SPECIAL REPORT:

OIL PRICE VOLATILITY AND THE IMPACT ON AFRICA IN 2019

Some of Africa’s largest oil producers are in a much stronger position to deal with price volatility than five years ago. Conversely, many African fuel importers are less likely to reap the economic benefits from lower oil prices in 2019.

Crude oil prices have started 2019 under pressure from rising output and an economic slowdown that could weaken demand. Oil prices fell in 2018 for the first year since 2015. The fourth quarter was marked by severe price volatility. Prices dropped nearly 25 percent in November 2018 alone, the biggest monthly loss in a decade, due to concerns over a possible glut in global supplies.

In terms of supply, record oil production in the world’s largest producers such as the United States, Russia, and Saudi Arabia has helped plummet oil prices to their lowest levels since October 2017. Demand-wise, a stronger US dollar has made crude more expensive for global importers, weighing on usage. And concerns over global economic growth and therefore oil demand have created a bear market.

How much will oil cost in 2019?

The key question is whether the oil price will continue to fall in 2019. Just a couple of months ago, major oil trading houses were predicting the return of USD 100 crude, yet oil prices are now standing at half that level.
Oil prices began 2019 at USD 54 per barrel for Brent crude and USD 45 for U.S. West Texas Intermediate crude oil futures. However, prices are still expected to rise as OPEC-led supply cuts come into effect in January, while US supply growth is expected to slow. Nevertheless, an average oil price below USD 60 in 2019 now seems a more realistic scenario than a few months ago. Even though most major investment banks have upgraded their forecasts above USD 60 over the past few weeks, the banks agree that unexpected volatility could still throw their expectations way off balance. It is this price volatility that will determine the impact on the world’s economies.

What implications does this scenario have for African oil producing countries and Africa’s largest importers of crude oil? This special report picks five countries of each category to assess their political and economic outlook for 2019.

**IMPACT ON MAJOR AFRICAN OIL PRODUCERS**

Africa’s largest oil producers are in much better stead to cope with price volatility than in 2014. Nigeria is betting on output increases in 2019 to soften the impact of an oil price drop below the 2019 budget benchmark. Angola will depend on IMF for support as it implements tough oil sector restructuring. Algeria and Egypt are counting on new revenues from shale reserves and natural gas respectively to cushion the blow of any drop in oil prices. However, unreformed oil sectors such as those in Sudan and South Sudan, as well as Libya, Equatorial Guinea, Gabon, and Republic of Congo, would again be in a weaker position to cope with price volatility in 2019, triggering balance of payment shortfalls and political instability with associated unrest risks.

**NIGERIA**

Output increases are likely to soften the impact of an oil price drop below the 2019 budget benchmark.

Nigeria’s 2019 budget has adopted USD 60 per barrel as its benchmark, which has been criticised as too ambitious by many local economists. The USD 23.6 billion budget was based on a USD 60 benchmark at a time the international oil price was around USD 75. Critics say government projections, especially total revenue projection and expenditure in the budget, may not be realised should volatility continue in the market. The Director-General of Nigeria’s Budget Office has since said that the government might consider lowering the benchmark. Yet such a budget revision seems unlikely given the tense political climate in the lead-up to the February 2019 elections.

Moreover, steady output increases are expected to match any concerns over price volatility. Nigeria has a targeted oil production of 2.3 million barrels per day (bpd) in 2019, up from 2.1 million bpd in 2018. Crucial to the production ramp-up is the flow of the Egina oil grade, which is expected to add an additional 200,000 barrels per day to Nigeria’s output. The first cargo of the Egina grade will be lifted in February 2019 by French major Total, the Nigerian National Petroleum Corporation (NNPC) and the China National Offshore Oil Corporation (CNOOC). Following the February elections, major changes are being lined up for Nigeria’s oil sector, including partial privatisations and asset sell-offs, which should further boost the 2019 budget.

See Nigeria Country Outlook

**ANGOLA**

IMF support and non-oil sector asset sell-offs will provide a buffer against further fiscal slippages.

