What’s Driving Gas Prices Higher?

Thomas C. Chester, CFP®, AIF®, CPFA®

Presented by ***Thomas C. Chester, CFP®, AIF®, CPFA®***

Whether you’ve seen the prices at the pump, clicked on the headlines, or overheard discussions in the grocery store, you know the rising cost of gas has everyone talking. At the start of the summer driving season, the average price of regular gasoline in the U.S. reached an all-time high, surpassing $4.50 per gallon. Inflationary pressures, including strong demand, supply chain disruptions, and low inventories, have caused price spikes for many consumer goods. As the cost of filling your tank rises, you’re likely wondering which markets factors caused the spike in gasoline prices.

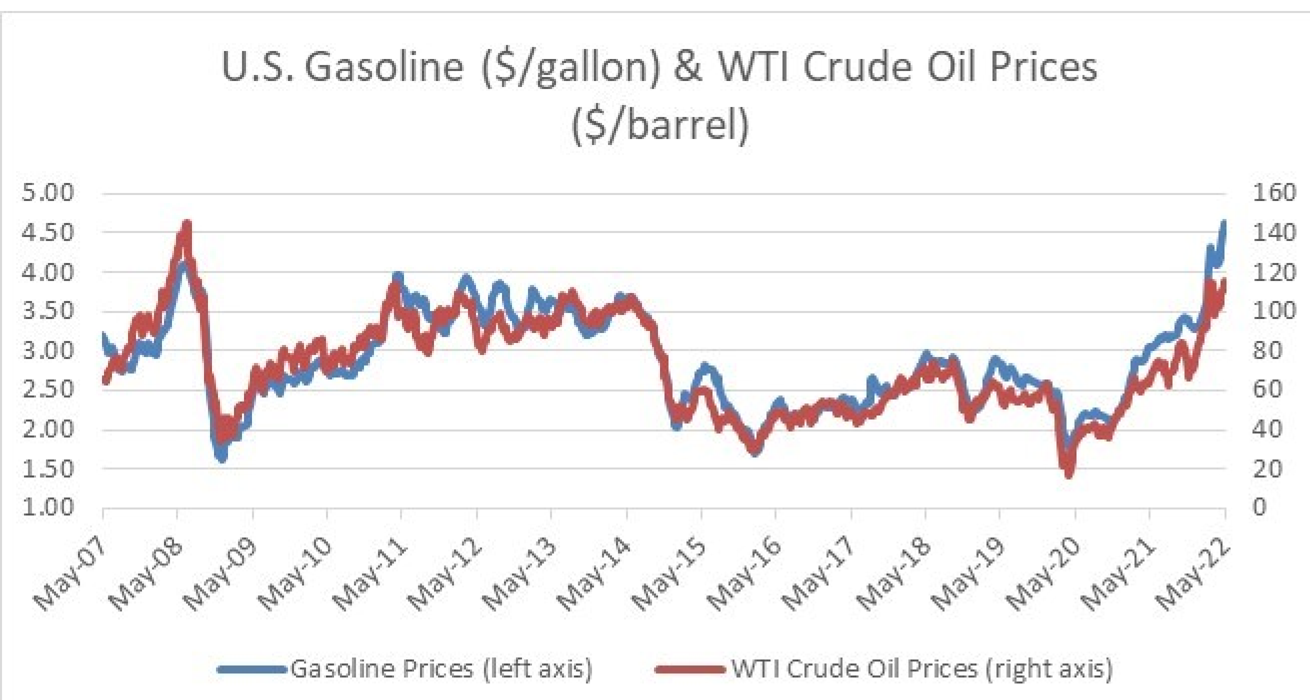
Costs and Taxes

Crude oil is the most important input cost for gasoline. This commodity is primarily refined into gasoline and other transportation fuels, including diesel and jet fuel. Ethanol, a fuel made from corn, is blended with crude oil to represent 10 percent of gasoline volume on average, according to the Energy Information Administration (EIA). Operating costs associated with refineries, transportation (e.g., pipelines, tankers, trucking), and gas stations, as well as federal, state, and local government taxes, contribute to gasoline prices. Differences in operating costs and taxes explain the wide range of gasoline prices across states.

