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Democracy Dies in Darkness

Surging gas prices are squeezing the U.S. economy — and the White House

The upward march of fuel costs has emerged as one of the chief domestic political threats to the Biden administration ahead of the midterm elections.

By Jeff Stein
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With the average price of gas nationwide topping $5/gallon early Saturday, surging fuel prices across the United States are creating new strains for millions of consumers and businesses, while compounding intractable political challenges for the Biden administration.

The spike in gas, oil and diesel prices has saddled all kinds of businesses with higher costs that will force them to raise prices on their customers and pull back on new investments. It risks a slowdown in consumer demand, as households cut back on other expenditures to accommodate their new fuel costs. Gas purchases on their own make up only a relatively small portion of most families' budgets, but energy is so crucial to the functioning of the economy more broadly that the price increases bring along higher prices in many other sectors.

The soaring prices show no sign of abating in the immediate future, as global forces continue to prevent disrupted supply from keeping up with strong demand from countries that are rebounding quickly from the pandemic. Western sanctions against Russia over its invasion of Ukraine have wreaked havoc with global energy markets, but the most dramatic measure — the European Union's ban on Russian oil imports — will not even go into effect until the end of this year. Gas prices could also be further pushed up by drivers hitting the road for summer vacations, and the lifting of covid restrictions in some Chinese cities is expected to lead to rebounding fuel demand there, putting further upward pressure on prices internationally.

Energy costs rose by 3.9 percent from April to May, while energy prices overall have spiked by 35 percent since last year, according to a Bureau of Labor Statistics report released Friday. Inflation overall reached 8.6 percent in May, the government reported Friday, the highest rate in 40 years.

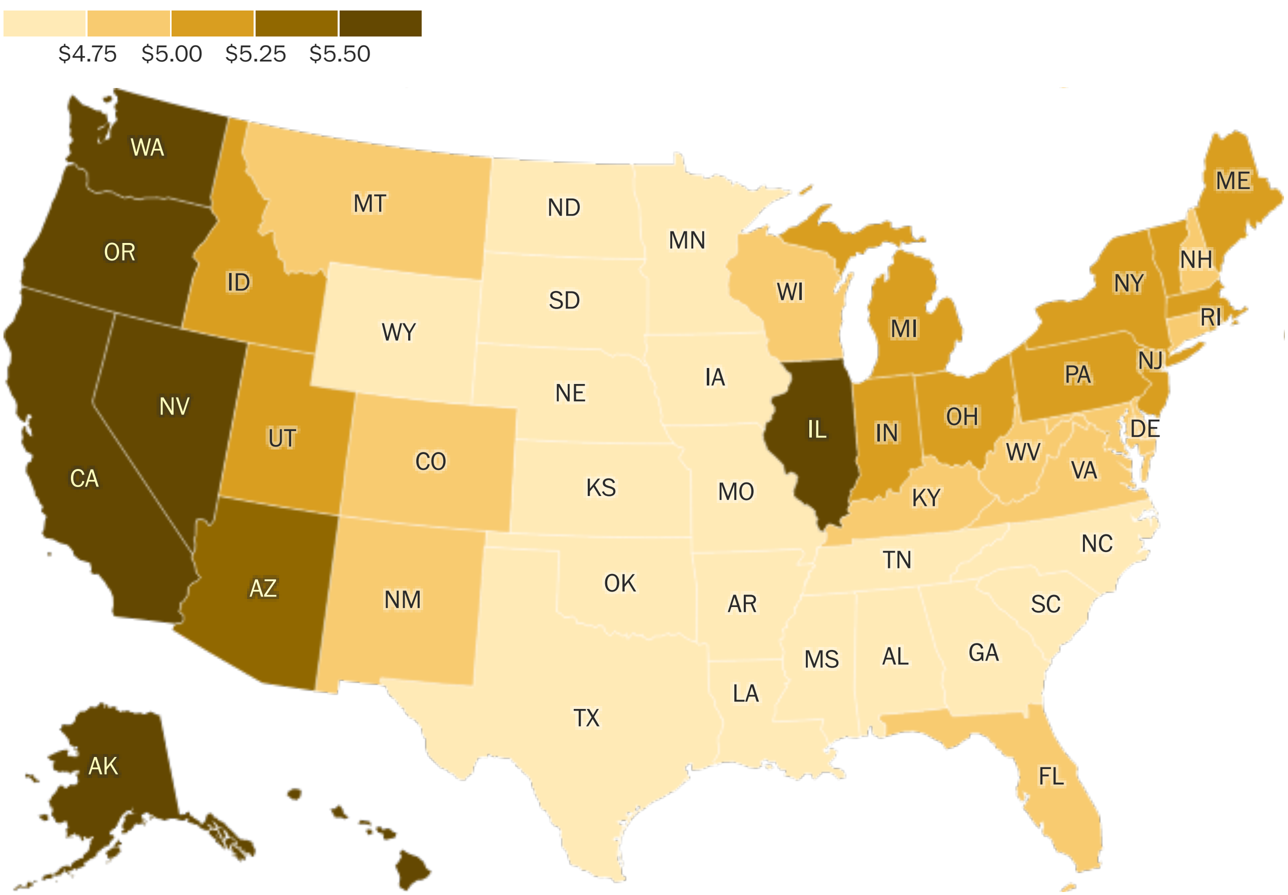
The unrelenting upward march of gas prices has emerged as one of the chief domestic political threats to the Biden administration ahead of this fall's midterm elections, and the White House has few obvious solutions to reverse the trend despite an intensive push by top aides and the president himself. The White House is now caught between liberals allies in Congress who are pushing for escalating a populist attack on oil and gas firms, and the views of some of their trusted economic experts who believe those efforts could prove counterproductive.

