

# Oil price shock could be followed by large geopolitical tremors

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Drone attacks on Saudi Aramco facilities by Houthi rebels over the weekend have sent oil prices spiking higher. Oil prices had been trending lower in the past 3 months, but there has been an abrupt change as of this morning when prices rose more than +20% (before paring initial gains to +10% as at the time of writing). Initial estimates of the damage point to a suspension of 5.7mn barrels of oil, which is more than half of Saudi Arabia's production. That is close to 5% of global supply. The Saudi Energy Minister Prince Abdulaziz bin Salman – who is only just over a week into his new job – said that 50% of gas production has also come off as a result of the attack.

The hit to production volume is large and could be larger if Houthi rebels follow through with their threat of further attacks. But larger still are the political ramifications. The Houthi rebels in Yemen are backed by Iran. The Saudi-Yemen (Houthi) war that has been waging since 2015 has been widely seen as a proxy war between Saudi Arabia and Iran. That could morph into an overt war with Iran. Iran had been rattling its sabres via its proxies – undertaking attacks on vessels moving in and around the Strait of Hormuz (the world's most important oil transit chokepoint) in May and June 2019. The relative absence of news from headlines had misled the market into believing there was a de-escalation of risks in the region. Only last week did oil prices fall more than 2% in a single day, when President Trump fired his National Security Advisor, John Bolton, who was widely viewed as an Iran-hawk. Cleary events of over the past few days fly in the face of de-escalation. We believe the geopolitical premium in oil will rise as the risk of military intervention in the region is growing by the day.

Gold is also likely to rise as a result of the geopolitical tension. After a pause the strong rally in the metal in recent months, today gold prices have resumed their upward trajectory, gaining close to 1% at the time of writing (16 September 2019) and breaking above the psychologically important US\$1500/oz mark.

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