Higher Gasoline and Crude Oil Prices

Figure 1 illustrates the strong correlation between the prices for gasoline and crude oil, which is currently around $115 per barrel for West Texas Intermediate (WTI), the U.S. index. Prices for both commodities have just about doubled since early 2021. Covid-19 lockdowns in China and plans by several countries to release strategic oil reserves helped ease oil prices in recent months. The price of gasoline, however, has continued to increase.

Figure 1. U.S. Gasoline and WTI Crude Oil Prices, 2007–2022



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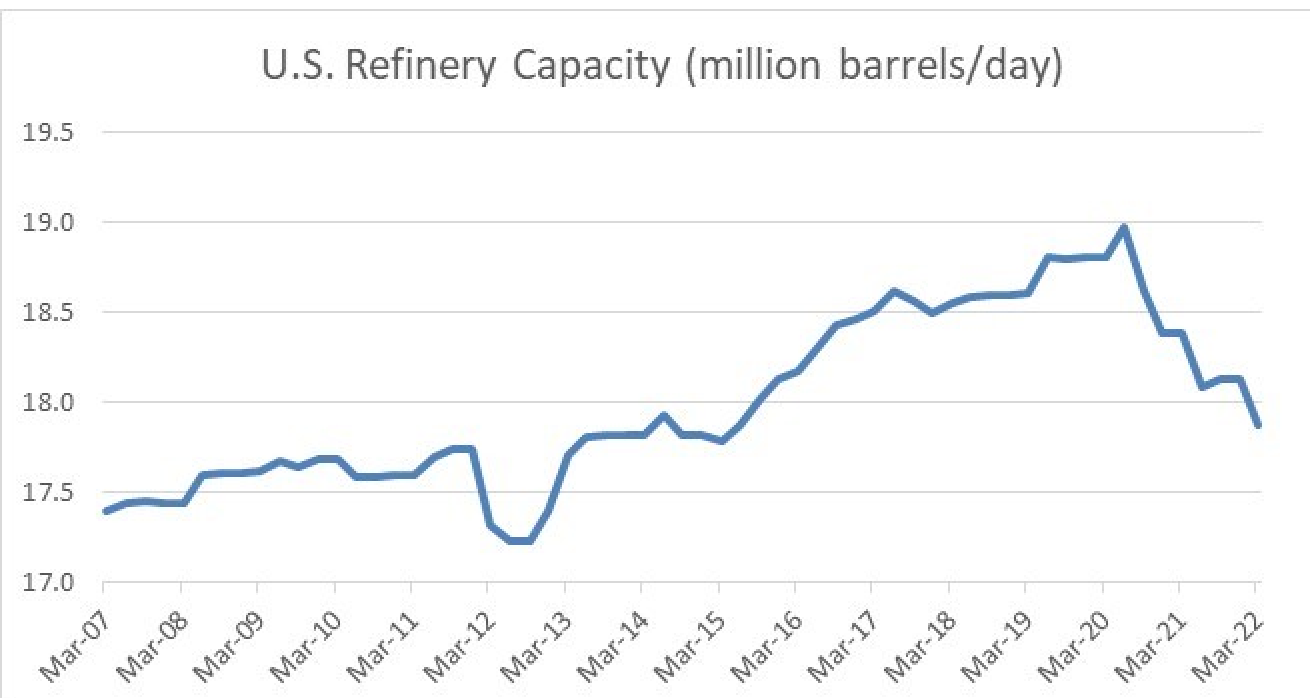
rce: Bloomberg

Decreased Refinery Capacity

Demand for transportation fuels, such as gasoline, dropped sharply early in the pandemic when consumers stayed home, causing several refineries to close permanently. Global refinery capacity fell in 2021 for the first time in 30 years, according to the International Energy Agency (IEA). U.S. refinery capacity dropped to 2015 levels, as shown in Figure 2. Additionally, existing U.S. refineries have limited spare capacity with utilization rates above 93 percent, the highest since December 2019. Meanwhile, refiners are generating record profits from strong demand, capacity constraints, and a higher spread between prices for oil and refined products, such as gasoline.

