

## Our View: Crude Oil Price Suppression

Philip K. Verleger, Jr.  
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The world's refiners are suppressing global crude oil prices to boost margins. With no loyalty to crude producers (less than ten percent of the petroleum products supplied to OECD countries come from firms that own refineries *and* crude production), refiners are doing everything they can to restrain crude prices.

The suppression has cost crude producers approximately \$20 per barrel or twenty percent of revenues received for the last year. The announcement of Valero's record profits last week heralded the effort's success.

Refiners have suppressed prices by several means:

*Boosting renewable diesel (RD) production in the United States.* RD replaces traditional diesel. Raising RD output adds significantly to refiner profits thanks to regulatory programs and reduces demand for crude.

*Working aggressively to minimize product stocks.* This action increases product-to-crude margins by boosting backwardation in product prices, which in turn adds to refining profits.

*Limiting spot crude oil purchases.* This constraint furthers price suppression by cutting backwardation in crude markets. Refiners seem to be trying hard to keep crude inventories in check, perhaps even cutting runs rather than bidding up prices for incremental supplies.

The refiners' efforts to suppress crude prices should not surprise anyone. These firms understand that retail consumers will buy fewer gallons or liters when prices are high than when they are low. Thus, they will do all they can to keep product prices down while still doing everything possible to maximize profits, and they can achieve both by suppressing crude prices.

The refiners' willingness to refrain from buying crude oil is reflected in the unwillingness of oil producers to invest heavily in exploration and production (E&P). The figure below illustrates oil producers' reluctance to increase spending on E&P even when prices are high.

Chevron's earnings announcement last week served as an acknowledgment that the leverage over crude prices is now in the refiners' hands. Further price suppression can be expected.

## Historical Investment in Oil and Gas Exploration vs. Average Dated Brent Price, 1985 to 2022

