



DOHA BROKERAGE

COMMODITY | INDIA

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CRUDE OIL 2012

WTI : \$120-\$130

BRENT : \$135-\$145

associate of DOHA BANK

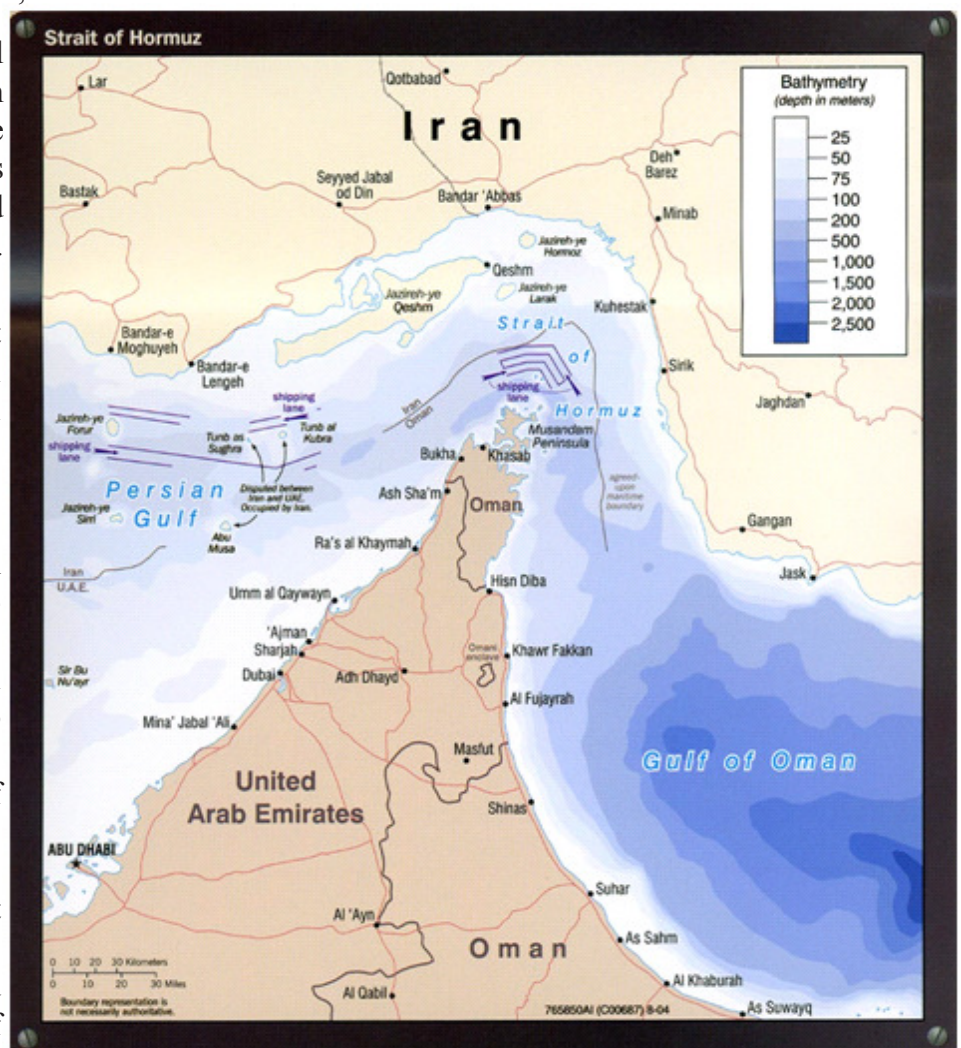


In 2011 when most of the commodities posted loss, crude ended its rally in elevated position with around 10% return. Arab uprising was the crux for building premium in crude in 2011. The focal point has now shifted towards Iran where, in 2011 it was over Libya. According to OPEC Iran exports 2.6mbd whose major buyers are China, EU, and India respectively. Italy is the biggest importer of Iranian oil in Europe, importing 183,000 barrels a day. Greece, Italy and Spain have been major buyers of Iranian oil in recent years, making the EU's sanctions strategy formidable. If Asian countries are also following the western path then it will affect the growth momentum of emerging economies. European countries are already placed at the brink of recession, so decision to ban Iranian crude will backfire. If global countries are losing Iranian crude then next alternate will be Saudi Arabia which is considered to be the last resort and is having 2.8mbd spare capacity according to latest data. So by utilizing the full capacity Saudi Arabia can compensate lost Iranian crude. Saudi Arabia's output in December rose to 10 million barrels a day, the highest level in at least 30 years, according to data from the EIA. The increase comes with a drop to 2.31 million barrels a day in OPEC spare capacity which means the group, would have less ability to respond with increased output if any supply disruptions occur in crude exporting countries besides Iranian crude embargo. But announcement of Iran to close the Strait of Hormuz changed the entire picture.

The Strait of Hormuz, a shipping lane bottleneck that sees through some 17 million barrels per day of crude oil, close to 20 percent of global demand. At its narrowest, the Strait is 21 miles wide, but there are only two traffic lanes, each two miles wide, one for inbound and the other for outbound traffic.

If Iran hinders flow of crude oil through Strait of Hormuz then only temporary solution would be release of crude from the world's strategic oil reserves which would override any short-term squeeze.

