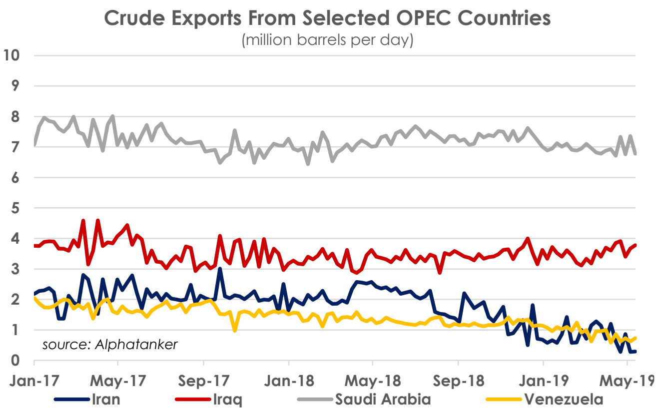
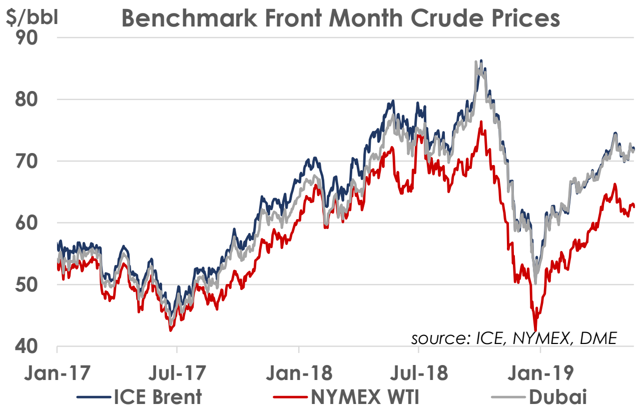
Tanker markets navigating treacherous geopolitical waters

The past few months have seen global geopolitical tensions soar to almost unprecedented levels as the US has flexed its muscles. This has seen shipping come under threat with Lloyds of London recently raising insurance risks for shipping in and around the Middle East Gulf. Accordingly, this week, we recap the major issues and the ripples which they are sending through oil and tanker markets.





Middle East tensions soaring. Tensions in the Middle East Gulf have reached boiling point over the past ten days as four commercial vessels were targeted off the Emirati port of Fujairah while the Saudi Arabian East – West crude oil pipeline was attacked by drones armed with explosives. Saudi and US officials have alleged Iranian involvement in both attacks. Indeed, Iran is at the centre of regional tensions as it finds itself increasingly backed into a corner as the US has attempted to cut off its revenue streams and strangle its economy by withdrawing waivers for buyers of its crude. Iran has subsequently stepped up rhetoric towards its immediate neighbours as it is becoming clear that they are now slipping in to take Iran's share of the global crude market. Indeed, preliminary data suggest that as Iranian exports have dropped from 1 mb/d to 0.3 mb/d over recent weeks, a number of Middle Eastern producers, notably Saudi Arabia and Iraq have stepped up supplies. Furthermore, this week Indian Oil Company (IOC) announced that it will import more Saudi Arabian crude in the second half of this year to make up for the loss of Iranian crude. Despite the slump in Iranian exports, our projections for Middle Eastern crude export volumes in 2H19 are that they will remain flat with 1H19 as regardless of OPEC's decision whether or not to extend supply cuts, we expect producers to continue to plug the hole vacated by Iran. However, when considering that NITCs represent 3.5% and 1.4% of world VLCC and Suezmax tonnage, respectively, their sanctioning should support spot rates going forward.

Shipping targeted. Of the four vessels which were attacked last week off Fujairah, three were tankers with two being Saudi Arabian-flagged Bahri tankers. This is an extremely worrying development for tanker markets as any attack so close to the strategically important Straits of Hormuz always raises fears of a disruption to flows out of the Middle East Gulf. Since the US announced stricter sanctions last year, Iran has repeatedly threatened to disrupt shipping in the Straits through which almost one third of global seaborne crude and products transit. Although we have previously discussed the impact of an attack on shipping in the Straits in detail (see *Alphatanker Weekly Newsletter* dated 12 July 2018 for more details), suffice to say that due to the immense volumes of oil which would be stranded in the Gulf, any disruption or blockage would be catastrophic for global tanker markets.

How safe is Saudi oil infrastructure? Considering that the Saudi East – West crude pipeline represents an alternative crude export route bypassing the Straits, an attack on this signals that there is no easy method of exporting crude out of the Middle East. Furthermore, this was the most significant attack on the Kingdom's oil infrastructure since the thwarted Al-Qaeda attack on the Alqaiq processing facility in 2006. Considering that the drones which attacked the pipeline are believed to have originated from Yemen, where Iranian-backed Houthi rebels are fighting government forces backed by Saudi Arabia and the UAE, this also places the safety of shipping in the Bab-el-Mandeb strait (through which 5.3 mb of oil passes daily) into question. Moreover, considering the reported 1000 km range of these drones, this also places an enormous quantity of Saudi oil infrastructure under threat. Although security has been increased at key installations since the Alqaiq attack, it is extremely difficult to protect pipelines and key installations from drone attacks with these able to evade radar due to their relatively small size. Finally, a significant potential threat to shipping is posed by a cyber-attack. Aramco's crude production, oil flows and tanker loadings are largely digitally controlled while security experts have highlighted that Iran is skilled in cyber warfare.

