

Do Not Give Gasoline All The Credit

Appearances Aside, There Is More To Stock Rally Than Rising Gasoline Prices

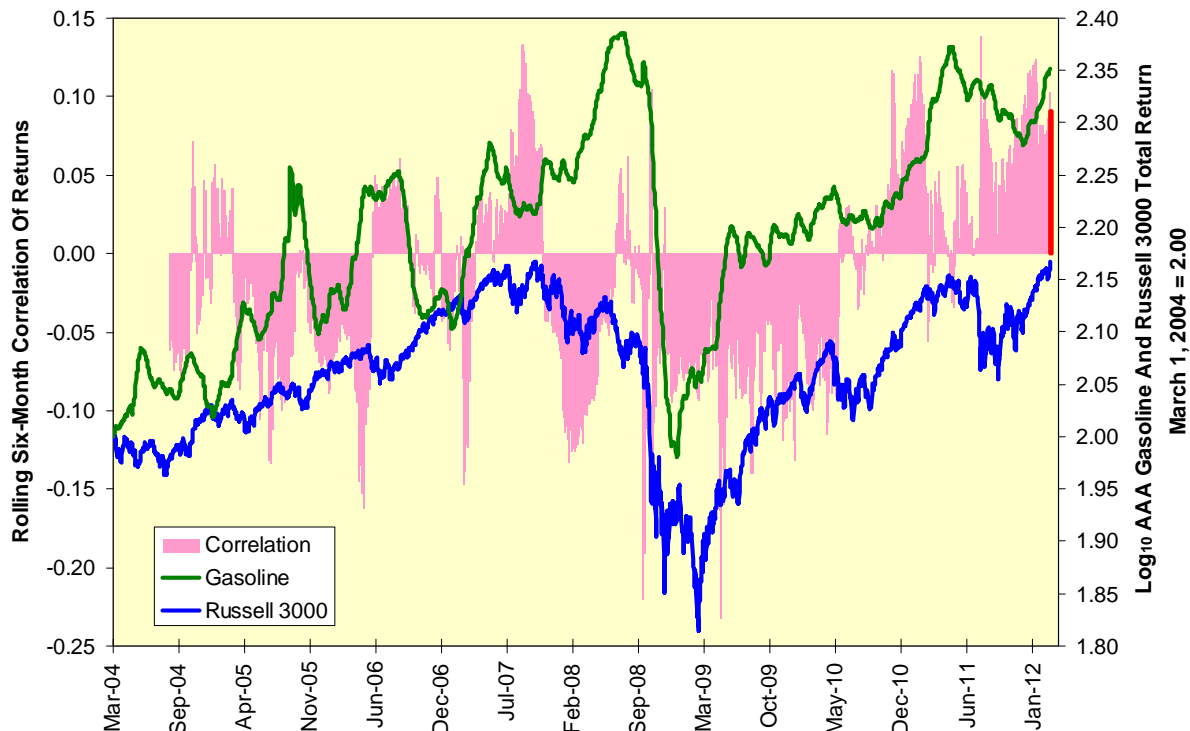
First, a 72-point disclaimer: Yes, this is a satirical piece. I used to write an annual tongue-in-cheek article on the oats-notes spread as a spoof on technical analysis and, much to my amazement, I had some readers take it so seriously they wanted to know if they could use the oats-notes spread to day-trade S&P 500 index futures. But the data and statistical analyses in both cases were and are real.

Second, I learned a long time ago the public's tolerance for higher gasoline prices was near zero; I was the man behind the one-way mirror at oil industry focus groups in the late 1970s and saw respondents' body language. To turn a *Godfather* aphorism around, this is not business; it is personal.

Dual Rallies

When asked about the effects of retail gasoline prices on the stock market, here measured by the total return on the Russell 3000 index (IWM), I shrug and reply they are both going up. While it may appear from the chart below that gasoline prices have led stocks coming out of the March 2009 low, do not let your eyes deceive you: I did a lead/lag analysis and found the mode of correlation occurs at lag zero. This was my first clue the stock market's rally has been more than the stepchild of the gasoline price surge.

Gasoline And U.S. Equity Returns



Second, let's take a look at the rolling six-month correlation of returns between gasoline and stocks. Sometimes it is negative, as it was during the financial crisis and its aftermath; sometimes it is positive, as it has been continuously since late July 2011. Regardless, its level is minor; it is statistically insignificant with an r^2 of .0002 (piffle) and hardly exhibits the properties of stationarity we should seek in defining a causal relationship.

Finally, and speaking of causation, I ran a Granger Causation analysis, last seen lurking around these parts in October 2011's [Why Corporate Bonds Do Not Lead Stocks](#), and found gasoline prices did not – I repeat, did not – Granger-Cause higher stock prices. Just because you want this to be so does not make it so.

Return From Frivolity

Please remember that I was being sarcastic, I played the data and analysis straight-up here. What we should be able to take away from this is gasoline's impact on one financial market, U.S. stocks, is not the negative one supposed

commonly. Yes, money spent at the pump is money not spent elsewhere, but we can say that about money spent at the grocery store, at the hardware store or any other retail outlet. I would gladly surrender control of my entire gasoline and household utilities costs to whomever in return for control of my tax liabilities; one dwarfs the other and never seems to go down. I just completed my Illinois state income taxes and found I was paying 66.7% more and receiving nothing more in return. At least gasoline can fly the Mission Accomplished banner when I put it in my car.