SA Economics

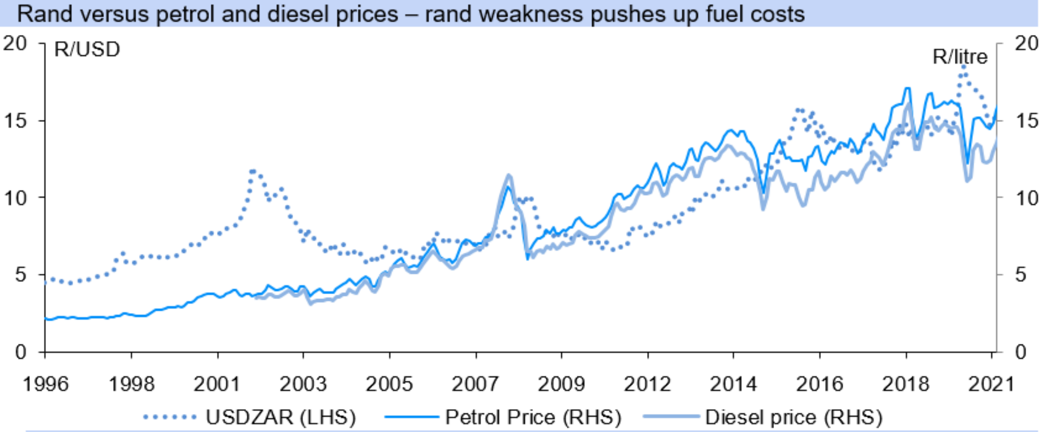
Wednesday 17 March 2021

Oil note: South Africa faces yet another fuel price hike this year, potentially a hefty 90c/litre in April as the international oil price continues to climb, which combined with the 26c/litre in fuel taxes, could push up inflation by 0.4% m/m

Oil price: Rand vs USD

Source: Iress

Rand versus petrol and diesel prices – rand weakness pushes up fuel costs



Source: Iress

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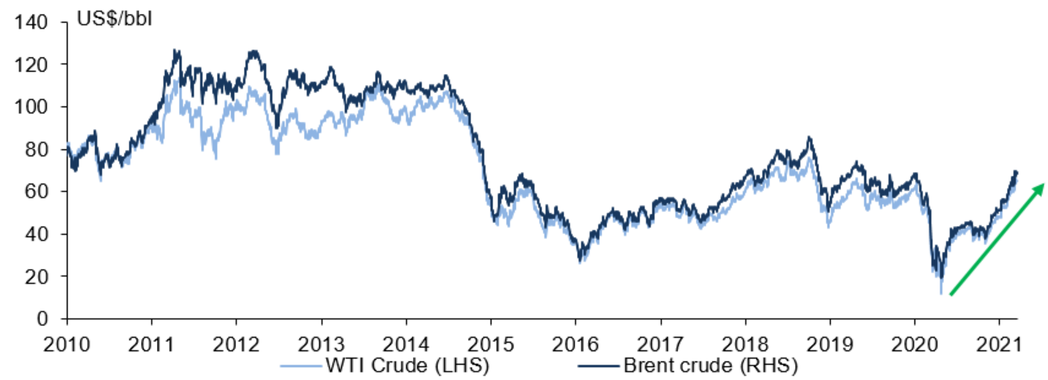
Brent crude oil vs WTI crude oil price



Source: Iress

- After an 81c/litre hike in the petrol price in February, and another of 65c/litre in March, a 90c/litre lift is brewing for April, which together with the Budget's fuel tax hikes, could lift CPI inflation by 0.4% m/m, and the petrol price above R17.00/litre – all in the month of April.
- The Brent crude oil price is currently around US$68/bbl, or R1 000/bbl, higher than the 17th of last month when it was at US$64/bbl or R950/bbl, with the volatile domestic currency also adding upward pressure to the rand oil price, of 15c/litre on its own.
- The rand has been fairly steady today, between R14.85/USD and R14.98/USD, currently at R14.85/USD, versus R14.64/USD a month ago, with this depreciation adding to the upwards pressure on the rand oil price, and so to likely higher domestic fuel prices next month.
- With the FOMC meeting underway, the rand has been robust, although other EM currencies have seen less firmness over the past week. The domestic currency is stronger by 1.5% week/week (w/w), leading the performance on the Bloomberg EM currency ranker.
- The Fed is not expected to alter its target rate tonight, nor is it expected to make immediate changes on its QE programme, although market concerns are high that the longer-term rate trajectory may begin to show some interest rate hikes in the dot plot for a few year's time.
- Such fears drive investor uncertainty for EM portfolio assets. However, the rand has benefited from strong commodity prices, with the rand also a commodity currency, and commodity prices, including the oil price, are higher on positive sentiment over economic growth.
- That is, the US economic outlook has improved somewhat recently, and there has been some commentary from US monetary authority officials seemingly supportive of a gentle lift in US interest rates towards the end of the forecast period of the dot plot.

