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Gas May Finally Cost Too Much

Highway traffic is falling as pump prices climb. Are Americans rethinking their auto addiction?

by Christopher Palmeri

For 20 years now, county workers in Palm Beach County, Fla., have been counting cars with sensors at strategic points along its 4,000 miles of roads. Nearly every year traffic volume has climbed at least 2%. But in 2007 there was a slight decline in the number of vehicles on the roads. This year traffic is down 7.5% through March. "We're seeing a very significant change," says county engineer George Webb. "We're having a good time speculating why."

It's not just Palm Beach. Traffic levels are trending downward nationwide. Preliminary figures from the Federal Highway Administration show it falling 1.4% last year. Now, with nationwide gasoline prices having passed the inflation-adjusted record of $3.40 a gallon set back in 1981, the U.S. Energy Information Administration is predicting that gasoline consumption will actually fall 0.3% this year. That would be the first annual decline since 1991. Others believe the falloff in consumption is steeper than the government's numbers show. "Our canaries out there tell us they are seeing demand drop much more considerably than the fraction the EIA is talking about," says Tom Kloza, chief oil analyst at Oil Price Information Service, a Gaithersburg (Md.) market research firm.

Is oil-guzzling America changing its ways? Some think so, though it's worth noting the U.S. still consumes one-third of the world's annual gasoline output. "It appears we've finally hit the ceiling that's causing the U.S. population to rethink how and where they use their vehicles," says Paul Weissgarber, who heads the energy practice at consulting firm A.T. Kearney.

Just look at the latest auto sales figures. Sales fell 8% overall during the first quarter of 2008, and those of gas-hungry SUVs and pickup trucks dropped off a cliff, down 27% and 14%, respectively. High gas prices are forcing even SUV lovers to shift gears. Fed up with spending $100 five times a month to fill up his Chevy Suburban, Ron Gesquere, an auto parts executive from suburban Detroit, recently bid $10,000 on eBay (EBAY) for a used Mini Cooper S. "I could make the payments on the Mini with the savings in gas," he says.

For years analysts have been surprised that gasoline consumption continued to rise even as prices kept climbing. Now that consumption has finally slowed, it remains to be seen if Americans are driving less just because the economy is doing poorly or if they are altering their behavior in a lasting way. Certainly consumers seem to be at a psychological turning point. Fuel prices are rising faster than incomes and show no sign of slowing down. Being green is trendy, and the war in Iraq has fanned concerns about U.S. dependence on oil from abroad.

Consider, too, that ridership on public transport climbed to a 50-year high in 2007, reports the American Public Transportation Assn., as more companies start to pick up part of the tab for employee commuter costs. (Such corporate subsidies became tax-deductible recently.) And sales of more fuel-efficient cars are up. The shift has not been lost on Detroit's Big Three, which heavily depend on SUV and pickup sales for profits. "Fuel economy as a selling point is absolutely here to stay," says James Farley, group vice-president for marketing at Ford Motor (F). "Our future plans revolve around the idea that gasoline is going sideways and up from here, not down."

A BOOMER SLOWDOWN

Demographic factors may also be driving down gasoline consumption. When the postwar march to the suburbs was in full swing and the nation's highways expanded, gas consumption grew by an average of 4% a year. In more recent years that rate has moderated to 1.2%. A study released in April by the EIA posited that part of the decline could be attributed to falling population growth and baby boomers exiting their peak driving years. That translates into fewer car sales on a per capita basis. Many analysts have been knocking down their estimates of growth in worldwide oil demand because of weaker consumption in the U.S.

Mind you, it's not yet certain that falling gas consumption is here to stay. Historically, consumption tends to dip during recessions, then rebounds with the economy. "There have really only been a few times Americans have cut back their gas consumption over a long period of time," says Geoff Sundstrom, a spokesperson for the American Automobile Assn. "Those occasions are where you've had high prices and a recession, such as 1974 and 1981. It looks like we're heading into another one of those." EIA researchers expect consumption growth will rise back up to 0.9% next year—though that's still below what the U.S. has averaged so far this decade.

So even if gas consumption does bounce back it's likely to do so at a slower pace. "Consumer habits are pretty sticky," says Adam Robinson, an energy analyst at Lehman Brothers (LEH). "We've seen a long period of high prices that has finally hit the consumer, and now they're going to shift their preferences."

Indeed, some commuters are finding public transport to their liking. Aly Cohen, a 27-year-old financial analyst at Costco Wholesale (COST), first tried taking the bus to work in January. Now, with her employer picking up most of the $63 tab for a monthly bus pass, she has stopped driving to work altogether and cut her gas consumption in half. "It's nice," she says. "I can take a nap or read." Such a shift in commuting habits, if copied on a large scale, may alter U.S. energy consumption in significant and surprising ways.

For more on rising gasoline prices and motorists' reactions, watch a video report at businessweek.com/go/tv/gas.

With David Kiley and David Welch in Detroit.
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