Figure 2. U.S. Refinery Capacity, 2007–2022



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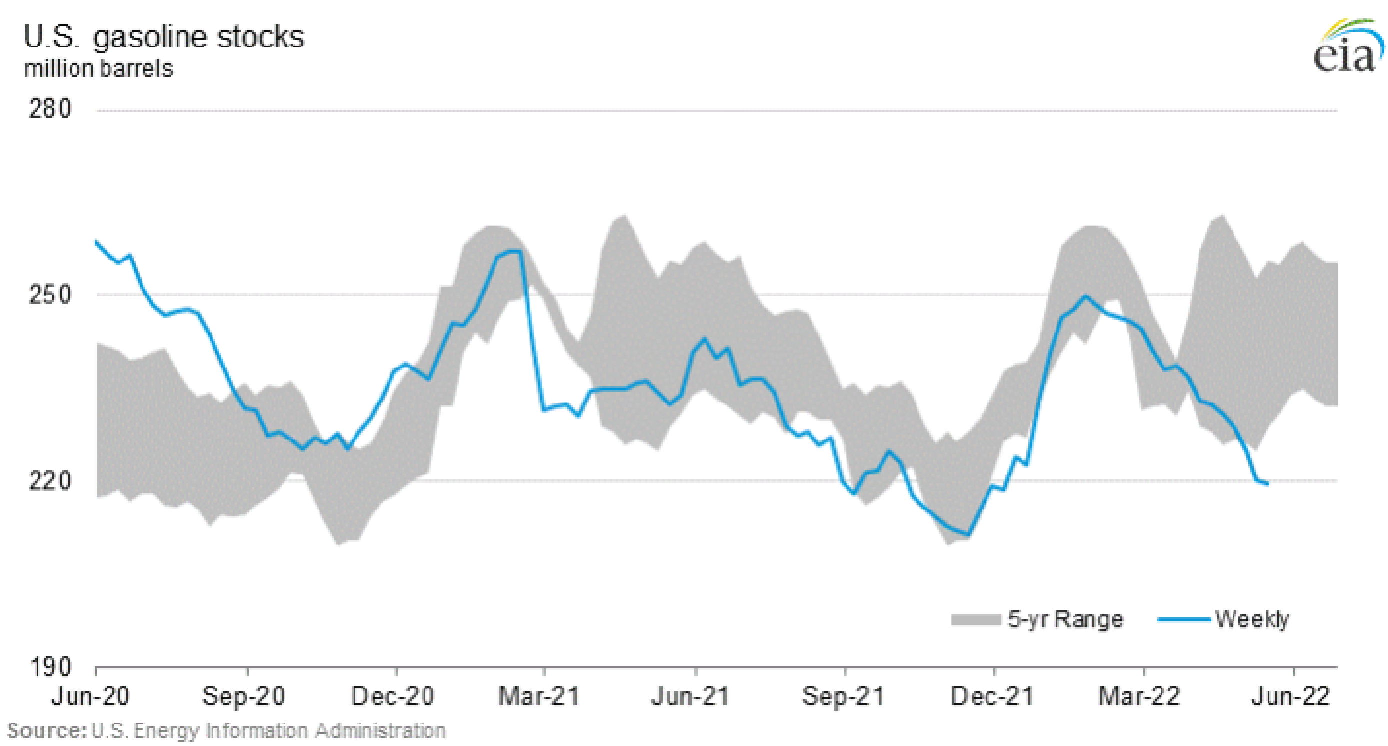
Lower Inventory and Higher Demand

Both U.S. gasoline and oil inventories are at low seasonal levels compared to the five-year range, as shown in Figure 3, which highlights U.S. gasoline inventories. Gasoline and oil demand recovered faster than supply over the past two years while the economy bounces back from the pandemic. Refineries typically boost output before demand peaks during the summer; however, capacity constraints limit supply increases. Although the U.S. still imports oil because its refineries were initially designed to process heavy crude produced from other countries, such as Canada and Venezuela, higher U.S. exports have reduced inventories as Europe seeks to reduce its reliance on Russia for energy imports.

