This Week in Petroleum 11-15-07

Posted by Robert Rapier on November 15, 2007 - 2:00pm
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2nd Update

Now, 30 minutes after the release of the report, the market is starting to react, and oil prices are falling. Are traders really that slow to react? Or is that some kind of mirage because there is a delay in getting trades executed and reported? I get the impression sometimes that I could make a small fortune trading within the first half hour after the release of the inventory report. Seriously, someone who trades, please fill me in on this. With a big surprise like this, you can probably predict the direction prices are headed short-term with a high rate of success. But the reaction seems to develop very slowly. My question: If I placed a trade at 1 minute past the release of the report, when would I expect it to execute?

Updated following the release

Surprise, surprise. I don't know that anyone expected a big rise in crude stocks, but that's what we got:

> U.S. commercial crude oil inventories (excluding those in the Strategic Petroleum Reserve) rose by 2.8 million barrels compared to the previous week. At 314.7 million barrels, U.S. crude oil inventories are in the upper half of the average range for this time of year. Total motor gasoline inventories increased by 0.7 million barrels last week, and are at the lower end of the average range.

Crude imports showed a big jump, but are still down over this time last year:

> U.S. crude oil imports averaged nearly 10.5 million barrels per day last week, up 831,000 barrels per day from the previous week. Over the last four weeks, crude oil imports have averaged nearly 9.7 million barrels per day, or 387,000 barrels per day less than averaged over the same four-week period last year.

And why were gasoline inventories up? As I said before the release, if utilization goes up, gasoline inventories should go up. Utilization was up to 87.7%, a sharp rise from last week. The prediction from the analysts didn't make much sense to me - refinery utilization up a good bit and a draw on gasoline inventories.

I didn't expect crude inventories to head up before next week. The market hasn't reacted much to this, which is surprising. Crude prices were down slightly before the inventory release, but typically I would expect a suprise of over 3.5 million barrels of crude to move the market more. So far, the market is barely reacting, but maybe I haven't given it enough time. I think I would have been prone to go short 30 seconds after I saw that report.

To be updated following the release of the report

This week's inventory report was of course delayed by a day due to Veterans Day in the U.S. Expectations are for another crude decline, which given the storms in the North Sea and the flooding in Mexico is a pretty good bet. Here were the predictions per Reuters:

> A Reuters poll shows that Thursday's U.S. inventory data is expected to show crude stocks dropped last week by an average of 800,000 barrels, which would be the fourth consecutive weekly decline.
>
> Analysts also expect 100,000 barrel draws in both distillate and gasoline stocks. Refinery runs were forecast to be up 0.5 percentage points.

(A poll by Dow Jones predicted a more modest 300,000 barrel crude decline).This week's report may not spur the typical market reaction. Oil prices rose on Wednesday, due to a combination of expectations of an inventory drop, as well as remarks from Saudi that they won't discuss a production boost at this weekend's OPEC meeting, but will instead delay that discussion until their December 5th meeting.

While a drop in crude inventories should typically favor a rise in price; 1). Some of that rise is already built in due to analysts' expectations of an inventory drop; and 2). The December WTI contract expires tomorrow, and there is a significant net speculative long interest that will probably be anxious to take profits. That may limit the upside. (There is also the factor that a large draw may cause crude prices to run up a few more dollars, but that would increase the pressure on Saudi to placate the markets at this weekend's meeting).

I do question the prediction that there will be a gasoline draw and a 0.5% increase in refinery utilization. Utilization has been lagging, but if the number ticks up this week, I would expect gasoline inventories to build. I think the recent uptick in gasoline prices will also cut into demand a bit, further improving the likelihood of a gasoline build. If utilization doesn't improve, then I would expect that we would see a draw on gasoline.

Of course gasoline stocks remain near record-low territory, so any negative surprises there could quickly impact prices. Gasoline prices have recently started to climb, but that climb has not kept pace with the climb in oil prices. Based on where gasoline inventories stand right now, it's going to take quite an inventory build at this point to avoid $4 gasoline in the spring.