Venezuela spirals ever lower. As Venezuela continues to teeter on the brink of collapse, preliminary *Alphatanker* oil export data suggest that its crude exports slumped by a further 100 kb/d to average 0.75 mb/d in April (production totalled 0.85 mb/d) compared with 1.4 mb/d shipped to international markets one year earlier. This collapse has been driven by US sanctions imposed upon PDVSA. Moreover, less and less tanker owners are now willing for their vessels to call at Venezuelan ports. Indeed, as well as directly impacting exports, these constraints have also seen imports of clean products into Venezuela slump. In turn, this has hit naphtha supplies, which are used to dilute extra heavy Orinoco crude. When combined with the lack of willing tankers to transport the upgraded crude, this has led to reports that upgraded crude output has slumped to 170 kb/d over recent weeks. Product supplies in Venezuela are also being curbed by steadily declining refinery output with recent estimates suggesting that throughputs have slumped to around 100 kb/d, a tiny 6% of nameplate capacity. This has led to reports of long queues for gasoline (which continues to be heavily subsidised despite PDVSA's financial woes). All told, we expect the situation to get worse before it gets better with crude production steadily declining for the foreseeable future. Considering that there are a plethora of indications that May production will be significantly lower than April, supply could be below 500 kb/d by end-summer. On a positive note, as US refiners have halted Venezuelan crude purchases, flows have been diverted to India and China which has added tonne-miles. Despite pressure from the US, India continues to be a willing buyer of Venezuelan barrels and this has helped to support western Atlantic VLCC demand, and is likely to for as long as PDVSA can sustain production at levels which makes pulling together a 2 mb cargo relatively easy. However, Chinese flows could drop depending on whether Venezuela becomes a bargaining chip in its negotiations with the US.

Trade war steps up. On the oil demand side, the past fortnight has been dominated by another escalation in the trade war between the US and China. Firstly, the US increased tariffs from 10% to 25% on $200 billion worth of Chinese goods. In retaliation, China imposed higher tariffs on $60 billion of US goods. Included in this list was LNG, on which tariffs were hiked from 10% to 25%. However, crude oil was again omitted. Despite crude's exclusion, we project that Chinese imports of US crude will remain low for as long as the trade war rumbles on. Since it commenced last summer, China has cut its imports of US crude from an average of 350 kb/d over 1H18 to 70 kb/d so far this year. However, it should be noted that, despite the escalation in tariffs, delegations of the two countries are continuing negotiations towards a settlement. The largest fallout of a persistent trade war would be its impact on global oil demand. Indeed, following the latest escalation, we have shaved our estimate of global oil demand growth this year by 0.1 mb/d which suggests that demand growth will decelerate in 2019 compared with our previous estimate for it to remain flat. Indeed, at 1.1 mb/d, oil demand growth is now lower than the historical average over 2000-18. Evidently, any slowing of oil demand growth sends a bearish signal across both clean and dirty tanker markets.

This week's market pointers ↑↓

The past week has seen crude take renewed strength from geopolitical tensions and as senior officials continue to telegraph that OPEC will decide to continue to limit production at its next meeting. Nonetheless, there remains bearish sentiment coming from a potential slowdown in global economic growth in the wake of an ongoing US – China trade war and as US oil inventories continue to build. Accordingly, ICE Brent was last trading at $71.70/bbl while NYMEX WTI stood at $63.00/bbl.

Refinery maintenance update. Chinese refiners continue to return from maintenance which saw throughputs hit a record in April. Furthermore, considering the start-up of recent start-up of the 0.4 mb/d Hengli refinery, throughputs are set to smash records in May. Meanwhile, reports suggest that the 0.4 mb/d Zhejiang Petrochemical refinery started up on 20 May. Elsewhere in Asia, BCPCL will shut its 120 kb/d refinery in Thailand during July. In the US, refineries continue to exit maintenance as such the most recent EIA weekly data suggested that throughputs grew by 200 kb/on the week. In Europe, reports suggest that BP has shut a CDU its 400 kb/d Rotterdam refinery while Total has shut its 210 kb/d Leuna refinery due to the ongoing contamination issues surrounding the Druzhba pipeline. In Turkey, Tupras has completed maintenance at its Izmit refinery while Germany's 208 kb/d Schwedt plant and the 120 kb/d refinery in Bratislava both remain under maintenance. In Russia, turnarounds have been completed at the Perm and Ukhta facilities while the 240 kb/d Tuapse plant should come back online this quarter. Finally, Saras have announced that their Sarroch plant will undergo maintenance in 4Q19.