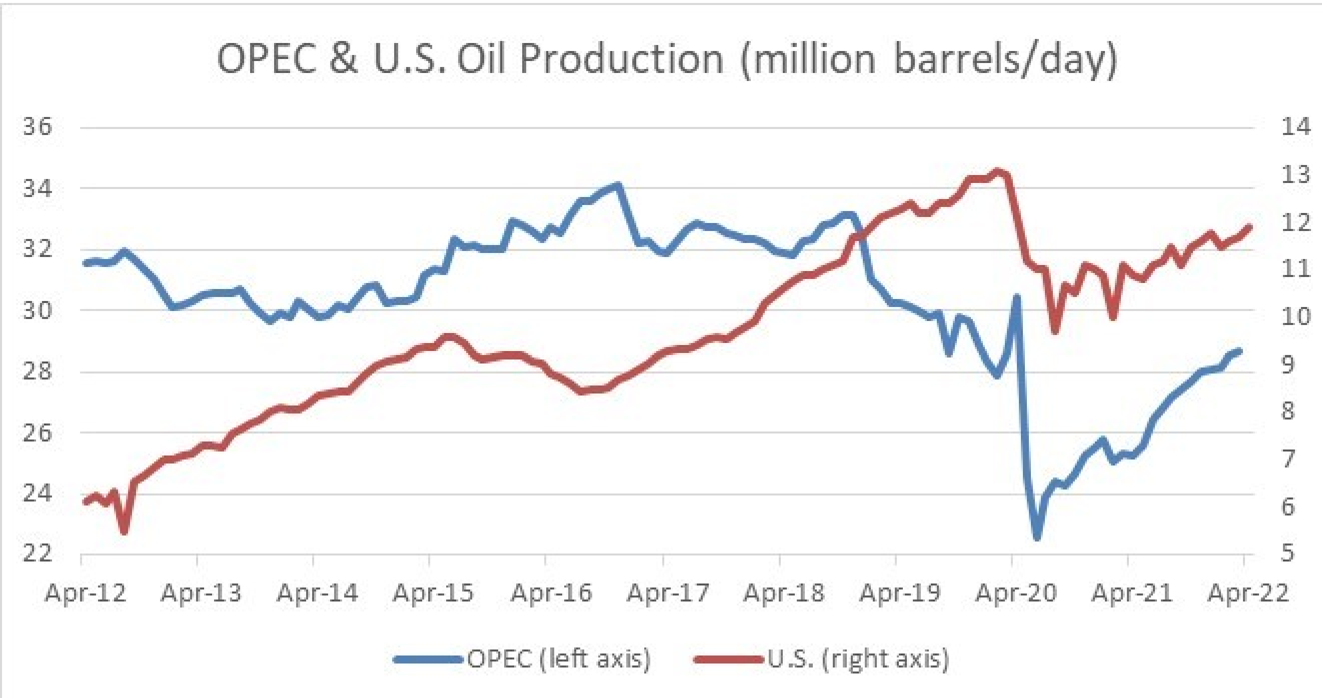
Figure 3. U.S. Gasoline Stocks, 2020–2022



Decline in Oil Supply

Global oil producers quickly cut capital expenditures early in the pandemic to preserve cash for debt servicing and other operating expenses amid highly uncertain oil demand and plummeting prices that fell to around $20 per barrel. Figure 4 illustrates the decline in oil production from the OPEC and the U.S., the world's two largest groups of producers. Supply from Russia, the world's third largest oil producing country behind Saudi Arabia, also declined after its invasion of Ukraine.

Figure 4. OPEC and U.S. Oil Production, 2012–2022



Source: Bloomberg

Oil Production Constraints

Global oil production is slowly recovering as producers have been more cautiously investing in long-term projects, such as offshore drilling, due to a highly uncertain demand outlook for oil. Traditional automakers, for instance, are investing heavily in electric vehicles amid policy support and plans by several countries to phase out internal combustion engines (e.g., gasoline, diesel) in the coming decades.

Furthermore, shareholders have forced publicly traded oil and gas producers to focus on capital discipline, profitability, reducing debt, and investor returns through dividends and stock buybacks. Production growth was the prior objective from a capital allocation standpoint, but producers struggled to generate positive cash flow and earnings following the 2014–2016 crash in oil prices.

Several other market developments have contributed to a slow recovery in oil production:

- U.S. oil producers focused on drilled but uncompleted wells (DUCs) to limit costs when oil demand began to recover after the pandemic. In other words, producers sacrificed future supply growth by completing existing wells at a faster rate than drilling new wells.
- A large portion of U.S. oil supply is produced from shale regions, such as the Permian Basin. Compared to conventional wells, shale wells have high depletion rates that average around 70 percent by the end of the first year, according to asset manager, GMO. This requires continuous capital expenditures to maintain or increase production levels by drilling new wells.
- Small private oil producers have been the main source of production growth in the U.S. as opposed to larger publicly traded producers given shareholder demands for capital discipline.
- Inflationary pressures and shortages for labor and materials, such as steel, reduced the operating capacity for oil field service companies, which supply oil rigs and other equipment to producers.

