The 2nd Middle East Oil Markets Workshop 2018

April 22nd, 2018 | Rosewood Hotel | Abu Dhabi

How Should the Middle East Leverage IMO 2020 to Create a Fujairah Oil Products Benchmark?

uniper

Port of Fujairah
ميناء الفجيرة
Port of Fujairah
United Arab Emirates

S&P Global
Platts

GI Consultancy
Gulf Intelligence

How Should the Middle East Leverage IMO 2020 to create a Fujairah Oil Products Benchmark?

The 2nd Middle East Oil Markets Workshop will bring together 50 senior stakeholders from across the region's Energy Industry to produce top recommendations on how to leverage IMO 2020 to create a Fujairah Oil Products Benchmark.

In October 2016, the International Maritime Organization (IMO) reduced the sulphur limits for bunker fuels worldwide from 3.5% to 0.5% by 2020, instead of the alternative of 2025. This conversation is nearly two decades old, but it still came as a quasi-surprise to refiners and the shipping industry. But for Middle Eastern refiners, the IMO's deadline should represent a golden opportunity. Equipped with a new, vast and flexible refining network, the region has the tools to get ahead of the competition in the race for the 2020 finish line. But quick action is required.

Fitting more Exhaust Gas Cleaning Systems (EGCS), which are better known as scrubbers, is a short cut to reducing marine sulphur emissions by 2020. Scrubbers enable ship owners to meet the cap while still burning high sulphur fuel oil by spraying alkaline water into a vessel's exhaust to remove sulfur. Fitting scrubbers to existing fleets and new ships – installation is a simpler process for the latter – would significantly ease the pressure on refiners up to 2020. But, retrofitting a vessel costs up to $5 million and a global glut of ships has stalled the pipeline for new ships, which leaves little clarity for refiners on the number of EGCS installations.

Global market opinion is divided on whether there will be enough supply of 0.5% product by 2020. Netherlands-based CE Delft expects there will be capacity to produce compliant fuels, despite its base-

case scenario forecasting the global demand for marine fuels to increase by 6.6% to 320 million tons in 2020, from 300 million tons in 2012. Conversely, US-based Ensys expects that up to 60%-75% of additional sulfur plant capacity will need to be built by 2020 to meet demand, compared with planned projects.

The marine fuel industry is embarking on a fundamental shift and it is critical for the marine fuels market, which is one of the most actively traded in the world, to ensure it is underpinned by robust methodology and pricing. Regional demand for fuel oil continues to propel discussions on the need for establishing oil products benchmarks in the Gulf and with the low sulphur fuel oil cap creeping round the corner, is there an opportunity to establish a Middle East fuel benchmark?

Creating a benchmark for fuel oil by an independent pricing agency – Platts and Argus, respectively, are the region's major agencies - would help facilitate the development of a healthy derivative market and mitigate financial risk. Back-to-back trading no longer occurs as oil companies now take large positions and put more oil into storage. Storing crude is especially common due to the current contango – when the spot price is cheaper than the futures delivery – which is the result of low oil prices since mid-June 2014.

"Historically, a hub would need a certain amount of light pricing, trade and capacity – boxes that Fujairah has ticked. However, trading regulations and standard operating practices around the world's major hubs have progressed."

The bar has essentially been raised when it comes to establishing global trading hubs and independent benchmarks are integral to growth. Historically, a hub would need a certain amount of light pricing, trade and capacity – boxes that Fujairah has ticked. However, trading regulations and standard operating practices around the world's major hubs have progressed.

There is a prerequisite to have a derivative market in order to develop a trading hub here in Fujairah, as the days of back-to-back trading are long gone. Oil companies take positions and have significant volumes in storage, which means that sophisticated risk management must be part of the game. Nearly every volume of oil nowadays is hedged financially, which you can only do if there is an instrument available for this hedging. The fuel oil that is stored and traded out of Fujairah, for example, only has the Singapore swap as an effective hedging instrument.

The Mean of Platts Arab Gulf (MOPAG) is already an important pricing point for the Middle East, Indian Subcontinent and East Africa. All three regions use that price for their physical pricing, which has always been derived by using the Singapore price minus freight. Historically, this system worked well as all fuel oil would either go one-way from Europe, Black Sea and the Baltic Sea via the Middle East to Singapore. This is no longer the case, with flows from the east heading back to the west, or from Singapore to the Middle East. Consequently, the freight factor that is included in the assessment of the MOPAG is no longer a reliable figure to hedge fuel oil that is stored in Fujairah.

