Collapse in oil prices: producers howl, consumers cheer, economists fret

The price of oil has fallen by nearly half in just six months, a surprising and steep plunge that has consumers cheering, producers howling and economists wringing their hands over whether this is a good or bad thing. In December 2014, the price of a barrel of oil is just under $56, down from a summer high of $107, and lower than at any time since 2009.

A global imbalance of supply and demand is rippling across the world economy. Years of high oil prices, interrupted briefly by the recession, inspired drillers around the world to scour the earth's crust for more oil.

The World of oil is divided into 2 groups: the countries that are part of Opec, like Saudi Arabia, and those that aren't, like Russia. Opec is a cartel whose members can fix oil prices. As the non-Opec countries produce more oil, however, Opec's power over oil prices is dwindling. Since 2008 oil companies in the US have increased production by 70%. That increase alone is more than the production of any Opec member other than Saudi Arabia.

Opec estimated that the world would need 28.9m barrels of its oil per day next year, the lowest in more than a decade. And Opec countries plan to produce 30m barrels of oil per day next year. That supply surplus is sending global prices lower.

Global demand is still expected to grow next year, but by far less than many thought earlier. The economies of China, Japan and western Europe - the top oil consumers after the US - all appear to be weakening. Oil demand falls when economic growth stalls.

The US is still the world's largest consumer, but more fuel-efficient cars and changing demographics mean demand for oil is not increasing. The Energy Department predicts a slight decrease in gasoline demand next year even though the price is expected to be lower and the economy is expected to grow.

For drivers, shippers, airlines and other consumers of fuel, there's nothing not to like about the drop in oil prices. The national average gasoline price has fallen to $2.55 a gallon, its lowest level since 2009, saving US households dozens of dollars each month.

Diesel and jet fuel prices have also plunged, helping boost the profits of airlines and shippers. Heating oil is the cheapest it has been in four years, reducing home heating prices for many in the chilly north-east. Falling fuel prices act like a tax cut and help boost consumer spending, which accounts for 70% of the US economy. But economists are concerned that there are other, more troublesome forces at play.

The depth of oil's plunge could be a signal that the global economy is struggling even more than economists think. A weak global economy could hurt the US economy by reducing exports, employment and spending, which together could outweigh the economic benefits of cheaper fuel.

For oil companies, oil-producing states and oil-exporting countries, the oil price collapse is painful. Oil companies generally keep producing oil from wells they've already drilled, but lower prices reduce revenue and force them to cut back spending on new exploration projects. BP announced last week it would try to trim $1 bn in spending next year in a move that could result in job cuts. States that rely on taxes from energy production such as Alaska, North Dakota, Oklahoma and Texas will see lower revenues and some have already had to trim budgets. Major oil exporters such as Iran, Iraq, Russia and Venezuela rely heavily on revenues from state-owned oil companies to run their governments and are struggling under major budget shortfalls.

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