

## A mixed bag for refined products

Refined products have had a strong year due to recovering demand and falling inventories. We expect that refinery margins will trend higher over 2022 as demand continues to recover. However, Covid-19 related restrictions are a risk to this view, particularly for jet fuel. Here is how we see products performing over 2022



Demand for refined products is increasing but Covid remains a downside risk especially for jet fuel

### Naphtha strength unlikely to last

The naphtha market has been strong for much of 2H21, with the prompt crack in NW Europe remaining in positive territory over the whole period. The naphtha market has been well supported by the strength that we have seen in the propane market, which in turn has been supported by the tight natural gas market.

Strong natural gas prices have meant that we would have seen some switching to LPG, which would have provided a boost to prices. The strength in the propane market meant that for large parts of the year propane has traded at a premium to naphtha, pushing those in the petrochemical industry with the flexibility to use naphtha as a feedstock. While spot propane prices have more recently moved back to a discount to naphtha, propane is still more than 90% of the naphtha price, which suggests that naphtha is still the likely preferred feedstock.

However, we would expect propane's discount to naphtha to widen as we move out of the

Northern hemisphere winter, which is in line with seasonal norms. This should remove some of the support that we have seen naphtha receive in recent months.

In addition, assuming we do not see any significant demand hits due to the Omicron variant, we expect that refinery run rates will continue to trend higher over the course of 2022 in order to meet broader oil demand growth. This suggests that naphtha supply will improve next year which should see NW Europe cracks return to negative territory.

We are currently forecasting that the NW European naphtha crack will average negative US\$2/bbl over 2022, compared to being basically flat this year.

## Limited upside for gasoline

While we expect the gasoline market to be well supported through 2022, we believe that upside relative to middle distillates will be more limited. The bulk of the demand recovery in gasoline has already occurred this year, suggesting that demand growth will be more limited next. For example, in the US, implied gasoline demand is basically already back at pre-Covid levels, with implied demand averaging almost 9.4MMbbls/d over 2H21, this compares to around 9.48MMbbls/d over the same period in 2019.

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### *Gasoline inventories are still low in most regions*

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Gasoline inventories are still low in most regions. In the US, stocks are at a 5-year low currently, whilst in NW Europe and Singapore, inventories are below the 5-year average. This should help to put a floor under gasoline cracks. What has helped to tighten up the gasoline market this year, particularly in the US, has been several supply disruptions coupled with rebounding demand.

With peak seasonal demand now behind us, we would expect gasoline inventories to start building which should cap the gasoline crack. We currently forecast that the Eurobob crack will average around US\$11/bbl in 2022, compared to an estimated US\$9/bbl in 2021.

## Middle distillates to be supported by jet recovery

The gasoil market still has further room to strengthen over 2022; this assumes that we do not see further tightening of Covid restrictions. Middle distillate inventories are below the 5-year averages in the US, NW Europe and Singapore. In fact, in NW Europe and Singapore inventories are at least at a 5-year low, while in the US they are not too far off from the 5-year low.

China has been a supportive factor for the gasoil market for much of this year. 2021 is shaping up to be the second consecutive year of YoY declines in gasoil exports. Lower flows last year were understandable given Covid-19. However, the lower exports this year reflect a tighter domestic products market in China and reduced export quotas for products. The tighter market has been partly due to consumption tax changes in the domestic market which has led to a fall in light cycle oil imports into China, which is used to blend into gasoil.

The Chinese market will likely be less supportive going into 2022. Refiners in the country have ramped up output to shore up domestic supply and as a result, we will likely start to see exports of

gasoil picking up as well as more product becomes available. However, whilst there is upside from the low levels seen in 2021, it's unlikely we'll see a return to export levels prior to Covid due to policy shifts.

Regardless, middle distillates should be relatively well supported through the winter, particularly given the tightness that we are seeing in other energy markets, which would lead to some switching. A continued recovery in international air travel in 2022 should provide further upside to the jet fuel market, which in turn should drag the gasoil market higher. Total global air travel is still down significantly. The latest numbers from IATA show that revenue passenger kilometres in October 2021 were still down by more than 49% from 2019 levels.

A combination of a further recovery in middle distillates' demand along with entering the new year with low inventories suggests that cracks will edge higher in 2022. We estimate that the ICE gasoil crack will average US\$13/bbl next year compared to around US\$8/bbl this year. Key downside risks will be Covid continuing to hold a grip on international air travel and Chinese gasoil export volumes returning to pre-Covid levels.

**ING forecasts**

	1Q22	2Q22	3Q22	4Q22	FY22
NWE Naphtha crack (\$/bbl)	1	-2	-4	-2	-2
Eurobob crack (\$/bbl)	9	11	12	11	11
ICE Gasoil crack (\$/bbl)	12	11	14	14	13

Source: ING Research

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