U.S. Production Forecasts

The U.S. is the world’s top oil-producing country with supply averaging 11.9 million barrels per day over the past two months. Forecasts from the U.S. EIA imply moderately higher production of about 200,000 barrels per day for the remainder of 2022. Oil production growth is expected to accelerate in 2023 and reach an all-time high, averaging more than 12.8 million barrels per day.

A Look Ahead

For the immediate future (this summer), it looks like gas and oil prices will remain high due to global supply issues, low inventories, and increased travel. There is hope for an ease or decline of prices later in the year with the potential for more supply and lower demand. Please contact my office with any questions or requests for more information on current prices or future forecasts.

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Authored by Brad McMillan, CFA®, CAIA, MAI, managing principal, chief investment officer, at Commonwealth Financial Network®.

Introducing our Summer 2022 Intern

Colby Mank, intern at Allen Insurance and Financial, right, and Abe Dugal of Allen Financial, intern program coordinator.

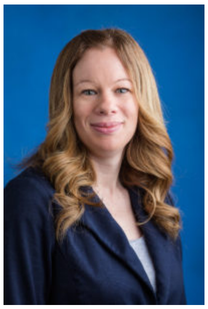
Colby Mank of Union is Allen Insurance and Financial’s 2022 summer intern.

Mank is a senior finance major at Thomas College in Waterville. He plans to graduate in December.

Allen Insurance and Financial’s summer internship program creates the opportunity to learn about each of the company’s insurance and financial planning departments.

“This internship is a great opportunity for my growth as a professional,” said Mank. “The Allen team has been welcoming and encouraging – and they have so much to offer. I’m looking forward to hands-on experience in three of the areas I’ve enjoyed most at college: Investment management, marketing and risk management.”

Busy Season is Here: A Quick Insurance Checklist



By Krissy Campbell

Summer is just here! Restaurants are open, shops are full and traffic is backed up. For local businesses of all sorts, this is good news: Whether you're a contractor taking on new projects, restaurants coming out of hibernation, shops stocking your shelves or hotels & motels bringing on seasonal staff. If you're one of the many businesses with seasonal influxes, let's make sure all that prep work you've done is covered as it should be. Be sure to call your insurance agent about:

- New employees
- Increases in current payroll
- Increase in sales and/or inventory
- New equipment
- New vehicles or drivers
- Seasonal operations
- New operations or projects
- Newly rented or leased locations
- New construction or acquisitions

Anna Moorman Now Licensed as an Insurance Consultant in Maine

Anna Moorman, a member of the benefits team at Allen Insurance and Financial specializing in individual health insurance and Medicare, is now a licensed life & health insurance consultant in Maine.

“Anna’s efforts demonstrate her deep commitment to continuing professional development,” said Mike Pierce, company president. “This commitment is important to all of our insurance divisions but it is especially so in the always-changing field of employee benefits.”

Moorman has been with Allen Insurance and Financial since 2012. She lives in Thomaston with her family.

Weekly Market Update, May 31, 2022

Presented by [Thomas C. Chester, CFP®, AIF®, CPFA®](#)

General Market News

- The Federal Open Market Committee (FOMC)'s most recent meeting minutes were released last Wednesday and provided further support for the market's expectation of back-to-back 50 basis point (bp) rate hikes at the June and July meetings. "Most participants judged that 50 basis point increases in the target range would likely be appropriate at the next couple of meetings," the minutes said. It was also reiterated that the Federal Reserve (Fed) may have to push interest rates beyond neutral and into restrictive territory to confidently quell inflation, stating that "a restrictive stance of policy may well become appropriate depending on the evolving economic outlook and the risks to the outlook." This type of open-ended language has been a staple in the Fed's recent guidance as they look to remain nimble, balance its desire to effectively fight inflation, and engineer a soft (or "softish") landing to avoid a recession. Treasury yields were down slightly last week. The 2-, 5-, 10-, and 30-year U.S. Treasury yields fell 4 bps (to 2.48 percent), 1 bp (to 2.71 percent), 3 bps (to 2.75 percent), and 1 bp (to 2.98 percent), respectively.

