



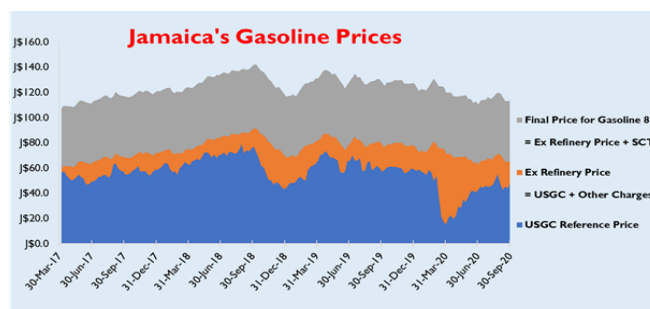
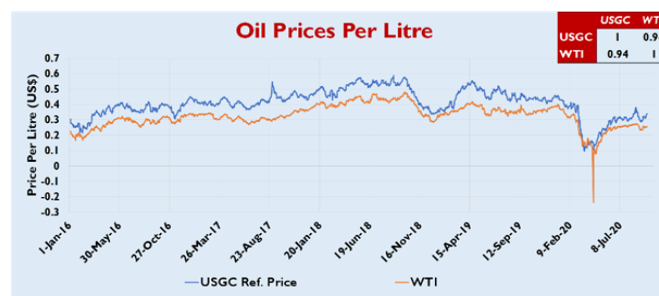
Demystifying the Changes in Local Gas Prices

Oil may be considered the lifeblood of industrialized nations and has become the most important source of energy since the mid-1950s. In Jamaica, oil and its by-products underpin much of the country's productivity, as it is the main source of energy for the manufacturing sector and providing fuel for ground and air transportation. Consequently, fluctuations in oil prices on the world markets get a lot of focus locally and the price of oil ultimately plays an integral role in the propensity to spend, both on a micro and macro level.

Petrojam, Jamaica's only petroleum refinery, supplies a full range of domestic, transportation and industrial petroleum products to the Jamaican market and is 100% owned by the Government of Jamaica. The company uses the principle of import parity to determine its ex-refinery prices and the product prices published by the company are independent of Petrojam's production costs. According to the company, it must be noted that petroleum products are supplied to its customers locally, not crude oil and very often the failure to distinguish the two is a source of misinterpretation.

There are several grades of crude oil available on the world market including the popular West Texas Intermediate (WTI). The movement in the price of the WTI is very transparent and watched closely by many people. However, the US Gulf Coast (USGC) price is an appropriate pricing reference for petroleum products for several reasons including transparency and liquidity of the market. Notwithstanding, the movement in the WTI gives some indication of the USGC movements as shown in the graph above. As depicted, there is a strong positive correlation between the WTI and the USGC, with a correlation coefficient of 0.94.

Jamaica currently imports crude oil primarily from Trinidad, Mexico and Venezuela with the cost denominated in US Dollars. In addition to the cost for the product, other charges including freight, ocean losses, terminal fees are also incurred, plus the acquisition differential. The acquisition differential is the difference between the supplier's selling price and the USGC reference price, to which Jamaica's petroleum products are indexed. These costs combined are then included in the pricing formula to produce the ex-refinery price. The Special Consumption Tax (SCT) is then levied on the ex-refinery price per litre in the form of a special tax of approximately



J\$37.50 for gasoline 87 for example and an ad valorem tax of 10% on the total to generate the final price for its gasoline and diesel products.

Critically, Petrojam's pricing mechanism includes "a cap" and "a floor" whereby the final price of its products are not allowed to rise or fall by an amount exceeding J\$3.00, in a given week. This mechanism is used to stabilize the market and isolate the local market from rapid movement in oil prices. For example, at the start of April when oil prices plummeted to negative territory, the USGC reference price decline by almost 74%. Notwithstanding the steep decline in the USGC, the final price of Gasoline in the week ended April 2, 2020, only saw a decline of approximately 6% when compared to the last week in December 2019. While we acknowledge that a depreciating Jamaican Dollar (JMD) could have erased some of the benefits of a reduction in prices, the currency only marginally depreciated over the period and therefore would not fully explain the movements in the final price.



While the pricing mechanism prevents wide swings in petroleum prices on a weekly basis, over time if price movements are persistently leaning to any one direction, the prices published by Petrojam are expected to gradually adjust. Take this year for example, up to the week ended September 24, 2020, the price of Gasoline 87 has seen about an 11% increase while the USGC has declined by approximately 27%. Therefore, once oil prices remain low, we could expect to see the benefits of the decline in oil prices. However, this is likely to be offset by a depreciating Jamaican Dollar given the reduction of foreign exchange flows due to coronavirus pandemic.

Date	September 24, 2020	April 2, 2020	December 26, 2019
USGC Ref. Price	\$43.97	\$15.59	\$59.88
JMD:USD	\$141.94	\$136.43	\$132.97
Ex Ref. Price	\$65.13	\$71.04	\$77.86
Diff (Ex Ref. – USGC)	\$21.16	\$55.45	\$17.98
SCT Special	\$37.78	\$37.78	\$37.78
SCT Ad-valorem	\$10.29	\$10.88	\$11.56
Final Price - Gasoline 87	\$113.20	\$119.70	\$127.20

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