CHAPTER TEN

Oil

Gas Prices

Derivatives

Peak Oil

Gas Prices

The cost of energy impacts all areas of economic life, making it critical to understand how oil prices work.

Five (5) main components to the price of fuel:

- Cost of crude oil (mainly responsible for the swinging price)
- Cost of refinement plus related profits
- Cost of distribution and marketing plus related profits
- Cost of storage
- Taxes

Gas Prices

Supply and demand impacts gas prices.

- **Price elasticity of demand**
  The variation in demand for a good service as a result of a change in price of that same good or service
- **Price elasticity of supply**
  A measure of the responsiveness of the quantity of a good or service supplied as a result of a change in the price of that same good or service

Supply and demand curves for oil are relatively inelastic.

Figure 10.3: Elasticity of Demand

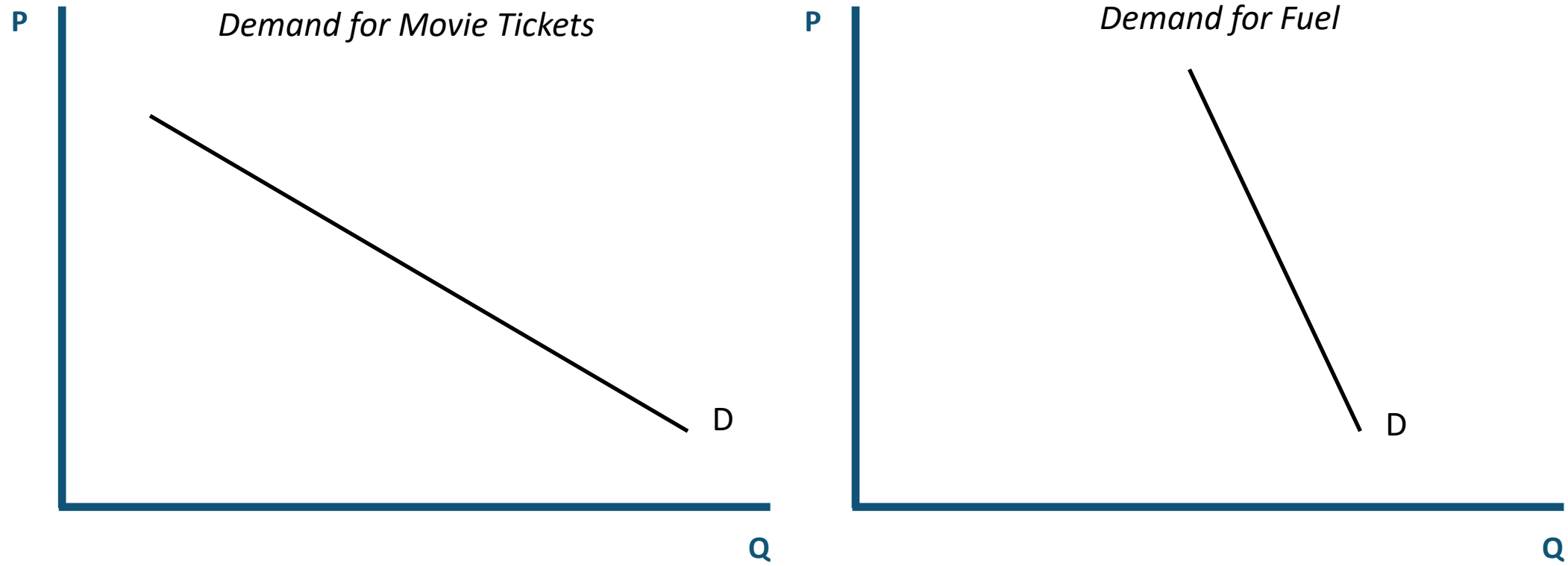
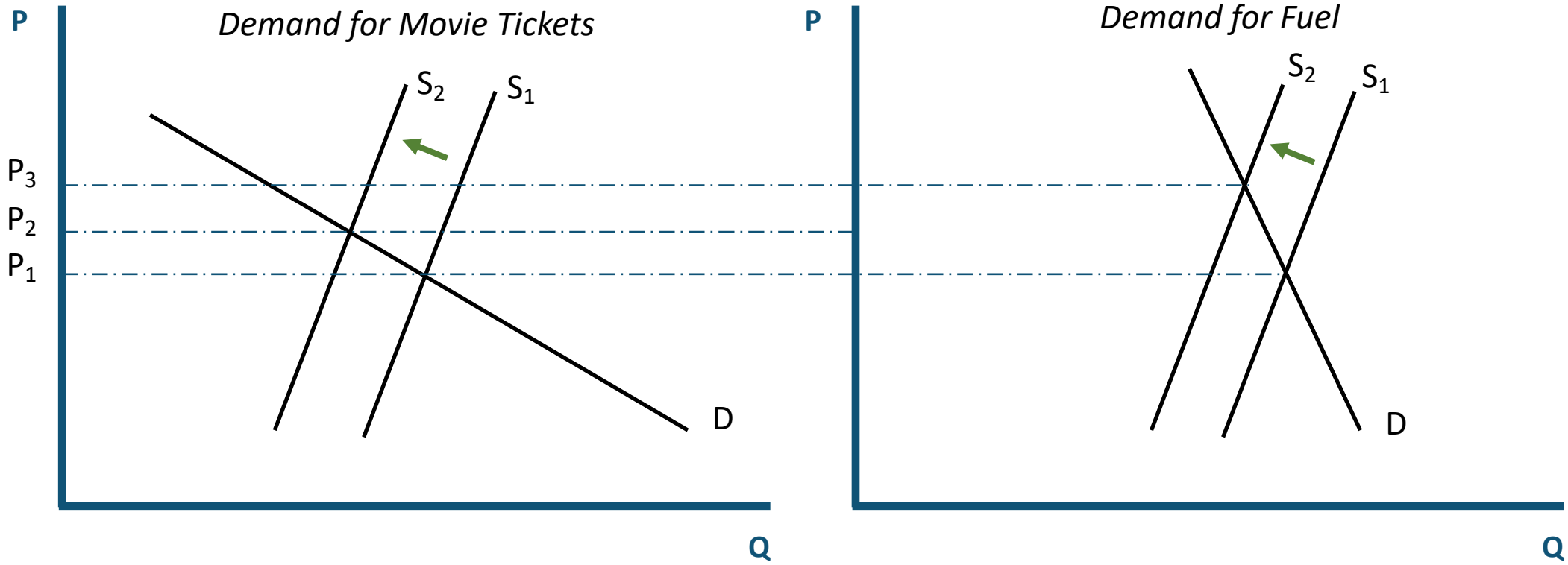


Figure 10.4: Elasticity of Demand and a Change in Supply



Comparing inelastic with elastic demand, we see a similar supply shift causes a larger price change when demand is inelastic.

Derivatives

Derivatives
A financial security whose return is derived from another asset.

Futures contract
A type of derivative where a buyer and a seller agree to trade at a predetermined future date at a predetermined future price.

Peak Oil

Peak Oil
The point at which an oil well or oil field reaches its maximum rate of production.

Oil is a non-renewable resource.