A poll released Thursday by The Washington Post and George Mason University's Schar School found that Americans were broadly concerned both with inflation generally and rising gas prices in particular. About 44 percent of drivers said they have only partially filled their car's gas tank as a result of higher prices, with 61 percent of those earning under $50,000 a year doing so. Roughly two-thirds of drivers reported making fewer trips to the grocery store because of rising gas prices.

"This is a huge economic and political albatross around the neck of the administration, and the difficulty is there really isn't an easy way to tackle this using the policy tools available to them," said Eswar Prasad, an economist at Cornell University.

Americans are not accustomed to seeing energy prices as high as they have been over the last several months. The average price for a gallon of gas in the U.S. hit $5.004 on Saturday, according to AAA. Already, at least 19 states have average gas prices of $5 or more, with California above $6 a gallon. Some analysts think America could near a nationwide average of $6 a gallon by the end of the summer. Diesel prices, particularly important to the trucking and construction industries, have jumped nationally from $3.21 last year to $5.74 on Friday, a record, according to GasBuddy, which tracks fuel prices.

Average price for regular unleaded gallon of gas



Data as of June 10

Source: AAA

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These higher energy prices seep into almost every major part of the economy. They drive up the costs for electricity, transportation, shipping, logistics, air travel, agriculture, fertilizer and the production of other commodities. They cut into corporate earnings: Walmart recently pointed to fuel and storage spikes as hurting its profits. Demand for natural gas is soaring globally to make up for Russian energy, and as a result so is demand for U.S. natural gas, creating new financial strains for domestic manufacturers and the nation's power grid — just as more and more Americans start to run their air conditioner this summer.

Higher energy prices are also often a harbinger of an economic downturn, as consumers respond to higher prices by reducing their spending on other goods and services. Historically, oil price spikes like the ones now facing the West have "always" preceded or led to an economic recession, according to a research note by Jeremy Grantham, an analyst at GMO, an investment and asset management firm.

"I'd be on high alert right now to see if the economy succumbs to this latest stab in the heart from higher energy prices," said Chris Rupkey, chief economist at Fwdbonds. "Realistically, it'll be a miracle if we don't go into a recession."

But the post-covid economy has repeatedly defied experts' expectations, and there is ample reason to believe strong growth could survive higher energy prices. Gasoline purchases accounted for roughly 3 percent of consumers' annual spending before the pandemic began, according to the Bureau of Labor Statistics. Unlike the 1970s, America is now a significant producer of global energy supply — meaning high prices benefit U.S. energy producers, rather than simply strain domestic household costs, as firms can increase hiring and spending with their higher revenues. Businesses are also less vulnerable to volatility in gas and oil prices than they once were, due in part to improved efficiency over the last several decades, according to Matthew J. Slaughter, an economist at Dartmouth College.

