

# Lower Projected Gasoline Prices

## in Texas MEAN BETTER BUSINESS THIS SUMMER

By Alan Lammey



**H**ouston business owners can breathe a sigh of relief this summer when it comes to automotive fuel expenses' impact on their bottom line: gasoline prices are down notably from last year and are expected to remain in check this year. Even better, lower prices at the pump also mean that consumers have more discretionary spending power, which is good news for Texas business in general.

We all know how rotten it feels to pump \$70 worth of gas into your car when it used to cost \$60 or even \$40 for a fill-up. The price that we pay at the pump is sometimes a financial barometer or metaphor of sorts for falling behind financially rather than moving ahead. But this summer, gasoline prices are falling—and the U.S. Department of Energy (DOE) projects that they will remain stable, if not drop lower, this summer and into

2014. That's worth celebrating in the business community.

Given the long-awaited economic recovery that appears finally to be taking root (though to a much stronger degree in Texas than in the rest of the country), economists normally would fear that rising gas prices might damage fragile consumer psyches and restrict family budgets enough to stall growth. But this year, just the opposite appears to be happening: U.S. oil inventories are at near-record highs, which is helping to keep a lid on gasoline prices.

Economists have been studying gas-price peaks and lulls for decades, from the gas-station lines of the 1970s to the still-hard-to-explain surge in oil prices in 2008 that pushed U.S. pump prices up above \$5 for the first time ever in some areas of the country, and above \$4 in parts of Texas.

But lots of "economic positives" tend to happen when gasoline prices fall, with some supporting data about how these forces might positively affect the Houston (and Texas) economy throughout the summer of 2013.

### Consumer Spending Increases

This time last year in 2012, gasoline prices at the pump were bumping up close to \$4 per gallon. In the U.S. as a whole, that's not good news, because the rule of thumb from an economic perspective is that every 10¢ rise per gallon in gas prices costs the U.S. economy about \$11 billion. In 2013, gasoline prices in Texas have fallen notably—to around \$3.30 a gallon, depending on where it's purchased. That equates to about a 15 percent to 20 percent decrease in gas prices, which means that spending on other things will usually rise by about 1 percent to 2 percent or more. That's because motor fuel accounts for about 5 percent of the typical consumer's spending, so most people will find themselves with extra cash when gasoline prices decline or remain the same. If spending on gasoline declines to 3 percent to 4 percent of the typical budget, spending on everything else usually increases from 93 percent to 95 percent, more or less.

Some shoppers will indulge in small things, like food and soda, which they might purchase at the gas station, but the impact of lower gas prices is felt immediately in other areas of the local economy as well.

For the most part, the lower fuel costs reduce overall spending stress; as a result, people won't be as inclined to put off bigger purchases, such as appliances, home-improvement projects, or even new vehicles. Some people may also be more apt to take vacations, since lower fuel costs are factored into family vacation expenses.

### Car Shoppers Buy More Domestic Cars, as Well as More Luxury Imports

Historically speaking, when gasoline prices either are actually lower, appear lower, or at least remain stable (i.e., not climbing), Americans are more likely to purchase less fuel-efficient luxury cars.

The exact opposite is typically true when gasoline prices bump up to the \$4 level or higher, as evidenced in a pullback in overall spending. That's what happened in 2008, when oil prices climbed to a record high of nearly \$150 a barrel and gasoline prices rocketed higher as well. Would-be auto buyers went into spending shock and stopped buying. Domestic automakers had few fuel-efficient models to offer, but Toyota and Honda sold out of hybrids and other gas-sippers. Since then, Detroit has learned its lesson: it has started building small cars that can compete with the best from Japan and Europe.

But when gasoline prices fall below \$3.50 a gallon, General Motors, Ford, and Chrysler all see sales of trucks and SUVs begin to climb. In fact, Houston and Dallas auto dealers are reporting that market share for American-made cars has increased as gasoline prices have moderated in recent weeks and months.

### Lower Gasoline Prices Create a Positive Ripple Effect

Higher gasoline prices can have a negative multiplier effect on the broader economy. In the past, as consumers cut back on durable goods purchases, U.S. companies were forced to cut back on their own spending and lay off some of their workers. This ripple effect can turn a 1 percent cutback in consumer spending into a 2 percent drop in overall spending when the regression in business activity is taken into account. But when gasoline prices are lower, companies don't feel the need to reduce staffing, which keeps money flowing.

### Consumer Confidence Increases

Economic forecasting research shows that every 10 percent increase in gas prices lowers consumer confidence by about 1.5 percent. The depressive effect more than doubles when prices crest a round number such as \$4, which intensifies media exposure and attracts even more attention. Conversely, when gasoline prices fall, consumers don't typically fear that future inflation is likely in the near term, so they more confidently spend money. But when gasoline prices are higher, consumers tend to be gloomy and rein in spending. This response is not always rational, because people tend to take less notice of things that are becoming less expensive and easing the strains on their budget. But rational or not, the psychological effect of costly gas can be powerful.

### Buying Behavior Is More Constant, Flexible Amid Lower Gasoline Prices

Changes in consumer behavior when gasoline prices are lower help keep confidence buoyant. People are inclined to drive more when gasoline costs less. This leads to more family excursions and outings, which in turn translates to increased revenue in retail sales and furniture, as well as an increase in revenue for the hotel and restaurant industries, among other sectors.

### It's Great Now, But Lots of Unknown Variables Remain

The DOE expects the price of regular gasoline across the United States as a whole to average \$3.53 per gallon over the summer (April through September). But Texas is a major refining area for the United States, so the presence of local fuel supplies could result in a dip into the low \$3-teens per gallon across areas of the Lone Star State. Gasoline prices typically climb from February to Memorial Day amid expectations of rising consumption and costlier summer-blend gas. But so far this year, gasoline prices hit a peak earlier in the year—and now appear to be moderating and slipping lower.

Lower gasoline prices are expected to contribute to an economic boom for Texas-based businesses this summer, but it's important to remember that the value of oil is also linked inversely to the value of the U.S. dollar. If the dollar falls in value against other world currencies,

it could result in higher U.S. oil prices, which translates to higher gasoline prices at the pump. Meanwhile, political unrest in the oil-rich Middle East, refinery woes, or prolonged natural disasters could cause additional spikes in crude-oil and wholesale-gas prices as well. Increased U.S. petroleum exports could also factor into domestic prices.

As it stands now, when it comes to the possibility of lower gasoline prices this summer, businesses in Texas should see a boost to their bottom line. And when you're in business, any revenue boost is a good boost. **N**

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