# *The drivers of oil prices and the macro-economic impact of low prices*

***A presentation at the SPE and EAN networking meeting***

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Economic Association of Namibia

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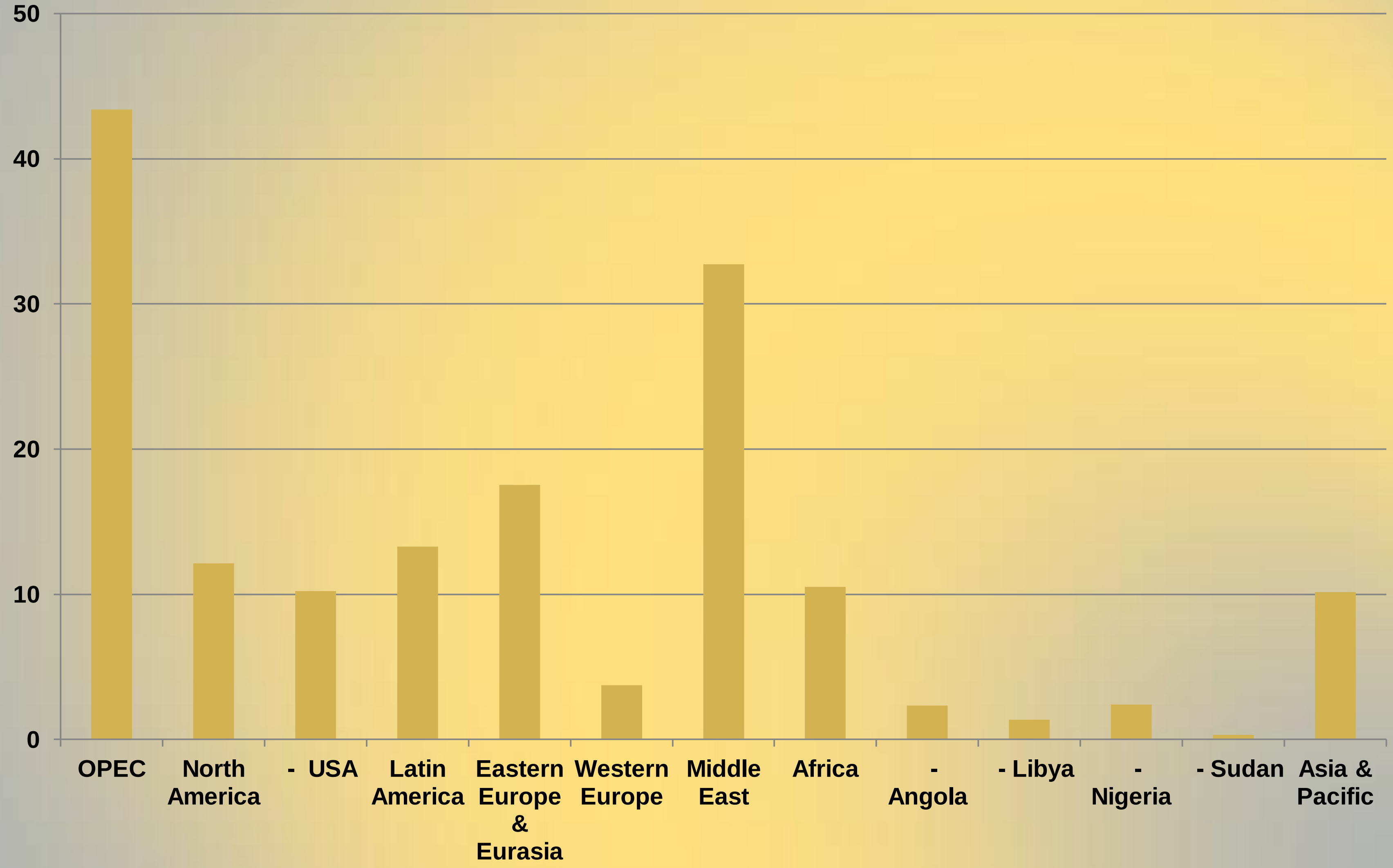
Determinants

