MARKET PERSPECTIVE

Refining & Fuels Marketing:
Normalization with Constraint-Driven Volatility

What operators and investors need to know navigating the mid-cycle

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THE BOTTOM LINE UP FRONT

23.5 View
Downstream refining is no longer living in the extraordinary post-2022 dislocation. The market is normalizing, but volatility remains constraint-driven and outcomes are increasingly dispersed. In this regime, the edge is not calling next quarter's cracks - it is converting the tape into durable advantage: reliability as a cash moat, differential and logistics leverage, disciplined capital allocation, and explicit management of policy exposure.

This brief synthesizes the structural forces shaping refining and fuels marketing today, the regional constraints that create winners and losers, and the operator-level decisions that matter most in a normalizing tape. For boards and investors, the question is not whether margins bounce next quarter - it is whether management teams are building repeatable capture and resilience at mid-cycle conditions.

FOUR FORCES DEFINING THE REGIME

1. The market is normalizing off the post-2022 dislocation
   - Benchmark cracks have reverted from extreme conditions, but the system remains sensitive to outages, turnarounds, and regional logistics.
   - Gasoline is a mature, highly seasonal demand pool; distillate and jet, plus exports, carry more of the marginal support.
   - Mid-cycle underwriting matters: the winners are built on repeatable execution, not peak-cycle luck.

2. Dispersion is increasingly execution-driven
   - Reliability and turnaround discipline are the primary determinants of who converts opportunity into cash as the tape normalizes.

- A sustained $1-2 per barrel delta in cash cost or capture compounds into meaningful through-cycle value - and is measurable quarter after quarter.
- Commercial excellence (crude procurement, blending, scheduling, and retail pricing) is the quiet differentiator when benchmarks look 'normal'.

3. Feedstock optionality and export clearing are the cleanest structural levers
   - Heavy/sour differentials reward complex kits; when discounts widen, the advantage is structural rather than cyclical.
   - Export connectivity - particularly in PADD 3 - determines whether the system clears efficiently or stocks build and margins compress.
   - Logistics flexibility (docks, pipelines, terminals) and product swing capability are the practical mechanisms for monetizing dislocations.

4. A rising constraint stack keeps volatility alive
   - Policy line items (RIN, LCFS, credits) remain a material earnings and cash-flow volatility source; best teams treat them as a risk-managed exposure, not a strategy.
   - Constrained micro-markets - especially California - behave differently than national benchmarks: outages, specs, and compliance costs dominate outcomes.
   - Safety and compliance are not 'cost centers' - they are license to operate, the key driver of downtime risk, and a direct determinant of valuation durability.

REGIONAL SNAPSHOT: WHERE THE MARGIN IS MADE

Region / Market	Constraint Position & Outlook
US Gulf Coast (PADD 3)	Structurally advantaged when connected to export clearing. Complex kits can monetize heavy/sour discounts and run hard, but hurricane and turnaround stacking risk is real.
Mid-Continent (PADD 2)	Advantaged access to Canadian barrels and inland logistics. Less export optionality; economics swing on local balance, pipeline constraints, and competition for placement.
East Coast (PADD 1)	Structurally challenged and import-dependent. Limited local refining system creates price-taking behavior; logistics and demand variability dominate.
West Coast / California (PADD 5)	Isolated, spec- and policy-intensive market that can earn a fragility premium. High compliance burden and outage sensitivity create the widest outcome dispersion.
Marketing & Branded Placement	A stabilizer and value-capture layer when managed as an integrated system (supply, pricing, logistics). Not risk-free: competition, volume mix, and retail execution determine durability.

WHAT SEPARATES WINNERS IN A NORMALIZING TAPE

In a normalizing market, survival and compounding are not the product of calling the cycle. They are the product of four durable attributes:

- 1. Reliability as a cash moat. Run length, turnaround discipline, and process safety convert a similar benchmark environment into very different realized dollars per barrel.
- 2. Feedstock advantage. Crude slate flexibility and differential capture (especially heavy/sour leverage) determine whether mid-cycle economics are attractive or merely tolerable.
- 3. Logistics and placement. Export capability, terminal networks, and branded outlets determine whether barrels clear at value or back up into inventory.
- 4. Capital allocation discipline. The balance sheet is optionality; payout frameworks, sustaining capex realism, and downside cases separate allocators from gamblers.

SECTOR POSITIONING: WHO COMPOUNDS, WHO STRUGGLES

Refiners are not like-for-like. Kit, footprint, logistics, and policy exposure vary materially. Positioning should be assessed by structural attributes, not labels.

HIGHEST RESILIENCE: The advantaged integrated platform

Large systems with export connectivity, crude flexibility, and disciplined capital allocation can compound through normalization. They are positioned to buy, build, or rationalize on their terms - not the market's.

