MARKETWATCH FIRST TAKE

Shell, BP amaze the analysts

Commentary: Crude prices paper over old performance measurements

By MarketWatch
Last update: 2:46 p.m. EDT April 29, 2008

Shell, BP profits astound the analysts - MarketWatch

SAN FRANCISCO (MarketWatch) - On Tuesday, Europe's biggest oil companies, Royal Dutch Shell and BP, reported first-quarter profits built on the back of record-high crude prices.

Those profits were so astounding that not even the industry's top equities analysts saw them coming, which itself is astonishing, given all the ruckus surrounding oil prices. See full story.

Shell's (RDSA) earnings came in about 14% higher than analysts predicted, while BP (BP) topped estimates by a whopping 23%.

They managed this with only slim production increases and much weaker refining margins, demonstrating once again the beauty of purveying a nonrenewable resource.

In a world that constantly craves more petroleum, nothing looms on the horizon to threaten that trend. Despite the best efforts of those developing alternative technology and alternative fuels, it looks like the internal combustion engine will be with us in one form or another for decades to come. And the oil companies know it.

In the U.S., the biggest oil burner of them all, we continue to drive like a gallon of gas still costs a mere $2, even though it's now double that. Meanwhile, overseas demand is still growing briskly, led by the likes of China -- now the second biggest oil consumer -- as its 1.3 billion citizens flock to car dealerships in record numbers.

This unrelenting demand curve gives Shell and BP more breathing space. In the past, their ability to boost profits hinged on expanding output and defending market share.

But when the value of their primary product -- crude oil -- jumps nearly 70% in just a year, the pressure is off their exploration and production divisions. The cash flow from existing output keeps getting better and better, outpacing shrinking margins in refining and marketing, the other end of their business.

Analysts still fret about old performance metrics and are dismayed by slow growth output and poor refining margins. But they've been slow to adjust their calculators to account for the incredible jump in crude prices, which in turn accounts for their low-balling Big Oil profits.

Exxon Mobil (XOM) and Chevron (CVX) are reporting their quarterly results Thursday and Friday, respectively. They, too, are expected to turn in record-high profits that could well surge past analysts' expectations.

But once Wall Street has had a chance to crunch this latest batch of earnings reports, they should have a better idea of which numbers matter most when forecasting oil-company profits -- and catch up with the realities of selling a nonrenewable commodity in a global marketplace constantly clamoring for more.

-- Jim Jelter