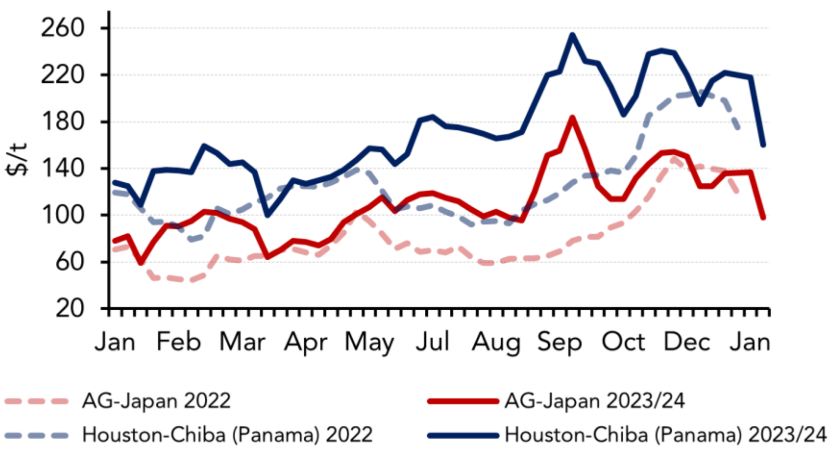
Freight Tumbles on Narrowing Arbs

Many ships including very large gas carriers (VLGCs) are avoiding the Suez Canal following reports that several ships are being attacked by Iranian-backed Houthi small boats while transiting the canal, adding further uncertainty to the shipping sector since mid-December.

Around late-December, a container ship issued distress calls twice after being hit by a projectile in one day and then attacked by four small boats attempting to board the vessel the following day.

Weekly Spot VLGC Rates



A multinational naval coalition is providing safeguards but there are daily reports of attempted attacks and hijacking. As a result, many VLGCs are opting to ballast back to the US Gulf Coast from the Far East around the Cape of Good Hope (COGH) instead of going through the Suez Canal.

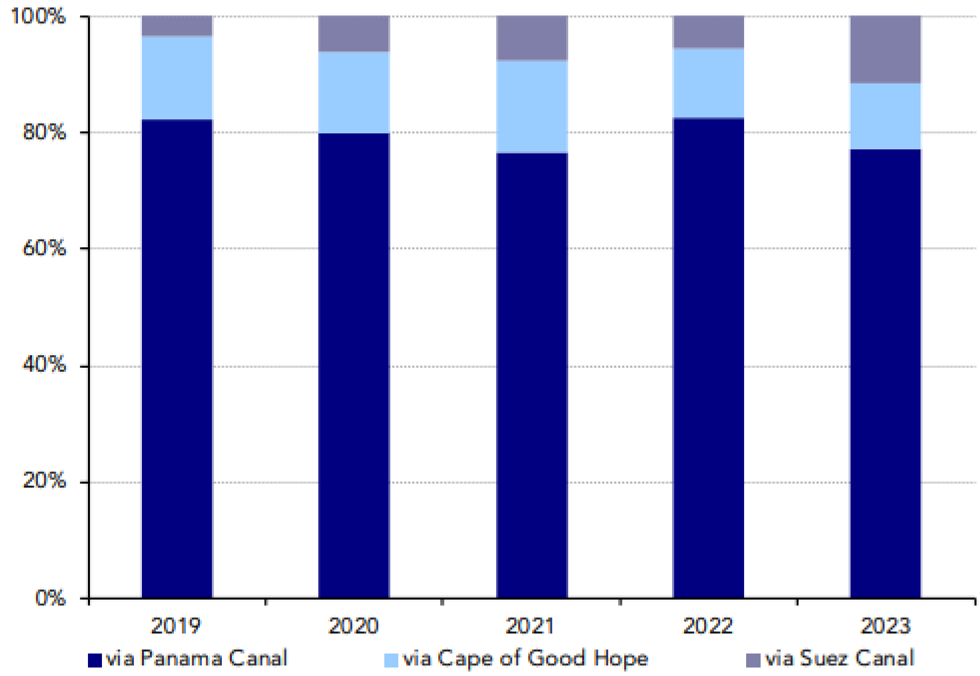
Going around the COGH instead of the Suez Canal can add four to seven additional days to reach the USGC. This has tightened the freight market, which has already been constrained due to the Panama Canal restrictions.

VLGC freight rates were trending down since mid-November but reversed course with the Houston to Chiba via Panama rate trading around $220/t in early January compared to $195/t before the Suez Canal disruption started. Ras Tanura to Chiba rates increased by around $10/t during that period to $135/t.