Successful benchmarks are borne from standardisation, which provides a level playing field, transparency through access to information and a healthy dose of liquidity. The Gulf is progressing on all fronts, but more is needed. What are the most effective steps that the Gulf can take to deepen the global reach of its current benchmarks and establish new, robust and widely-used benchmarks? ■

The 2nd Middle East
Oil Markets Workshop 2018

Vitol S&P Global Platts

RECORD OIL INVENTORY ERA ENDS!

"How Should Oil Storage Hubs Navigate Persistent Backwardation in 2018 to Avoid Price War?"

FEATURED SPEAKERS
- Dave Ernsberger, Global Head of Energy Pricing and Co-Head of Content, S&P Global Platts
- Chris Bake, Member of the Executive Committee, Vitol

MODERATOR:
Sean Evers, Managing Partner, Gulf Intelligence

Sean Evers: Are we likely to see this backwardation in the market continuing through 2018 and how should market players tackle this?
Chris Bake: What we are seeing today is a result of a series of events that first triggered an unprecedented rise in oil stocks and then last year, a lowering in oil stocks. The emergence of US shale oil in 2009-2010 surprised us all – and since then, year on year and with the help of capital markets, US production has incrementally produced 1 million barrels a day of oil. The surprise triggered OPEC to respond with its market share strategy in 2014 – the taps were opened, refining margins remained robust and crude and products ballooned at an exponential level – a bonanza for incremental oil storage. The geopolitics in the Middle East also lead to a natural imbalance – with the eastern flow of oil from Iran to other locations having to be stored instead of going to market for example. Which leads us to 2016 – when OPEC decided to cut production to support the market – and this was coupled with strong demand during 2016-2017. Demand estimates were revised and they continue to be so with 2018 also looking strong. Within that context, OPEC has remained disciplined on its output agreement and the consequences have been a visible drawdown in oil inventories. About half a billion barrels of oil has been drawn down in a short period of time and that has had a knock-on effect and lead to the backwardated structure which we see today. So the incentive to carry oil is not there and there has been a dramatic effect in use of tankage – the velocity of the barrel is going to increase.

Sean Evers: Did the industry miscalculate how much new storage capacity to build during the period you just outlined?
Chris Bake: The market reacts to immediate indicators so as long as there are short term reasons, it will always be justifiable to build capacity. There has also been a change in trading patterns, changes in specifications, which have influenced why tankage has been built.

Sean Evers: Dave – what's your outlook for the structure of the market in the year ahead?
Dave Erneberger: The view on backwardation depends on where you are in the barrel – fuel bunkering or middle distillates or gasoline - so it looks a little different in coming months for different players. If you look at publicly reported inventories – they are not down as much as one might think. We are getting back to 5-year averages on inventories but we are not at the bottom of the tank. Storage is there for purposes other than managing the structure of the forward market curve and taking advantage of profits. There is a lot of demand which is going to change significantly in the coming two years on the blending side of the market which will ask two core questions for storage: should tank farms be optimised for crude or products and this will be influenced by new trade flows in the market such as new crudes coming to Asia for example. The second and more challenging question is whether operators should build clean or dirty tanks and this is impacted by the point of view of where fuel oil is going to go as we approach 2020 when the new IMO sulphur cap comes in. Are fuel oil inventories going to balloon due to insufficient coking capacity and will fuel oil have a role in the bunker pool? We could have a situation where we have a contango in fuel but backwardation in middle distillates and a spread between fuel and gasoil. Whether there will be a fuel build or middles build will impact where to position in the next 18 months. We also need to remember to look at the data – in Fujairah in the UAE for example, today light distillates are 60% of inventories and fuel is 40% but in December it was the other way around. So that dynamic impacts the tactical decisions that are being made.

Sean Evers: Chris – should the different hubs – Rotterdam, Fujeirah, Singapore – have the same strategies in the current cycle?
Chris Bake: The overall impact has hit all major markets in terms of the incremental barrel of oil not making its way into tank today. But each region also has geographic differences driven by certain conditions. For example, Singapore's recent dramatic change to tax legislation and import legislation that impacts components that used to go from Southeast Asia to China for gasoline blending and conversion. Another example would be the incremental outward flows of crude oil from the US Gulf coast which has now rendered it both an importing and exporting hub. So each region has its own idiosyncrasies.