While a burgeoning oil market shielded the country’s structural deficiencies for decades, these were laid
bared by the 2014 oil crash from which the country has yet to recover. For a country that derives approximately 95 percent of its export revenue from oil, the reduced productivity and diminished revenue has left Angola exposed to fiscal slippages and balance of payments shortfalls. Not only do the productivity losses undermine efforts to trim the fiscal deficit down from its high of 7 percent to 3.4 percent – and debt from approximately 60 percent to around 55 percent – but they also weigh on the country’s ability to finance regular expenditures.

Nevertheless, IMF financing is expected to compensate for immediate funding shortfalls in an indeterminate global oil environment. In December 2018, the IMF approved a three-year USD 3.7 billion credit facility. Moreover, broad-based structural reforms in the oil sector have improved productivity. Greater observation of macroeconomic fundamentals and policy anchorage under the IMF programme indicate that market optimism on an already promising Angolan economy is likely to firm up in 2019. State-owned oil company Sonangol plans to exit 52 of more than 100 companies not related to the production or sale of crude, which should further buffer the budget.

See Angola Country Outlook

ALGERIA

Oil sector reform and recent unconventional exploration should cushion against any oil price shocks.

Algeria’s economy has recently benefited from increased gas output, a relative recovery in the Eurozone, and higher oil prices. The country has been trying to boost domestic output and cut imports in an attempt to cope with financial pressures caused by a fall in energy earnings since 2014. Energy earnings have risen in 2018, reducing the country’s trade deficit by more than half. Yet a sudden oil price fall in 2019 could undermine Algeria’s economic recovery and thus raise associated risks of civil unrest and political instability in a crucial election year. However, a number of factors indicate that Algeria is better prepared than previously for any oil price volatility.

State oil company Sonatrach’s chief executive Abdelmoumen Ould has encouraged improved relations with international oil companies, which has advanced foreign investment. Italian oil major Eni has struck a deal to team up with France’s Total to explore oil and gas in Algeria. A new hydrocarbon law will allow for a bigger variety of contracts – in addition to currently used production sharing agreements, concessions and risk service agreements will also become feasible, while new tax remissions are also being considered. Moreover, the recent rebound in prices has allowed Sonatrach to invest in petrochemicals, offshore exploration, and develop Algeria’s heretofore off-limits shale gas deposits.

See Algeria Country Outlook

EGYPT

Gas self-sufficiency and gradual subsidy cuts are likely to mitigate the impact of lower oil revenues.

Egypt has budgeted its 2018/2019 finances assuming oil prices at USD 67 a barrel, which no longer seems realistic under the current climate of price volatility. The IMF has provided a USD 12 billion credit facility, yet disbursements will depend on continued progress on implementing economic reforms, such as subsidy cuts and tax hikes. The main threat to the government lies in Egypt’s systemic economic imbalances, austerity policies, and subsequent risks of civil unrest. To mitigate unrest risks the government is delaying some subsidy cuts and increasing interest rates to calm consumer price inflation.

In 2018, Egypt became self-sufficient in liquefied
natural gas (LNG), thus shoring up its budget by saving around USD 2 billion a year from natural gas imports. The country continues to depend on imports for gasoline and diesel, although lower oil prices would mean that the government will be spending less on fuel subsidies this fiscal year through June 2019, when it plans to have phased out the support for fuel prices. The monthly import bill for fuel and natural gas has declined to about USD 550 million during the current fiscal year compared to an average of USD 700 million previously. The lower import bill will underpin Egypt’s continued economic recovery through 2019, even if oil price volatility continues.

See Egypt Country Outlook

SUDAN & SOUTH SUDAN

While South Sudan is attracting fresh oil sector investment, dependency on Sudan undercuts stability.

South Sudan’s oil production remains dependent on Sudan’s export terminals, underscoring the interlinkages between the two countries’ oil sectors. South Sudan is targeting oil output of 200,000 bpd, from a current 155,000 barrels, after the restarting of the country’s northern Unity field in December 2018.

