PORTLAND MARKET REPORT

JULY IN VIEW

THE OIL WORLD WAS TAKEN BY SURPRISE IN JULY BY AN UNEXEPCTED PORTFOLIO ANNOUNCEMENT FROM BP

In July, BP made the shock announcement that they would be completely exiting the Petrochemicals market. For a cool $5bn, they would sell their global business lock, stock and barrel to Ineos (part-owners of Grangemouth Refinery), who now have responsibility for 14 petrochemical refineries, manufacturing 10m tonnes of petrochem products each year. Even with a pandemic raging, the petrochemicals sector remains buoyant and with a very significant track record in chemicals, BP's move definitely took the oil world by surprise.

Petrochemicals have always sat in an odd place when it comes to the oil industry. Yes, they come from crude oil and yes they are made in the same way (refining, cracking and steam reforming) as other oil products. But their usage and consumption is entirely different and infinitely more complicated than bog-standard petrol and diesel. After all, the latter are simply combusted for their energy content, making them the ultimate "one trick ponies". Petrochemicals on the other hand are virtuoso multi-instrumentalists that can turn their hand to anything. Propylene makes paints and packaging. Ethylene gets stuck into adhesives and detergents. Benzene operates in pharmaceuticals and medicines, at the same time that toluene colours our world with inks and dyes. Butadiene gets a bounce from making tyres and ammonia has really grown into its role as a fertiliser component. And whilst paraxylene wants to have airs and graces because of its high-tech work in computers and solar panels, most of us can't see beyond the plastic bags.

Global growth in the chemicals sector is predicted to be 5% year on year for the next 10 years, as increases in the world's population support product demand. The impact this will have on the oil industry is illustrated by the fact that the International Energy Agency predicts that 50% of the corresponding growth in oil demand will be generated by petrochemical production. Much of the affinity that oil company executives have for petrochemicals is because the steady, rateable revenues generated by the likes of plastic, provide a natural hedge against the crazy volatility provided by commoditised transport fuels. This has never been more true than today, where low oil prices are being offset by booming demand for single use plastics – be that for medical PPE, hand sanitisers or new "Covid-safe" workspaces. Remember also that low oil prices are good news for petrochemical refiners, because low feedstock costs (cheap oil) means higher sales margins on the end-product.

On top of all these very positive commercial factors, the petrochemical sector has the added benefit of being at the greener end of the oil industry. Granted, that may be difficult to believe when you drive up the A19 past Middlesbrough, and CO2 is of course emitted in the production of petrochemicals.

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But once the products are produced, they become "permanent", rather than simply being combusted, as is the case with transport fuels. The result means there is no double-whammy effect of duplicated CO2 emissions and furthermore, it is infinitely easier to limit, re-use or sequestrate gaseous discharges from a refinery, than it is to control emissions from individual transport vehicles.

All of this explains why the chemicals industry (up until now including BP) are currently investing around $50bn annually into capacity upgrades. Compare this to the current moribund investment levels for oil exploration or look at the likes of Saudi Aramco, who have splashed a whopping $70bn on SABIC (a huge and sprawling Saudi chemicals corporation), in an attempt to diversify away from their bog-standard crude oil operations. This massive investment has also been (almost) matched by the Abu Dhabi National Oil Company – another oil producer looking to diversify – who has just invested $45bn into its own petrochemical expansion.

50% OF THE CORRESPONDING GROWTH IN OIL DEMAND WILL BE GENERATED BY PETROCHEMICAL PRODUCTION

Why then has BP decided to sell a very profitable part of its portfolio, with (some) green credentials and operating in a buoyant marketplace? The official line is that BP Chemicals was not sufficiently integrated into the rest of BP, whilst those of a cynical nature believe that because of low oil prices, BP needed a cash boost to support their balance sheet. There may be some truth in both these suggestions, although BP has faced enough crises in its time to weather this particular storm, and as for non-integrated parts of the business, that's hardly unusual for a global oil major. What seems most likely is that new BP CEO Bernard Looney (wanting to make his mark?) concluded that with profits and product demand high, there wouldn't be a better time to sell the petrochemicals division and that potential suitors would be happy to pay top dollar. If that is the case, then it looks like we have quite a wheeler-dealer sitting at the top of the oil industry. What will be next?

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