Factors Affecting Gas Prices

Summer heat, global debt crisis, and oil reserves and production decisions affected prices we pay at the gas pump. In the course of this year, the average retail price of reformulated gasoline in the United States peaked from $3.15 in the first week of January to $4.09 in the second week of May. Prices then began to decline to $3.67 in the first week of June after talks of a sale of 30 million barrels of light, low-sulfur crude from the U.S. Strategic Petroleum Reserve. In addition, sale of another 30 million barrels from the International Energy Agency (IEA) member nations increased the supply. Nonetheless, the average price of gasoline climbed back to $3.73 in the second week of August. The following factors contributed to the price hike during the summer months.

From Texas to the Dakotas to the Midwest in Illinois and Indiana and to the East Coast in Massachusetts and New York unusually intense heat waves brought about temperatures and humidity levels in excess of 100 degrees. This year’s summer heat has given a boost to the demand for gasoline due to increased driving and vacationing. The increased demand for gasoline has lifted prices at the pump.
Worries about the U.S. and Greece defaulting on their debt moved prices to opposite directions. Concerns about U.S. default moved oil prices down in the commodities market, as investors were cautious about taking risky investments at a time of uncertainty. These price fluctuations were not felt at the pump since the U.S. Congress avoided default on the national debt. On the other hand, a brighter outlook for a bailout of Greece’s debt by the European Union lifted oil prices. Although a further downgrade in its credit rating may drive those prices down again.

Of all the factors affecting prices, the oil released from reserves has had the biggest controversy and has raised many questions as to whether it will in fact lower prices. Only a week after the end of the sale prices are once again on a significant rise as analysts debate whether the source of the price increase has stemmed from either the U.S. and European default fear or from the buyers of the reserve oil that may be manipulating the market and storing the oil, then releasing it into the supply stream once prices are higher. Iran’s governor for the Organization of Petroleum Exporting Countries (OPEC) has even gone on record to say that the IEA failed in its endeavor to intervene with oil and gas prices.

Members of the OPEC were split on production decisions as an inside report found that OPEC crude production in May averaged 28.97 million barrels per day while the demand for crude was estimated at 29.90 million barrels per day by the year’s end. Saudi Arabia, Kuwait, Qatar, and the United Arab Emirates were unable to push the OPEC to raise production ceilings to meet the market demand. Iran and other OPEC members opposed raising production quotas. Iraqi oil minister Abdul-Karim Elaibi has stated his opposition by saying that a price between $100 and $120 is “reasonable” for the market.

From a demand-supply perspective, the rise in the market price for oil is not necessarily a “fair-value price,” but the price at which consumers are willing to pay in order to acquire the oil that the producer is unwilling to supply. In the long run, though, consumers will find ways to conserve gas by traveling less and budgeting gas mileage; an example would be the end of this year’s busy summer and the vacation season, this would lead to a drop in the demand for oil near the supply, thus lowering the price. Also, an addition to the supply from the IEA’s oil reserves may raise supply levels at or near the demand. In the short-run, there will always be fluctuations in the price of oil as markets react to different news and events. In the long-run, however, markets return to at or near fair market prices as those events pass. In an uncertain and unpredictable oil market, at least one thing is certain… it’s time to fill up the tank!

Sources:
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