Houston Welcomes $70 Oil

U.S. crude prices topped $70 per barrel in early May, a level not seen since late November '14. A host of factors have contributed to the rise.

The U.S. economy continues to grow. April marked the 97th consecutive month of net U.S. job gains. Gross domestic product (GDP) has grown in 33 of the past 36 quarters. The U.S. unemployment rate, 3.9 percent in April, is below the level many economists consider to be full employment.

The global economy continues to expand. The International Monetary Fund reports global growth hit 3.0 percent in '17, up from 2.4 percent in '16, and is expected to average 3.1 percent this year. The Economist Intelligence Unit forecasts global trade in goods and commodities to grow 4.6 percent this year and 4.0 percent the next.

Global oil consumption continues to set records. Demand topped 96.2 million barrels per day (b/d) in '16, 97.8 million b/d in '17, and is projected to top 100 million b/d by the end of '18.

OPEC and its allies have complied with the terms of their agreement to limit crude production. The first agreement —reached in November '16, then renewed in November '17—has kept more than 1.8 million barrels of daily production off the market. The group will meet again in June to reassess the agreement.

President Trump threatened to withdraw the U.S. from the Iran nuclear accords. Re-imposing sanctions could remove 0.5 to 1.0 million barrels of daily crude production from global markets. In the two months leading up to the announcement, commodity traders bid up the price of crude by $10 per barrel. The day after the announcement, the price was essentially unchanged.

Crude inventories continues to dwindle. Since January '17, global inventories have declined by an average of 0.5 million barrels per day. The U.S. Energy Information Administration (EIA) estimates OECD inventories exceeded 3.1 billion barrels in Q1/17. By Q1/18, OECD inventories had fallen to 2.8 billion barrels.

Venezuela's production continues to decline. The International Energy Agency (IEA) projects the country's crude output will tumble to 1.38 million b/d by the end of the year, the lowest level in 70 years.

Geopolitical conflicts have added an uncertainty premium to crude prices. Traders worry that unrest in Libya and Nigeria could disrupt global supplies and that the civil war in Syria could spread beyond its borders. The jump in prices has spurred U.S. drilling activity. The U.S. drilling fleet has added 92 oil rigs since so far this year. Through April of this year, well starts are up 40.2 percent over the comparable period in '17. Permits to drill are up 45.9 percent through April. And over the past 12 months, the industry has added 1.1 million b/d to U.S. production. Higher oil prices have not led to a surge in local hiring. The industry has added only 10,300 jobs in Houston since December '16, far short of the 86,400 lost in the downturn. EIA projects that U.S. output will average 10.7 million b/d in '18, up from 9.4 million b/d in '17. As recently as '08, domestic output was less than 5.0 million b/d. Production in the Permian Basin, the focus of the current boom, has grown so fast that some drillers can ship their crude to refineries and export terminals only via trucks and rail cars. EIA expects pipeline constraints to ease by the end of next year as additional capacity comes on line.

HARVEY IMPACT BEGINS TO FADE

Metro Houston created 10,500 jobs in March. That's below the long-term average of 12,800 for the month. Factor out recession years, and the long-term average jumps to 14,900. For the 12 months ending March '18, the region created 62,500 jobs, a dip from the 70,100 created in the 12 months ending February '18. The data suggest that Houston's 12-month growth peaked in February and has begun to trend down.
The shift in job growth was expected. Houston typically receives a short-term economic boost immediately after a major hurricane. Repair work jolts construction activity, the need to replace damaged household goods lifts retail sales, displaced residents dine out because they can't eat at home, and companies bring on temporary workers to handle specific recovery needs.

Typically, a post-hurricane stimulus lasts half a year, then begins to wind down. Hurricane Harvey made landfall in late August and six months had elapsed in February. As repairs are completed and families return home, demand for labor tied to Harvey recovery efforts will taper off. Without a surge in hiring elsewhere, the 12-month job total should continue to slip.

A few metrics indicating possible growth not associated with Harvey: The North American drilling fleet broke the 1,000-rig mark in early April. TWC already reports year-to-date job growth in the manufacturing of oil field equipment and fabricated metal products. The Houston Purchasing Manager's index, a leading indicator for regional growth, registered 56.6 in April. Readings above 50 indicate expansion over the next three to four months. The PMI slipped below 50 in the three months immediately after Harvey. The PMI is now at its highest level since October '14. The U.S. economy continues to grow at a healthy pace. The U.S. Bureau of Economic Analysis reports that over the past four quarters U.S. GDP growth has averaged 2.9 percent. However, the ongoing trade dispute with China, and possible spillover into relations with other countries, would hurt sectors of Houston's economy tied to global trade. The impact would likely be felt later this year.

The Greater Houston Partnership's employment forecast, based on the assumption that crude would average $50 per barrel in '18, calls for the region to create 45,500 jobs this year. The U.S. E.I.A. forecasts West Texas Intermediate (WT), the U.S. benchmark for light, sweet crude, to average $65.58 through the remainder of the year. If that forecast hold true, growth will be more robust later this year and jobs gains will be stronger than the Partnership initially projected.

Sources: Greater Houston Partnership; Houston Chronicle; Houston Business Journal