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POTEN TANKER OPINION

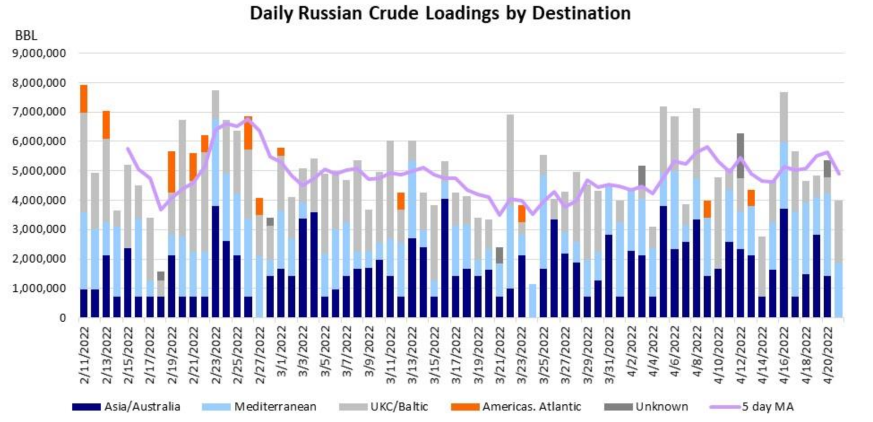
The Great Reshuffle

Trade flows around Russian crude oil exports are changing

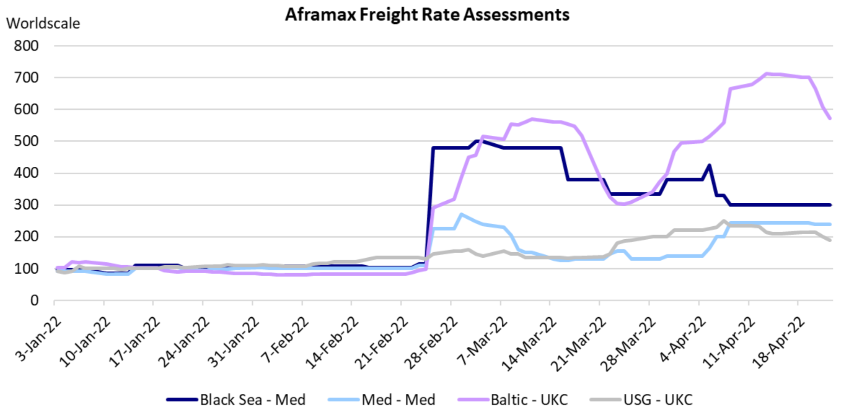
On 24 February 2022, Russia invaded Ukraine. This triggered widespread condemnation and a broad range of sanctions. Western countries in particular have been targeting Russia's financial institutions, the country's oligarchs, and the Russian energy industry. This has created turmoil in the oil and tanker markets. Initially, oil prices and tanker rates spiked as the markets scrambled to adjust. However, now that we are two months into the conflict, things are settling down somewhat and we are seeing some trends developing.

There seems to be a disconnect between Russian crude oil production and seaborne exports. Various sources have indicated that Russian production in March was down to 10.6 million barrels per day (Mb/d), which would be the lowest level since September 2021. A number of oil market forecasters expect April production to fall by an additional 1-1.5 Mb/d, as Russia may struggle to maintain clients. The Russian Deputy Prime Minister Alexander Novak said that the declines in oil production are related to "changes in logistics and financing". While production is declining, seaborne exports seem to be holding up quite well (see figure 1). Around the time of the invasion, Russian crude oil exports peaked at around 7 Mb/d. Since then volumes have averaged slightly below 5 Mb/d. The chart shows that daily volumes are quite volatile, but it is difficult to detect a clear downward trend so far.

Anecdotal information seems to suggest that more Russian oil is moving to Asia and less to Europe and the U.S. The U.S. has indeed banned crude oil from Russia, but Europe remains an important customer. The European countries are much more dependent on Russian oil and it will take time to find replacement barrels. The expectation is that by the end of the year, very little Russian crude will be sold in Europe. This means that Russian producers will have to sell more crude oil into other regions, primarily Asia. India has been buying more crude from Russia in recent months, primarily from the Black Sea but occasionally also from the Baltic. China has always been a large customer, but it has not increased its purchases significantly since the start of the Russia – Ukraine conflict. However, this has probably more to do with the recent Covid outbreaks in China that have caused widespread lockdowns and a noticeable slowdown in oil demand. Once China gets on top of the pandemic and/or relaxes its zero-covid policy, we expect Chinese demand for Russian crude to increase, especially at the current discounted prices. Another factor that could drive more Russian oil away from the Atlantic Basin and into the Pacific is the expiration of the supply contracts from Western refiners and traders. This is expected to happen in the next few weeks/months.



Source: Lloyd's List Intelligence



Source: Poten & Partners

The conflict has had multiple implications for the tanker market. Initially, rates moved up sharply, especially for Aframaxes and Suezmaxes serving the Baltic and Black Sea areas. As the situation was very fluid in the early weeks and new sanctions were announced almost daily, very few owners were willing to take the risk of loading in a Russian port. The ones that did were able to extract a huge premium. Since then, the situation has normalized somewhat. Some owners, mainly the ones that are publicly listed, continue to self-sanction. Many others are increasingly willing to take some reputational risk to be able to take advantage of a premium voyage. Not surprisingly, since owners have lived through dismal markets since the collapse of tanker rates in mid-2020.

The main beneficiary of the conflict seems to be the Aframax segment. They are the vessel of choice for exports from the Baltic and play a major role in the Black Sea trades as well. Sanctions against Russian owners have also disproportionately affected Aframaxes. Owners like Sovcomflot have a significant presence in the Aframax and Suezmax markets, while their participation in the VLCC segment is negligible. Russian owned tonnage is hard to trade now and this has contributed to a tight Aframax market. Aframaxes are also increasingly used for transatlantic U.S. crude oil exports (which have reached record highs recently) and for reverse lightering. Eventually new (more efficient) trading patterns will develop that will likely boost Suezmax and VLCC employment, but for the moment Aframaxes are enjoying their day in the sun.