Meanwhile, the CFR Far East propane prices have been trending down since the start of the new year which has significantly narrowed the arbitrage between the US and the Far East; traders are staying away from buying spot cargoes from the US.

VLGC spot rates fell sharply in the second week of January with the Houston to Chiba via Panama tumbling to $160/t. Some market players turned bearish on freight rates as a result of the tightening arb and amid a lack of deals.

US VLGC Liftings for East of Suez Discharge



Source: Poten, Shiptracking data

Despite the Panama and Suez disruptions, propane prices in the Far East did not experience any sharp increase due to both lackluster demand from the petrochemical sector and several VLGCs managing to reserve southbound slots at a relatively lower cost in recent weeks, indicating supply will be ample in the region in coming months.

Meanwhile, weak petrochemical margins and ongoing disruptions could limit consumption from the petrochemical sector. Additionally, Iranian LPG exports which are estimated at around 9.5 MMt, are expected to further increase in 2024 with higher gas plant production, which could also limit incremental imports from the US. Overall PDH operating rates in China have been hovering around 60% in recent weeks and are expected to remain around that level through February.

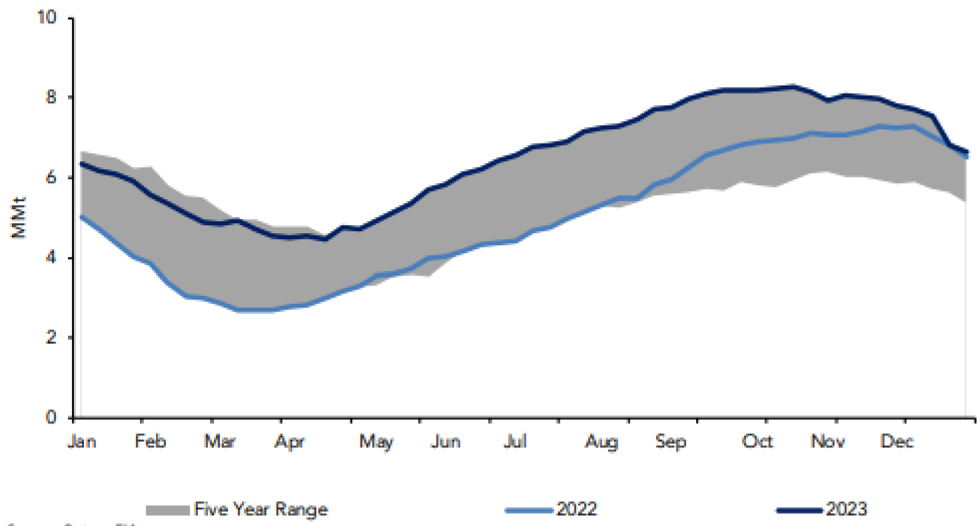
Chinese manufacturing activity historically slows down for several weeks around the Chinese New Year celebration. This year, the new year will be celebrated from Feb. 10 to Feb 17. This should also keep the country's supply/demand balance long in 1Q 2024. It is still uncertain if the lower Far East propane price will increase buying interests from PDH.

The earthquake in Japan affected parts of the country that are mostly not connected to city gas networks and which normally consume LPG for heating during the winter. There are expectations that winter demand could be lower than normal in those regions.

An increasing volume of US exports have been heading to Northwest Europe since the Panama Canal reduced the number of available transits. With the ongoing drought at the Panama Canal and now with the Red Sea disruptions, this trend is expected to continue.

As a result, the Europe and Mediterranean region is expected to be well supplied in the coming months – driving some recovery in LPG intake from regional mixedfeed crackers, which fell sharply in November from the previous month. LPG intake from mixed crackers increased 14.5% in December from the previous month to an estimated 420,000 t, according to OPIS.

US Weekly Propane/Propylene Storage



Source: Poten, EIA

The propane-naphtha spreads averaged about -$134/t in November and -$136/t in December and forward prices indicate the spread will remain well above -$100/t through 3Q 2024 falling below -$100/t in 4Q 2024 but are still favorable. US propane inventories finished 2023 at 82.6 MMbbls, just 2% higher than a year before. Propane inventories at the beginning of 4Q 2023 were 20% higher than the previous year.

There was a 9 MMbbl reduction in inventories in the week ending Dec 22 – surprising the market – as exports were steady and domestic demand was lower than normal. However, the EIA explained that the PADD 2 propane/propylene stocks were overstated in the Nov. 15, 2023, through Dec. 20, 2023, publications. The sharp reduction was due to necessary corrections.

The sharp decline did not lend much support to Mont Belvieu prices and the arbitrage for US exports remains open. However, the growth in US exports for 2024 will be lower than previous projections which were made under the assumptions of high inventories and amid limited spare export terminal capacity.