is actually taken – and there is a possibility that these upcoming negotiations could end without any agreement in November. Moreover, OPEC member countries are notorious for producing above target levels, which would just prolong the rebalancing process.
- OPEC will likely try to get some commitment from some non-OPEC producers – namely Russia – to help rein in production. With Russia's output currently at record levels and bumping up against capacity constraints, the country could agree to a production freeze at the very least.
- All told, while OPEC's willingness to reach a deal is positive, prices are not likely to gain much further traction on a sustained basis. OPEC cuts won't take place for some time, leaving the current oversupply situation in place. We continue to expect prices to remain in the US\$40-50 per barrel range in the near term, before gradually trending above US\$50 per barrel in 2017 as the market moves into a more balanced position.

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