

Investment Analysis, Oil prices and the strength of the Dollar

Agenda

Why oil prices have fallen?
Trends on decreasing oil prices
Effect on Saudi Arabia, Russia, Venezuela and USA (Exporters)
Effect on Europe, USA and China (Importers)
Positive & Negative Effect on the UK economy
Analysis
Conclusion

Why oil prices has fallen?

Low demand - weak economic activity, decrease consumption (The Economist, 2014, online)
OPEC quotas - maintained 30 million barrels p/d, when demand is low (HudAllstone, 2014, online)
High supply - US largest producer, technology is a shifter of supply (Smith, 2014, online)
Saudi's market position - strategy to maintain market share, push out competition (Solomon, 2014, online)



Supply and Demand



The Decline of Oil Prices



Effect on Exporters

	Short term	Long term
Saudi Arabia	Decrease in GDP due to lower oil prices, leading to lower government revenue and higher unemployment.	Over the long term, Saudi Arabia's economy is heavily dependent on oil. Lower prices could lead to a structural shift towards other sectors, but this is a long-term process.
USA	Lower oil prices reduce costs for US oil producers, leading to higher profits and potential investment in new production.	Over the long term, the US oil industry may expand, leading to higher energy security and potentially higher GDP.
Russia	Lower oil prices reduce revenue for Russia, which is heavily dependent on oil exports. This could lead to budget deficits and higher unemployment.	Over the long term, Russia may face economic challenges due to lower oil prices, potentially leading to a shift in focus towards other sectors.
Venezuela	Lower oil prices reduce revenue for Venezuela, which is heavily dependent on oil exports. This could lead to budget deficits and higher unemployment.	Over the long term, Venezuela's economy is heavily dependent on oil. Lower prices could lead to significant economic challenges.

Effect on Importers

	Short term	Long term
China	Lower oil prices reduce costs for China, leading to lower inflation and higher consumer spending. This could lead to higher GDP.	Over the long term, lower oil prices could lead to higher economic growth in China, as lower costs reduce inflation and increase consumer spending.
USA	Lower oil prices reduce costs for the USA, leading to lower inflation and higher consumer spending. This could lead to higher GDP.	Over the long term, lower oil prices could lead to higher economic growth in the USA, as lower costs reduce inflation and increase consumer spending.
Europe	Lower oil prices reduce costs for Europe, leading to lower inflation and higher consumer spending. This could lead to higher GDP.	Over the long term, lower oil prices could lead to higher economic growth in Europe, as lower costs reduce inflation and increase consumer spending.
Qatar	Lower oil prices reduce revenue for Qatar, which is heavily dependent on oil exports. This could lead to budget deficits and higher unemployment.	Over the long term, Qatar's economy is heavily dependent on oil. Lower prices could lead to significant economic challenges.



Importers and Exporters GDP change



Positive Effect on the UK Economy

Lower oil prices help to reduce the cost of living. Oil related transport costs will directly fall, leading to lower cost of living and a lower inflation rate. Falling oil prices is one reason behind the recent fall in UK inflation to 0.5% (Prestiger, 2014, online)
"In theory the fall in oil prices could lead to higher spending on other goods and services and add to real GDP" (Prestiger, 2014, online)
"If oil falls to \$40 per barrel in the near term, it could add 0.4pc to the UK's GDP growth" (Crislow, 2015, online)
Low oil price + low inflation, more disposable income, interest rates stay, better for the average Briton (BBC, 2014, online)



Example

"Mr Osborne has already launched an investigation into whether companies are passing on the benefits of lower prices quickly enough to consumers. The Treasury wants to see \$50 oil and lower natural gas wholesale prices translating into cheaper energy bills, train fares and airline tickets" (Crislow, 2015, online)
"SSE cut prices by 4.1% due to pressure from government and consumer groups" (BBC, 2015, online)



Negative Effect on the UK economy

Low inflation is not always good - possibly no income tax policy, cant inflate away the value of debt, value of the debt increases possible concerns (BBC, 2014, online)
Business concerns: BP cut 300 jobs from the North Sea (BBC, 2015, online)
Low oil price would mean falling investment in North Sea oil and "significant workforce reductions" in the energy sector worldwide (The Week, 2015, online)

Analysis

It is a case between Saudi Arabia vs. US - Who will blink first? US is likely to stop production of shale oil as it would be uneconomical however, how long can Saudi Arabia last?
In the short term, importers are benefiting however exporters will struggle to survive
Oil prices will not dramatically increase so consumers should feel positive long term effects

Conclusion

Oil is a key determinant on an economy
Good for world economy but there will be winners and losers within some economies
Oil has short and long term effects on economies
UK should benefit as inflation decreases

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Supply and Demand



The Decline of Oil Prices



Effect on Exporters

	Short term	Long term
Saudi Arabia	Decrease in GDP due to lower oil prices, leading to a decrease in government revenue.	Decrease in government revenue, leading to a decrease in public services and infrastructure investment.
USA	Lower oil prices lead to a decrease in the cost of production for US oil companies, leading to a decrease in their profits.	Decrease in profits, leading to a decrease in investment in oil exploration and production.
Russia	Lower oil prices lead to a decrease in the value of Russia's oil exports, leading to a decrease in government revenue.	Decrease in government revenue, leading to a decrease in public services and infrastructure investment.
Venezuela	Lower oil prices lead to a decrease in the value of Venezuela's oil exports, leading to a decrease in government revenue.	Decrease in government revenue, leading to a decrease in public services and infrastructure investment.

Effect on Importers

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USA	Lower oil prices lead to a decrease in the cost of production for US companies, leading to a decrease in their profits.	Decrease in profits, leading to a decrease in investment in oil exploration and production.
Europe	Lower oil prices lead to a decrease in the cost of production for European companies, leading to a decrease in their profits.	Decrease in profits, leading to a decrease in investment in oil exploration and production.
Qatar	Lower oil prices lead to a decrease in the value of Qatar's oil exports, leading to a decrease in government revenue.	Decrease in government revenue, leading to a decrease in public services and infrastructure investment.



Importers and Exporters GDP change



Positive Effect on the UK Economy

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- In theory the fall in oil prices could lead to higher spending on other goods and services and add to real GDP (Prestiger, 2014, online)
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