- Global equities posted sharp gains last week. Investors focused on inflation, which showed hints of easing as the Fed’s favorite inflation gauge, the Core Personal Consumption Expenditure Price Index, fell from a 0.9 percent increase in March to a 0.2 percent increase in April. Additionally, we saw China issue support for its economy and a reopening within Shanghai, which is a start to alleviating supply chain issues within the region. We also saw softening in policy from the Fed as Atlanta Fed Chairman Raphael Bostic stated he would like to see a pause in September after back-to-back 50 bp federal funds rate hikes. Inventories rose within the retail sector, leading to potential relief to inflationary pressure. As a result, the top-performing sectors were consumer discretionary, energy, technology, and financials. The worst-performing sectors were health care, telecom, and utilities. We’ll monitor if the shift in sentiment sticks in the upcoming weeks.
- On Wednesday, the preliminary estimate for the April durable goods orders report was released. The report showed that orders of durable goods grew 0.4 percent during the month, slightly less than the expected 0.6 percent increase. Core durable goods orders, which strip out the impact of volatile transportation orders, increased 0.3 percent against calls for a 0.6 percent increase. This marks two consecutive months with core durable goods orders growth, which is a good sign for overall business spending because core durable goods orders are often viewed as a proxy for business investment. Business spending has seen solid growth throughout most of the past year, as businesses have invested in equipment and other capital expenditures to increase productivity and meet high levels of consumer

demand. Given the tight labor market, continued business investment is expected throughout the start of summer.

- On Friday, the April personal income and personal spending reports were released. Personal spending increased more than expected, rising 0.9 percent against calls for a 0.8 percent increase. March’s spending growth was also revised up, from an initial report of 1.1 percent to 1.4 percent. Although some spending growth in March and April was due to rising prices, even real personal spending figures improved more than expected in April, signaling high levels of consumer resilience despite inflationary pressure. This strong result, which echoes better-than-expected growth for retail sales in April, was driven by increased consumer spending on goods and services. Personal income increased 0.4 percent, slightly below the 0.5 percent increase that was expected. Although personal income growth missed modestly against forecasts, this was still a solid result that marked seven consecutive months with rising incomes, highlighting the strength of the labor market recovery over that period.

Equity Index	Week-to-Date	Month-to-Date	Year-to-Date	12-Month
S&P 500	6.62%	0.81%	–12.21%	0.32%
Nasdaq Composite	6.85%	–1.53%	–22.21%	–11.17%
DJIA	6.28%	0.96%	–7.85%	–2.03%
MSCI EAFE	3.48%	0.63%	–11.45%	–10.77%
MSCI Emerging Markets	0.91%	–2.82%	–14.63%	–21.53%
Russell 2000	6.49%	1.41%	–15.51%	–15.87%

Source: Bloomberg, as of May 27, 2022

Fixed Income Index	Month-to-Date	Year-to-Date	12-Month
U.S. Broad Market	1.14%	–8.47%	–7.77%
U.S. Treasury	0.75%	–7.81%	–6.98%
U.S. Mortgages	1.62%	–6.83%	–7.12%
Municipal Bond	1.35%	–7.59%	–6.92%

Source: Morningstar Direct, as of May 27, 2022

What to Look Forward To

On Tuesday, the **Conference Board Consumer Confidence** survey for May was released. Consumer confidence declined by less than expected during the month. The index fell from an upwardly revised 108.6 in April to 106.4 in May, against calls for a further drop to 103.6. This result left the index above the recent low of 105.7 recorded in February 2022. Confidence has been challenged since last summer largely due to concerns about inflation and the pandemic. The index hit a post-lockdown high of 128.9 in June 2021. Since then, the declines we’ve seen highlight the negative impact of concerns about inflation and Covid-19 infections over the past year. Looking forward we’ll likely need to see further signs of slower inflation before confidence returns to the highs of last summer. That said, although confidence has been challenged over the past year, consumer spending growth has remained relatively strong. This fact is an encouraging sign that consumers remain willing and able to purchase goods and services, despite rising concerns about the economy.

On Wednesday, the **ISM Manufacturing Index** for May is set to be released. Economists expect the index to fall modestly, from 55.4 in April to 55 in May. This is a diffusion index, where values above 50 indicate growth. Accordingly, this result would signal continued expansion for manufacturers, just at a slightly slower rate. We’ve seen solid improvements for manufacturing output throughout the course of the year, supported by high demand for manufactured goods. That said, a potential slowdown in growth in the months ahead is possible, given the headwinds created by rising prices for goods and labor. Slower growth is still growth, however, so the expected result would indicate continued expansion for manufacturers despite these headwinds.