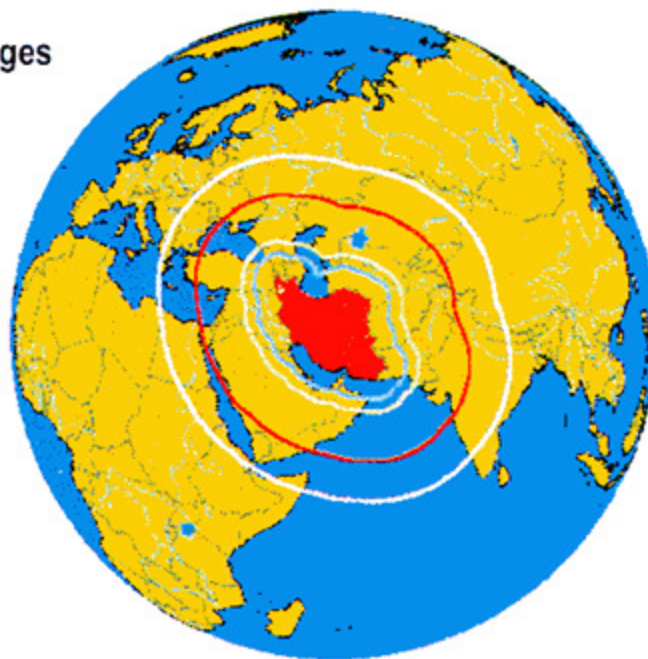
Then only major alternative outlet for some of the Gulf crude oil would be through the Saudi Arabian to port of Yanbu on the Red Sea, limited to roughly five million barrels per day. The strategic reserves crude held in storage in case of emergencies - total nearly 1.6 billion barrels, according to the International Energy Agency. That's enough to replace the 17 million barrels flowing daily through the Strait of Hormuz for 94 days. But it's highly unlikely that the Iranians could keep the strait blocked that long since U.S. fifth fleet has presence in the area, and shouldered the responsibility of keeping those sea lanes open.



Source: CIA, DBFS Research

Approximate Maximum Ranges of Iranian Missiles

- Inner Ring—SCUD B
- Second Ring—SCUD C
- Third Ring—MRBM 1
- Outer Ring—MRBM 2



Source: Federation of American scientists, DBFS Research

On Jan 23 European Union agreed in principle to enact an embargo on all purchases of Iranian oil effective from July 1, 2012, significantly increasing the West's financial war on Tehran. During severe economic crisis, Europe is taking wager in the anticipation that such an move would induce Iran to come to the negotiating table to discuss its nuclear ambitions and production of nuclear weapons. Date for the embargo might be fixed on the hope that the situation in Libya would stabilize and by then countries can find out alternate source so that the loss of Iranian supplies could be adequately compensated. But tit-for-tat Iran might halt crude exports to European nations before the July 1, so that EU will not get adequate time to find alternatives and even strategic petroleum reserves might not help to ease soaring crude price.

Crude Oil Spare Capacity (Million Barrels / Day)

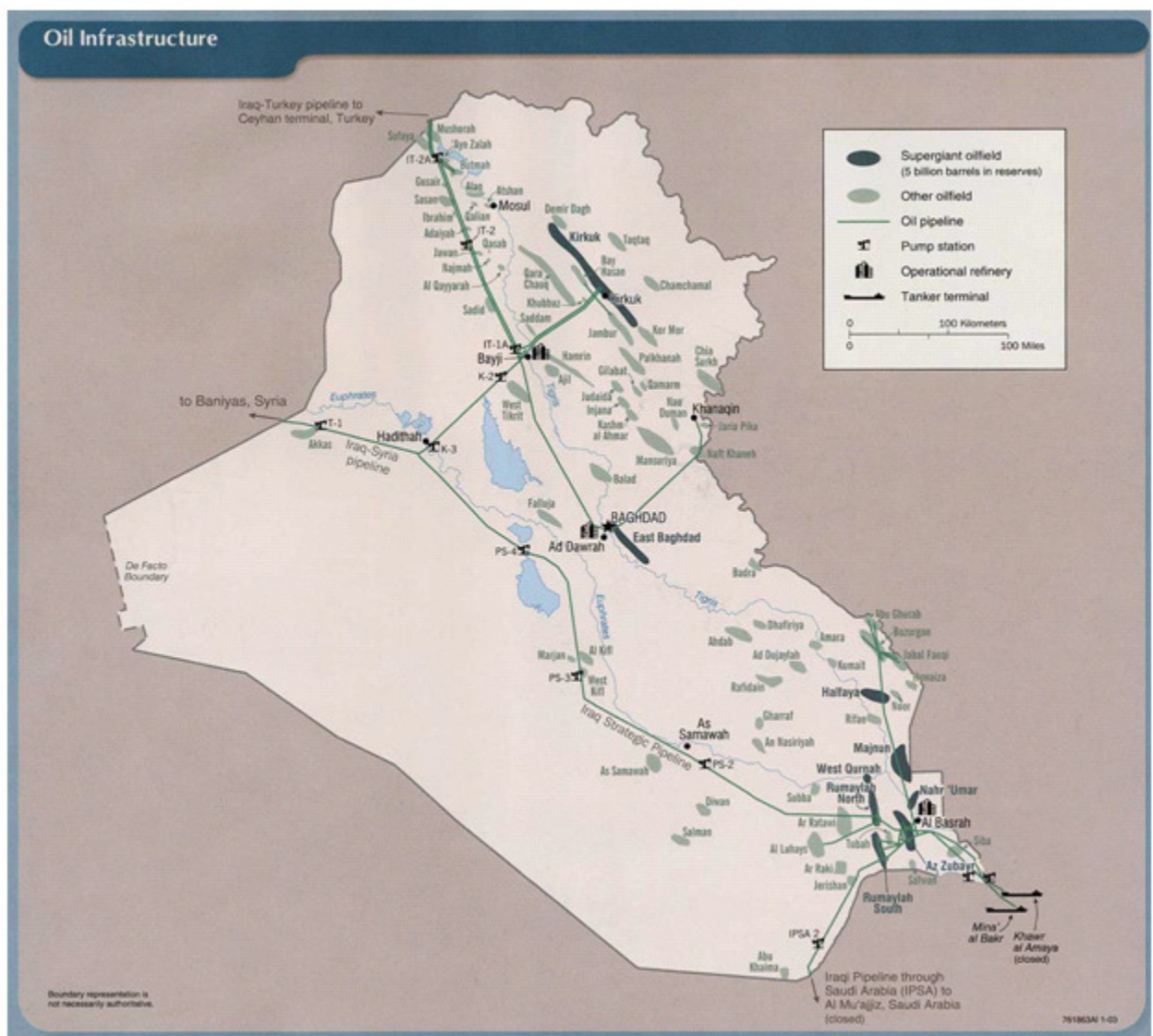
November 2011	Production	Capacity	Spare	Spare Capacity %	% of Spare Capacity
Algeria	1.27	1.27	0.00	0.0%	0.0%
Angola	1.85	1.85	0.00	0.0%	0.0%
Ecuador	0.48	0.48	0.00	0.0%	0.0%
Iran	3.60	3.60	0.00	0.0%	0.0%
Iraq	2.60	2.60	0.00	0.0%	0.0%
Kuwait	2.55	2.55	0.00	0.0%	0.0%
Libya	0.55	0.55	0.00	0.0%	0.0%
Nigeria	2.20	2.20	0.00	0.0%	0.0%
Qatar	0.85	0.85	0.00	0.0%	0.0%
Saudi Arabia	9.40	12.25	2.85	23.3%	97.9%
U.A.E.	2.60	2.66	0.06	2.3%	2.1%
Venezuela	2.20	2.20	0.00	0.0%	0.0%
OPEC Total	30.15	33.06	2.91	8.8%	100.0%