New refinery to be constructed in Fujairah. Brooge Petroleum and Gas Investment Co (BPGIC) will partner with Sahara Energy to construct a 250 kb/d refinery in the UAE bunkering hub of Fujairah. Reports suggest that it will be geared to producing compliant marine fuels and the first phase of the project will be completed by the end of 1Q20 while BPGIC will also increase their oil storage capacity at the hub.

IEA cuts oil demand forecast. In its most recent *Monthly Oil Market Report*, released last week, the IEA has shaved its forecast of oil demand growth to 1.3 mb/d this year. However, a similar revision was made to 2018 data and thus oil demand is still seen higher in 2019 versus 2018. The non-OECD is seen contributing 85% of growth in 2019. The Agency assesses global oil supply to have dropped by 0.3 mb/d month-on-month in April with losses from non-OPEC more-than-offsetting a 60 kb/d rise in OPEC crude production. Meanwhile, European refinery throughput is assessed to have fallen by 100 kb/d in the wake of disruption to flows through the Druzhba Pipeline and counter-seasonal crude draws pressured OECD oil inventories lower.

Field issues lowering North Sea exports. Reports suggest that flows of the UK's Flotta Blend crude have been shut in following a leaking valve at the Claymore platform. Meanwhile, Norwegian production is also being disrupted by shutdowns at the Oseberg and Statfjord facilities following separate technical issues. These outages have helped to support Dated Brent over recent days. *Alphatanker* data suggest that North Sea loadings fell by 160 kb/d week-on-week to average 1.2 mb/d in the week ending 17 May.

Houston Ship Channel reopens to two-way traffic. Following a spill 10 days ago which saw around 11,000 barrels of gasoline enter the channel, one-way traffic restrictions were put in place which saw delays to transit the channel soar. These restrictions were relaxed after four days and by the time of writing, Alphatanker data indicate that 31 tankers were waiting to enter the channel, a fall on the 41 tankers one week earlier.

Panama Canal restricts draft levels again. Following the persistent low water levels dry to a dryer-than-usual 'dry' season, the Panama Canal Authority has reduced the maximum draft of vessels transiting the neopanamax locks to 43 ft while the panama locks remains at 38.5 ft. At the start of this year the restriction at the neopanamax locks was 50 ft.

Eight new demolition yards set to be added to EU's list of approved recycling yards. The European Commission has announced that 8 new yards will be added to their approved list over the coming weeks. Although the individual facilities have not yet been disclosed, they are expected to be located in Denmark, Norway and Turkey and not include any in the Indian subcontinent where the vast majority of deep sea tanker demolitions take place.

MEPC completes IMO2020 guidelines. The 74th session of the IMO's Marine Environment Protection Committee completed a comprehensive set of guidelines concerning the practical implementation and enforcement of the 0.5% sulphur cap. These include guidelines for ports and fuel sampling and are subject to approval at the IMO's June meeting.

Seaborne Crude Exports[1] for Selected Countries for week ending 17 May 2019 Million barrels per day				
	12-month rolling average	4-week rolling average	latest week (17 May)	change from previous week
Algeria	0.41	0.48	0.39	0.10
Angola	1.31	1.43	1.41	0.30
Gabon	0.18	0.17	0.14	-0.14
Iran	1.37	0.47	0.28	-0.28
Iraq	3.46	3.69	3.67	0.11
Kuwait	1.90	2.00	1.85	0.57
Libya	0.76	1.07	1.08	0.19
Nigeria	1.94	1.87	1.77	-0.19
Qatar	0.64	0.71	0.72	-0.03
Saudi Arabia	7.21	7.06	7.36	-0.58
UAE	1.98	2.27	2.09	0.34
Venezuela	1.11	0.68	0.62	0.11
Azerbaijan[2]	0.79	0.73	0.67	0.01
Kazakhstan[3]	1.15	1.13	1.21	-0.16
Russia[4]	3.41	3.41	3.39	0.18
Oman	0.82	0.85	0.90	-0.01
Sudan	0.12	0.15	0.14	-0.14
Brazil	1.19	1.08	0.95	0.07
Colombia	0.44	0.60	0.54	0.16
Mexico	1.10	1.09	1.41	-0.49
Canada[5]	0.24	0.24	0.29	-0.16
US	2.21	2.69	3.22	-0.33
North Sea[6]	1.03	1.12	1.19	-0.16

Source: Alphatanker

[1] does not include pipeline flows

[2] adjusted for Turkmenistan re-exports

[3] does not include volumes exported via the Atasu - Alashankou pipeline, includes volumes exported via Russian ports

[4] does not include volumes exported via the Druzhba or Daqing ESPO Spur pipelines

[5] Does not include volumes re-exported via US ports

[5] Only includes volumes exported outside of UK or Norway

Oil counted as exported when a vessel exits national territorial waters, includes volumes built on vessels over previous weeks

Data are subject to revision

Latest Crude, Refined Product and Bunker Prices and Freight Rates