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- However, the Fed is unlikely to make any rash announcements, and is also unlikely to wish to precipitate any financial market instability. Indeed it is always careful, like any well regarded monetary authority, to seek to try and achieve financial market stability.
- The Fed has previously indicated that the recent lift in US treasury yields more likely reflects optimism on future strengthening in US economic growth rather than anything more sinister. A slight lift in the 2023/2024 dot plot forecasts might consequently ensue tonight (SA time).

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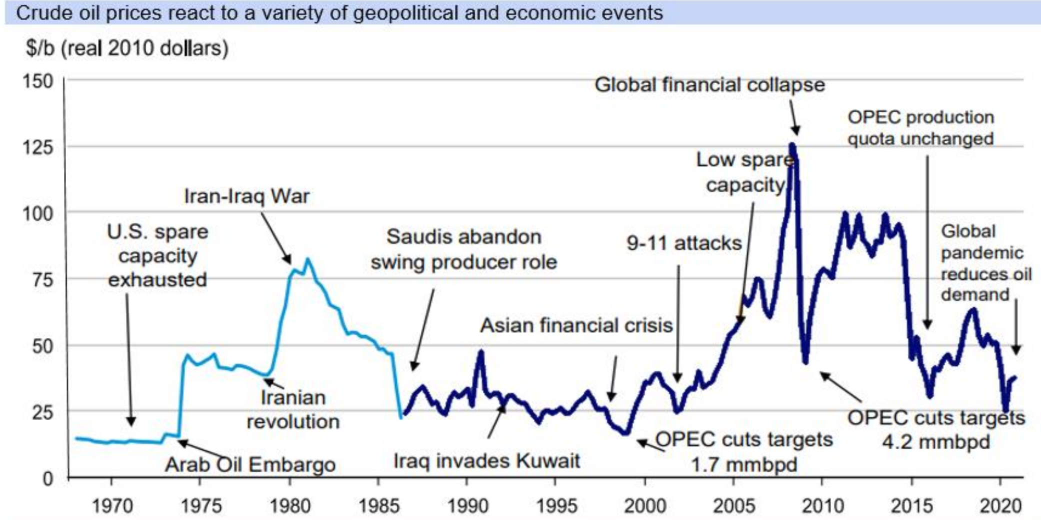
Crude oil prices react to a variety of geopolitical and economic events