Source: OPEC, DBFS Research

The Energy Information Administration said global oil demand rose by about 1 million barrels a day last year, with a drop of 420,000 barrels a day in demand from the major industrialized nations cutting the impact of a 1.46 million barrel-a-day rise in demand from emerging nations, led by China. China's full-year crude imports totaled 253.78 million tons, or about 5.1 million barrels a day, up 6.0% from 2010, the data from General Administration of Customs shows. In 2012, Chinese demand is expected to rise by 5.4%, to 10.36 million barrels a day, while 2013 demand will average 10.92 million barrels a day, up 5.1% EIA said.

Demand in the industrialized nations in the Organization for Economic Cooperation and Development is expected to drop by a slower rate, of 120,000 barrels a day this year, and inch higher in 2013. Global demand will average 89.38 million barrels a day this year, up from 88.11 million barrels a day in 2011. In 2013, demand is forecast to climb to 90.85 million barrels a day. Oil production outside of the Organization of Petroleum Exporting Countries will rise 900,000 barrels a day in 2012, and by 800,000 barrels a day in 2013, meaning it won't keep pace with rising global oil demand.

Weak domestic oil demand last year led to the U.S. becoming a net exporter of refined petroleum products for the first time since 1949, at a rate of 380,000 barrels a day. Net exports are expected to average 310,000 barrels a day in 2012 and 290,000 barrels a day in 2013 according to EIA. The Energy Information Administration said it sees total oil use in the U.S., the world's biggest oil user, at 18.96 million barrels a day this year, up 0.5%, or 90,000 barrels a day from the year earlier and in 2013, demand will inch up 50,000 barrels a day, or 0.3%, to 19.01 million barrels a day.



Source: CIA, DBFS Research

Iraq's crude oil production has jumped to more than 3 million barrels per day, and is expected to rise to 3.4 million by the end of 2012. Iraq's first single-point mooring facility for oil tankers is expected to inaugurate recently, with a second unit to be in place within six months, a third by the end of 2012, and a fourth in 2013. Each facility will expand Iraq's exporting capacity by 850,000 barrels per day. After long 8 years of invasion American troops retreat from the country, marks a transition of power that has given Iraq's new government full control of the country. There is still dark cloud over the Iran's political stability after the annihilation of Saddam Hussein's regime and frequent vandalism is reporting from the country which might target pipelines and related energy facilities. Since the news of sabotage in Iran might bolster crude oil price, we cannot consider free flow of crude from the country. Whenever spare capacity runs out there is high probability of rising in crude price when market absorbs supply disruption news. Any independent decision from Israel - an unforeseeable factor on Iran will act as a catalyst in boiling tension in Middle East.

Sanctions on Iran

In 1979, after the U.S. permitted the exiled Shah of Iran to enter the United States for medical treatment, and after rumors of another U.S. backed coup and re-installation of the Shah, a group of radical students took action in Tehran by seizing the American Embassy and taking hostage the people inside. The United States responded and President Carter issued Executive Order 12170 in November 1979 freezing about \$12 billion in Iranian assets, including bank deposits, gold and other properties. This is the first incident for rivalry between and Iran. Goods or services from Iran cannot be imported into the United States, either directly or through third countries, with the following exceptions: gifts valued at \$US100 or less; information or informational materials; foodstuffs intended for human consumption; certain carpets and other textile floor coverings and carpets used as wall hangings.

After the 1983 bombing of the U.S. embassy and Marine barracks in Lebanon, the Reagan administration officially declared Iran "a sponsor of international terrorism" in January 1984. This designation rendered Iran ineligible for various forms of U.S. foreign assistance. The Reagan administration additionally withheld funds from international organizations in 1985 that were equal to the amounts allocated by those organizations for Iran. Reagan ordered U.S. executive directors at international financial institutions, such as the World Bank and the International Monetary Fund, to vote against issuing loans to Iran in 1988. Given the leading role of the United States at these institutions, this significantly limited their support for Tehran. The passage of the U.S. Arms Export Control Act in August 1986 prohibited the sale of U.S. arms, including spare parts, to Iran.

In March 1995, President Clinton issued Executive Order 12957 prohibiting U.S. trade in Iran's oil industry. In May 1995, President Clinton issued Executive Order 12959 prohibiting any U.S. trade with Iran.

In 1996, the United States Congress passed the Iran-Libya Sanctions Act (ILSA). Under ILSA, all foreign companies that provide investments over \$20 million for the development of petroleum resources in Iran will have imposed against them two out of seven possible penalties by the U.S. a step taken to reduce the risk that sanctions would place U.S. firms at a disadvantage.

