

The Commodities Feed: Druzhba pipeline concerns

Your daily roundup of commodities news and ING views



Source: Shutterstock

Energy

Quite a bit which has changed in the oil market over the past two weeks. Two weeks ago sentiment was fairly negative, given the continued demand concerns. This negative sentiment appears to have only intensified, with Brent last week trading to as low as US\$92.78/bbl- its lowest levels since February and Russia's invasion of Ukraine. However, what is noticeably different from the flat price weakness seen in June and early July compared to early August is that previously the timespreads held up relatively well. This time around, the weakness in the flat price has been accompanied by weakness in the timespreads. While the forward curve is still in backwardation, it certainly isn't as wide as it was a month or so ago. In addition, refinery margins, whilst historically still high, have come off considerably from their highs seen in June.

On the supply side, several factors have helped. Libya appears to be seeing a recovery in supply following months of disruptions. There will be question marks around how reliable Libyan supply will be in the months ahead. In addition, there could also be a breakthrough in Iranian nuclear talks. The EU has submitted its final draft for a deal, which will need to be approved by the US and Iran. If approved, this would open the door for an increase in Iranian oil exports. This is a big "if". Negotiations have been going on for over a year, with parties failing to come to an agreement so far. In our balance sheet we are still assuming that Iranian supply will only start to edge higher

from early next year. Clearly, there is a risk that this supply starts making a return to the market quicker than we are currently anticipating.

Clearly it is not all great news for the supply side at the moment. There is still plenty of uncertainty as highlighted yesterday, with oil flows along the southern section of the Druzhba pipeline coming to a halt. Russia's Transneft has blamed the stoppage on the fact that sanctions have prevented it from paying transit fees to Ukraine. The Southern leg of the Druzhba pipeline supplies Slovakia, Hungary and the Czech Republic, with flows transiting through Ukraine. This section of the pipeline supplies in the region of 250Mbbbls/d of crude oil. Flows along the northern route of the pipeline, which supplies Poland and Germany, remain unaffected. The Czech pipeline operator expects that flows along the southern route will resume in the coming days, which has provided some comfort to the market. Clearly there is uncertainty over this and the market will be eagerly awaiting for confirmation of a restart in flows.

On the demand side, growing recession risk has weighed on the demand outlook. This is reflected in a number of agencies having revised lower their demand growth forecasts several times this year. The higher prices seen for much of this year would have also led to some demand destruction. EIA weekly data shows that implied gasoline demand in the US has been seasonally weak so far this summer, given the higher pump prices. The more recent weakness in prices may limit the demand destruction that some may feel is needed in order to keep the market balanced.

What is clear is that the oil market is still struggling with both supply and demand uncertainty, and as a result the market is struggling to convincingly find direction. This uncertainty, combined with the lower traded volumes over the summer months, means that prices remain fairly volatile.

Metals

Despite reports yesterday of an accident at a Chinese aluminium smelter, LME aluminium prices have come under some pressure this morning. According to Shanghai Metals Market an accident at a 200ktpa aluminium smelter in Sichuan province has disrupted about 190kt of its capacity. Meanwhile inventories continue to tighten, with LME aluminium inventories declining for a fifth straight session - total stocks fell by 3.2kt to 284.3kt as of yesterday. Stocks have dropped by around 650kt since the start of the year.

China locked down urban areas in Guixi city yesterday due to Covid. The region is a major hub for copper smelting facilities. Jiangxi Copper Co., the nation's largest copper producer is also located in Guixi. The details of the lockdown and its potential impact on copper smelting in the region are scarce for now - the uncertainty could offer some support to prices in the short term.

Author

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group*

(being for this purpose ING Group N.V. and its subsidiary and affiliated companies). The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.