

THE VAN DER VALK PRICE ADVISORY FOR 10-28-08

The Gas Guy advises to WAIT, WAIT, WAIT, WAIT!

Never in the West Coast petroleum industry history has the gasoline market imploded so quickly. Gasoline prices have continued to crash all up and down the coast. The region's average prices rushed right by the \$3 mark and continued to slide right by it with no apparent bottom. They may well be below \$2.50 per gallon by Election Day and heading down to the magic \$2 per gallon price by Christmas. Most dealers who are lucky enough to sell independent unbranded gas are already capable of pricing their product at \$2.25 a gallon. (See The Gas Guy's explanation about gasoline zone pricing below).

What we predicted last Thursday:

We predicted a high-octane price slide this weekend with no brakes on lower prices and price cuts of between 8 and 19 cents a gallon by Tuesday morning for regular unleaded, and 2 to 6 cents a gallon for diesel. We got price cuts in spades.

What happened: Regular unleaded prices dropped 14 cents since our last report, and between 24 to 31 cents per gallon depending on the area in the last week. Diesel dropped 12 cents since our last report and 19 cents in the last seven days.

What we predict by Friday: Daily price drops in the average price with an average decrease from two to five cents per day by Friday morning (6 to 15 cents a gallon).

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GASOLINE ZONE PRICING 101

Generally speaking, there are two types of gas stations - major oil branded stations and independently owned unbranded stations. Dealers who operate major oil brand named stations have no control over their wholesale prices, which are known in the trade as Dealer Tank Wagon or DTW prices for short). Those prices are set by the major oil pricing manager for the brand of gasoline the dealer sells. Most major oil company branded gas stations fall into a specific price "zone" that is established by the oil companies.

This type of redlining allows Big Oil to curb competition by maintaining high wholesale prices to its dealers. It is also a tool that enables them to contain price wars. As long as all of the major brands charge a high wholesale (DTW) prices in a specific zone, profit-harming price slides can be controlled. The practice is also used to limit dealer profit margins from between ten to fifteen cents per gallon, on average. The inverse happens when the market goes up with the effect of seeing pump prices "Shoot up like a rocket and drift down like a feather".

Unbranded dealers, on the other hand, buy spot market gasoline from different suppliers at posted rack prices. Often, the wholesale rack price of the gasoline is much cheaper than the prices offered to major oil brand-name dealers. At this time, many unbranded dealers could sell their gasoline for less than \$2.25 a gallon and still make a profit.

The reason those dealers are not offering lower priced gas is that they don't have to or until the major oil company brands start passing on the benefits of lower oil costs to their retailers.