Tired of Record High Oil Prices? They're Anything But!

By Vaclav Smil

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TCS

You've heard it and read it for weeks as yet another TV announcer, another expert talking head, another pontificating columnist tell us about "record high" oil prices. The ubiquity and persistence of this pathetic phenomenon shows to what levels of basic innumeracy has the news-making and commentatory elite of the country sank. One would expect that they are educated enough to know that there is such a process as inflation, they are surely old enough to remember that during the 1960s imported Volkswagens cost less than $1,000, and on the Web they could find in less than 10 seconds that in 1900 an excellent three-course dinner (without wine) could be had for much less than $1.00. Yet still they blabber -- and so here is the briefest kindergarten primer on record oil prices.

The years of the highest oil prices were 1980 and 1981 (thanks to Ayatollah Khomeini and fall of the Pahlavi dynasty in Iran) when the Arabian Light/Dubai crude traded at nearly $36/bbl and when the West Texas Intermediate went for almost $38. In 2004 monies this is, rounded for easy memorization, between $ 70-75. The peak of the last few days -- $ 55/bbl -- is obviously well above what will be the annual mean for the year 2004 and it is no more than 73-78% of the record averages. But this is a wholly inadequate adjustment. Between 1980 and 2003 the amount of oil that the US economy used to generate an average dollar of its GDP fell by 43% as its oil intensity declined somewhat faster than the overall relative energy use.

And so in order to get an approximate but realistic comparison of how much today's prices impact an average manufacturer or average household purchases we should multiply the current high price of $55/bbl by 0.57 to get an effective comparable price of around $30, or no more than 40% of the average record price we paid in 1980. Moreover, between 1980 and 2003 average hourly earnings in services, where most new jobs were created, rose by about 30% and so another adjustment taking into account this higher earning power reduces the comparable price to just over $20. Other, more sophisticated adjustments, are possible but this one is easy to execute and easy to remember: the effective -- that is inflation-, oil/$GDP- and earning power-adjusted -- cost of oil at $(2004)53-55 is no more than about 30% of the average record price we paid in 1980 and 1981. That is why recent "record" oil prices have not had any substantial effect on the way this

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continent uses, and wastes, the most convenient of all fossil fuels.

Vaclav Smil's latest book is Energy at the Crossroads (The MIT Press 2003).