What's in store for 2021 and beyond?

APICORP's Top Picks 2021

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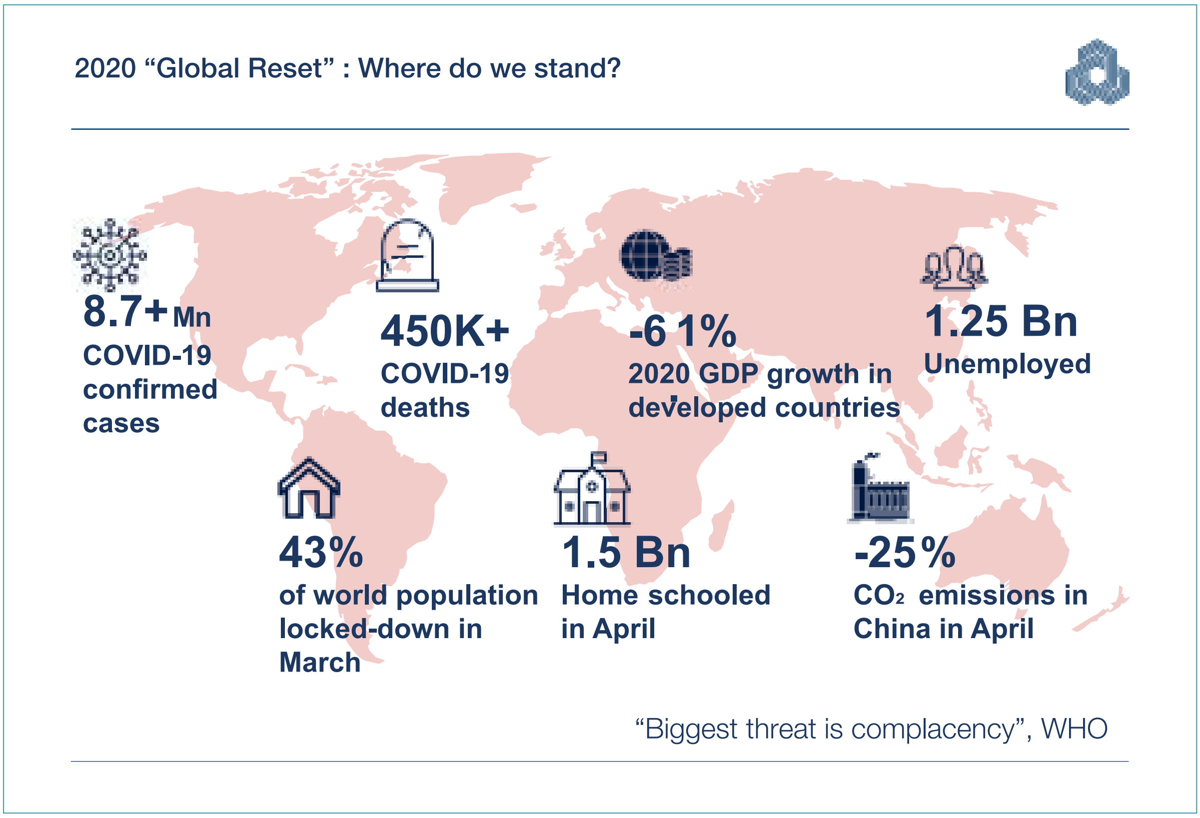
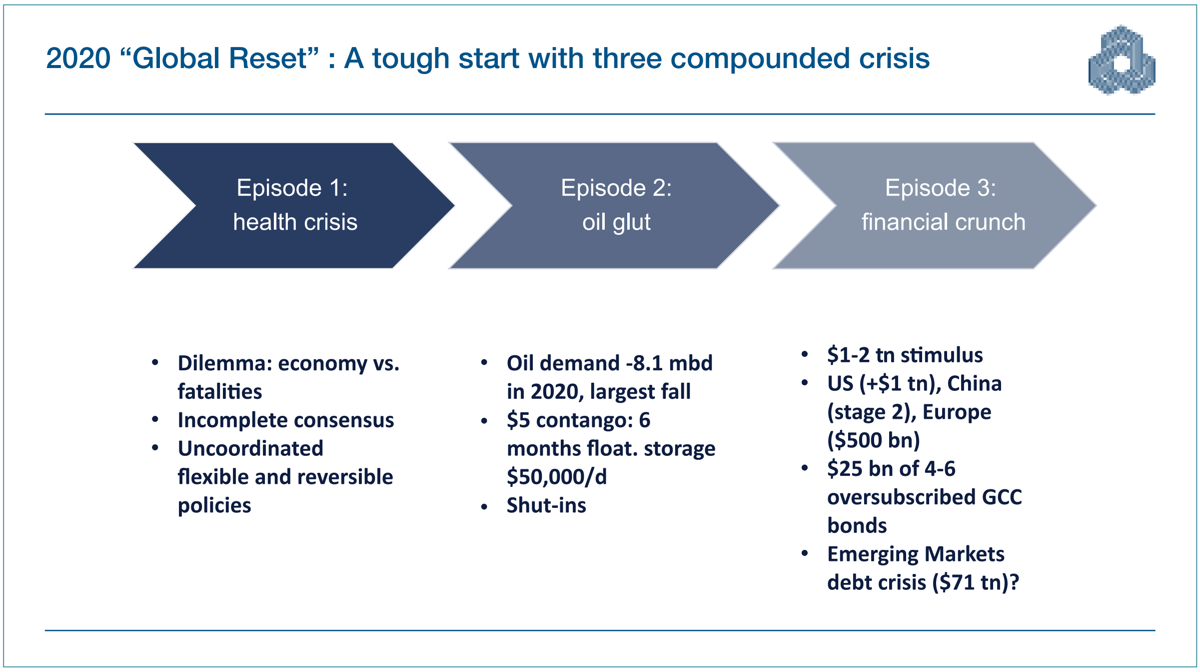
"Optimism", "recovery", "rotation", "rebalancing", "reset"; these are the buzzwords dominating the narratives of the various recent outlooks. Financial and energy market outlooks in particular contrast the short-term anxiety with medium-term optimism.