- denial of Export-Import Bank assistance;
- denial of export licenses for exports to the violating company;
- prohibition on loans or credits from U.S. financial institutions of over \$10 million in any 12-month period;
- prohibition on designation as a primary dealer for U.S. government debt instruments;
- prohibition on serving as an agent of the United States or as a repository for U.S. government funds;
- denial of U.S. government procurement opportunities (consistent with WTO obligations); and
- a ban on all or some imports of the violating company.

In September 2006, the U.S. government imposed sanctions on Bank Saderat Iran, barring it from dealing with U.S. financial institutions, even indirectly. The move was announced by Stuart Levey, the undersecretary for treasury, who accused the major state-owned bank in Iran of transferring funds for certain groups, including Hezbollah. Levey said that since 2001 a Hezbollah-controlled organization had received 50 million U.S. dollars directly from Iran through Bank Saderat. As of November 2007, the following Iranian banks were prohibited from transferring money to or from United States banks.

- Bank Sepah
- Bank Saderat Iran
- Bank Melli Iran
- Bank Kargoshaee (aka Kargosa'i Bank)
- Arian Bank (aka Aryan Bank)

In October 2007 Washington imposed sanctions on Bank Melli, Bank Mellat and Bank Saderat and branded the Revolutionary Guards a proliferator of weapons of mass destruction. In October 2009, the Treasury also sanctioned Bank Mellat in Malaysia and its chairman.

Congress approved tough new unilateral sanctions on June 24, 2010, aimed at squeezing Iran's energy and banking sectors, which could also hurt companies from other countries doing business with Tehran. The June, 2010 law imposes penalties on firms that supply Iran with refined petroleum products worth more than \$5 million over 12 months. It also effectively deprives foreign banks of access to the U.S. financial system if they do business with Iranian banks or the Revolutionary Guards. The Treasury also took a separate step to squeeze Iran's energy sector by identifying some 20 petroleum and petrochemical companies as being under Iranian government control - an action that puts them off limits to U.S. businesses under a general trade embargo.

In July 2010 the Treasury added Post Bank of Iran to its list of specially designated proliferators of weapons of mass destruction, marking the 16th bank in Iran that it has sought to cut off from the international financial system. Since Bank Sepah was sanctioned in 2007, Post Bank has stepped in to handle and disguise international transactions on its behalf.



Courtesy: BBC, DBFS Research

In May 2011 United States hit Venezuelan state oil company and six other smaller oil and shipping firms for engaging in trade with Iran in violation of the U.S. ban, prompting fury from Hugo Chavez's government. Venezuela's oil-reliant economy ships roughly 45 percent of its crude to the United States, making up about 10 percent of U.S. imports. The other companies covered by the new U.S. sanctions are PCCI, the Royal Oyster Group and Speedy Ship of the United Arab Emirates, Tanker Pacific of Singapore, Ofer Brothers Group of Israel and Associated Shipbroking of Monaco.

In June 2011 Washington prohibited U.S. entities from any transactions with Tidewater Middle East Co., which operates seven port facilities in Iran, and Iran Air, which serves 35 international and 25 domestic destinations with a fleet of about 40 aircraft.

On Nov 2011 the United States named Iran as well as its central bank as an area of "primary money laundering concern," a step designed to dissuade non-U.S. banks from dealing with it. The United States also blacklisted 11 entities suspected of aiding its nuclear programmes; and expanded sanctions to target companies that aid its oil and petrochemical industries.

On Dec. 31, 2011, U.S. President Barack Obama signed into law a defence funding bill that imposes sanctions on financial institutions dealing with Iran's central bank, which is the main conduit for oil revenues. Sanctioned institutions would be frozen out of the U.S. financial markets. The sanctions would take effect after a 2-6 month warning period. Under the law, the president can issue waivers if doing so is in the national security interest of the United States.

On 23rd Jan 2012 Washington sanctioned Iran's third-largest bank, Bank Tejarat, closing off one of Tehran's only remaining conduits for trade with the Western world. The Treasury specifically charged Bank Tejarat with assisting Iran's Atomic Energy Organization with trying to procure uranium from the international market last year. The Treasury's sanctioning of Bank Tejarat marks the 23rd Iranian-linked financial institution blacklisted by the U.S. since 2006.

Britain on Nov. 21, in a coordinated action with the United States and Canada, Britain ordered all British financial institutions to stop doing business with their Iranian counterparts, including the Iranian central bank.

Canada announced on Nov. 21 it would immediately ban the export to Iran of all goods used in the petrochemical, oil and gas industry, as part of an international sanctions package.

Switzerland added five people and 111 organisations to its list of Iranian entities under sanction on Nov. 18. Earlier sanctions included a ban on certain financial transactions and Swiss companies selling or delivering so-called dual use goods.

The European Union has broadened its sanctions against Iran to target 180 new individuals and organisations linked to the Islamic republic's shipping line and the Revolutionary Guards Corps, suspected of involvement in a covert nuclear weapons programme.



Source: CIA, DBFS Research

Japan imposed a ban on transactions with some Iranian banks, investments with the Iranian energy sector, and asset freezes against individuals and entities involved with Iran's nuclear program

India enacted a ban on the export of all items, materials, equipment, goods, and technology that could contribute to Iran's nuclear program

Australia has imposed financial sanctions and travel bans on individuals and entities involved in Iran's nuclear and missile programs or assist Iran in violating sanctions, and an arms embargo.

South Korea imposed sanctions on 126 Iranian individuals and companies.

Israel banned business with or unauthorized travel to Iran under a law banning ties with enemy states. Israel has also enacted legislation that imposes sanctions on any companies that violate international sanctions. Israel later extended the sanctions by imposing a series of administrative and regulatory measures to prevent Israeli companies from trading with Iran, and announced the establishment of a national directorate to implement the sanctions.

