Goldman Sachs Exchanges: The Markets

The impact of rising oil prices

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Recorded: September 21, 2023

Sam Grobart: The Fed's not hiking this week. But OPEC is. This is The Markets.

Hi, I'm Sam Grobart. Today, I'm joined by Daan Stryuven, head of oil research here at Goldman Sachs. And we're going to talk about the rise in oil prices and what it means for the overall economy. Daan, thanks so much for joining us today.

Daan Stryuven: Thanks for having me, Sam.

Sam Grobart: Daan, you published a report this week on the recent rise in oil prices. What are we seeing? And what's behind that price escalation?

Daan Stryuven: So, since late June international brands crude prices are up by about 30 percent. We did hit $95 per barrel. The main driver is really a rise in oil demand to an all-time record high this summer, plus the extension of OPEC supply cuts by Saudi Arabia and Russia.

Sam Grobart: In an earlier forecast, you expected oil to reach around $93 a barrel over the next 12 months. You've since upgraded that forecast to $100 a barrel. What changed?

Daan Stryuven: We now have a forecast 12 months ahead, indeed, of triple digits. $100 per barrel because of the expectation that lower OPEC supply for longer, in particular lower crude supply by Saudi Arabia and firmer than expected demands will lead to sharper draws in global oil stocks.

Sam Grobart: And when you talk about demand, what factors are driving that? Where are you seeing that?

Daan Stryuven: Global oil demand reached an all-time high this summer and should continue to rise at a solid clip next year by around 1.5 percent on a Q4-Q4 basis. That's solid because the Goldman view on the global economy is constructive, 2.5 percent global GDP growth.

And because the services sector and, in particular, transportation services, which is critical for oil demand, continues to outperform the broader economy.

Sam Grobart: So, OPEC+ has pricing power today. But presumably there are some limits to that, right?

Daan Stryuven: Yeah, absolutely. So, pricing power, basically the ability to push up prices while limiting the damage to demand for your own barrels is quite elevated at the moment for OPEC+, both through the alliance with Russia, which is boosting its market share. And because the flexibility, the ability of US shale to respond to higher prices is still significant, but less elevated, than in the hyper growth era of US shale about ten years ago.

So, OPEC pricing power is evaluated. But still, two constraints to it. Number one, extremely elevated prices would destroy long run demand for OPEC barrels. That's why we think oil is not going to go above, call it, $105 per barrel. And the second constraint is the fact that US shale is not dead.

Sam Grobart: Let's take a look at this in a macro context. There is growing consensus that the US economy can achieve a soft landing, threading the needle between inflation and recession. We saw that the Fed paused rate hikes. The Bank of England did the same this week. That adds to that sentiment. How do these rises in oil prices affect that forecast?

Daan Stryuven: All things equal, higher oil prices mean higher headline inflation, which put upward pressure on central bank rates. That said, we don't think that higher oil prices derail our forecasts for a soft landing and for the view that the Fed is done hiking. Both because higher oil prices also have an offsetting effect through lower growth, which all the things equal, is lowering the outlook for policy rates. And second, the broader inflation backdrop is much more favorable than during the 2022/2021, a broad surge, not only in core inflation, but also in food prices and gas prices.

If the other components of the inflation basket are moderating, it's easier for central banks to look through the rally in oil prices.

Sam Grobart: Last question, Daan, what will you be paying attention to next week?

Daan Stryuven: Very focused on our nowcast of Russian supply. Because one of the key drivers of Saudi pricing power is cooperation with the Russians. Second, our nowcast for China demands. Because we expect most of the solid growth next year to still come from China and the rest of Asia. Last but not least, the so-called recount of US production to check how quickly US producers are responding to the sum rally.

Sam Grobart: Daan, great stuff. Thank you very much.

Daan Stryuven: Thanks a lot.

Sam Grobart: That does it for another episode of The Markets. Be sure to find us on Apple Podcasts, Spotify, or wherever you get your podcasts.

I'm Sam Grobart. Thanks so much for listening.

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