- Supply
- Demand
- OPEC Politics
- Relative USD strength
- Speculation

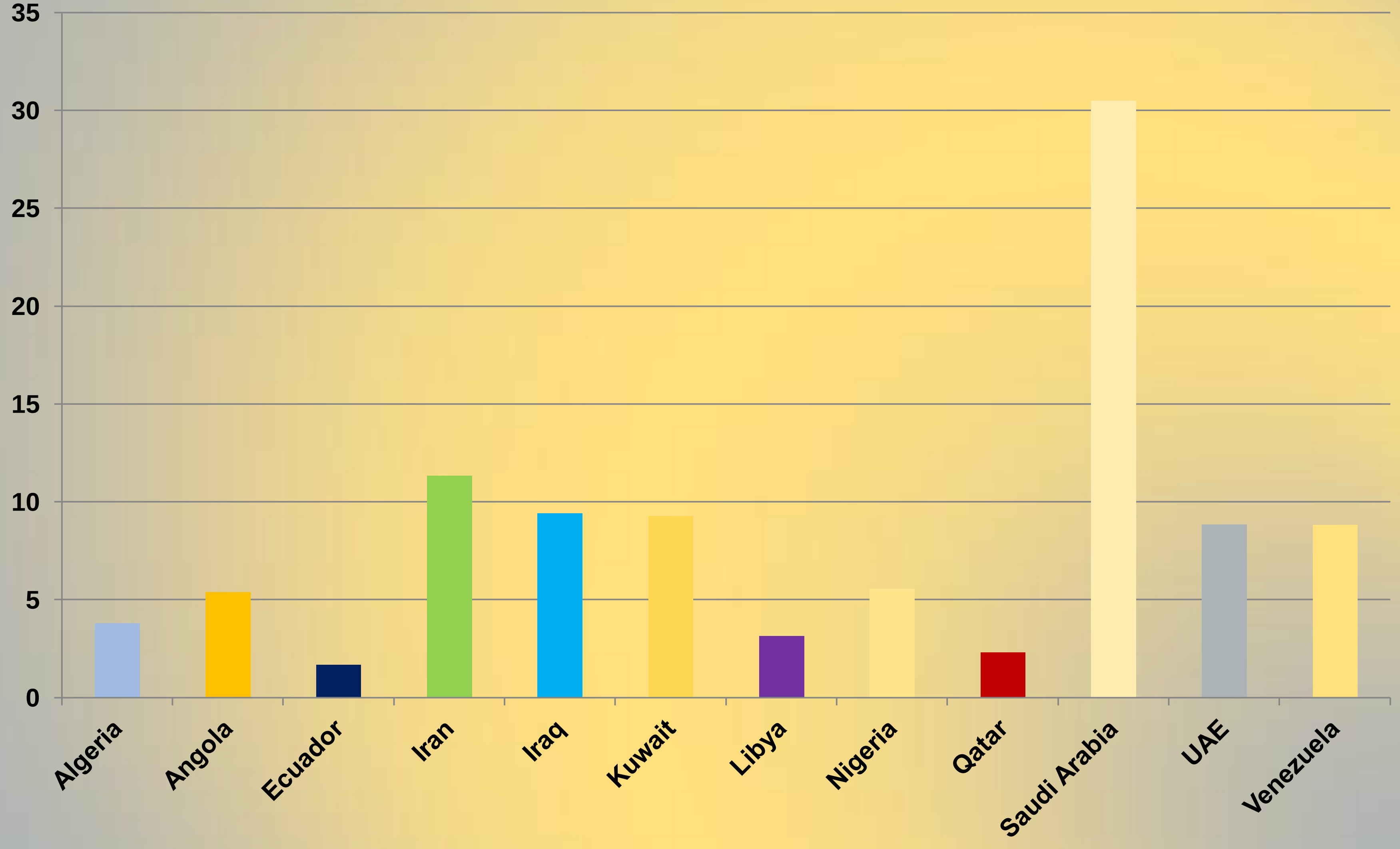
Macro-economic impact

- Trade balance
- Foreign currency reserves
- Angolan demand for Namibian goods and services
- Input / production costs
- Consumers' disposable income
- Exploration activities (investment)