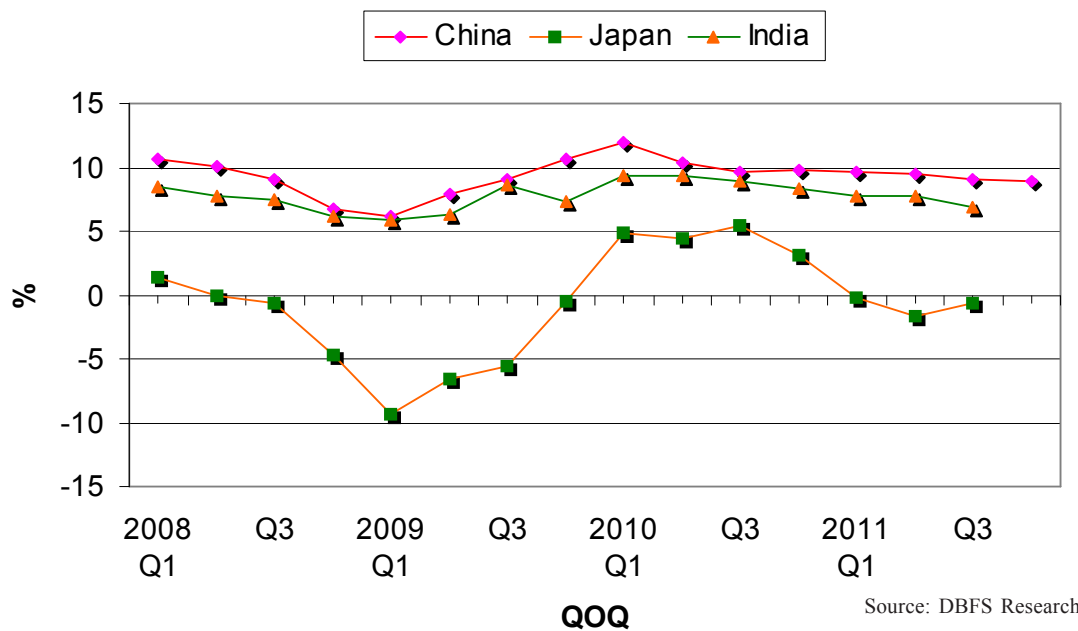
U.N. SANCTIONS:

- The Security Council has imposed four sets of sanctions on Iran, in December 2006, March 2007, March 2008 and June 2010.
- The first covered sensitive nuclear materials and froze the assets of Iranian individuals and companies linked with the nuclear programme.
- The second included new arms and financial sanctions. It extended an asset freeze to 28 more groups, companies and individuals engaged in or supporting sensitive nuclear work or the development of ballistic missiles.
- The third increased travel and financial curbs on individuals and companies. It expanded a partial ban on trade in items with both civilian and military uses to cover sales of all such technology to Iran.
- A Security Council resolution passed on June 9, 2010, called for measures against new Iranian banks abroad if a connection to the nuclear or missile programmes was suspected. - It expanded a U.N. arms embargo against Tehran and blacklisted three firms controlled by IRISL and 15 belonging to the Islamic Revolutionary Guard Corps. The resolution called for setting up a cargo inspection regime.

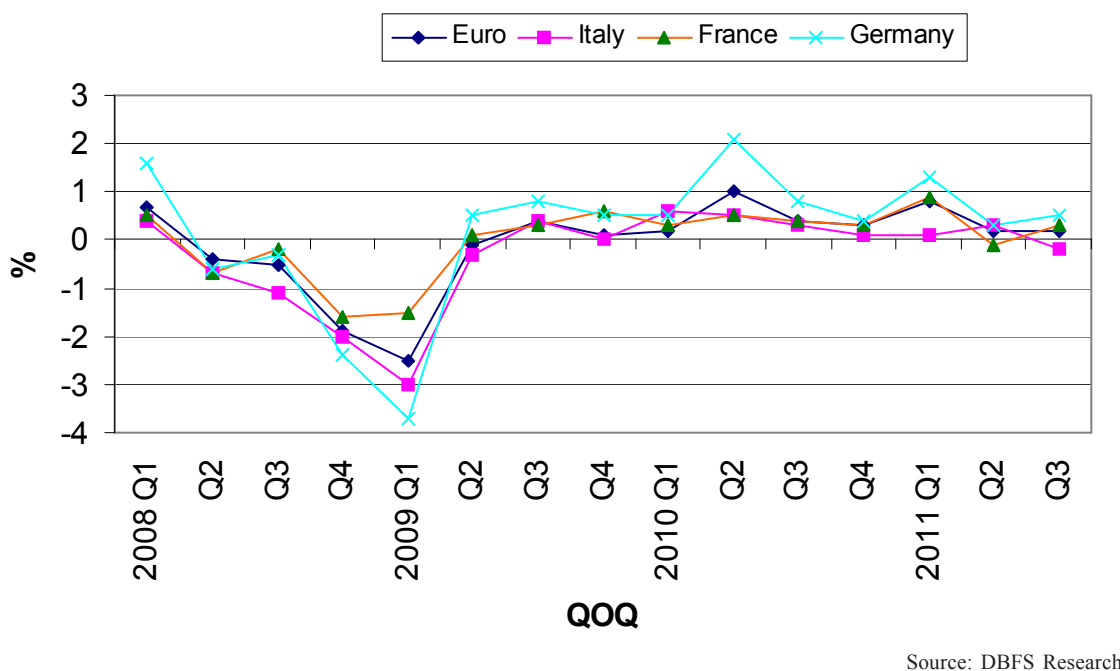
Global Economic Trend

Year 2011 started with a mixed growth rate across global economies – Strong first quarter GDP growth rate was reported from euro zone while GDP data from Asian economies shows that growth was hampered and US GDP growth rate has landed just above zero percent growth rate. Devastating earthquake and followed by tsunami in Japan leads to supply disruptions and sharp contraction in domestic demand which reflected in Asian growth rates.

