



# PORTLAND MARKET REPORT

## February update

It says something about the current oil market that the conflagration between Saudi Arabia and Iran at the beginning of the year, generated little more than a slight upward blip in prices. Ditto the muted market reaction to an apparent hydrogen bomb test by comedy Teletubby leader of North Korea, Kim Jong-un. As recently as 2013, these kind of events would have sent prices sky-rocketing. But such is the current level of over-supply in the oil markets that prices only momentarily headed up, before continuing their relentless drive downwards. The only clear conclusion can be that – however bad things are in the world – geo-political concerns are very much playing second fiddle to the basic dynamics of supply and demand.

The current over supply situation has been well documented; fracked oil flooding US markets, OPEC refusing to cut production in an attempt to maintain market share and now, Iran's bounteous harvest of oil (4th largest producer in the world) ready to overwhelm the market further. But at the same time, we now have a concurrent narrative around slackening demand. In the past, Portland has taken a fairly sanguine view of this supposed reduction in global oil demand – preferring to call it a slow-down in demand growth rather than an actual reduction in consumption. But now with China's economy potentially going into (minor?) meltdown, can we be so confident that demand will hold up? The markets would seem to suggest not, with each month heralding another unceremonious breaching of another "agreed minimum price for oil".

**\$10 PER BARREL?  
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\$50...\$40...\$30... Each "price floor" has been swept aside and we are now getting to the point where we might have to accept Goldman Sachs' \$20 per barrel prediction after all. In fact, the odds on even more outlandish predictions (\$10 from Standard Chartered) are shortening by the day. Maybe we are heading back to the 1990s, when crude prices largely stayed below \$20 and even dropped as low as \$7 in 1997! And do bear in mind that nobody was walking around in 1997, head in hands, thinking that \$7 was the end of the world. It was just the norm and the refineries kept refining, the pipelines kept flowing and the petrol stations kept pumping....

**JANUARY 2016 SAW A  
RECORD AMOUNT OF  
OIL IMPORTED INTO  
CHINESE PORTS – AND  
"ONLY" 6% GDP GROWTH  
MEANS CHINA WILL STILL  
CREATE AN ECONOMY  
THE SIZE OF POLAND  
OVER THE NEXT 12  
MONTHS!**

But whilst at the current juncture, \$20 a barrel now seems a distinct possibility, 2016 is certainly not 1997. Firstly, the world has 1.5bn more people (!) to feed, heat and transport. And if demand is looking a little more patchy, it is still growing – and most definitely growing in China. OK, the Chinese Stock Market seems to be collapsing under the weight of its own unsustainable expectations (and may well be a harbinger of future economic problems), but these factors seem unlikely to affect current oil consumption. In fact, January 2016 saw a record amount of oil imported into Chinese ports and anyway, "only" 6% GDP growth means that China will still create an economy the size of Poland over the next 12 months! Plus, there's the actions of the China's Oil Stocking Agency to take into consideration. This Government body is busily seizing the

moment and buying as much low-priced oil as possible. It has already acknowledged its desire to increase the national stock holding to 90 days of reserves (in line with countries in the EU and IEA = International Energy Agency) and although accurate data is difficult to come by, most estimates put current Chinese stock reserves at between 20 and 30 days. That leaves circa 65 "days" of oil to purchase and based on daily consumption (circa 1.5bn litres), that's 100bn litres of incremental demand. A reasonable amount by any standards...

There is also a supply related reason why prices may not hit \$20 and even if they do, will certainly not stay there for very long. When we talk about crude being at \$20 a barrel, we are in fact talking about the benchmark crudes of Brent and WTI (West Texas Intermediate). But these grades make up only a small percentage of the crude oil sold around the world. The vast majority of crude oil is sold at a discount to these two grades. So when we talk about \$20 a barrel, "light-tight oil" from the fracking heartlands of the USA for example is actually selling at a discount of up to \$5 versus these benchmarks – such is the tricky, truck-based logistics required to deliver fracked oil to US Gulf Coast refineries. And God Forbid you are producing sour crudes from the Canadian Oil Sands. Here the quality give-away is huge (lower quality crude means refineries have to work harder to process cleaner refined products), such that in January, Canadian Oil Sands actually fell below \$10 per barrel.... ouch!

Such rock bottom prices are of course not sustainable and the sands of time must be running out for oil producers at these low value levels. So put simply, something has to give. Whether it will be OPEC introducing strict production quotas or perhaps that independent oil producers will not be able to hang on any longer. Or maybe oil buyers will conclude that demand is not so weak after all. One way or another, these super low oil prices will not last and a level around the \$40-\$50 mark, seems likely by the end of this year.



For more pricing information, see page 22

Portland Fuel Price Protection  
[www.portland-fuel-price-protection.com](http://www.portland-fuel-price-protection.com)