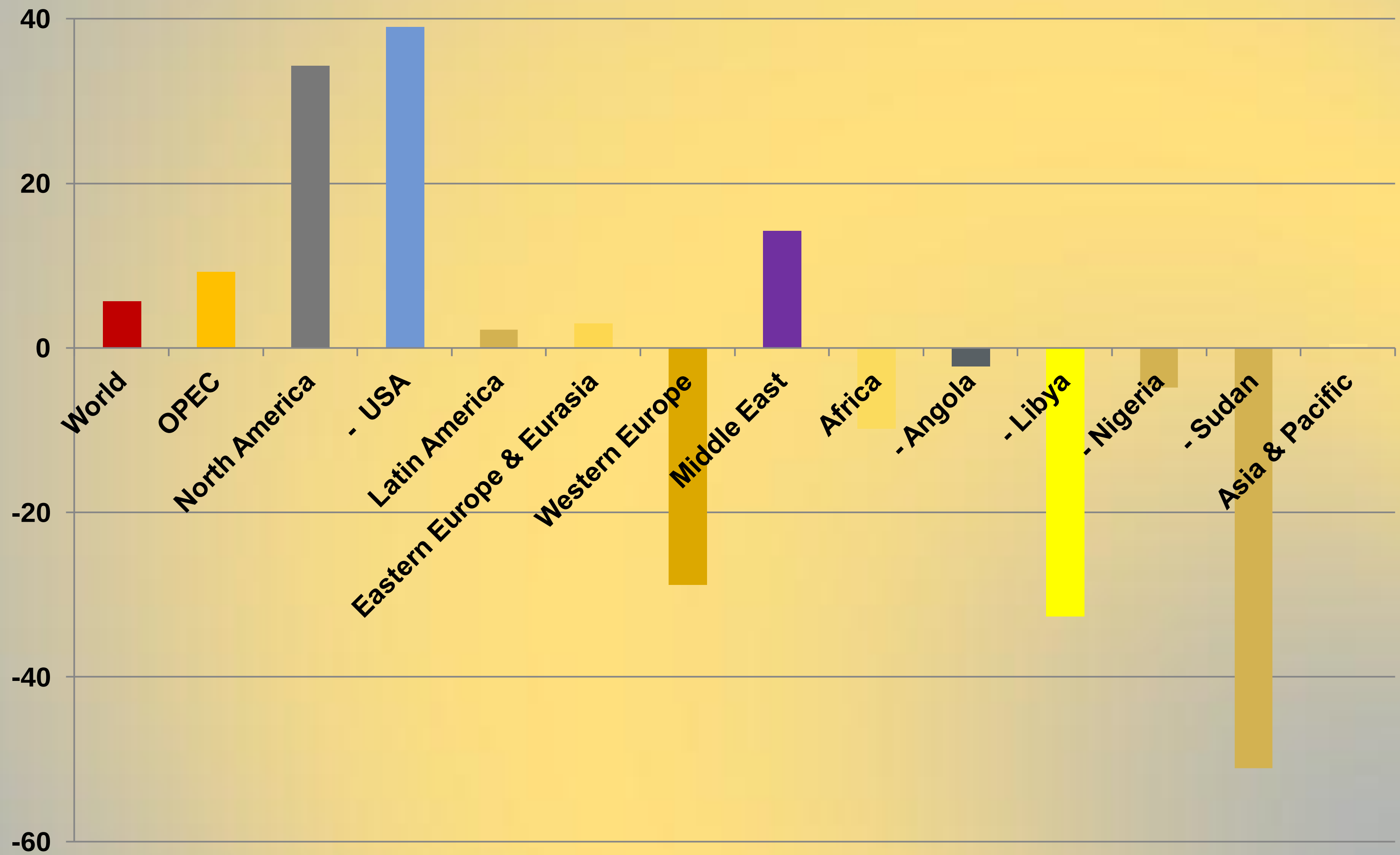
# Relevant oil producers - 2013



# OPEC producers



# Increase in oil production by country 2009 to 2013

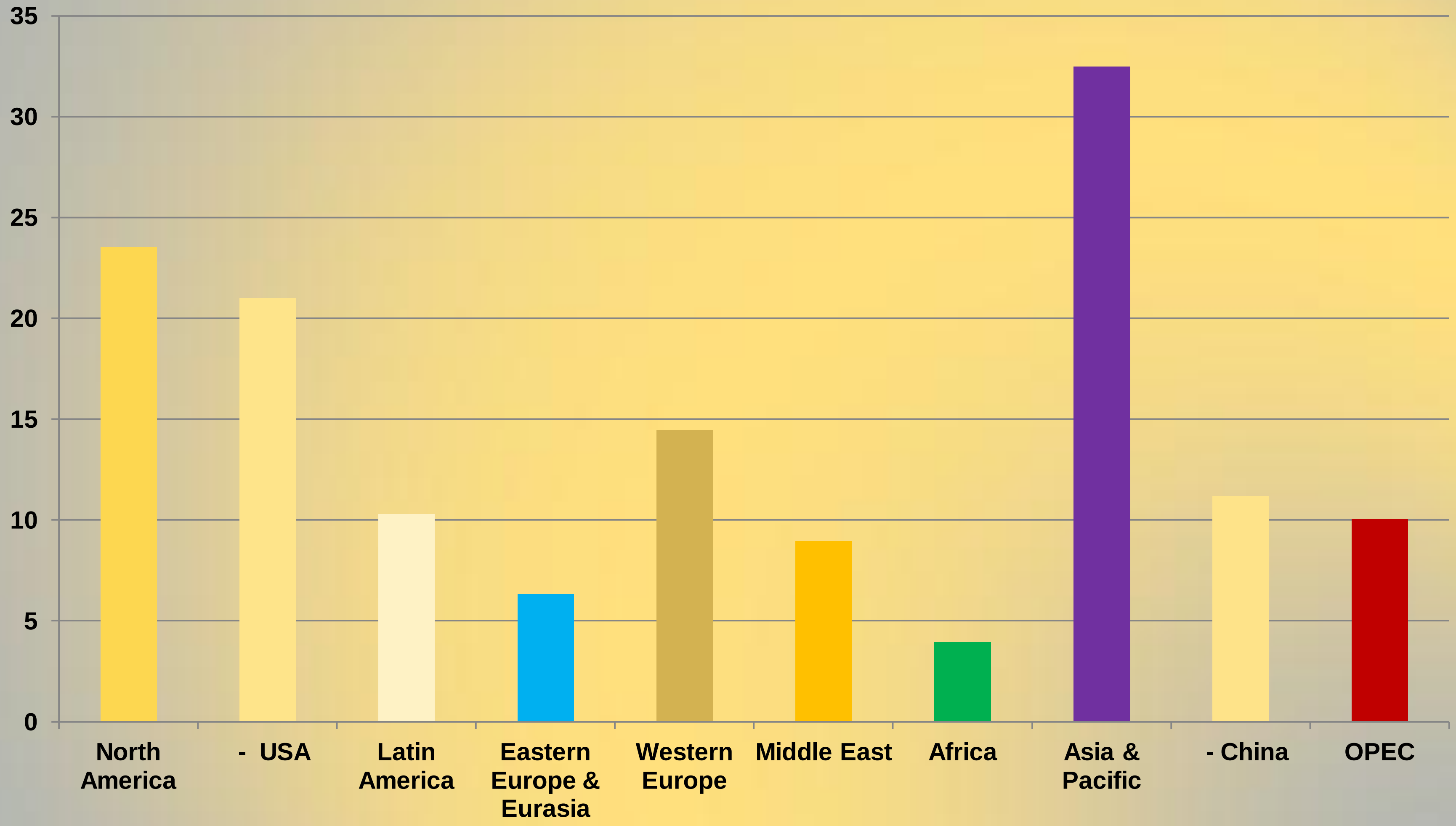


# Oil production – some numbers

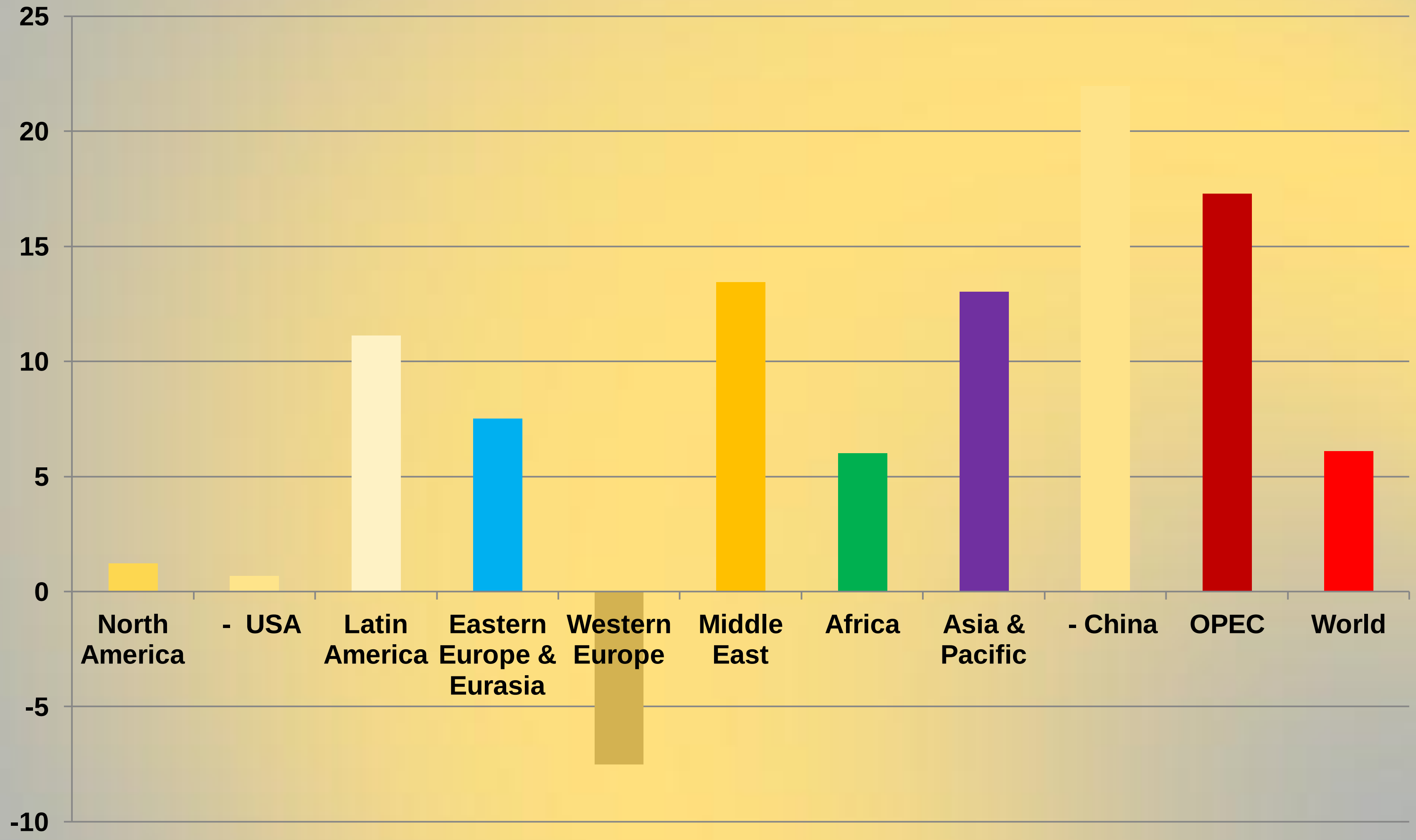
- Nigeria largest African producer in 2013 slightly ahead of Angola (2.4 vs. 2.3 per cent of total global crude oil production)
- African oil production dropped between 2009 and 2013 from 8.5mb/d to 7.6 mb/d
- USA production increased by 39 per cent from 5.4 mb/d to 7.4 mb/d; almost on par with total production in Africa
- Saudi Arabia 9.63 mb/d
- USA about 1,770 oil rigs compared to 540 in Middle East and 150 in Saudi Arabia
- Marginal costs of most shale producers in USA reportedly between USD10 and USD20 per barrel, similar to Middle East.
- Worldwide, based on survey in Jan 2015 of some 2,222 wells, only 1.6 per cent have negative cash flow below USD40 pb – put it differently their marginal cost is above USD40 pb

