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Why you probably won’t be seeing gasoline at 99 cents a gallon

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Refiners cut to output as profit margins suffer along with crude oil

Maintenance season for U.S. refineries comes every year at this time, tightening supplies of gasoline and lifting prices at the pump with it.

But this year, the season comes at a time when oil prices CLH6, +7.63% have dropped to levels not seen since 2003. Retail gasoline is near its lowest price since the Great Recession. That combination can eat into profit margins for refiners, who may soon chose to cut back fuel production even further.

This is the “climactic chaos” that we’ve been looking for in the first quarter, said Tom Kloza, global head of energy analysis at the Oil Price Information Service.

Already, some refineries have begun annual maintenance and “they are running less crude, even as the global and domestic surplus continues unchecked,” he said.

And with prices for petroleum products such as gasoline recently trading for less than the price of crude in many parts of the Midwest, some refiners may cut output rather than sell products “in a market that doesn’t fetch a profit,” Kloza said.

Patrick DeHaan, senior petroleum analyst at GasBuddy.com, said several refiners in the Midwest have already cut refinery runs and, combined with recent strong gas demand figures, spot prices for the fuel reacted by bouncing back from Tuesday’s intraday low.

On Tuesday, GasBuddy had said the “previously unthinkable” 99-cent gasoline was becoming a “strong possibility.”

But DeHaan admitted Thursday that with talk of refinery output cuts, “short term, the likelihood of 99-cent gas … has vaporized.”

Michael Green, a spokesman for AAA, wouldn’t go quite that far.

“Some lucky drivers in the Midwest may see gas as 99 cents or less this month, but that vast majority of us will be stuck paying significantly more at the pumps,” said Green.

Crack spreads

Refinery maintenance will make the glut of crude supplies even worse, sinking prices for oil even more and reducing crack spreads — the amount of profit from processing oil into products.

Earlier this week, Chicago gasoline sold for some $7 to $8 a barrel under the price of West Texas Intermediate crude, so crack spreads were negative, said Kloza. That’s changed a bit, with Chicago gasoline now about $3.20 over WTI.

“The additional [refinery] run cuts could mean that there is 250,000 to 500,000 barrels a day less demand for crude in the next 30 days than what folks had been counting on,” said Kloza. That would add to an already flooded market.

For now, margins on Nymex are “fine,” Kloza said, with gasoline selling for about $13.20 a barrel over crude for March.

On Thursday, WTI crude dropped to $26.21 a barrel on Nymex, its lowest level since May of 2003. Gasoline futures RBH6,_+6.89% meanwhile, settled at 94.17 cents a gallon, their lowest since late 2008. That works out to about $39.55 per barrel of gasoline.

At the retail level, a gallon of regular gas sold for an average $1.703 on Thursday, according to AAA.

WTI and other North American crude blends are under “tremendous pressure,” and if six refiners run 500,000 barrels a day less crude, “that might fortify the gasoline or diesel market, but it will do so at the expense of the crude market,” he said.

And Thursday’s sub-$27 WTI oil price just might be too low for refiners.

Refiners need at least $5 a barrel to cover processing costs, Kloza said. “You can’t buy crude for $27 a barrel and sell refined products for $25 a barrel.”