On Friday, we'll see the release of the May **employment report**. Economists expect to see 329,000 jobs added during the month, down from the 428,000 jobs added in April but still strong on a historical basis. If estimates prove accurate, the May report would mark 17 consecutive months with strong job growth, highlighting the impressive labor market recovery over the past year and a half. The underlying data is also expected to show positive signs. The unemployment rate is set to drop from 3.6 percent in April to 3.5 percent in May. In February 2020, the unemployment rate bottomed out at 3.5 percent, so a return to this historically low level in little more than 2 years would be another example of the labor market's strong improvement over the course of the pandemic. Finally, wage growth is expected to increase 5.2 percent on a year-over-year basis in May, down from 5.5 percent in April. This would be a positive result for the Fed, given concerns about widespread inflationary pressure.

We'll finish the week with Friday's release of the **ISM Services Index** for May. This measure of service sector confidence is expected to drop from 57.1 in April to 56.3 in May. As with the manufacturing survey, this is a diffusion index, where values above 50 indicate expansion. Service sector confidence has dropped this year, after hitting a record high of 68.4 in November 2021. Rising medical risks earlier in the year and persistent inflation have served as headwinds in 2022. That said, due to high consumer and business demand for services, confidence should remain largely in line with pre-pandemic levels in the months ahead. We've seen spending patterns start to shift from goods to services over the past few months. Pent-up demand and diminishing pandemic fears have boosted service sector spending.

Disclosures: *Certain sections of this commentary contain forward-looking statements that are based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. All indices are unmanaged and are not available for direct investment by the public. Past performance is not indicative of future results. The S&P 500 is based on the average performance of the 500 industrial stocks monitored by Standard & Poor's. The Nasdaq Composite Index measures the performance of all issues listed in the Nasdaq Stock Market, except for rights, warrants, units, and convertible debentures. The Dow Jones Industrial Average is computed by summing the prices of the stocks of 30 large companies and then dividing that total by an adjusted value, one which has been adjusted over the years to account for the effects of stock splits on the prices of the 30 companies. Dividends are reinvested to reflect the actual performance of the underlying securities. The MSCI EAFE Index is a float-adjusted market capitalization index designed to measure developed market equity performance, excluding the U.S. and Canada. The MSCI Emerging Markets Index is a market capitalization-weighted index composed of companies representative of the market structure of 26 emerging market countries in Europe, Latin America, and the Pacific Basin. The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index. The Bloomberg US Aggregate Bond Index is an unmanaged market value-weighted performance benchmark for investment-grade fixed-rate debt issues, including government, corporate, asset-backed, and mortgage-backed securities with maturities of at least one year.*

The U.S. Treasury Index is based on the auctions of U.S. Treasury bills, or on the U.S. Treasury's daily yield curve. The Bloomberg US Mortgage Backed Securities (MBS) Index is an unmanaged market value-weighted index of 15- and 30-year fixed-rate securities backed by mortgage pools of the Government National Mortgage Association (GNMA), Federal National Mortgage Association (Fannie Mae), and the Federal Home Loan Mortgage Corporation (FHLMC), and balloon mortgages with fixed-rate coupons. The Bloomberg US Municipal Index includes investment-grade, tax-exempt, and fixed-rate bonds with long-term maturities (greater than 2 years) selected from issues larger than $50 million. One basis point is equal to 1/100th of 1 percent, or 0.01 percent.

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Tom Chester is located at 31 Chestnut St., Camden, Maine 04843 and can be reached at 207-236-4311.

Deb McDonald Earns CIC Designation

Deb McDonald, a member of the business insurance team at Allen Insurance and Financial, has earned the designation of Certified Insurance Counselor, one of the insurance industry's most highly respected designations.

Deb is an account manager, working with businesses across Maine and the U.S.

The Certified Insurance Counselor program is maintained by the National Alliance for Insurance Education & Research. Earning the designation is just a first step on a path of rigorous, annual continuing education.

Be A Savvy Senior: Know the Warning Signs of Elder Fraud

Just browse through the latest true crime documentaries on your preferred streaming network and you'll see that people of all ages and income levels are vulnerable to financial scammers. Unfortunately, as we get older, certain factors put us at greater risk. Social isolation, recent loss of a spouse or close family member, diminished cognitive abilities, and accumulated wealth can make those over age 60 especially attractive to fraudsters.