MIXED POSITION: Advantage in some levers, volatility in others

Diversified downstream portfolios can reduce earnings beta via marketing, lubes, or midstream, but investors will discount the story without transparent segment economics and a clear policy-volatility framework.

MOST CHALLENGED: High-beta turnarounds and isolated exposure

Leverage, large project execution, and exposure to fragile micro-markets can create upside - but only with proof density. In this tier, margin of safety is driven by liquidity, run length, and a short list of measurable execution wins.

Signals worth noting (FY2025 filings and Q4 2025 calls):

- **Marathon:** ~$250MM planned to expand branded stations (secured offtake thesis) alongside MPLX growth capital directed primarily to Natural Gas & NGL services.
- **Valero:** inventory builds were framed as a function of high utilization concentrated in PADD 3; exports remain the system's clearing valve.
- **Phillips 66**: portfolio actions included acquiring the remaining 50% of WRB and idling Los Angeles; the test is whether structural capture improves with transparency.
- **HF Sinclair:** small refinery RIN waivers drove a $313MM uplift to adjusted refining gross margin in Q4 - a reminder that policy line items can dominate quarters.
- **PBF:** $230MM of achieved efficiencies in 2025; targeting $350MM run-rate savings by end-2026 - execution proof remains the fulcrum.

THE OPERATOR'S PLAYBOOK: 6 / 18 / 36 MONTHS

Horizon	Priorities
6 Months (Stabilize)	Protect run length and manage turnarounds as a margin system. Make capture measurable (realized vs benchmark, crude diff capture, blend economics, freight). Treat RIN/LCFS/credit exposure as an explicit sensitivity with guardrails. Preserve balance-sheet optionality and avoid funding payouts at the expense of resilience.
18 Months (Reshape)	Prioritize reliability and high-return debottlenecks over speculative growth. Reassess asset fit where structural disadvantage is durable (isolated markets, taxed kits, chronic downtime). Invest in logistics and placement that improves clearing (terminals, docks, branded pull-

Horizon	Priorities
	through) with clear unit economics. Align incentives to ROIC, cash conversion, and uptime - not volume.
36 Months (Compound)	In normalization, the strong consolidate. Pursue disciplined M&A or partnerships only where the balance sheet is unquestionable and downside is protected. Build low-carbon participation with a defined risk budget rather than narrative. Institutionalize the operating system: maintenance planning, reliability engineering, and commercial governance that repeat through the cycle.

WHAT BOARDS SHOULD BE TRACKING MONTHLY

The KPI architecture for a normalizing refining tape should be deliberately simple. If the board cannot see the per-barrel story, it cannot govern it. Five categories matter:

1) **Safety**. Process safety events and incident rates - the leading indicator for downtime risk and license to operate.

2) **Reliability**. Utilization vs plan, unplanned downtime, and turnaround schedule integrity - the fastest ROI lever in the system.

3) **Capture**. Realized margin vs benchmark, crude differential capture, blending economics, and marketing/retail margin - where execution becomes dollars.

4) **Cash and capital**. Working capital, sustaining capex adherence, liquidity headroom, and payout discipline anchored to mid-cycle assumptions.

5) **Policy and compliance.** RIN/LCFS/credit sensitivities and mitigants treated as a risk register with guardrails, not a quarterly surprise.

SIGNPOSTS: WHAT CHANGES THE REGIME?

The following indicators, tracked consistently, will signal a shift in regime before earnings do:

- Export clearing weakening (especially PADD 3) with persistent inventory builds not explained by temporary run-ups.
- A sustained utilization downshift outside turnaround season (mid-80s or lower) signaling the system is no longer earning the right to run.
- Structural compression in heavy/sour differentials or reduced availability that erodes complex-kit advantage.
- A measurable step-change in policy economics or enforcement (RFS/waivers, LCFS, credit regimes) that alters baseline profitability.
- A cluster of operational incidents and extended outages indicating reliability regression across the system.
- Capital allocation drifting toward peak-cycle behavior: aggressive buybacks funded by leverage, or growth capex without downside-protected returns.

23.5 STRATEGIES PERSPECTIVE

Downstream businesses do not need more macro noise. They need clarity on where they sit in the constraint system, the discipline to treat reliability and capture as a per-barrel operating system, and a capital allocation framework built for mid-cycle reality.

23.5 Strategies works with operators, owners, and investors navigating exactly this environment - not as consultants delivering decks, but as operator-strategists who understand where value is trapped, where it is permanently impaired, and how to build repeatable advantage.

If this perspective is relevant to a situation you are navigating - a portfolio review, an operational turnaround, a capital program reset, or a transaction - we welcome the conversation.

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