GDP Growth Rate



GDP Growth Rate



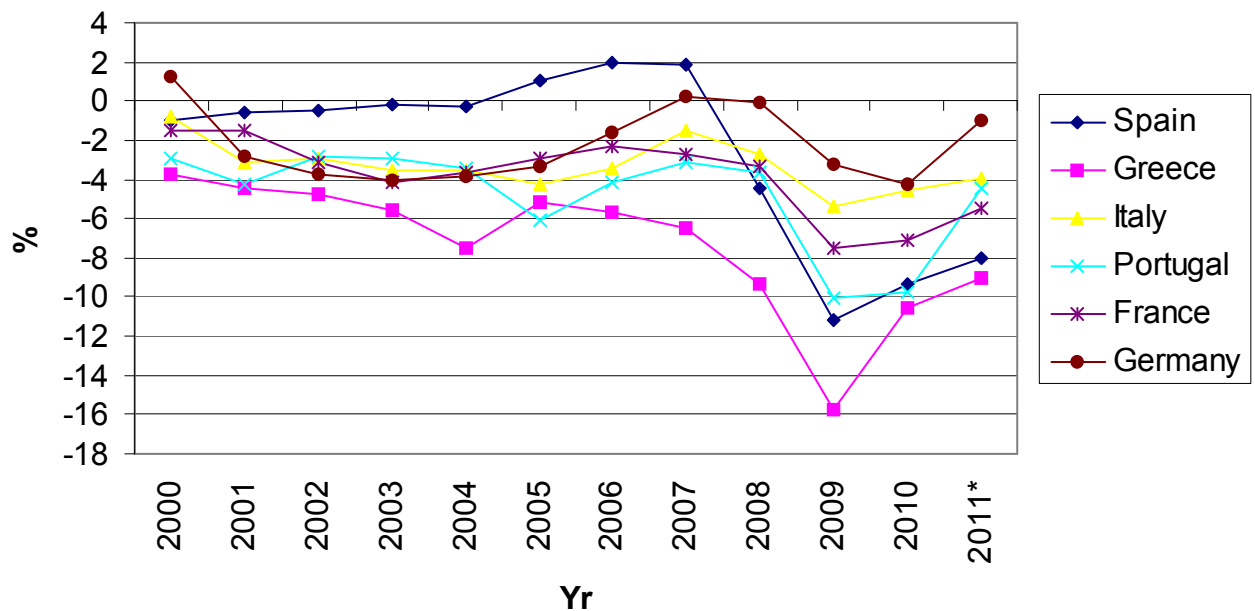
From second quarter onwards, sovereign debt crisis in Europe surfaced, with Greece borrowing costs started to rise again and country is unable to dig itself out of crisis with policies that can only deepen recession. Wide protests were staged across the streets of Athens against austerity measures which eat into the layman's pocket.

Meanwhile many uphill economies are facing with soaring inflation rates – to an extent hike in crude oil price due to the Arab uprising underpinned inflation rate. To tackle the skyrocketing inflation rate many countries have adopted tightening measures to reduce liquidity in the economy.

In August S&P came out with bold decision to lower its long term sovereign credit rating on USA to AA+ from AAA, which shattered the financial markets. S&P pointed out that prolonged controversy over raising the statutory debt ceiling and the related fiscal policy debate indicates that further near-term progress containing the growth in public spending, especially on entitlements, or on reaching an agreement on raising revenues is less likely than they previously assumed and will remain a contentious and fitful process. The move reflects the deterioration in the global economic standing of the United States, which has had a AAA credit rating from S&P since 1941.

Heightened financial turmoil due to sovereign debt crisis and several credit downgrades led the capital flows to developing countries have weakened sharply as investors withdrew substantial sums from developing-country markets in the second half of the year. Overall, gross capital flows to developing countries plunged to \$170 billion in the second half of 2011, only 55 percent of the \$309 billion received during the like period of 2010.

Govt Budget (% of GDP)