According to the FBI, there was a 74 percent increase in losses reported by victims over age 60 in 2021 compared with losses reported by the same age group in 2020. To keep yourself and loved ones safe from senior scams, ask yourself these questions before you transfer money.

Is there an urgency attached to the request for funds? Government agencies, well-known companies, and banks don’t typically ask for immediate money transfers. If you find yourself being rushed to provide cash as soon as possible, start with the assumption that the request isn’t legitimate. One way to do this is to call the institution back at a phone number you’ve used before or that you find on its website, not the contact information in the request.

Don’t give out personal information or verify an authentication code to anyone who called you, regardless of who they claim to be or what phone number appears on your screen. Even if the urgent request seems to come from a close friend or family member, you’ll want to call that person to verify their identity and confirm the need for money.

Does the method of payment make it impossible to recover your funds (if necessary)? If you’re asked to send money by mailing cash, gift cards, or prepaid cards, or transferring bitcoin, those are all red flags. Once such funds are sent they can be very difficult, if not impossible, to get back. Another sign of a scam might be a person requesting money and instructing you to pay a third party.

For example, a fraudster may claim to be from the IRS but ask you to mail cash to an individual at a residential address, claiming the person is an attorney for the IRS. A con artist in a romance scam might ask for funds to be sent to someone they claim is a personal assistant or an accountant. Involving a third party makes the transaction harder to trace.

Does this transfer raise any alarms with your financial advisor? If someone contacts you and says you owe them money and the rationale isn't clear to you, contact your financial advisor as a trusted resource to help you determine whether the request is valid.

If you answered "yes" to any of the above questions regarding a request for money, there's a chance you could be the victim of a scam. Depending on your specific situation, consider taking these steps:

- Stop communicating with the requestor immediately.
- If you did send any checks or wire transfers, contact your financial institution and ask if they can stop payment or recall a wire transfer.
- If you sent payment through the mail, contact the carrier service you used to report the fraud and ask if they can stop delivery. (A tracking number is helpful in this type of scenario.)
- Contact your local police.
- Report the incident to ic3.gov (the FBI) or the Federal Trade Commission through their online reporting portals.
- Change your email and online banking passwords.
- Initiate a credit freeze through the major credit bureaus.
- Stay on high alert for subsequent scams. Once a person becomes a victim of fraud, other criminals might target the same individual from a different email address or phone number.
- If you continue to get fraudulent calls and emails,

consider changing your email or phone number.

As we get older and potentially more vulnerable, we hope to be surrounded by people we can trust. But senior scams are unfortunately on the rise. Your best protection against elder fraud is to be aware of warning signs; talk to loyal family, friends, and advisors about financial issues; and thoroughly vet any party requesting funds from you.

This material has been provided for general informational purposes only and does not constitute either tax or legal advice. Although we go to great lengths to make sure our information is accurate and useful, we recommend you consult a tax preparer, professional tax advisor, or lawyer. Third party links are provided to you as a courtesy and are for informational purposes only. We make no representation as to the completeness or accuracy of information provided at these websites.

New: The Navigating Risks and Rewards Podcast

Successes achieved and challenges faced. Hear from entrepreneurs and business leaders in Maine on the new Allen Insurance and Financial Navigating Life’s Risks and Rewards podcast.

With a new episode dropping every three weeks or so, host Patrick Chamberlin brings stories from guests from across the state.

You can listen and learn more at AllenIF.com/podcast

Chris Richmond Earns CIC Designation

Chris Richmond, AAI, CMIP

Chris Richmond, a member of the business insurance team at Allen Insurance and Financial, has earned the designation of Certified Insurance Counselor, one of the insurance industry's most highly respected designations.

"CICs are recognized for expertise and commitment to the industry and it is no surprise this is a designation Chris has chosen to pursue," said Michael Pierce, president of Allen Insurance and Financial. "A CIC designation is a benefit to Chris, to his clients and to everyone at our agency."

Based at Allen's office in Camden, Richmond works with a range of business insurance clients, specializing in marine-related industries.

He also holds the Accredited Advisor in Insurance (AAI) and the Certified Marine Insurance Professional (CMIP) designations.

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