➢ Total global oil production increased by 5.7 per cent, while OPEC output rose by 9.3 per cent

# Oil demand by country / region



# Change in oil demand 2009 to 2013



# Oil demand

Determinants

- Global economic growth and in particular growth in China
- Shift in production structure from primary to tertiary sector
- Technological advance – resource saving technologies

➢ 1990: USD5.40 value added per kilogramme of oil

➢ 2010: USD7.20

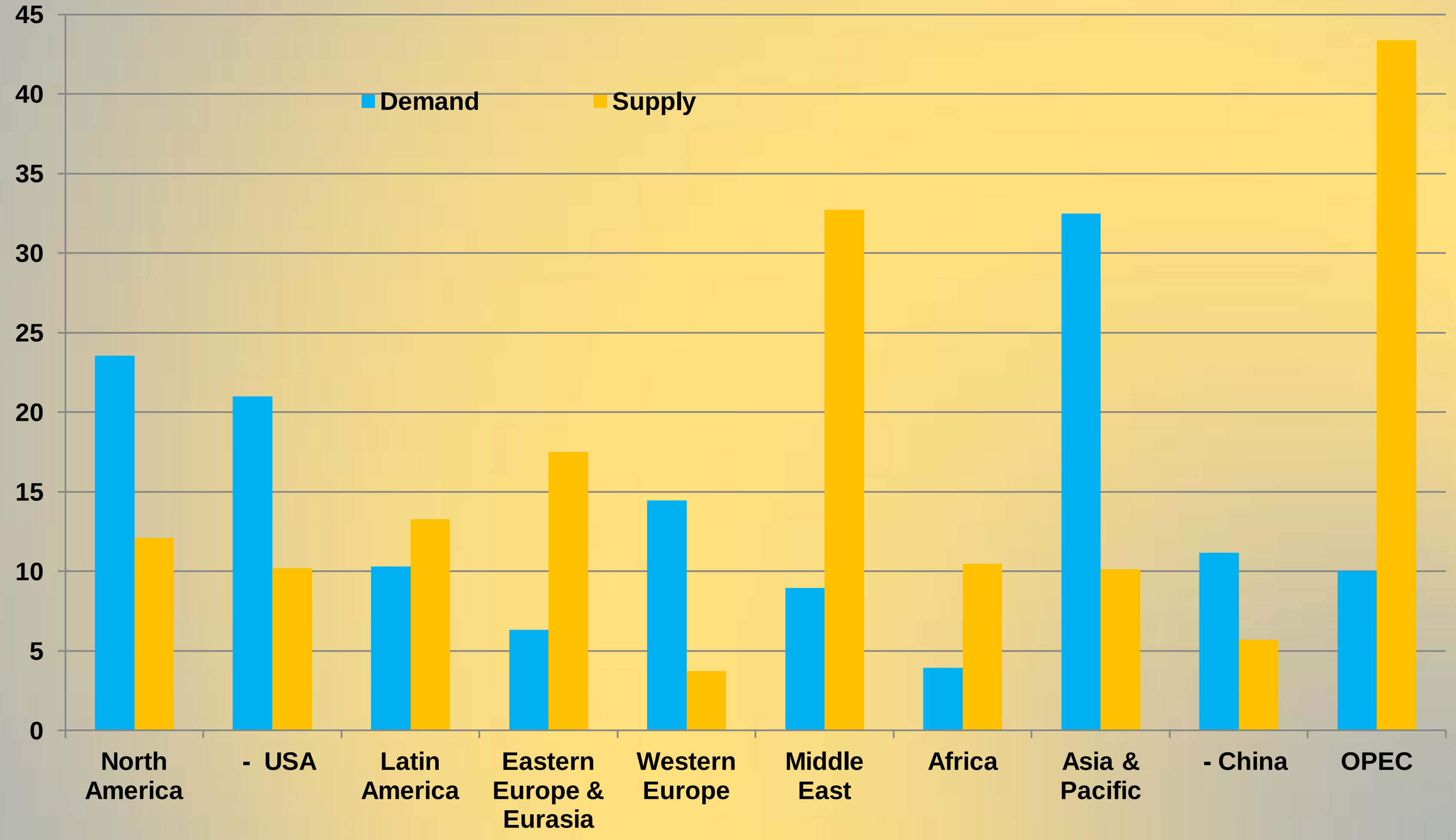
➢ 2011: USD7.30 (increase by 35 per cent compared to 1990)

