360 Insights

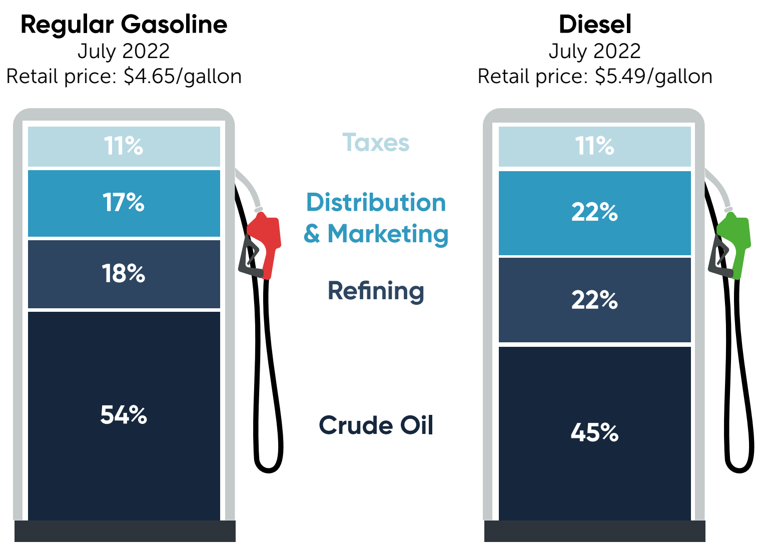
What's In Store For Prices At The Pump - And Winter Heating Bills

By Daniel Campbell, CFA

As we move toward colder months, we're starting to see more concern around the future of energy prices at home and abroad. The U.S. Energy Information Administration (EIA) expects the price of a barrel of oil to remain close to $100 by year end—up from around $40 in 2020 and $70 in 2021.[1] However, citing the invasion of Ukraine, the effect of sanctions against Russia and production decisions of OPEC+, the EIA notes that the price of oil could be anywhere between $55 and $150 by December. And because the price of oil is what primarily determines the price we pay at the pump, consumers planning Thanksgiving road trips may find it difficult to anticipate their travel budgets.

Both the U.S. and Europe are also facing uncertainty around natural gas prices. The situation is more dire in Europe, which is heavily dependent on Russia for gas and has been grappling with soaring prices for most of the year. There are fears that the European Union won't have enough supply to meet demand this winter, which has led to an agreement to reduce gas consumption to prevent rationing.[2] Because the U.S. exports more natural gas than it imports, with plenty of reserves to make it through winter, it's doubtful we'll see constraints on usage, but that doesn't mean we won't see higher heating bills: the EIA expects the price of natural gas to be $7.68 per million British thermal units (Btu), more than twice the rate last December at $3.76.[3]

It's key to remember that these expectations are baked into current prices. Future price movements of energy (or anything that is produced using oil or natural gas) will depend on how supply and demand change. For example, weaker demand relative to expected U.S. production or a milder winter could lead to lower prices. Financial science teaches us that the more uncertainty, the more we should expect large price swings. We call this volatility, and with so many external factors driving both supply and demand, energy prices will likely dominate the headlines as we move into winter.



Source: U.S. Energy Information Administration, Gasoline and Diesel Fuel Update.

Price Summary	2020	2021	2022*	2023*
WTI Crude Oil[a] (dollars per barrel)	39.17	68.21	98.71	89.13
Brent Crude Oil[a] (dollars per barrel)	41.69	70.89	104.78	95.13
Gasoline[b] (dollars per gallon)	2.18	3.02	4.07	3.59
Diesel[c] (dollars per gallon)	2.56	3.29	4.81	4.14
Heating Oil[d] (dollars per gallon)	2.44	3.00	4.52	3.98
WTI Crude Oil[d] (dollars per thousand cubic feel)	10.76	12.27	14.58	14.95
Electricity[d] (cents per kilowatthour)	13.16	13.72	14.56	14.93

a West Texas Intermediate.
b Average regular pump price.
c On-highway retail.
d U.S. Residential average.

*2022 and 2023 prices are forecasts.
Source: U.S. Energy Information Administration's Short-Term Energy Outlook, released Aug. 9, 2022.

