WHY ARE GAS PRICES ON THE RISE?

Concepts Addressed:

- Determinants of Supply and Demand
- Market Interaction

Teacher's Notes:

The demand curve for gasoline has shifted to the right indicating a change in consumer expectations as we become less concerned with the virus and more willing to return to public life.

The supply curve, is shifting to the right more tentatively as producers show more skepticism that the virus is behind us. Thus, the equilibrium price is higher because the equilibrium quantity isn't back to pre-Covid levels.

The rising price of oil will impact the price of things in other markets since it is a key ingredient in many areas of the economy and a compliment to many activities we enjoy.

Why Gas Prices Are on the Rise

Prices at the gas pump are significantly higher than last November — threatening to hit $3 a gallon by summer and even $4 in some places. While overall inflation remains subdued, some economists are worried that prices, especially for fuel, could rise faster this year than they have in some time. That would hurt working-class families more because they tend to drive older, less efficient vehicles and spend a higher share of their income on fuel.

Gasoline price hikes are a result of rising demand and stagnant supply. If we did not have vaccines, oil prices would not have gone up. An accelerating rollout of vaccines in the United States is expected to turbocharge the American economy this spring and summer, encouraging people to travel, shop and commute. In addition, President Biden's pandemic relief package will put more money in the pockets of consumers, especially those who are still out of work.

Although gasoline demand is climbing, Americans are still consuming 9% less now than before the pandemic while U.S. daily oil production remains 20% below the 13.3-million-barrel pre-pandemic peak, citing statistics from the U.S. Energy Information Administration.

Only 544 drilling rigs are currently in operation in the United States and Canada compared to 996 a year ago. North American oil producers, still shaken by the unprecedented 60% drop in gasoline demand over two weeks last spring, are being cautious about restarting idled drilling rigs, which is allowing renewed demand to outstrip supply and keeping prices high. In addition, market forces pushing prices up now include the Texas deep freeze last month that shut down many refineries and temporarily reduced gasoline production.

BELL Ringers

Florida Council On Economic Education

WHY ARE GAS PRICES ON THE RISE?

In recent weeks oil prices have surged to over $65 a barrel, a level that would have seemed impossible only a year ago, when some traders were forced to pay buyers to take oil off their hands. Oil prices fell by more than $50 a barrel in a single day last April, to less than zero.

Globally, the discipline to support higher prices is needed for the recovery of economies dependent on oil as their primary export. Many oil producing nations saw their economies crushed last year and need higher oil prices to balance their budgets and service their debts. They could be holding the line on supply for a while.

Questions:

1. If gasoline prices continue to rise, what other prices will rise in a typical family budget?
2. If we have a resurgence of Covid variant cases this summer, what do you suspect will happen to oil/gasoline prices?
3. Generally, when oil prices rise, drilling picks up flooding the market with oil which moderates prices. Why not this time?
4. What areas of the economy should benefit this summer from the consumer optimism?

WHY ARE GAS PRICES ON THE RISE?

Answer Key:

1. Anything that is produced with petroleum as an ingredient, delivery costs, air travel, food, manufacturing.

2. Oil and gasoline prices will fall if the resurgence of Covid leads to less economic activity.

3. In the U.S., much of the oil produced comes from the very costly process called fracking. The plummeting of oil prices last year put a lot of operations out of business and there needs to be hard evidence that we have beaten the pandemic before investors will be willing to open new wells. In countries outside of the U.S. that depend very heavily on oil revenues to run their economies, they need high prices for a while to repay their debt and get their devastated markets back on track.

4. The hardest hit industries in the spring of 2020 are hoping for a resurgence this summer. That would include restaurants, brick and mortar retail, hospitality, theme parks and the service sector.