On the financial front, Goldman Sachs thinks "the path may be tricky as the market balances spot growth weakness with a forward outlook that is more supportive," while Barclays overweighs "risk assets over core bonds". In energy, the market faces a boringly wide consensus of moderate oil and gas prices for the large part of 2021, barring any black swans. Daniel Yergin, a leading authority on energy, sees a 'Virus Alley' of $40-50 per barrel that is conditioned by the virus to the downside and by the deployment of effective vaccines to the upside.

From APICORP's perspective, and as we wrote in March 2020 in our *MENA Energy Investment Outlook 2020-2024*, we see that "projections extend shutdowns to 4Q2020 in countries considered today as extreme cases, but plans are increasingly flexible and – more importantly – reversible."

By June 2020, the idea of a 'Global Reset' in the sectors most severely impacted by the pandemic - including energy - had taken root in parallel with the unprecedented pandemic. For 2021, we therefore aim to explore the ensuing diverging paths between countries, corporations and investors.





Source: APICORP MENA Energy Investment Outlook webinar presentation (June 2020)

Balancing caution and optimism: A long winter drag and light at the end of the tunnel

Assuming the deployment of effective vaccines and absence of future virus mutations, the path to economic and energy recovery will continue to be shaped by policy (e.g. fiscal and monetary accommodation, first Fed hike unlikely until 2024, a mix of unilateral and multilateral oil production management, etc.). Consequently, the recovery itself will also be mixed, asynchronous and not necessarily sustainable for all. Sluggish domestic demand and inflation, coupled with a weak dollar and a pile of debt and stimulus packages, will likely lead to a rebound in 2021. The question here is how sustainable that recovery will turn out to be.

APICORP's *Beyond energy: How MENA Economies Emerge Post-2021* white paper, which was issued in November 2020, highlighted the diverging paths between countries, noting that while a few countries in the region face difficult yet manageable trade-offs, others face rather daunting choices.

For hydrocarbon importers, much will depend on their ability to quickly capture the opportunities of the post-COVID-19 world, namely the restructuring of certain global value chains (GVCs). For hydrocarbons producers, the next decade might prove to be the last window for low-cost low-carbon MENA oil and gas producers to firmly re-establish their market share.

On aggregate, only a few countries possess the ingredients in terms of governance, policy credibility, public finances management and strong economic basis, to translate the sizeable economic stimulus packages that were deployed to counter the pandemic into productive debt and sustainable recovery. Where MENA economies stand one year later will be an important and interesting exercise in the second half of 2021.

On the geopolitical front, in scenario planning, it is generally accepted that a deep recession can bring solidarity in MENA. 2020 might have brought the end of embargoes, yet these steps are not sufficient to achieve sustainable economic development in the region, especially with the widening income gaps between countries due to the 'Global Reset'.

As far as oil and gas prices are concerned, our main concern has been the volatility resulting from extreme market conditions and investment cuts. Admittedly, the historic negative West Texas Intermediate (WTI) prices in April 20, 2020 were shrugged off by commentators as a one-off aberration in futures. However, the Japan-Korea Marker (JKM) jumping to an all-time high of $28.2 per MMbtu on January 11, 2021, was a strong reminder of the possibility of a faster-than-expected market tightness, including in oil markets.

In theory, digitalization and data are supposed to enhance market stability by improving transparency, particularly in commodities where price volatility could also be induced by non-physical trading (e.g. xxx), and we intend to shed more light on the role of financial players in this linkage between digitalization and market stability in our 2021 reports.

Keeping energy investments and sector transformation in check:

Faced with a 20%+ year-on-year decline in global energy investments exceeding (source: International Energy Agency) and a recovery that is likely to take longer than it did post-2014, the energy sector is amid a 'Global Reset" that will likely result in industry consolidations, mergers and acquisitions and strategic jostling and repositioning by industry players.

