Portland Energy Market Report

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In all the noise and chaos that is surrounding the ongoing crisis in the Middle East, the decision by the United Arab Emirates (UAE) to leave OPEC with "immediate effect" (May 1st) was certainly a surprise. Was the timing deliberate, because attention was elsewhere and thus the news could be buried? Or was it the opposite - an intentional attempt to ratchet up crisis levels? And why would one of the long-standing members of OPEC choose to leave the organisation anyway?

The UAE as a country was only formed in 1971, when the process of independence (from Britain) brought together seven separate Emirates; Abu Dhabi, Dubai, Sharjah, Ajman, Umm Al Quwain, Fujairah, and Ras Al Khaimah. Over 50 years later, this "new" country with a population of 11 million is the 4th largest economy in the Middle East (after Turkey, Saudi Arabia and Israel), has a prosperously high GDP per person (~$50K) and extremely low unemployment levels (less than 2%).

As you have might guessed, much of this wealth comes from the UAE's oil industry, which accounts for around 30% of GDP. The country has the 7th largest oil reserves in the world, with the first discovery of oil being made in 1958 (Umm Shaif field). By 1971, the Abu Dhabi National Oil Company (ADNOC) had been formed to manage all oil and gas resources and further diversification of the oil production "model" soon followed. Refinery construction began at pace (8 in total) and this culminated in the completion of the flagship Ruwais complex in 1982, which today is the 4th largest refinery in the world (800,000 barrels per day). Alongside oil refining, the Petrochemicals sector was also developed, which continued the shift from crude oil exports to higher-value chemical and plastics production.

OPEC was established in 1960, but the UAE was not a founding (Iran, Iraq, Saudi, Kuwait and Venezuela) member. Abu Dhabi joined the organisation as an individual Emirate in 1967 and (what then became) the UAE has since been a loyal and non-dissenting participant. The UAE rarely quibbled about the production quotas set, even though by the 1980's, the state has had the capacity to produce far more oil than OPEC's permitted limits. Over the last 10 years however, policy differences and a desire to increase oil revenues, have been growing. In 2021, the UAE came out with a "Net Zero by 2050 Strategic Initiative" and this put it at odds with most other OPEC members. On the surface, this seemed to be a laudable ambition to move the needle "greenwards" and without doubt, the UAE has invested heavily in renewables (not least in the use of solar energy to power their multiple desalination plants). Dig a little deeper though and we see a more calculated game at play. There is a fear amongst Emiratis that oil consumption will reduce over time as a result of decarbonisation and in line with Net Zero targets. Therefore, it makes sense to monetise oil reserves as soon as possible, before demand starts to dry up. This Machiavellian strategy requires the increasing of oil production here and now, which only an exit from OPEC will allow.

Prior to the war in Iran, the UAE was producing 3.4m barrels per day (bpd), which was bang on the quota set by OPEC. However, the country has the capacity to produce over 4m bpd and the Department of Energy has mooted a 2027 target of over 5m bpd. In addition to the clear economic benefit of selling an extra 1.5m bpd on global markets, the decision to leave OPEC also generates political capital. The UAE is a close ally of the USA and the current Trump Administration has frequently called for the break-up of OPEC. By leaving the cartel, the UAE is falling in line with US wishes, whilst also freeing up Abu Dhabi's $1.7trn Sovereign Wealth Fund (Abu Dhabi Investment Authority = ADIA) to invest in global markets, energy diversification and military hardware; all of which increasingly need to be disconnected from OPEC quotas.

However, the decision of the Emirates to leave OPEC has had, and will have, minimal impact on current market conditions. Even if the UAE was able to export their increased production out of Fujairah (which crucially is located outside of the Strait of Hormuz), that would still not be enough to offset the total amount of oil blockaded inside the Strait. In the longer-term, the UAE will of course become a bigger oil player, but it will still be supplying less than 5% of the world's oil. And the impact on OPEC itself will be similarly muted. Without the UAE, the cartel continues to control almost a third of global oil supplies and with the OPEC + part (Russia, Mexico etc), that volume goes up to 40%. These figures would surely indicate that the organisation will have few problems maintaining their global significance.

Nonetheless, this event marks one of the most high-profile exits from OPEC and a symbolic one at that. Previous departees (Ecuador, Angola, Indonesia) were much smaller producers, significantly less politically stable and none of them had anything like the same geo-political influence in their respective regions. Some observers have also pointed out that along with Saudi Arabia, the UAE was the only OPEC member with significant spare capacity. In theory, this allowed it to ease prices by pumping more oil, but OPEC's aim has never really been to reduce prices, so this point has few "real world" implications. Which takes us to the overall headline conclusion and that is the loss of the UAE from OPEC's membership, will have little impact on either global markets or the cartel itself.