POTEN TANKER OPINION

Will Naphtha Keep Cracking?

Naphtha has been a key driver for the LR product trades

Naphtha refers to a range of volatile and flammable liquids produced by the distillation of petroleum. The liquids have various uses, including as components of gasoline and kerosene. Naphtha is also widely used as a solvent. However, one of the key uses of naphtha is as a feedstock for the manufacture of olefins by the petrochemical industry. In this opinion piece we discuss some of the main trade flows and prospects that impact this important commodity for long-range product tankers.

Worldwide naphtha demand and tradeflows are closely tied to the petrochemical industry. Most petrochemicals are made from naphtha (70-75%) while the rest is made from ethane and propane. Olefins (ethylene, propylene and butadiene) make up 90% of the petrochemical production, and are the building blocks to almost all other petrochemicals and polymers. These petrochemicals are commodity products, making this market cost-driven and very price sensitive.

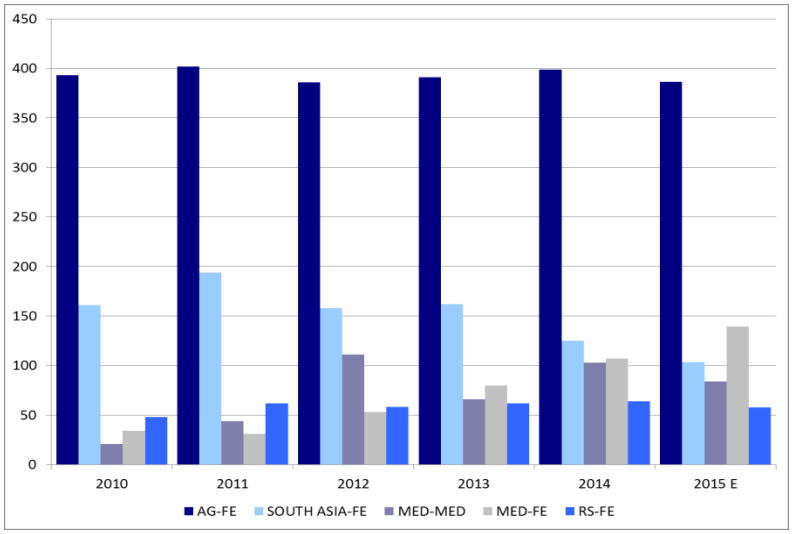
The large trading companies have a prominent position in the naphtha business. The top charterers include many of the well-known commodity traders, such as Vitol, Glencore, Trafigura and Clearlake. Given that Asia is the key trading area for this commodity, it is not surprising to find the large Japanese trading houses, like Marubeni, Itochu and Idemitsu on the list as well.

Traditionally, the seaborne naphtha trade has been dominated by movements to the Far East. By far the biggest route is the one from the Arabian Gulf to the Far East. In the period 2010 – 2015 to date, Poten recorded 2,132 fixtures on this route; almost triple the volume on the next largest trade route: South Asia (India) – Far East. The remaining trades are significantly smaller still. Figure 1 shows the continued domination of the AG – East naphtha trade. Due to the nature of this trade (long-haul, high volume) and because the port and terminal infrastructure in both the load and discharge areas can accommodate large vessels, these trades are largely done on the larger product carriers, the LR2 and LR1 vessels. In recent years we have even seen occasional Suezmax sized (LR3) cargoes originating from the Middle East. Naphtha movements outside the Far East, such as the trades in the Mediterranean and across the Atlantic are still done predominantly on MR product tankers.

The Middle East is expected to remain a significant source of naphtha over the next five years. Over the past decade, Middle East oil producers have increasingly invested directly in emerging markets; some of these investments are in petrochemicals. Such moves are designed to assure outlets for these Middle Eastern countries' hydrocarbons in the markets that remain the key drivers of oil-consumption growth. Expansion of the domestic petrochemical sector is also an important instrument for growth since the Middle East sits on immense reserves of oil and gas.

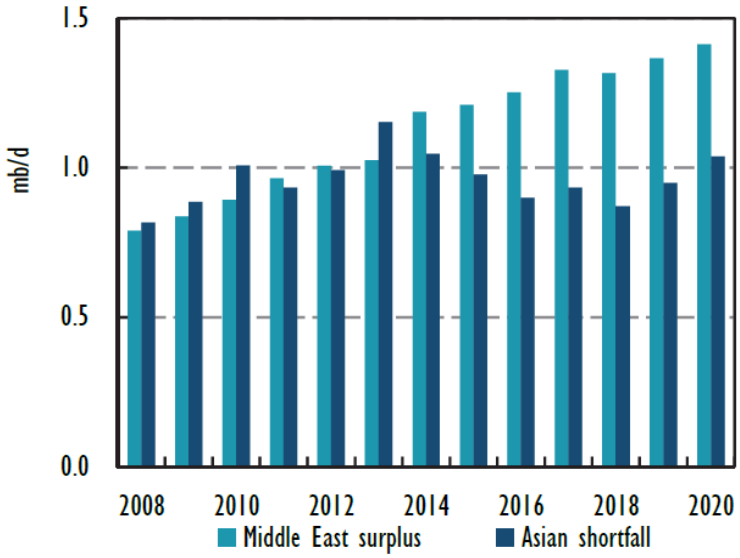
The IEA forecasts that Asian demand growth will slow and that the region's shortfall of naphtha will decline over the coming years before recovering later during the period. While the producers in the Arabian Gulf are the cheapest producers of and will likely maintain their market share, it may (temporarily) limit the growth potential for product carriers in other long-range trades.

Fig. 1: Main naphtha trade flows



Source: EIA

Fig. 2: Forecasted Asian naphtha balances



Source: IEA