

The Commodities Feed: Russian supply risks still very real

Your daily roundup of commodities news and ING views



There has been some limited easing of Covid restrictions in Shanghai over the past couple of days

Energy

Growing demand risks due to the Covid situation in China, combined with a significant amount of oil set to be released from US and IEA member's strategic reserves, has eased concerns over immediate tightness in the oil market. ICE Brent settled more than 4% lower yesterday, which saw the market close below US\$100/bbl for the first time since mid-March. Easing concerns over tightness are also well reflected in the Brent timespreads. The prompt spread continues to come under pressure, with it trading at a backwardation of around US\$0.20/bbl, compared to around US\$3.50/bbl a month ago. The prompt spread is at its weakest level since the war started and in fact is at its lowest level since December. The flat price has rebounded somewhat in the Asian morning session today, given some limited easing of Covid restrictions in Shanghai.

There is also still plenty of uncertainty over how the supply will evolve in the weeks and months ahead. Clearly, this will be largely dependent on what happens on the ground in Ukraine. An escalation could push the EU towards banning Russian oil, which would potentially see a significant tightening up in the market. There are unconfirmed reports about the use of chemical weapons in Mariupol. If confirmed, this would only put further pressure on the EU to target Russian oil imports. A ban on Russian oil would mean the need for a change in trade flows and/or increased output from other producers. However, OPEC's secretary-general has already warned the EU that OPEC

does not have sufficient spare capacity to offset a full loss in export supply from Russia.

A potential EU ban would also need to see refiners finding an appropriate substitute for Russian urals. Urals are generally a medium sour crude oil, and so refiners would want to replace them with a similar grade. Substituting with different grades will have an impact on the products that refineries yield. So for example, increased use of lighter grades, such as US WTI, would mean that refiners would yield fewer middle distillates. And obviously, this would only further reduce the supply of middle distillates in Europe at a time when the [market is already extremely tight](#).

Today will see OPEC release its latest monthly market report, which will include OPEC production numbers for March, as well as the market outlook for the remainder of the year. In last month's report, OPEC made little in the way of revisions. However, for this month there is the potential to see revisions in Russian supply, along with obviously downward revisions in Chinese oil demand, given the ongoing lockdowns. This report will be followed by the EIA's Short Term Energy Outlook, which will include the latest forecasts for US crude oil production for the remainder of this year and 2023.

Metals

Metals came under pressure yesterday amid macro and fundamentals headwinds. A stronger dollar along with surging long-end US Treasury yields weighed heavily on the commodity complex.

The market is taking a hit with Covid developments in China, whilst there is uncertainty about how this all plays out. So far, activity from China's two most significant metropolitan areas, the Yangtze River Delta (YRD) and the Pearl River Delta (PRD) have been severely impacted. Inventory build-up is not a good sign, and it is hurting sentiment. That said, part of the demand hit we are seeing is delayed rather than destroyed. A silver lining is that some regions continue to see inventory net outflows as the logistical situation is better than others. There are also reports from the physical market that demand has improved somewhat after a pullback in prices attracted consumers back to the market.

Logistical bottlenecks are a concern for economic activity and this has caught the attention of senior officials. On Monday, the State Council urged local governments to ensure smooth movement of freight, and it also said that any shutdowns of the highway, port terminals, railways etc. without authorisation is strictly forbidden. The situation could improve if Beijing puts more effort into unblocking the logistical bottlenecks.

Looking to aluminium and EN+ Group said in a statement that the European Council announcement regarding sanctions against Rusal founder, Oleg Deripaska, has no impact on the company, and its subsidiary Rusal remains free from sanctions worldwide. This could see some risk premium evaporate. Still, there are worries that self-sectioning from supply chain participants will become a de facto sanctioning on Rusal, disrupting flows.

As for nickel, the LME market is likely being dragged down by the Shanghai stainless steel market. Shanghai stainless steel has fallen for three consecutive days amid a weaker demand outlook in China.

Agriculture

The USDA's latest weekly crop progress report shows that the winter wheat crop marginally

improved over the last week; although it remains significantly below levels seen last year. The USDA rated 32% of the winter wheat crop in good-to-excellent condition as of 10 April compared to 30% a week ago and 53% at this point in the season last year. For corn, the USDA reported that 2% of the crop is planted as of date, the same level as last week and marginally smaller than 4% a year ago.

The Ukrainian Grain Association (UGA) estimates that domestic wheat output could drop by around 45% year-on-year to 18.2mt in 2022 with exports of around just 10mt for the marketing year 2022/23. For comparison, the USDA estimates wheat exports from Ukraine at 19mt for the 2021/22 season. For corn, the UGA estimates domestic output to drop 39% year-on-year to 23.1mt in 2022 with exports seen at 20mt for the marketing year 2022/23. Export capacity remains a major concern as ports remain closed and alternative export capacity is limited to around 600kt per month currently.

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