1 Based on the West Texas Intermediate (WTI) crude oil price. Source: EIA. August Short-Term Energy Outlook. https://www.eia.gov/outlooks/steo/

2 WSJ: https://www.wsj.com/articles/europe-braces-for-russia-gas-disruption-this-weekand-years-of-higher-energy-prices-ahead-11661858795 and Economist: https://www.economist.com/finance-and-economics/2022/08/25/how-to-avoid-energy-rationing

3 Based on the Henry Hub Natural gas price and futures contracts. Source: EIA. August Short-Term Energy Outlook. https://www.eia.gov/outlooks/steo/

How Big Will The Social Security Cost of Living Adjustment Be For 2023?

By Jonathan Scheid, CFA, AIF®

Inflation has been the buzz word since the early stages of the COVID-19 pandemic. We all have experienced the frustration of rising prices whether from higher grocery bills, gas prices or virtually anything we want to purchase.

To help combat rising prices, workers typically receive increases in their paychecks. Of course, every company handles raises differently, and they may not offer them at all. For those not working and receiving Social Security checks, the Social Security Administration annually reviews the rate of inflation and adjusts the amount paid to beneficiaries.

Because the administration calculates the cost-of-living adjustment (COLA) based on inflation, we believe this year retirees could see their monthly benefits increase by an estimated 8%-10%—the largest percentage increase since the early 1980s.

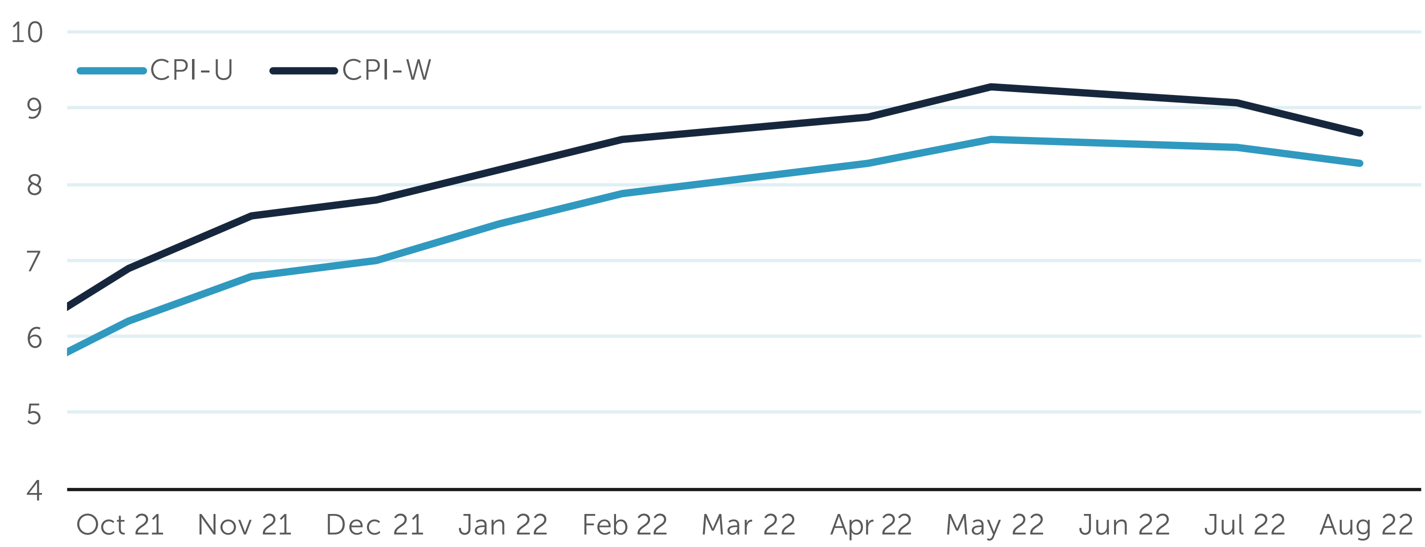
How is COLA calculated?

In mid-October of every year, the Social Security Administration reviews how much prices have changed from the year before, and it uses the information to change the COLA used to calculate the next year's Social Security benefits. If there is no increase, there is no change in COLA.

When the administration calculates the adjustment, it doesn't use the widely reported Consumer Price Index for All Urban Consumers (CPI-U, generally just referred to as CPI) or the Federal Reserve's preferred measure of inflation, Personal Consumption Expenditures (PCE) Index. Instead, it uses the Consumer Price Index for All Urban Wage Earners and Clerical Workers (CPI-W). It's an interesting choice since it doesn't reflect the inflation experienced by the retired individuals receiving Social Security, but rather the inflation experienced by a subset of active workers still contributing to Social Security.