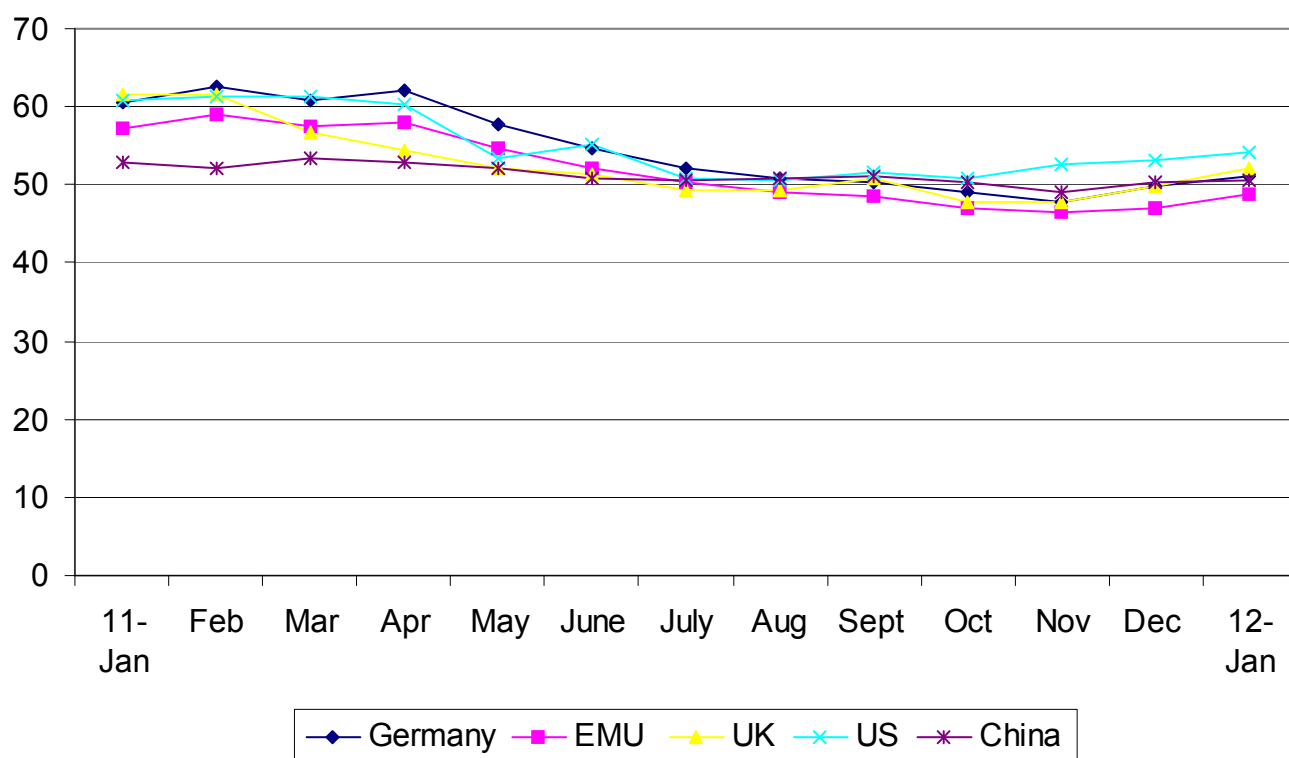
Source: DBFS Research

A spear was struck in the heart of investors when Italian borrowing costs spiked above 7% in November, raising fears the country will be forced to seek a bailout that could break Europe financially. Portugal and Ireland were forced to seek out bailout package after sovereign debt surpassed perilous 7% level. It is essential to keep Italian bond yields less than 7% because unlike other nations, Italy is too big to bail out.

From halfway of 2011 onwards PMI data from major economies shows contraction and Asian exporters lost orders from Europe which is a key market. Due to tightening liquidity and debt crisis in Europe, growth rate of Asian economies including China dived to trough with many feared hard landing is possible on Asian giant.

To avoid hard landing the People's Bank of China lowered its reserve requirement ratio for financial institutions by half a percentage point in the end of November 2011. It was the first such cut in the ratio since 2008, and a change in course after the ratio was raised five times in 2011. The move is intended to increase liquidity, ramping up the flow of money into the economy to make up for concerns about slackening demand for Chinese products both domestically and abroad, particularly from Europe. Lowering the reserve requirement by half a percentage point was equivalent to injecting 400 billion yuan, or \$63 billion, into the banking industry. Country is likely to cut its reserve requirement ratio for banks at least twice again during the first half of 2012.

Global PMI Data

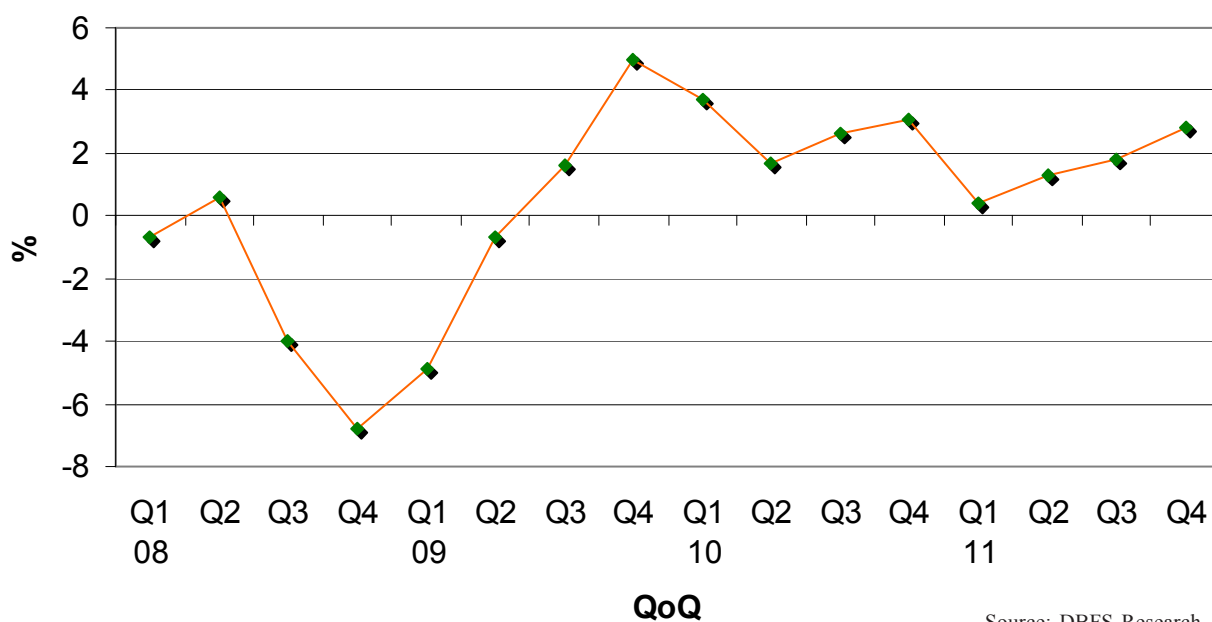


Source: DBFS Research

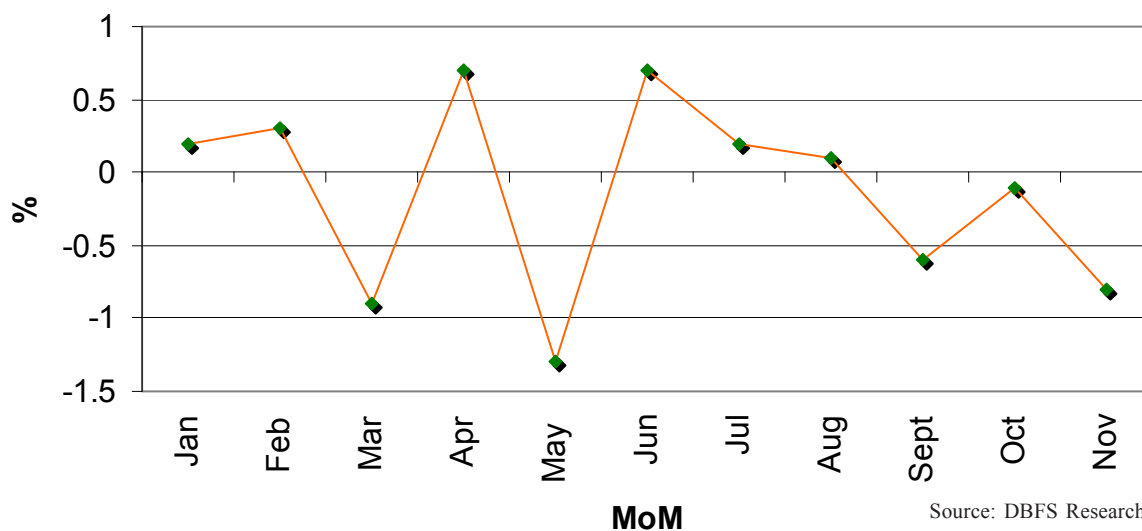
In December, the ECB channeled hundreds of billions of euros to the region's banks through a new program offering three-year loans at low interest rates. The program gave the market an important psychological boost by ensuring the region's banks had access to financing. The central bank's program has enabled lenders to borrow cheaply from the ECB and use that money to buy higher-yielding government debt, pocketing the difference in yield which leads to surge in demand for government bonds that eased bond yields.

