The Daily Dish

It’s (Not) All About Oil Prices

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Some people check the weather. Others look at the box scores. I suppose a few go straight for Kafka. But Eakinomics rolls out of bed and checks oil prices. Nobody should walk the dog before nailing down the cost of a barrel of West Texas Intermediate (WTI) or Brent crude. Right?

It wasn’t always this way. But since the war in Iran—which is not materially different than the negotiations with Iran or the ceasefire with Iran—oil prices have been front and center. And so when there was a return to open hostilities, Eakinomics went on full alert. Would WTI, which peaked at nearly $115 a barrel earlier this year, head straight north? What would the implications be for price pressures and 2nd quarter growth?

As it turns out, WTI has settled in the vicinity of $80 a barrel, which seems manageable. But gasoline prices are going up and the national average is in the vicinity of $4.00. As it turns out, crude oil and refined oil products are two different things, and it is not all about crude oil prices.

Refineries buy crude oil and refine it—which is known as “cracking” it—into hydrocarbons such as gasoline, jet fuel, and heating oil. A measure of the profitability of this activity is the difference between the cost of the raw material and the wholesale price of the refined products. A standard measure of this is the “3-2-1 crack spread.” It assumes that three barrels of crude will yield two barrels of gasoline and one barrel of distillate (diesel or heating oil). To learn more, read this AAF insight.

Of note, Bloomberg reports:

> *The 3-2-1 crack spread—the standard proxy for refining margins (it estimates the profit from turning three barrels of crude into two barrels of gasoline and one of diesel)—is currently at a multi-year high of $70. …[T]his is more than six times its historical*

> *average, “suggesting refined products reflect a considerably tighter physical market than crude alone.”*

That’s a sobering thought. The world responded to the onset of the war by turning on the pumps at the Strategic Petroleum Reserve and its international counterparts. There is no comparably easy way to ease shortages in refined product markets.

Tomorrow morning? WTI, Brent, 3-2-1 crack spread, and coffee. The perfect start to the day.