Economic growth has remained strong in the United States since shortly after early pandemic closures were lifted, and policymakers have hoped demand would cool, as inflation is way up with the fastest increases in consumer prices in roughly four decades. Higher spending on energy could, some economists hope, deplete demand in other sectors, allowing for other price pressures to ease. That might hurt in the short term, but it could help overall.

"It sounds harsh to say, but we need a slowdown in aggregate demand," Slaughter said. "And it's not that large relative to other things in the consumption basket."

But even as higher gas prices help slow the economy and tame inflation, they're also squeezing politicians. And lawmakers and the Biden administration are desperate to reverse the trend. The White House has taken a range of actions aimed at easing the gas price crunch, such as committing to releasing 1 million barrels a day from the nation's Strategic Petroleum Reserve and deploying the Defense Production Act to encourage production of critical minerals. The White House has also permitted a gasoline blend composed in part by ethanol to be sold over the summer despite resistance from environmental groups, which argue the move will worsen air pollution.

The president is also reportedly planning a trip to Saudi Arabia, as the U.S. looks to other parts of the world for increasing oil production to reduce global dependence on Russia, the world's third-largest oil supplier before the war in Ukraine. Biden had once vowed to make Saudi Arabia a "pariah," given its treatment of women and other human rights abuses. But the White House has defended the potential trip, both to help broker diplomatic talks in the Middle East and to increase oil production. The U.S. government has also tried to work with Venezuela and other oil producers on increasing supply since Russia's war began.

White House officials have grown frustrated, though, as their efforts to this point have been confounded by global forces. Earlier this month, a group of oil-producing nations known as OPEC Plus announced that they had committed to a bigger boost in production for this summer — a move quickly praised by the Biden administration. Internally, White House officials hoped the announcement would lead to a drop in oil prices, two people familiar with the matter said. Instead, prices continued to rise.

“They were perplexed that there wasn’t a more durable reaction,” said one person briefed by White House officials, speaking on the condition of anonymity to describe private conversations. “They were like, ‘Man, we can’t catch a break.’ ”

Biden on Friday blamed large oil and gas companies for not doing more to increase production, accusing them of choosing profits over lower prices for Americans. “They’re not drilling. Why aren’t they drilling? Because they make more money not producing more oil,” Biden said. “The price goes up.”

The Post-Schar School poll found 72 percent of Americans blamed corporations for trying to increase profits for rising gas prices, including 86 percent of Democrats, 52 percent of Republicans and 76 percent of independents. The overall figure blaming corporations was higher than the share who blamed Biden or disruptions caused by the pandemic (both 58 percent) and about the same share who blamed Russia’s invasion of Ukraine (69 percent).

Biden has stopped short of embracing some of the actions pushed by Democratic allies in Congress to target oil producers. Sens. Sheldon Whitehouse (D-R.I.) and Elizabeth Warren (D-Mass.) have pushed a tax on the profits of oil and gas firms that would return revenue to consumers, with similar measures already enacted by the United Kingdom, Italy and some other European countries.

“U.S. policymakers should quickly follow suit or risk continued profiteering and pain at the pump,” said Lindsay Owens, executive director of the Groundwork Collaborative, a left-leaning group. The Groundwork Collaborative found that the largest 24 oil and gas companies recorded $174 billion in profits last year — the highest increase in seven years.

The White House has said it is studying that approach, as embracing such a measure could give the administration an effective political response to higher gas prices. But it would lead to a fierce blowback from industry, centrist economists and the GOP. Critics warn that taxing oil and gas companies would discourage them from increasing production, which in the long run could hurt prices.

Bob McNally, an energy analyst at Rapidan Energy Group who served in the George W. Bush administration, said the White House has no options that would immediately improve the gas price crunch. He said it is critical that Biden avoid embracing solutions such as price caps and an oil profits tax that he said would make the problem worse.

“The White House has two options: They can do symbolic things that don’t really lower prices, and they can do really dumb things that are counterproductive,” McNally said. “Despite my many reservations about the president’s energy policies, it is nonetheless impressive that he has so far resisted reaching into the dumb basket.”