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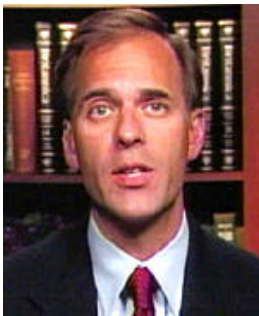
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TRANSCRIPT
Analysis

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Stock Market High, Dropping Gas Prices Signal Possible Economic Boom

Dropping gas prices and a peaking stock market have created hopes for an economic turnaround, yet housing sales continue to fall. Financial experts decode the mixed economic signals.



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GWEN IFILL: And finally tonight, our economic update.

In recent weeks, gas prices have dropped like a stone. The stock market is approaching a record, yet sales of existing homes are sinking. What to make of this mix of good and bad economic news?

Here to help us out, Mark Zandi, chief economist at MoodysEconomy.com; and John Kilduff, senior vice president for energy risk management at Fimat USA, a global financial services company.

John Kilduff, gas prices have dropped by 50 cents in the last month. Why?

JOHN KILDUFF, Fimat USA: We got through the summer in a big way. The fears over Iran, the fears over the hurricane season, and the fears over the government's implementation of ethanol as an additive for clean air rules throughout the country all passed without our worst fears being realized. As a result, the market, the marketplace has basically exhaled and said, "We have enough supply. Prices, come down."

GWEN IFILL: If you had to balance the domestic concerns, which you talked about, weather and other concerns, against the geopolitical concerns, about what was going to happen with the oil supply in the Middle East, for instance -- Venezuela, other places -- what would you say had the greater impact?

JOHN KILDUFF: Well, certainly, the strong U.S. consumer demand for gasoline that was unrelenting, despite the \$3 price mark, fed into the whole situation. But I think the greatest fears, the culmination of the \$80 crude oil or the \$78 crude oil, was the Hezbollah situation with Iran as a central player, not only as a backer of the Hezbollah, but also over their nuclear ambitions.

We had President Bush saying that the matter over Iran's nuclear ambitions would be resolved in a matter of weeks, not months, so it looked as though a showdown was imminent. And when it comes to oil and gasoline prices, when you're talking about Iran, the stakes are just huge, and that's why traders run for cover, and buy up, and push up the price.

The stock market

GWEN IFILL: So, Mark Zandi, let's talk about the stock market for a moment. We saw the market was flirting again today with new records, didn't quite get there. It was dampened somewhat. But what has been driving it so high when there are all these other indicators which would seem to be counter-indications?

MARK ZANDI, MoodysEconomy.com: Well, the lower oil prices certainly helped. There's nothing better for the economy than lowered fuel costs. It boosts growth, and it takes the edge off inflation. Corporate earnings were strong.

And the most fundamental reason for optimism in the economy is that businesses, with a few exceptions, are doing very, very well financially. So all of those things -- and, obviously, lower rates have helped, too, and the Federal Reserve is putting monetary policy and the tightening cycle on hold. So all those things together have clearly come together and helped investors get into the market in a bigger way.

GWEN IFILL: It was only a few years ago when we saw the last big record broken. We did the same, following breathlessly, day by day, waiting to see what was going to happen. What's different this time? Or is anything different this time?

MARK ZANDI: Well, I think equity prices, stock prices are more consistent with the economy today. Back around the turn of the decade, there was a lot of froth in the stock market, a lot of speculators, particularly in technology stocks.

So stock prices, I think, got ahead of the economy. Stock prices today are a clear reflection of the economy. They're much more consistent with what actually is happening. So the records today are real; they're not fake.

Oil prices

GWEN IFILL: John Kilduff, how do we begin to square the good news about oil prices -- certainly, when I fill up, I think it's good news -- against all the other indicators, when we pick up headlines and hear about layoffs, and weakness in manufacturing, in automaking, and all of these other industries, airlines? How do we square those two things?

JOHN KILDUFF: Well, unfortunately, as I like to sort of twist the analogy, there's a gray lining to this silver cloud of low oil prices. They are coming down in part -- and maybe to a very large degree -- as a result of the slowing economic environment.