The country is also attracting fresh foreign investment from new and traditional sources as its fragile peace process begins to take hold. However, dependence on Sudan undercuts some of these recent gains. Disruptions in oil production, disputes over oil revenue sharing, and lower oil prices have had a negative effect on the economies of both Sudan and South Sudan.

Sudan is already facing an economic and financial crisis. Depreciated oil prices, in addition to a downturn in production at its major refineries, have seen government revenues garnered from its mainstay economic activity plummet. Equally, a decrease in oil production and revenues have left the state with a lack of foreign currency to import fuel and basic commodities, leaving few avenues of respite for a government that is facing an increasingly desperate and agitated population. Violent protests have raged over December in large parts of the country, which would be further aggravated in case of even lower oil prices in 2019.

See Sudan and South Sudan Country Outlook

IMPACT ON MAJOR AFRICAN FUEL IMPORTERS

Unreformed African economies that depend on fuel imports will see negligible benefit from lower oil prices in 2019, due to currency volatility, entrenched external imbalances, and rising debt concerns. Countries like South Africa will not see an immediate economic recovery as fuel prices drop, while Kenya’s trade deficit may only be narrowed once a pipeline for crude oil exports is complete. Ethiopia is in a better position in 2019 to pay its fuel import bill than last year, despite ongoing hard currency shortages. Other large fuel importers like Morocco will need to depend on export growth to balance the import bill, even if international oil prices fall.

SOUTH AFRICA

A falling import bill is insufficient to turn around the struggling economy, as debt concerns mount.

Falling international oil prices have recently outweighed the impact of the weakening rand. The country’s department of energy has already announced a sharp drop in fuel prices for January 2019 after surging to a record high in October 2018. This will boost
the governing ANC party’s re-election chances towards the middle of the year, while also offering some much-needed budgetary relief. It should also boost South Africa’s chances of retaining its debt assets within Citi Group’s prestigious World Government Bond Index (WGBI) and with that the trajectory of South Africa’s investment inflows.

However, a falling import bill is unlikely to spur a broader economic upswing. Growth projections for 2018 have already been revised downwards from 1.5 percent to 0.7 percent. Fiscal consolidation is similarly off the mark. Contrary to expectations, the deficit is forecast to widen to 4 percent and 4.2 percent in 2019/20, while debt will peak at a high of 59.6 percent a year later than expected in 2023/2024. Finance Minister Tito Mboweni has warned that should the country’s debt reach the 60 percent mark, it would be forced to turn to the IMF for assistance. Associated servicing costs are also scheduled to escalate from the current 13.9 percent to 15.1 of revenue by 2020/21, adding further pressure to the country’s limited fiscus.

See South Africa Country Outlook

KENYA

Long term weakening of Kenya’s external position will not be reversed by lower oil prices in 2019.

In June 2018, Kenya began its first ever crude oil exports from the northern Turkana region. However, until a planned pipeline allows for larger-scale commercial oil exports, Kenya will not be able to offset its sizable fuel import bill with crude exports. For most of 2018, Kenya’s oil import bill has eaten into the country’s export earnings, exerting pressure on the local currency. Kenya’s deteriorating external position is underlined further by the price stability in its soft commodity export, despite remarkable volatility in the oil price. The amount of money spent by Kenya on oil has risen by 70 per cent from 2016 to 2018, while exports increased by six per cent.

The recent fall in crude oil price bodes well for Kenya’s inflation outlook and eases the pressure on the shilling. Petroleum products account for about 16 percent of Kenya’s import bill, and thus are a significant driver of dollar demand in the domestic market. The Central Bank of Kenya believes overall inflation will remain within the target range in the near term. However, Kenya’s lack of refining capacity remains a serious drag on the budget – the country closed its only refinery in 2013. Lower fuel prices will however make the recent imposition of a petroleum tax more palatable, despite heavy opposition the levy was approved in October.