We won't get into all the technical differences between the inflation measures, but the good thing is that CPI-U and CPI-W are typically not too far off. Consider last year's COLA of 5.9%. It was similar to the CPI-U's increase of 5.4% for the same time period, according to the Bureau of Labor Statistics.

Year-Over-Year Percent Change In CPI-U And CPI-W Since October 2021



CPI-U is Consumer Price Index for All Urban Consumers. CPI-W is Consumer Price Index for Urban Wage Earners and Clerical Workers. Source: Bureau of Labor Statistics.

To get an idea of what the annual increase to Social Security is going to be, we can look at recent reports of CPI-W. While the Social Security Administration uses the full third-quarter inflation for year-over-year comparisons, we'll use a recent month. In the August 2022 report, CPI-W posted an 8.7% year-over-year increase in prices. A good portion of that increase occurred this year, so it is possible that the Social Security increase will be close to that level, but it could be higher or lower.

If the administration based the adjustment on August's annual increase in prices, the current average monthly Social Security retirement benefit of $1,625 would increase to $1,766 starting in January of next year. That would lead to an average total of $21,192 paid to each beneficiary in 2023 compared with $19,500 in 2022—an extra $1,692 for the full calendar year.

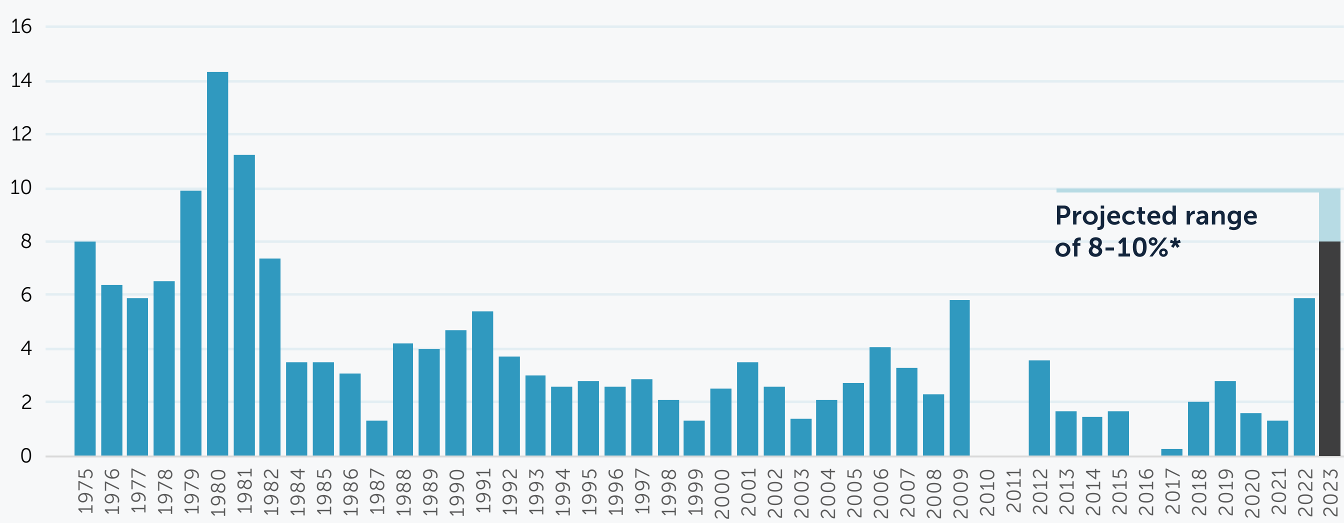
Is it enough?

Given how quickly prices have increased, many people wonder if it will be enough to offset the higher prices we currently face. The inflation that everyone experiences is different. For some, an increase like we estimate above could be ample; for others it won't suffice. This is where having a meaningful conversation with your financial advisor can be helpful. Your advisor can evaluate your personal situation and help you ensure you are on the right track or suggest course corrections to get you back in the right direction.

If you haven't started receiving your Social Security retirement benefit yet, your advisor can also help you estimate your monthly payments and determine when the optimal time is to start receiving your benefits. Inflation adjustments benefit individuals that haven't filed yet by increasing the starting benefit amount. In addition to inflation, the administration calculates your payments based on other factors, such as your earnings during your career, the age you started receiving benefits and your birth year.

