This Week in Petroleum 10-24-07

Posted by Robert Rapier on October 24, 2007 - 6:00pm
Topic: Supply/Production
Tags: eia, gas inventories, gas prices, oil inventories, original, twip [list all tags]

Whoa! The analysts missed this one by a mile. Here were the predictions, prior to the release of the report:

> Analysts surveyed by Dow Jones Newswires on average predict crude inventories rose 300,000 barrels during the week ended Oct. 19, and Vienna's PVM Oil Associates also noted that "expectations for this week's U.S. oil inventory data are for a rise in crude oil stocks."
>
> However, some analysts predict a decrease of up to 2 million barrels. Analysts also predict the EIA report will show refinery utilization rose 0.3 percentage point; gasoline supplies, still near record lows, rose 1.1 million barrels; and distillate stockpiles, which include heating oil and diesel, rose 200,000 barrels.

Here's what they got:

> **U.S. commercial crude oil inventories fell by 5.3 million barrels** compared to the previous week. At 316.6 million barrels, U.S. crude oil inventories are near the upper end of the average range for this time of year. **Total motor gasoline inventories decreased by 2.0 million barrels last week**, and are at the lower end of the average range.
>
> Both finished gasoline inventories and gasoline blending components fell last week. **Distillate fuel inventories decreased by 1.8 million barrels**, and are at the upper limit of the average range for this time of year. Propane/propylene inventories increased 0.6 million barrels last week. Total commercial petroleum inventories decreased by 7.9 million barrels last week, but are in the upper half of the average range for this time of year.

I suspect crude will be off to the races again. I had called a (short-term) top on front-month WTI a week ago at $89, and in fact oil was down almost every day since then. But this inventory report will provide a lot of fuel for the bulls for another week.

Here is the rest of the report:

> U.S. crude oil refinery inputs averaged 14.9 million barrels per day during the week ending October 19, down 183,000 barrels per day from the previous week's average. Refineries operated at 87.1 percent of their operable capacity last week. Gasoline production rose compared to the previous week, averaging nearly 9.0 million barrels per day. Distillate fuel production fell last week, averaging 3.9 million barrels per day.
>
> U.S. crude oil imports averaged 9.1 million barrels per day last week, down 1,305,000 barrels per day from the previous week. Over the last four weeks, crude oil imports have averaged 9.9 million barrels per day, or 414,000 barrels per day less than averaged over the same four-week period last year. Total motor gasoline imports (including both finished gasoline and gasoline blending components) last week averaged 838,000 barrels per day. Distillate fuel imports averaged 235,000 barrels per day last week.
>
> Total products supplied over the last four-week period has averaged nearly 20.8 million barrels per day, up by 0.4 percent compared to the similar period last year. Over the last four weeks, motor gasoline demand has averaged 9.2 million barrels per day, or 0.2 percent below the same period last year. Distillate fuel demand has averaged nearly 4.3 million barrels per day over the last four weeks, up 1.0 percent compared to the same period last year. Jet fuel demand is down 3.3 percent over the last four weeks compared to the same four-week period last year.

It is going to be a close call on the $1,000 bet. (The real irony is that the primary risk factor I saw with respect to the bet - the potential for falling Saudi production - has not been an issue. Saudi production has been steady all year, and is now set to rise). I do believe the fundamentals for higher oil prices are generally worse now than they were 3 months ago. Peak driving season has passed, OPEC is already pumping more crude, and prices have had a dramatic run-up. On the other hand crude inventories, while still high, have been pulled down (although they are at about the same level they started the year at), and gasoline inventories continue to hover near record-low levels. But, the sentiment has certainly turned in favor of higher oil prices. And the sentiment of the market can move it quite a bit in a short period of time. You can see some of the analysts on CNBC - after having missed out on most of the run-up - have now moved their clients into oil and so are talking up the price.

But the recent fast run-up in prices, followed by OPEC's decision to pump more crude, would make me very cautious about buying oil at this level. You might make some money, but it is a much bigger risk than it was earlier in the year when the fundamentals for higher oil prices looked better (at least to me). Of course over the long haul, I am bullish on oil prices and have been for 5 years. I thought $100 oil in 2008 was likely, but a move from $60.77 (the crude price the first week of January) to $100 in a single year would be unprecedented.

I would also add just a bit on refinery utilization. Analysts had predicted utilization to come up this week. Generally, refineries are coming out of their turnarounds now, and you would expect to see utilization at a higher level at the end of October. But you have to take the current crack spreads into account. When crack spreads are at $30/bbl, as they were earlier in the year, you do everything you can to maximize your utilization rate. If that means paying overtime, or paying extra to have equipment fabricated and delivered quickly, you do it. Money is not an object; you get your refinery up and running as quickly as possible.

But when crack spreads are $5/bbl, as they are now, you don't do those things. You still want to have your refinery up and running, but it doesn't make economic sense to go all out to boost your utilization. That $5/bbl margin will disappear pretty quickly if you throw money around. So, utilization rates will be less robust in times of low margins. It has absolutely nothing to do with inability to secure crude - as some have suggested. It has everything to do with economics. But given where gasoline inventories are currently setting, I don't expect margins to stay soft for long.