Source: EIA

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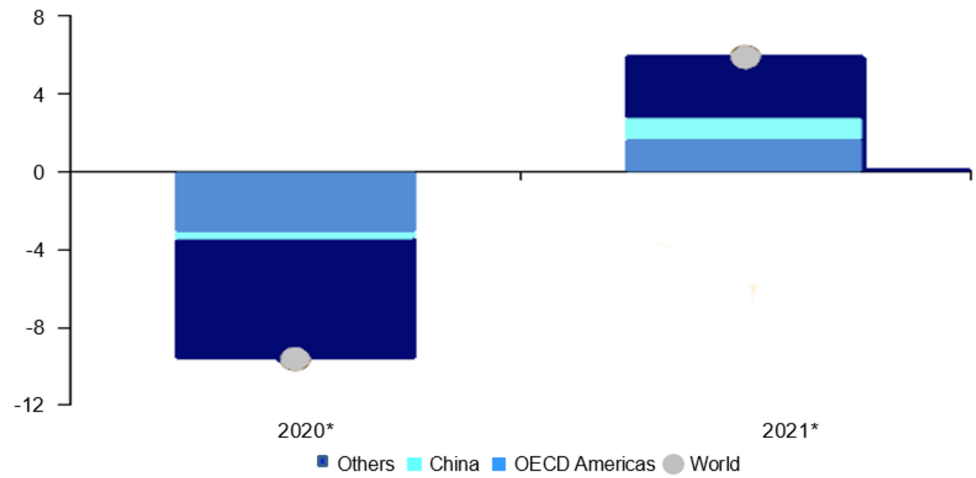
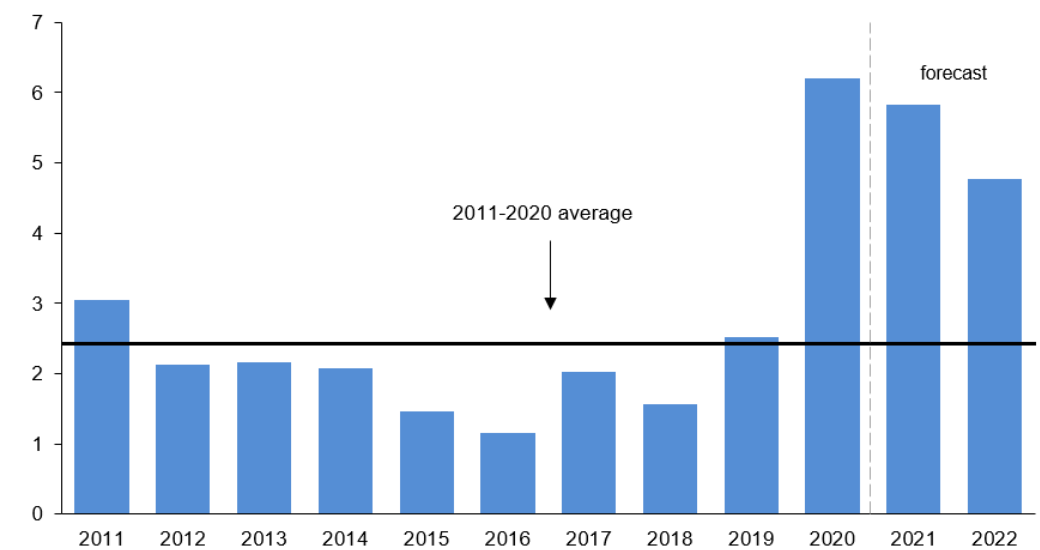
World oil demand growth in 2020-2021



Source: OPEC

OPEC surplus crude oil production capacity



EIA, March 2021

Note: Black line represents 2011-2020 average (2.4 million barrels per day).

- That is, some very small lift in the US's FOMC members interest rate views towards the long-end of their interest rate projection horizon may be what the Fed views appropriate in the face of the very large incoming US fiscal stimulus package.

- It has continued to promote the message that a steeper yield curve is positive for the outlook as it denotes market confidence in economic recovery and that economic activity is expected to drive a pick-up in inflation and so prompt higher interest rates in the longer-term.
- The Fed itself has also intimated in the past that there is little more it can do to promote economic growth without substantial additional fiscal stimulus as interest rates are zero bound and QE is substantial. Tonight, it is likely to state it will continue with its QE programme.
- Improved global economic growth expectations, on the lift in the US economic outlook, have supported oil prices, as has the cold in Asia, Europe and the US, while market expectations for economic growth, and hence oil demand, continue to be buoyed by vaccine deployment.
- The OPEC+ cartel is extending the majority of its agreed production cuts to the month of April as well, which is also supporting oil prices. Additionally, expectations now for better than previously expected future US industrial production is also providing some price support.
- The oil price has been climbing towards the US$70/bbl mark (all oil prices mentioned in this note are Brent crude unless otherwise stated), although today it has fallen back marginally, as markets focus on the substantial nature of inventories and available supply.
- The IEA (International Energy Association) today said “global oil demand is set to rise every year through 2026” and that “Asia will continue to dominate growth in global oil demand, accounting for 90% of the increase between 2019 and 2026.”
- “By contrast, demand in many advanced economies, where vehicle ownership and oil use per capita are much higher, is not expected to return to pre-crisis levels. … Achieving an orderly transition away from oil is essential to meet climate goals”.
- However, this shift away from fossil fuels is likely to be longer-term in nature. The current lift in oil prices, and the potential 0.4% m/m contribution to South Africa’s CPI inflation in April could see the CPI rise by 4.4% y/y in that month, lifting the trajectory for the year.