See Kenya Country Outlook

ZAMBIA

A deprecating local currency counter-acts lower oil prices with little benefit to deficit reduction.

Despite lower oil prices, Zambia’s Energy Regulations Board has planned no adjustment of fuel prices. This is due to the depreciation of the kwacha currency, which has left the country’s import bill effectively unchanged. In November, Zambia’s total fuel import bill stood at USD 152 million. During the period of importation, the kwacha was still depreciating while international oil prices were still relatively high. Yet the prospect of lower fuel prices remains remote even if the kwacha stabilises and the oil prices remain relatively low as
Zambia’s government implements austerity measures for deficit reduction.

Disconcertingly, with the kwacha rapidly ceding to the USD and the outlook on the mainstay copper industry appearing highly speculative there is the feeling that the worst is yet to come for the externally vulnerable market. Indeed, further bullishness from the US Federal Reserve Bank or tariffs on copper could see the kwacha depreciate more, revenue streams dry-up, and foreign short-term payment requirements tread further into default territory as portended by recent ratings downgrades. A lower fuel import bill might alleviate some budgetary pressure, but is highly unlikely to reverse Zambia’s economic decline.

See Zambia Country Outlook

ETHIOPIA

Ongoing economic reforms and a stabilising currency mitigate risk of non-payment on fuel imports.

Landlocked Ethiopia imports all of its petroleum products, which are critical for transportation, industrial, and household uses. The Ethiopian Petroleum Supply Enterprise (EPSE) therefore plays a crucial strategic role for the economy. Ethiopian fuel imports have been growing at a rate of 10 percent every year and now amount to three million metric tons valued at over USD 3 billion. Fuel imports are so important to Ethiopia that it continues to seek greater diversification of supply. Capacity limitations at the Djibouti oil terminal have prompted the Ethiopian
government to start planning to build an oil terminal at the Port of Djibouti. The Ethiopian government, which fully funds EPSE’s import bill, is unlikely to risk any disruption to the strategically important fuel supply.

Ongoing hard currency shortages, rising inflation, and below target exports are key concerns at a time of continued fiscal expansion and dwindling economic momentum. This has raised concerns over non-payment of Ethiopia’s fuel import bill. However, lower oil prices, a stabilising currency, broad-based economic reforms indicate an improved balance of payments position for 2019. Moreover, syndicated credit facilities with multilateral participation are being prioritised for payment by the Ethiopian government. Ethiopia is also using its expanding goodwill to acquire condition-free multilateral funding, which should further ensure timely payment on the country’s fuel imports.

See Ethiopia Country Outlook

MOROCCO

Liberalisation has not brought lower fuel costs, yet longer term diversification plans are underway.

The deregulation of fuel costs has backfired on the Moroccan government amid falling oil prices in the international market. The Moroccan government liberalised fuel prices in December 2015, leaving them to be determined by market forces. However, the country’s sole oil refinery ceased operations in 2015. Additionally, high taxes keep the fuel price artificially high. Taxes represent around 46 percent of the final price of the litre of fuel in Morocco. Subsequently, consumers have been prevented from taking advantage of the benefits of liberalisation.

Over the past few months transportation workers have gone on strike to protest soaring fuel prices, which disrupted fruit and vegetable supplies, forcing an increase in food prices. The last time oil prices crashed in 2014, Morocco’s government took advantage to wean its economy off fuel subsidies. Yet, incomplete sector liberalisation has not allowed Morocco to reap the benefits of lower oil prices. Longer term plans are being laid out to reduce Morocco’s dependence on foreign oil and coal. The government is inviting bids for a liquefied natural gas project in Jorf Lasfar worth USD 4.5 billion. Meanwhile, booming exports of vehicles, phosphates, aeronautics, and agricultural products are set to underpin export growth in 2019. Morocco’s account deficit is set to shrink to 3.3 percent of GDP in 2018 and 2.2 percent in 2019, down from 3.6 percent in 2017.

See Morocco Country Outlook