

An analysis by McQueen Financial Advisors

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MFA Economic Outlook For Q2 2026

Three years ago, I was flying home from a beach vacation, and I feverishly read and developed a presentation on the failure of Silicon Valley Bank (SVB). Today, I am flying home from a repeat of the vacation with the same people. This time, the conversations have been focused on the war in Iran and the Middle East.

We discussed the effects of the blockade of the Straits of Hormuz and the attack on the natural gas processing hub in Qatar. The situation that we are unpacking is the cost of natural gas, gasoline, and diesel fuel, and the ramifications on the economy. We have the following facts on the oil and natural gas situation:

Oil:

- Historically, 21 million barrels of oil passed through the Straits of Hormuz every day (until last week). This is just over 25% of all seaborne oil at any time.
- Thailand, Vietnam, and the Philippines are enacting work-from-home requirements as fuel reserves run low. Thailand has roughly a 90-day supply of gas and diesel
- The average cost of diesel fuel has increased over the last 12 months from \$3.60 to \$5.20 a gallon.
- The average cost of regular gas has increased over the last 12 months from \$3.12 to \$3.92 a gallon

Natural gas:

- 50% of all Liquefied Natural Gas (LNG) transport ships are stuck in the Persian Gulf.
- 17% of all LNG production is exported from the damaged Qatar site.
- The Qatari plant will take roughly 5 years to fix.
- 43% of power in the USA is generated by natural gas.
- The cost of natural gas is volatile and seasonal, and it is close to its average price for the last 12 months at \$3.50 MMBtu.

The USA and Oil & Natural Gas Production:

The USA has been a net exporter of oil and natural gas since 2019. We should all be thankful for the technological advances and pro-energy decisions that we have made to be energy independent. Since we (the United States of America) are the owners of the natural resource, we are paying Americans for the fuel. This will be positive for the gas production regions of the country. Also, as one would expect, the higher prices will hurt the economy due to the higher costs.

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Automotive Impact:

We should also realize that the fuel efficiency of cars and trucks has improved by over 40% since 2004, reaching over 27 miles per gallon. A \$1 per gallon increase in gas costs will add roughly \$700 a year in expenses to the typical American family, according to AAA. I know that I fill up my car once a week with 20 gallons of gas. This results in \$20 more a week or \$1,040 a year (I know I drive too much.... Kid things).

Trucking Impact:

Diesel-powered trucks typically get about 6 to 7 miles per gallon. A \$1 increase in diesel fuel results in an additional 14 cents per mile. One of the biggest effects of higher diesel prices on consumers is the price of produce. Every pound of produce goes up in cost by roughly 2 cents with every \$1 increase in diesel.

Psychological:

There are several studies that have determined that \$4 a gallon of gas is mentally difficult for the average consumer to process. This results in a pullback in spending. I have not found any studies from the last few years after the significant COVID lockdown and spending-based inflation to ensure the continued accuracy of the \$4 gallon effect.

Consumer Impact:

The consumer will have fewer dollars for discretionary consumption. While the individual consumer may have higher gas costs of roughly \$50 to \$60 a month, consumers combined will have closer to a \$150 billion annual cost (reduction in spending).

Consumers in the lower-income strata will have a much harder time dealing with the higher costs. We would expect that this group will see delinquency and charge-off rates rise. This will be seen in:

- Sub-prime auto
- Near-prime auto
- Credit cards
- Buy now, pay later (BLPL)

Financial Institutions:

The effect will be different for each institution depending on your customer/member base. The following scenarios are ones that we see the potential for higher delinquency and charge-offs:

- Lending to lower credit consumers.
- Lending to high-energy consumption businesses that have a difficult time raising prices.
- Rural areas with greater daily driving distances.

The Federal Funds Rate and Gasoline & Diesel Prices:

As I read the news over the past week, I see the talking heads on the internet starting to line up, pushing the thought of interest rate increases. This type of groupthink (possibly AI-generated eco chambers) is wholly inaccurate.

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The Federal Open Market Committee (FOMC) has learned from the past and views shocks in the cost of gasoline and diesel as effectively a tax on consumers, reducing their spending power. A reduction in spending will naturally slow down the economy. The FOMC will initially pause (as they did last week) to understand what is going on with war and energy prices. If energy prices remain high, the economy will slow, and the FOMC will continue to lower rates. If energy prices decline, the FOMC will judge the level of economic expansion (or contraction) and potentially continue to lower rates.

Housing:

The housing market has a combination of two problems. One – Not enough sellers. Two – Mortgage rates are too high for affordability. The FOMC knows that the best way to get the housing market moving again is to lower interest rates. By lowering rates, homeowners can afford to sell and lose their 3.00% mortgage and move into a different house. The key here is what level will allow consumers to move? I believe that we need to be near 4.00% to 4.50% to mentally allow consumers to move.

Today, I see many financial institutions offering five-year ARM (Adjustable-Rate Mortgage) in the range of 5.00% to 5.75%. Therefore, the FOMC needs to lower the Federal Funds rate by an additional 0.50% to open the housing market. The MFA 2026 economic projections called for a 0.75% reduction in the Federal Funds rate. We expect that by year end, we will receive three 0.25% cuts.

Summation:

While uncertainty is high, the situation is also fluid. On Sunday, Iran decided to allow some ships to pass through the Straits of Hormuz. Ships that are registered with countries with which they are not at war. This will help reduce gas and diesel prices.

Higher energy costs will increase inflation in the short term. Over time, people will spend less on other items, and inflation will decline. This should keep the FOMC on pause or lower the Federal Funds rate.

As we look forward, we should focus on two significant situations. One, solid credit decisions are paramount. Two, preparing for lower interest rates and margin compression will allow you to continue to thrive into 2027.