Sean Evers: Dave – after inventories have come off so dramatically in the last year, some forecasts are now saying they will remain stable.
Dave Erneberger: We forecast that stock inventories will continue to fall but maybe not at the same pace as the last 14 months or so. Commercial inventory drivers are still competitive in the short-term spot market on the products side. On the crude side, there is growing consensus on the view that US shale producers are being held to higher standards on their business models and return on investment in this second wave of production and that the exuberance of the run up to 2014 may be tempered this time around.

Audience: With supply chains moving as they are and 'just in time' inventories moving even more, what is the capacity utilisation in the storage area now and what's it likely to be in the commercial space and by region. How is all this impacting a shipping market which seems oversupplied?
Chris Bake: The percentage of utilization is very terminal specific and it is really a fact of investment as to what tanks terminals can hold. There are also different specs of tanks and they are not purely interchangeable for crude or gasoline blending. Tankage usage is down 20% year on year approximately and so there is bigger availability of tankage today and we don't see any change in that in the short term. The real cliff in the room is how the world handles the new IMO 2020 sulphur regulation and how marine gasoil and heavy fuel oil will fare; what the world does with surplus heavy fuel oil as more developing economies go into gas is critical. It will either have to burn or convert the fuel oil or not make it at all anymore. If the IMO regulations are effective in the bunker market, then we will need an alternative to high Sulphur fuel oil – and that will be gasoil, in which case marine gasoil will have to build for latent 2020 demand and fuel oil will also build due to lack of natural demand from the market. There will be an inflection point of when the storage requirement has to change as a result of this and that will play out over the next six months or so. Shipping-wise, there are big dislocations in pricing right now and an over exuberance on trying to build super-efficient or dual purpose ships which are not always necessarily required.

Audience: Is floating storage going to disappear in this backwardated market?
Dave Erneberger: We can probably assume that FSUs will be removed first for scrapping. If you happen to have a flexible contract agreement with the owner, it's possible you could give back the ship but if not, it would go to scrap.

Chris Bake: I agree – we have seen floating storage of 28 million barrels sitting off the coast of Iran incrementally disappear as well as Singapore fuel storage.

Sean Evers: What advice would you give to storage hubs to prepare for the next opportunity and manage their way through this backwardation?
Chris Bake: Responsiveness and flexibility are key to any operator. The ability to manipulate a barrel quickly – to blend it, upgrade it, convert it – has to be paramount during this backwardation period. Terminal and port operators have to show a huge degree of flexibility to incentivise that barrel to come onshore and enable that incremental refining margin to be achieved. They have to realise that their assets will be challenged more in this environment than when the market is in a natural contango.

Audience: How will the IMO regulation impact shipping, terminal operators and charters?
Dave Erneberger: Every party thinks the other is taking care of it but the reality is there has been no ability to agree around the table yet. Should refineries be building cokers? Without knowing, there is a lack of clarity on how to respond. One thing is clear though – tolerance for not implementing the IMO will be very low by the likes of the United Nations, MARPOL or other authorities. The turnaround for IMO has become acute in the last two months with talk of enforcement with drones and satellites and no tolerance for cheating and and yet, the way it will play out is likely to be last minute. Fines for non-compliance may not be very high but reputational damage will be.

Chris Bake: The pressure in IMO is paramount. As an industry we need to give certainty to the market. We missed the wave of investing in putting scrubbers on ships so now it comes down to refiners, port authorities and blenders to give clarity on enforcement and on what the requirements are in different areas. Some players are already providing alternatives to destroying high sulphur and to changing refinery slates as soon as everything is defined clearly. The industry can react when the conditions are there but the message has to be coherent on how to for example, extract waivers, how to handle high sulphur fuel oil and what the other enforcements are going to be across the board as well as knowing there will be equal standards between ports.

Audience: Where do you see the demand and supply balance at the end of 2018 on draws on crude and products and what's your forecast for 2019?
Chris Bake: The drawdown in inventories will stabilize in the second quarter with refinery turnarounds, assuming economic conditions stay as they are and demand and investment stay strong. But going into 2019, it will be a combination of price and economic cycle and as we are currently at the peak of this cycle, there will be vulnerabilities in market.

Dave Erneberger: We can look at demand and supply but also need to factor in geopolitics. For example, if the Saudi Aramco IPO is successful, it could alter decision-making within OPEC regarding production cuts and so forecasting changes beyond 2018 is hard to do.

