



Gasoline Prices and The Economy

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No doubt you have noticed the price of gasoline lately! Nationwide the average price of unleaded regular gas was \$1.72 last week. And, unfortunately, I have no good news. Gasoline prices typically rise with the advent of the summer driving season, so \$2 per gallon is likely by Memorial Day.

There are a number of reasons for this gloomy picture. First of all, crude oil prices have increased dramatically, and this is the main reason that gasoline prices are up. Crude prices started up when OPEC announced it would cut production by one million barrels per day, and they appear to be doing it. This situation is exacerbated by the continuing unrest in Venezuela and President Chavez's threats against the U.S. All of this comes at a time when crude stockpiles are very low, so that disruptions to the marketplace cause big spikes in prices.

Second, the world economy is rebounding. Economic growth in China and Japan is picking up, and with it is a sharp increase in the demand for energy generally, and oil in particular.

Third, environmental mandates to clean up the air have resulted in a fragmented gasoline marketplace, with different formulations required in different locations. California, New York, and Connecticut are the most vulnerable.

Higher energy prices are, in effect, a tax on the economy that drains money from the system. The reduction in purchasing power alone will lower the growth in GDP. In addition, gas prices are the most visible of all prices a consumer pays.

Higher prices undermine consumer confidence. As a general rule of thumb, for every \$5 increase in the price of a barrel of crude oil, economic growth slows by

4/10ths of one percent, and the effect is non-linear. So if prices rise from current levels the impact will be about 1/2 percent for every \$5 increase.

But no one expects crude prices to continue rising much past \$40 per barrel and these prices will ease. OPEC cannot maintain perfect discipline. At these high prices oil producers will find ways to cash in; soon even more Iraqi oil will be flowing, and this will push prices down. Nevertheless, the high price of gasoline will limit the growth of the U.S. and Florida economies somewhat compared to what might have been.

That said, although higher gasoline prices are most unwelcome, they are not so high as to trigger a recession or to stop Florida's economy.

This is Hank Fishkind for 90.7 FM, WMFE News.

Fishkind and Associates, Inc.