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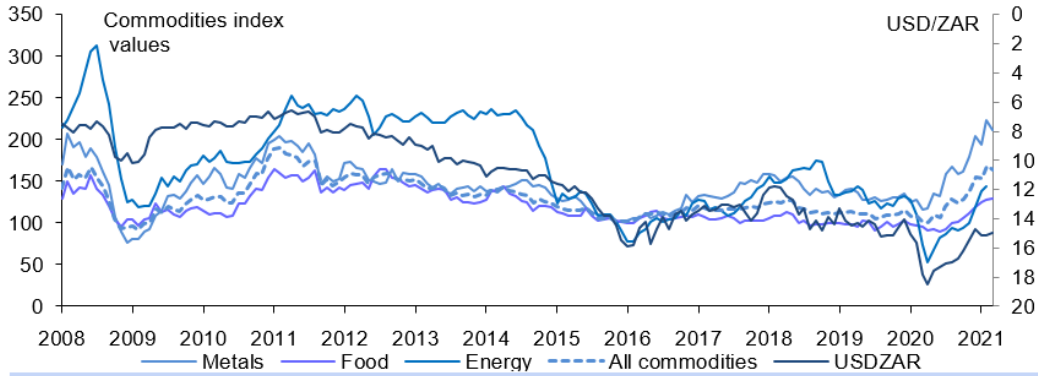
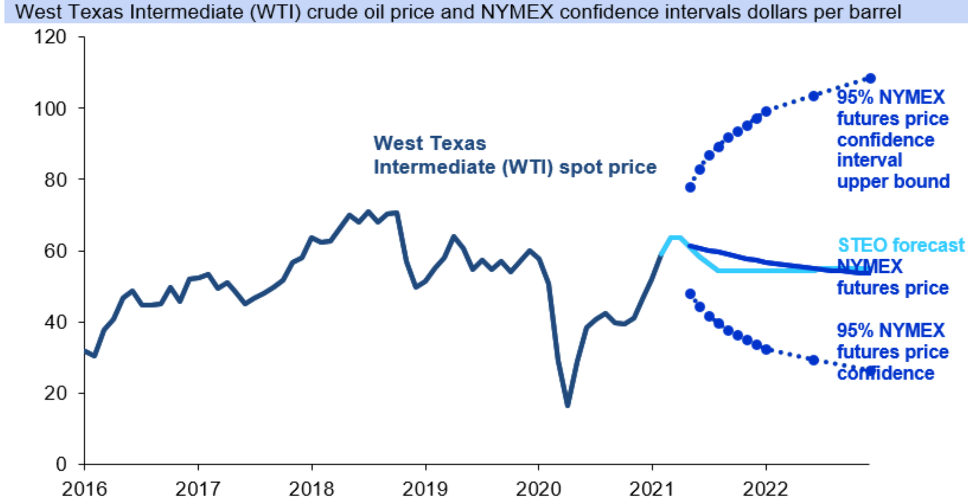
Commodities price indices vs rand



Source: IMF, Iress

West Texas Intermediate (WTI) crude oil price and NYMEX confidence intervals dollars per barrel



Source: EIA, March 2021

Note: Confidence interval derived from options market information for the five trading days ending Mar 4, 2021. Intervals not calculated for months with sparse trading in near-the-money options contracts.

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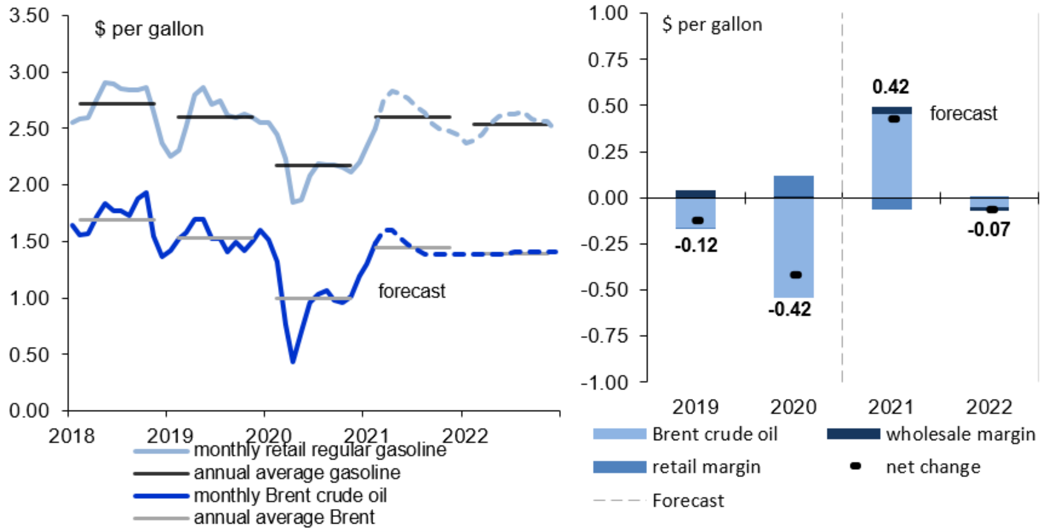
US gasoline and crude oil prices and components of annual gasoline prices changes



EIA, March 2021