

Energy

Gap Between Domestic and International Crude Prices Shrinks

Second Quarter 2013

The difference between West Texas Intermediate (WTI) and Brent crude oil narrowed significantly in the second quarter. WTI, a barometer for conditions in the middle part of the U.S., was unchanged from the first quarter at \$94 a barrel (*Chart 1*). Brent, which broadly reflects global market conditions, declined \$9 from the first quarter to average \$103. Several factors may be behind the narrowing spread, including timing differences between refinery maintenance in the U.S. and other parts of the world, and further increases in shipments by rail of landlocked U.S. crude to coastal areas of the U.S. and Canada.

Gasoline prices increased in the U.S. over the last quarter, while diesel prices declined. Regular-grade gasoline averaged \$3.60 in the second quarter, \$0.04 more than in the first (*Chart 2*). Diesel averaged \$3.90 a gallon in the second quarter, compared with \$4.03 in the first. While the East Coast and Gulf Coast both saw lower gasoline prices in the second quarter, prices in other parts of the country increased. Regional supply issues in May and June caused gasoline prices to spike in the Midwest. In mid-June, prices in the area temporarily surpassed those on the West Coast, which typically has the nation's highest gas prices.

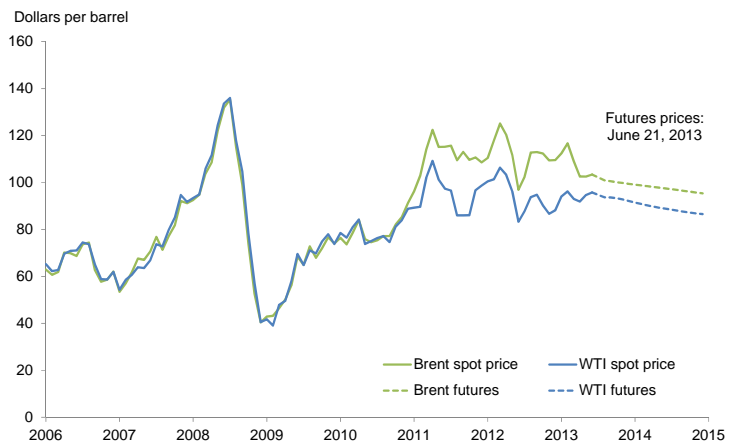
The U.S. Energy Information Administration (EIA) expects gasoline to average \$3.53 per gallon for the summer driving season, a decrease of 16 cents from last summer. The EIA also predicts a lower average diesel price for this summer at \$3.83 per gallon, down from last summer's \$3.95.

Seasonal Factors Driving Global Oil Demand

Global demand for oil products seasonally falls in the second quarter because of the onset of warmer weather and refinery maintenance season. Global production is expected to outpace consumption during second quarter 2013, increasing global inventories (*Chart 3*).¹ Demand will seasonally grow in the third quarter, boosted by the summer driving season in the Northern Hemisphere and increased power generation needs in the Middle East.

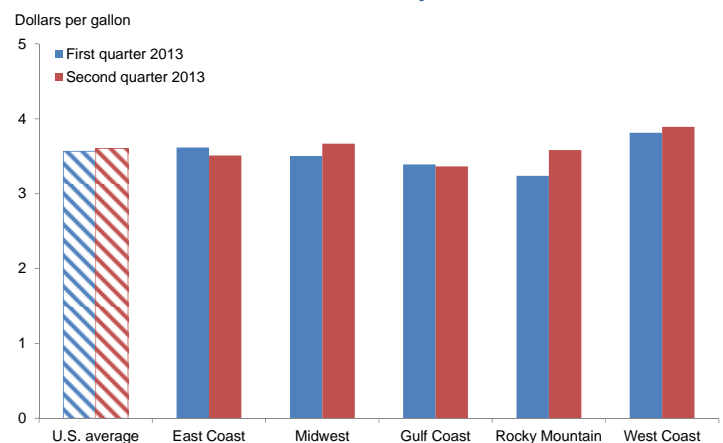
The world continues to consume more oil products. The EIA currently predicts 2013 consumption will grow 0.9 million barrels per day (mb/d) over 2012 consumption. Asian countries not part of the Organization for Economic Cooperation and Development (OECD), particularly China, contribute the most to demand growth. Supply is expected to grow continuously for the rest of the year, with big increases coming from North America.

Chart 1
Brent—WTI Differential Narrows in Second Quarter



SOURCES: Wall Street Journal; Bloomberg.

Chart 2
U.S. Retail Gasoline Price Increases Modestly



SOURCE: Energy Information Administration.