Demand trends

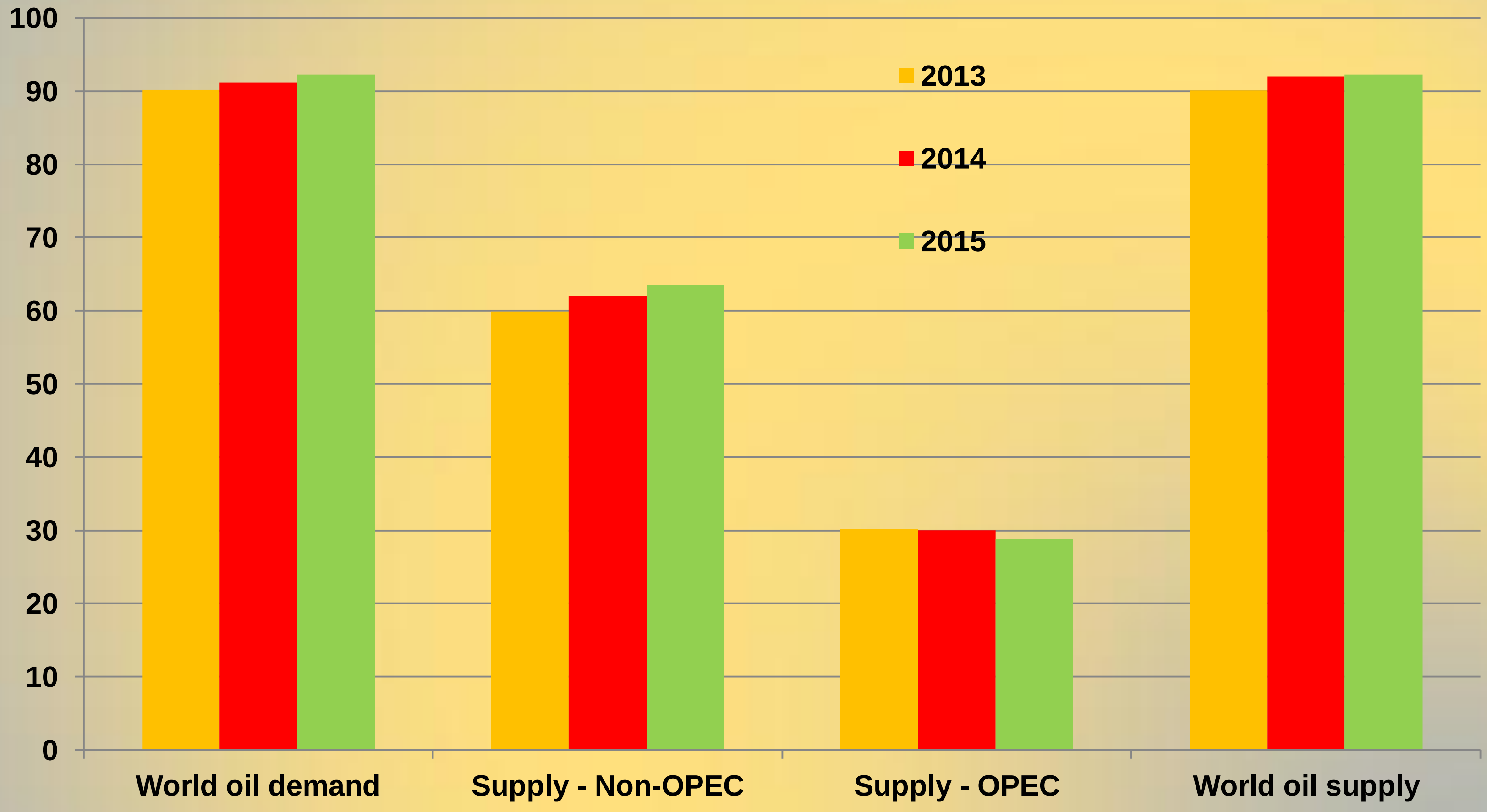
➢ Increase by 1.5 per cent annually between 2009 and 2013, but only 1.1 per cent between 2013 and 2014