While rest of the advanced economies faced downside in the fourth quarter, US stay apart from those even after S&P downgrades its credit ratings. Economic indicators pointed out the improvement in the health of US economy with GDP quarter growth rate stands at 2.8% and the unemployment rate fell to 8.5 percent in December of 2011, the lowest since February 2009.

US GDP Growth Rate

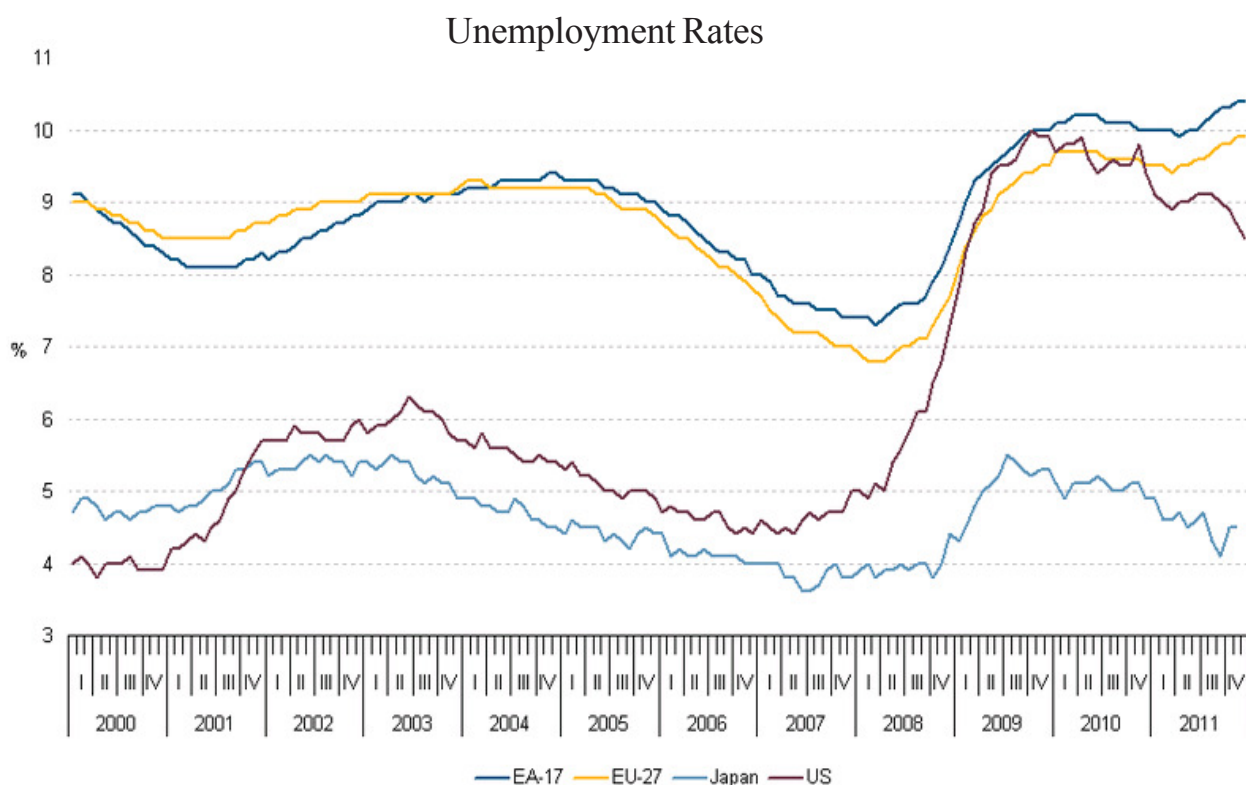


EU Retail Sales



In 2012 Europe will have hard time because government will have to bring down budget deficit, for that countries have already introduced stringent austerity measures. But these austerity steps will not be adequate so that we can expect more in this year also. These draconian measures will pull the people from spending and continent will slide to mild recession since there is less domestic demand. By analyzing the EU retail sales from mid of 2011 we can understand consumer expenditure is coming down which is the reflection of implementing austerity measures. Soaring unemployment is another threat EU governments facing. The greatest challenge for the global economy in this slow growth environment is to raise productivity without losing job opportunities for the millions who are looking for reasonably paid jobs to support their living standards.

IMF is expecting world GDP growth of 3.3% in 2012, down from the 4.1% it forecast in September and the World Bank is now expecting global economy to expand 2.5 percent in 2012 versus the 3.6 percent projected in June.



Source: Eurostat, DBFS Research

Conclusion:

Two major incidents which will result in tug of war in crude price will be friction between Iran and western countries and Euro recession. If Iran issue gets settled then crude price will stay between \$85-\$100 levels otherwise we can expect a spike to \$150 and then WTI might settle around \$120-130 levels and Brent to trade in the range \$135-\$145 levels.

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