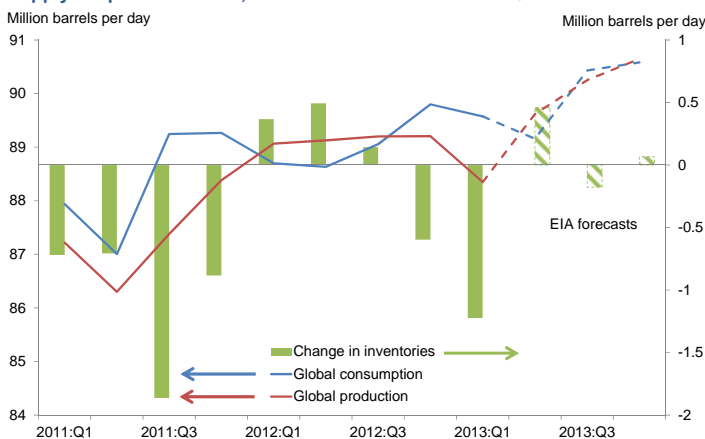
U.S. Crude Production Continues to Grow

U.S. crude production is estimated at 7.23 mb/d in the second quarter, up from 7.1 mb/d in the first. Production continues to increase due to hydraulic fracturing and horizontal drilling for oil that is inaccessible through conventional methods. Higher production levels in recent years have occurred primarily in Texas, North Dakota and a handful of other states (*Chart 4*). The EIA projects that by year-end, the U.S. will produce almost 7.6 mb/d of crude oil.

Natural Gas Prices Increase

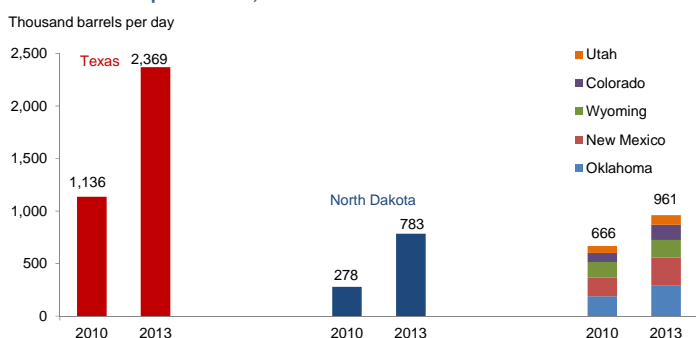
The Henry Hub spot price for natural gas averaged \$4.09 per million British thermal units (mmBtu) in the second

Chart 3
Supply Outpaces Demand, Inventories Grow in Second Quarter



SOURCE: Energy Information Administration.

Chart 4
Production Jumps in Texas, Several Other States



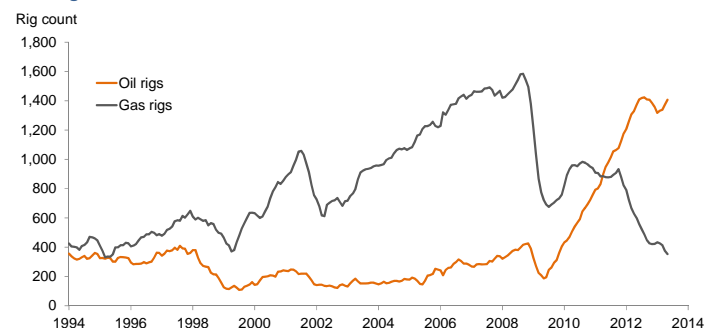
NOTES: Production data are released with a lag; March 2013 is the latest available. The chart compares production in March 2010 with March 2013.
SOURCE: Energy Information Administration.

Chart 5
Natural Gas Prices Increase from First Quarter



SOURCES: Wall Street Journal, Bloomberg.

Chart 6
Drilling Shifts from Gas to Oil



SOURCE: Baker Hughes.

quarter, an increase from the \$3.50 average in the first (Chart 5). Cold weather in April unexpectedly boosted demand for natural gas, causing its price to increase. Natural gas prices have come down in June, mostly due to reduced demand from power plants. The EIA is forecasting the Henry Hub price to average \$3.92 per mmbtu in 2013.

Drilling is once again shifting from natural gas to oil. The U.S. natural gas rig count dropped from an average of 424 in the first quarter to 360 in the second (Chart 6). Meanwhile, oil rigs are up from an average of 1,329 in the first quarter to 1,395 in the second. The total number of U.S. rigs remains essentially unchanged.

Total marketed production of natural gas is estimated at 70.2 billion cubic feet per day (bcf/d) in the second quarter, an increase of 0.92 bcf/d over the previous quarter. The EIA is expecting U.S. natural gas production to average 70 bcf/d in 2013. U.S. consumption is estimated at 59.73 bcf/d in the second quarter, down from 88.06 bcf/d in the first. Demand is high during colder months because natural gas is used to generate heat for homes.

Summer Residential Electricity Use Expected to Drop

The EIA forecasts that U.S. residential consumers will use an average of 3,200 kilowatt hours of electricity this summer (June through August), a 4.6 percent decrease from last summer. The average U.S. residential electric bill is forecast to be \$395 this summer, a 2.5 percent reduction compared with last year. Lower consumption of electricity offsets slightly higher electricity prices.

Higher natural gas prices are leading some electric generators to switch from natural gas to coal. The EIA forecasts that the electric-generation sector will use 8.5 percent more coal this year than last, while natural gas use will decline 8.2 percent. Although natural gas use in the sector may decline, use remains high compared with previous years.

—Amy Jordan and Michael Plante

Note

1. EIA data include production, consumption and inventory changes in crude oil and crude oil products, ethanol and other biofuels, and natural gas liquids.

About the Authors

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