A Tale of Three Charts

“Come listen to a story about a man named Jed
A poor mountaineer, barely kept his family fed,
Then one day he was shootin’ at some food,
And up from the ground came a bubblin’ crude.
Oil that is, black gold, Texas tea.”

This tune is from one of the classics of all time . . . the Beverly Hillbillies. The one thing that remains true about this story is the fact that oil has always been and will always one of the most important commodities in the world. That will never change . . . however, it doesn’t mean this commodity won’t have its ups and downs. Below are three charts that illustrate the impact of oil on the market and the ups and downs.

Chart 1: The price of Light Sweet Crude

The price of oil has fallen nearly 40% from it’s June 2014 high of $104 per barrel. As it stands today the price per barrel is $67.50.

Chart 2: Energy Stocks (XLE Energy ETF)

As the price of oil falls, the price of oil companies also fall. The impact can be significant in the short to intermediate term. These oil companies rely on high oil prices to increase margins. As the price per oil falls ,the margins of oil companies also fall resulting in a sell off in energy related stocks. The XLE ETF highlighted above is an example of this. This ETFs largest holdings are Exxon Mobil, Chevron, Schlumberger, and ConocoPhillips. The XLE is currently the worst performing sector of 2014, down 9% as I type this.

Another way to look at is that the break even price for many of the drillers is right around $65 – $70 per barrel. The farther the price of oil falls, the bigger impact on these companies bottom line. With a break even price of $65, and oil trading right around $65, there is no benefit for companies to keep producing. When companies stop producing we will see a decrease in supply which will push the price of oil higher . . . this is the situation they (the oil companies) currently find themselves. Time will tell what they do.

Chart 3: The Average Price of Gasoline in America

The positive impact of falling oil prices means falling gasoline prices. The average price of gasoline is $2.75, this is the lowest that we have seen since 2010. This good news puts more money in the hands of consumers to do one of two things . . . either save it, perhaps use the money to contribute to an IRA or to spend it. (My hope is that consumers save the extra dough but I'm also realistic as well!) My guess is that consumers will spend the extra money they are saving for Christmas presents or for other things that they may not need.

If you position yourself right you could be both a saver and take advantage (of those that do not save) by being invested in the right areas of the market.

Happy investing!