In their December 2020 report, the International Energy Forum and Boston Consulting Group highlight that "because the industry has removed significant costs from upstream operations since the price downturn of 2014, twice as much production is available at $50 per barrel as was available prior to the downturn. Still, several changes in the industry tend to increase the likelihood of price spikes and more prolonged elevated prices."

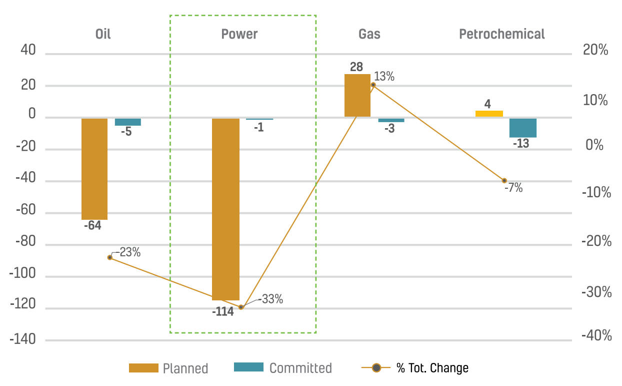
Our hypothesis is that only a few energy producers – specifically low-cost oil and gas and low-carbon power producers – will be able to emerge as clear winners in the post-Covid-19 world. A few of these potential winners are from the MENA region, but will they be more consolidated and integrated?

As we noted in our *MENA Gas & Petrochemicals Outlook 2020-2024*, committed gas investments in the MENA region held steady in stark contrast to the considerable reduction in global oil and gas investments. Planned investments meanwhile jumped by 29% due to increased commitment to gas-to-power projects, improved monetization of gas as a feedstock, and strategic market share positioning for gas exports.

The subsequent *MENA Power Investment Outlook 2020-2024* positioned the MENA region as a strong candidate for becoming a major hydrogen-exporting region and other net-zero carriers (e.g. ammonia) due to the combination of low-cost gas resources and low-cost renewable energy.

Even if reduced by 20%, APICORP's five-year energy investment outlook will still require substantial input from the private sector. This remains true even if the MENA region continues to tap the debt capital markets at unprecedented levels, as witnessed in 2020 when GCC governments and companies issued a record

Outlook Y-O-Y Change in Investments by Sector



Source: APICORP

$126 billion in U.S. Dollar and Islamic securities. We maintain that "the current vicious circle of low revenue, low investment, low output needs to be broken, and a virtuous cycle of investments in lower cost, lower carbon, sustainable assets needs to be induced."

As a result, we plan on consolidating APICORP's flagship MENA Energy Investment Outlook 2021-2025 and its sectoral deep-dive outlooks into a single integrated report covering gas, petrochemicals and power. "

Financing energy transition in an era of heightened investor expectations (returns and ESG):

This coming decade will be defined by three historic global challenges: Building a resilient recovery from the pandemic, achieving the UN goal of universal access to sustainable energy for all populations (SE4ALL) and charting an ambitious course for tackling the climate emergency.

Nobody was seriously expecting a fast market rebalancing in oil and gas. More importantly, this is a dramatically entrenched industry that has been hit by three crises in one decade. With its modest growth expectations even before the 2020 crisis hit, the sector witnessed an investor exodus and reached the dubious position as the provider of – by far – the lowest returns to shareholders over the past decade.

In our paper *Energy after Covid-19: Financing a Neo-Renaissance,* we argue that funding is key to enable energy technologies and existing and new low-carbon to bring their respective intrinsic values to the table. Even if renewable energy is perceived by investors as one of the preferred infrastructure sectors, it generally does not yet offer all the characteristics that conventional funding looks for in terms of market capitalization, dividends, and liquidity. While renewables benefited from new financing mechanisms, the rest of the low-carbon value chain – such as carbon capture, utilization and storage (CCUS) – is lagging.

Therefore, APICORP contributed alongside other banks and financial institutions under the auspices of the Clean Energy Ministerial to the *Ten Financing Principles for CCUS*, which aims to "establish a business case for CCUS and kick-start the financing of CCUS projects globally[1].

With the 26th UN Climate Change Conference of the Parties (COP26) set to take place in Glasgow in November, supporting the energy industry in the global debate on the actual implications of net-zero targets by 2050 will require a reframing of the energy transition debate (i.e. a lot of engagement and no exclusion). In essence, all technologies will be needed.

Conclusion:

Is January 2021 too early for optimism? For investors, commodities players, producers and consumers at least, last year's cacophony over V, W, U, or even L-shaped recoveries is now a distant memory. Keep the Faith. With a capital K*.

*(*a K-shaped recovery is characterized by a divergence in the recovery paths- where parts of the economy experiences a V-shaped recovery while other parts suffer from a slower more protracted L-shaped recession).*

1. https://ieaghg.org/ccs-resources/blog/key-financing-principles-for-ccus-launch-event-by-cem-ccus-initiative