Mark will have a better opinion as to whether or not the U.S. is looking at a recession next year or not. But certainly a big part of what's pulled the rug out from under oil prices and gasoline prices is the backdrop of robust economic demand and growth, which translates into even greater amounts of energy usage that producers are having a hard time keeping up with right now, coming out of the equation and helping to push prices lower.

GWEN IFILL: More of a supply...

JOHN KILDUFF: And they've done their damage. They've done their damage, obviously, energy prices have.

GWEN IFILL: More of a supply question, you believe?

JOHN KILDUFF: It is definitely not a supply question right now. I mean, that's been bedeviling, I think, to anyone who's looked at this whole picture, because, back in June, crude oil inventories in storage in the U.S. hit multi-year high, and then we had almost \$80 crude oil. It's not about that.

What's being priced into this market is growing demand and fears about the continuity of supply, whether oil will get knocked offline in countries like Iran, Iraq, Saudi Arabia, even Venezuela, for that matter. So we're pricing in the fact that we might not have it coming online next month or the months ahead, not what we have on hand today.

Housing market

GWEN IFILL: Now, Mark Zandi, let's talk about the potential for other drags on the economy in the future, because even though today we saw good numbers, positive numbers on new home sales, we've seen consistently poor numbers on existing home sales, and mortgage applications, and other things, which show that there's a fundamental slowdown. How much of a concern is that?

MARK ZANDI: Well, it is the most significant concern to the economy. The housing downturn is quite severe. The market peaked a year ago. We've seen sales off 15 percent. Unsold inventories are up 50 percent. And now, for the first time since the early 1990s, house prices are falling nationally.

So all of this is a very significant drag on the economy, and that's why growth is slowing and will continue to slow. At this point, I don't think it's enough to send the economy into recession. We're not seeing the ill effects of the housing problems bleed out into the rest of the economy, but, clearly, it is a reason to suspect that growth will be measurably slower in the coming year, compared to the past couple, three years.

GWEN IFILL: And what do you say to John Kilduff about recession?

JOHN KILDUFF: No. I think the odds -- they're obviously up from where they were a year ago, but they're still very low. I put them close to one in four, which is not insignificant. It's measurable, but still low in the broad historical scheme of things.

GWEN IFILL: Well, as long as we're looking to the future, John Kilduff, let's ask again about what happens with these gas prices and these oil prices. We're about to enter the winter heating season. Everyone's keeping an eye on the cost of oil and the cost of gasoline. What do you see happening?

JOHN KILDUFF: They're going to continue to lower. The price at the pump is going to continue to fall. We could see the national average actually get down around \$2 a gallon, maybe even dip below it, just in time for the holiday season, which should help bail out the retailers and, I think, help out the overall economy, maybe even prevent what was partly -- if a recession was on the horizon, was a high-energy-price-driven one.

We're also seeing, it appears, alternative investors who have put money in commodities, like hedge funds and pensions and endowments, cycle out, basically move their money out of commodities into the equity markets and allowing prices to fall, as well.

Effects of falling prices

GWEN IFILL: Well, let me ask Mark Zandi about that, because, in fact, if one effect -- that is to say, these declining house prices and the declining gas prices -- are there other effects that are just under the surface that we're not necessarily seeing, when we look at that price drop at the pump?

MARK ZANDI: Well, one of the things to note is that the benefit of lower oil prices, gasoline prices, goes mostly to lower- and middle-income households. They devote a much larger share of their budget to energy and, of course, have fewer financial resources.

So when energy prices, gasoline prices are up, they really have to make some hard choices. Now that they're down, that really does help, particularly as we make our way into the Christmas buying season. So one of the more positive dimensions of this decline in oil and gasoline prices and home heating prices is that it really benefits the people who need that help the most.

GWEN IFILL: But what does the continued weakness in the housing market do to buyers who are trying to get into the market or are trying to sell?

MARK ZANDI: Well, yes, the housing market is the economy's weak link. It will remain the economy's most significant problem and threat, and so that can't be discounted. That clearly is the thing that we need to worry about the most at this point.

GWEN IFILL: You just can't help but stay worried. Mark Zandi, John Kilduff, thank you both very much.

MARK ZANDI: Thank you.

JOHN KILDUFF: Thank you. Good evening.

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