



877. 825.7579

[www.realwealthradio.com](http://www.realwealthradio.com)

## *Weekly Financial Article for the Week of May 19, 2008*

Reprinted with permission of Peter Montoya, Inc

### **WHY ARE OIL & GAS PRICES SO HIGH?**

*When will they come down? What's keeping them up?*

**What is going on?** Before 2002, oil prices usually hovered around \$20 a barrel. By early 2006, they were above \$60 a barrel.<sup>1</sup> They were at \$62 a barrel in May 2007.<sup>2</sup> One year later, oil prices have doubled. In October 2004, a gallon of regular unleaded gas averaged just under \$2.00.<sup>3</sup> Now it might cost you twice that.

Is this just a supply-and-demand story? Has demand for oil and gas doubled in the last four years? Have worldwide supplies shrunk notably over the same period? It's a bit more complex than that. Let's look at some of the factors analysts cite for the soaring prices.

**The commodities market.** We've seen a historic bull market in commodities recently, with oil, soybean, wheat, gold, and silver prices at record inflation-adjusted highs. It isn't cooling down just yet. All the speculators investing in the commodities market have helped to drive prices higher.

**The weak dollar.** What fueled the commodities bull market? Many economists point to the dollar, which has declined about 35% in value against other benchmark currencies since February 2002.<sup>4</sup> When the dollar weakens, investors tend to buy commodities like oil futures as a hedge against inflation. Also, when the dollar loses value against other currencies like the euro and the pound, it makes oil cheaper for overseas investors.

The Federal Reserve has signaled that it is through cutting interest rates for the near future, and many people think that this will boost the dollar's value against other major currencies. (The dollar tends to slide when the Fed cuts the key interest rate.) So that may encourage a drop in oil prices, and in retail gas prices.

**Sustained demand.** If somebody told you to cut back on your driving, would you do it? Could you? Many Americans can't. We complain about higher and higher gasoline prices, but we ultimately sigh and put up with them. In addition

to ongoing American consumer demand for gasoline, industries worldwide demand crude oil. As the economies of China, India and other new major-league economic players have developed, their needs for oil and gas have correspondingly increased, raising demand a bit.

**What will make prices fall?** As mentioned, some analysts believe a recovering dollar will be the big factor. Others point to reduced worldwide demand for oil as an effect of record prices. OPEC has revised its demand forecasts downward twice in the last three months.<sup>5</sup>

Industrial needs aside, the American driver might be a major factor here. Change is occurring; SUV and truck sales are declining; people are adjusting their driving habits, and driving less. The U.S. is a prime market for oil exporters, and if consumer demand for gasoline lessens, oil prices seemingly have to fall. So your consumer sacrifice might send a message to Big Oil.

**How is your money?** When you see headlines about the economy, it may make you think of your financial situation, and what you might be able to do to improve it. In times like these, it's a good idea to talk with me about topics like investing, saving and retirement. Think about scheduling such a talk today, for what you learn might help you not only this year, but for years to follow.

*(Real Wealth® and Woodbury Financial Services, Inc. are not affiliated entities.)*