Given the trends in inflation, it's clear that Social Security benefits are going up next year to help retirees with higher prices. The Fed has also indicated it will continue to raise interest rates to bring down inflation. If inflation cools in the new year, we likely won't be talking about the historically big increase in COLA next year. Instead, we may be talking about how it returned to the low levels of the last decade.

Social Security Cost of Living Adjustments Since 1975



*Our estimate based on recent CPI-W results. The actual 2022 COLA adjustment may fall outside this range. Source: Social Security Administration.

Your Portfolio And Midterm Elections: Key Questions Answered

By Daniel Campbell, CFA

What are the main issues that could affect your investment portfolio?

You can expect plenty of discussions around Joe Biden's handling of the pandemic, the response to Russia's invasion of Ukraine and our current economic landscape. With the Federal Reserve reiterating its intent for further interest-rate hikes to quell historically high inflation, voters will likely be tuned into how each party plans to handle the precarious position of our economy.

Is there any pattern between a change in the control of Congress and future returns in the market?

On average, we've seen positive returns for U.S. stocks during years when Republicans controlled Congress, when Democrats controlled Congress and when Congress was split. Over the last 90 years, elections that led to a change in power in either the House or Senate have been followed by a positive year in the stock market each time. Although headwinds to the growth of U.S. stocks will likely continue over the next few years (like high valuations, rising cost of debt and tighter budgets for consumers), the impact of a change in control of Congress isn't high on that list.

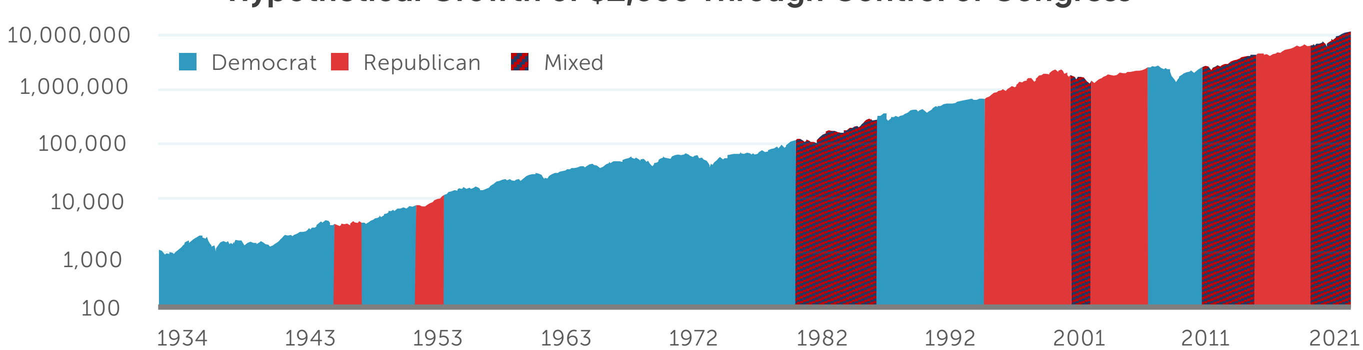
Should you reposition your portfolio to take advantage of the changing agenda in Washington?

An applicable saying is that there's nothing new in investing, just investment history we don't yet know. Before making any changes to your portfolio, consider that history teaches us to expect the president's party to lose seats during midterm elections. So, we can reasonably assume this expectation is baked into stock prices, and we shouldn't bank on huge swings if Democrats lose seats in Congress.

So, what should you do with your portfolio?

Stick to your plan. Everyone wants to see their portfolio grow, but most investors fail not during times of growth, but by panic selling when their portfolio starts to decline. If you are concerned about the volatility in stocks or the higher cost of living, speak with your advisor about investment strategies that can help mitigate these risks. Your portfolio may already be positioned to address them. But evidence shows that trying to guess what the stock market will do before and after elections is not an optimal strategy.

Hypothetical Growth of $1,000 Through Control of Congress



U.S. Market is a value weighted return of all CRSP firms incorporated in the U.S. and listed on the NYSE, AMEX, or NASDAQ. Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio nor do indices represent results of actual trading. Information from sources deemed reliable, but its accuracy cannot be guaranteed. Performance is historical and does not guarantee future results. Total return includes reinvestment of dividends and capital gains. Source: Ken French Data Library, house.gov and senate.gov.