PORTLAND MARKET REPORT

DECEMBER IN VIEW

IS THIS REALLY THE END OF THE ROAD FOR GRANGEMOUTH REFINERY?

November's announcement by Petroineos to close their Grangemouth oil refinery in 2025 not only took the industry by surprise, but it simultaneously blindsided both the UK and Scottish Governments. The closure of a core industrial asset and the country's only North Sea fed refinery is indeed big news, but it is also a commercially surprising decision. With refinery margins at unprecedented highs, and with most oil majors clamouring to increase – not close down – their refining capacity, the decision is not an easy one to understand.

Grangemouth is owned as a 50 / 50 Joint Venture between the Chemicals company Ineos (owned by Britain's richest man, and new Man Utd shareholder, Jim Ratcliffe) and the state-owned Chinese oil company, PetroChina. The official closure announcement cited the infeasibility of continued operations at Grangemouth due to the pressures of refining over-capacity in North-West Europe coupled with the future decline in demand for road fuels (due to vehicle electrification). Neither of these reasons entirely stack up. It is definitely true to say that in recent times, there has been refining over-capacity in Europe, but if that was the case today, why would margins now be at record highs? Moreover, whilst long-term demand decline for road fuels is inevitable, the tail on this one will be a long one and Grangemouth's captive markets of Scotland and Northern England, actually make the Scottish refinery better suited than most to deal with this issue.

Built in 1924 by Scottish Oils (a pre-cursor company to what became BP), Grangemouth has long been one of the UK's core oil processing plants. Up until 1975, crude oil from the Middle East was imported by ship, but the discovery of North Sea Oil brought about the commissioning of the Forties pipeline, which brought North Sea oil direct to the refinery. In the early days of operations, pipeline supply offered Grangemouth a distinct advantage over other UK refineries. Whilst the latter were open to the vagaries of supply reliability, shipping markets and inconsistent product quality, Grangemouth enjoyed total supply resilience from constant, high grade, sweet crude oil from the North Sea. Fast forward 50 years though and these advantages have diminished. In fact, the over reliance on North Sea crude has limited the ability of the refinery to process lower quality, non-North Sea crudes which, crucially, cost less. In effect, Grangemouth is designed around only processing sweet crudes from the North Sea and this leads to a much greater problem. In the face of increased public opposition to North Sea oil, legislative changes and oil field maturity, why would you want a refinery in Grangemouth, when there may be no more North Sea oil in the next 10-20 years?

> "IS IT POSSIBLE THEN THAT THE CLOSURE ANNOUNCEMENT IS PART OF A POLITICAL GAME?"

In this light, it would seem reasonable for the refinery to start the process of diversifying its facilities, but this still isn't the same as closing manufacturing down entirely. So, what other factors might be at play? Well first, Grangemouth has traditionally had a strongly unionised and, occasionally, militant workforce. On two separate previous occasions (in 2013 and 2018), Jim Ratcliffe has publicly threatened to shut Grangemouth down, unless the unions accepted management working proposals. Possibly as a result of this confrontational behaviour, the site has often found itself squaring up to a devolved government in Edinburgh that, in turn, has handled the relationship in a frankly cack-handed manner. Taking their playbook straight out of the 6th Form Debating Club (and egged on by their junior partners in Government from the Green Party), the refinery has been consistently demonised for its high carbon legacy whilst, at the same time, constantly shifting environmental targets have deeply frustrated the Chinese JV partners.

Is it possible then that the closure announcement is part of a political game of poker aimed at the Unions (to change working practices), the Scottish Administration (to generally back-off!) and the UK Government (to ensure further North Sea Oil licenses are granted)? When Portland started in the oil industry in the early 1990s the UK had twelve refineries – now there are six. Whilst consecutive UK Governments have largely taken a laissez-faire position on these closures, the removal of Grangemouth might generate a different reaction. Unofficially, there is a blueprint for UK refining that focuses on basic geographic coverage, whereby core refining facilities in the North (Grangemouth), the East (Humber), the South (Fawley) and the West (e.g., Pembroke) provide sufficient coverage. But, take out a core asset, particularly one so wedded to the domestic market (60% of Grangemouth production is gasoline, diesel and jet fuel for UK consumption) and that is an altogether different story.

It would, therefore, be a surprise if the proposed closure of Grangemouth is not causing significant concern to the newly created Department for Energy Security and Net Zero. On that basis, and despite the announcement, we see a full closure of the refinery as unlikely. Next door is the Grangemouth petrochemical site, which is wholly owned by Ineos and, notably, there has been no suggestion that this plant will close. It makes little commercial sense to terminate manufacturing at an adjacent oil facility, that shares both feedstocks and processes, and definitely not when refinery margins are so healthy. And, if PetroIneos really is serious about closing, then do not be surprised if the UK or Scottish Government steps in to keep the place running. The refinery itself has been under state control several times in the past (Anglo-Persian, the war years, ShellMex-BP) and, by 2025, we will almost certainly have a new government in place, who may take a very different view on the nationalisation of core industries…

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