

Relative oil prices and differential oil profits

Editor

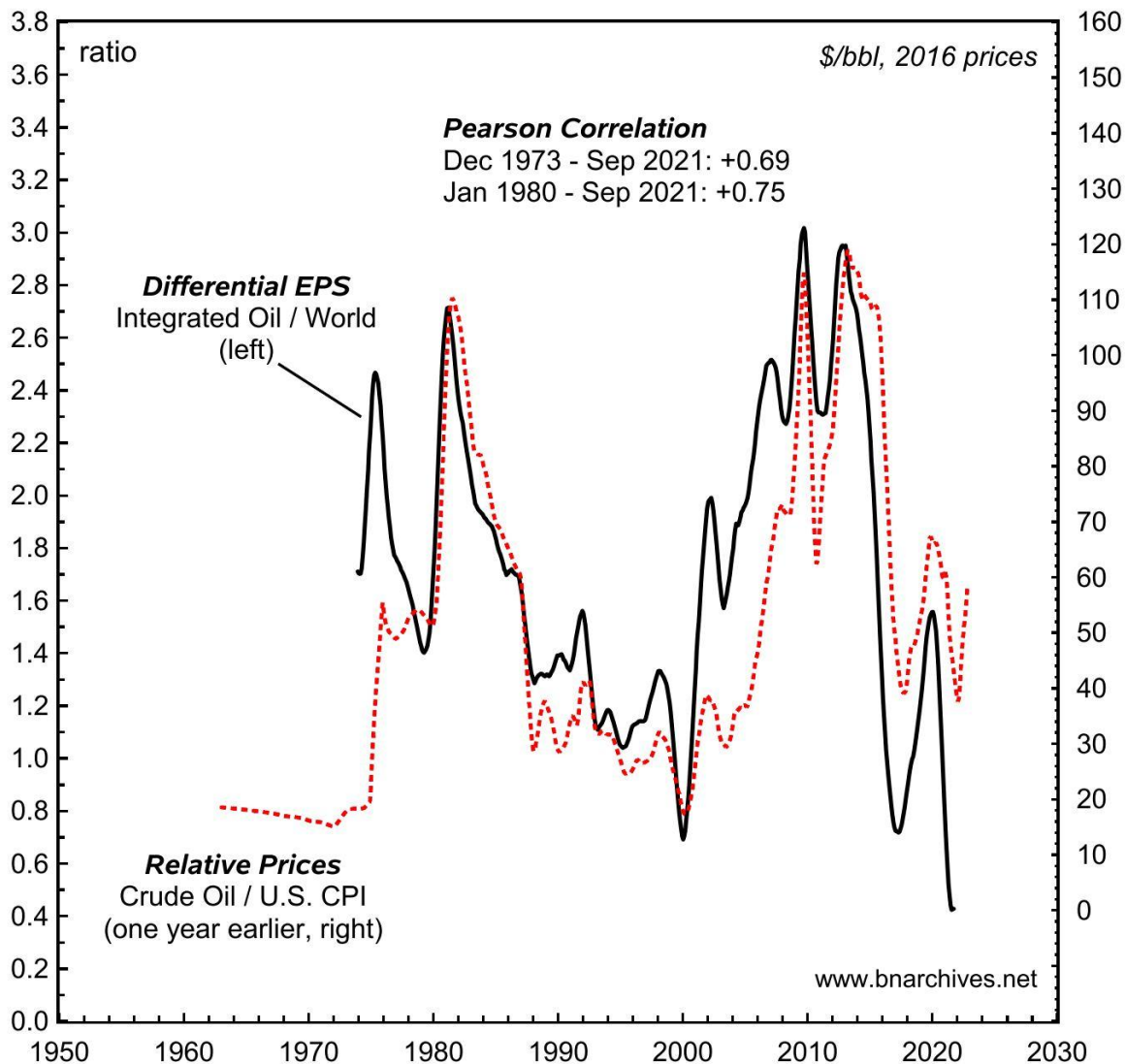
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from **Shimshon Bichler** and **Jonathan Nitzan**

If you thought that oil profits are about producing oil, think again.

The enclosed chart, updated from our 2015 *Real-World Economics Review* paper, '[Still About Oil?](#)', shows that the main determinant of oil profit — and specifically of *differential* oil profit — is not output, but prices.

The figure shows the correlation between two series: (1) the differential oil profits of the world's integrated oil companies, computed as the ratio between their earnings per share and the earnings per share of all listed firms; and (2) the relative price of oil one year earlier, measured by the \$ price of crude oil relative to the U.S. consumer price index. (The reason for the annual lag is that 'current' profits represent a trailing average of earnings recorded over the past 12 months.)



Differential Earnings per Share and the Relative Price of Crude Oil

NOTE: Series show monthly data smoothed as 12-month trailing averages. EPS denotes earnings per share and is calculated by dividing the stock price index by the price-earnings ratio. Differential EPS is calculated by dividing the EPS of the integrated oil index by the EPS of the world index. The relative price of oil is the average crude price deflated by the U.S. CPI. The last data points are September 2021 for the differential EPS and October 2021 (October 2022 lagged) for the relative price of oil.

SOURCE: Updated from Shimshon Bichler and Jonathan Nitzan, 'Still About Oil?' *Real-World Economics Review*, No. 70 (February), 2015, Figure 3, p. 12. Datastream (series codes: TOTMKWD(PI) and TOTMKWD(PE) for the price index and price-earnings ratio of all listed firms, respectively; OILINWD(PI) and OILINWD(PE) for the price index and price-earnings ratio of all listed integrated oil firms, respectively). OPEC via IHS Markit (series code: WORNCOPOPEC for OPEC spot basket crude oil reference price in \$US); IMF International Financial Statistics through IHS Markit (series codes: L64@C111 for the U.S. CPI).

When we wrote the article in 2015, differential oil profits and the relative price of oil were both at record highs; nowadays, they brush against record lows. And that pattern is to be expected. As the chart shows, the correlation between these two measures remains positive and tight, with a Pearson coefficient of +0.69 for the entire period since Dec 1973, and +0.75 since January 1980.

Inflation is always and everywhere a re-distributional phenomenon.

(And expect differential oil profits to rise next year.)