➢ 1.3 per cent increase expected for 2015 to 92.3 mb/d

# Demand & Supply by country / region



# World demand & supply 2013 to 2015 in mb/d



# OPEC politics

Cartel aimed at maintaining oil price within certain price range by regulating output

- Saudi Arabia used to be swing producer, but no longer willing to lose market shares
- Geopolitical rivalry with Iran (second largest OPEC oil producer)

# Strength of USD

- Appreciation of USD (depreciation of local currency) increases revenue in domestic currency
- Somehow mitigates for lower oil prices in USD
- Euro depreciated from some EU1.39 (18 Mar 14) to EUR1,06 (18Mar15) against USD [or USD0.72 to USD 0.95 per EUR]
  - ➢ Depreciation by 24 per cent
- GBP1.66 (16Mar14) to GBP1.47 against USD
  - ➢ Depreciation by 11 per cent
- ✓ 'Currency war' increases USD attractiveness as well as expected gradual interest rate increase later this year

# Macro-economic impact on Namibia - Trade

Improvement in Balance of Trade

- Oil imports accounted for 9.2 per cent of total imports over 2007 to 2013 period
- NAD7 billion in 2013
- Third largest import item behind Transport equipment and Chemicals/rubber/plastic

Improvement in foreign exchange reserves

- International benchmark: 3 month import cover
- SADC benchmark: 6 month import cover
- ➢ Currently below 3 months, but net international investment position strong
- ➢ Relevant to maintain currency peg to ZAR

# Macro-economic impact – exports to Angola

Depreciation of Angolan Kwanza

Disposable income of Angolans could decline, depending on

- duration of low oil prices; and
- devaluation of Angolan Kwanza

could result in

- Declining direct exports to Angola since becoming more expensive compared to local products and due to potentially lower demand
- Declining demand of Angolans in Namibia for services (health, education although less likely since investment into future) and goods (shopping tourism – more likely, property etc.)

# Macro-economic impact - prices

- Lower input / production costs in particular for energy-intensive operations such as fishing, transport, mining
- ➢ Could increase competitiveness dependent on competitors' input cost reduction
- Declining inflation rate
- ➢ Increasing disposable income in particular for motorists
- ➢ Non-motorists (often the poorer groups in society) benefit to lower degree
- ➢ Could result in increasing imports despite recent interest rate increase
- ✓ Monetary policy determined by currency peg rather than inflation rate

# Macro-economic impact - Investment

- Mineral exploration increased continuously from NAD 500 million (2007) to NAD3,153 million (2013)
- Accounting for on average 6.2 per cent of total investment over period 2007 to 2013, but 9.7 per cent in 2013.
- Major exploration activities most likely focusing on minerals rather than oil & gas
- ➢ No oil drilling planned for Namibia in 2015, but for 2016
- ➢ Long-term investment decisions informed by a number of factors, not only by current price levels

# Conclusion

No significant output cut expected since:

- ➢ quite a number of oil exporters depend heavily on oil revenues
- ➢ In particular USA shale oil producers have to maintain output to service their debts
- ➢ prices still above marginal production costs
- ➢ risk of losing market shares
- ✓ However, depleted wells might not immediately be replaced with new wells
- ✓ Price fluctuations rather than clear price trend can be expected

Overall positive impact on Namibian consumer and producers

- ➢ Whether it can be turned into competitive advantage remains to be seen

Loser could be the environment and the renewable energy industry

# Thank you for your attention