Sean Evers: Final piece of advice to hubs in 2018?
Dave Erneberger: To remember that storage use is not just short term and to stay above the fray of tensions in market. Focus on long term relationships and on being a service provider operating storage as a commercial proposition. Safe harbour is what people are looking for.

Chris Bake: Flexibility and certainty to the extent that it is possible. IMO is going to drive the dynamics of the market for the next 18 to 24 months so being able to cater to that for the business as a whole is going to be paramount –for ports, storage and refiners. ■

What are the Next Steps required to establish a liquid trading hub in the Gulf by 2020?

Easy access to capital, ever-growing infrastructure, healthy volumes of trade and robust oil price benchmarks underscored by transparent methodologies are the key ingredients needed to deepen the Gulf's global trading footprint.

Fujairah's location south of the Straits of Hormuz in the UAE makes it the region's most strategic spot to bolster the Middle East's global trading presence, according to 83% of respondents to a Gulf Intelligence (GI) Industry Survey in April 2016.

Surprisingly, Sohar in Oman and Bahrain did not receive a single vote, with 11% preferring Dubai.

Part of Fujairah's popularity is its offering as a one-stop shop, with the port able to provide supplies, bunkering, crews and so on. Today's 9 million (m) tons of oil storage is expected to climb to 14m by 2020. Fujairah's crude offering is ever-widening as well, such as UAE Murban, Iraqi Basrah Light and Masila from Yemen featuring on the product list. Part of the attraction, for traders especially, is that Fujairah is largely a deregulated market compared to the eagle-eyed regulators monitoring Singapore and Rotterdam.

While Fujairah's tool box is filling up, some elements need sharpening. All stakeholders, including Fujairah, must make an effort to run a tighter operation that meets the global standards set by other trading behemoths, notably Singapore and Rotterdam. It is equally worth noting that Singapore has had over a century of practice, from when Sir Stamford Raffles founded modern Singapore as a free port in 1819, to it becoming the world's largest container port for the first time in 1990.

83%

Fujairah is best-placed to become the Middle East's major trading hub, according to 83% of GI Industry Survey respondents.

Historically, a hub would need pricing guidance, trade and capacity – boxes that Fujairah has already ticked. But the emirate still needs to elevate its operations to meet the standard global transparency operating practices, which includes regular and easily accessible data sets.

The three winning recommendations of the Oil Markets Workshop address the most effective 'next steps' that could be made to bolster Fujairah's offering as a global hub. All the recommendations are intertwined, from establishing an independent benchmark for fuel oil, to publishing storage data and improving the overall legal architecture.

Other top recommendations – coming in fourth and fifth, respectively – was the need to improve the connectivity between third party storage and Abu Dhabi's National Oil Company (ADNOC) at Fujairah and bolstering the region's small trading community.

Linking ADNOC's facilities, which carry Murban crude, with third party storage would help promote transparency, flexibility and volume growth for ADNOC, Fujairah and all the port's customers. Nearly all (92%) of survey respondents said Abu Dhabi would benefit from maximising the opportunity to build a global trading hub in the UAE – an oft-discussed point that has yet to gain traction.

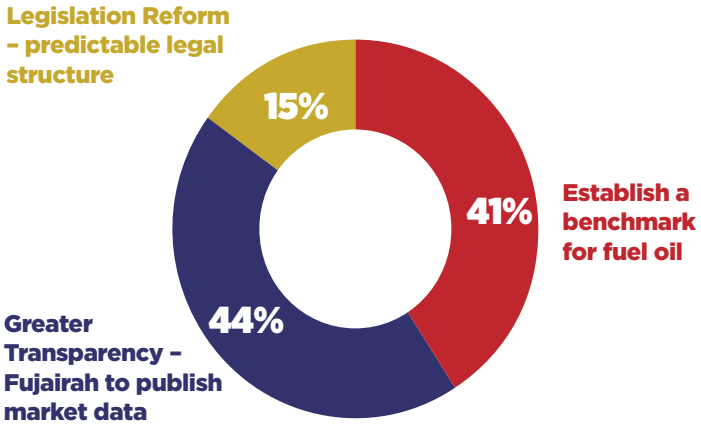
Meanwhile, the limited trading community in Fujairah and the wider Gulf is seen as an untapped opportunity, especially considering the region has an advantageous time zone as it is nestled between Europe and Asia.

The tightening regulatory control and lower salaries in Europe should theoretically encourage traders and relevant professionals – brokers, lawyers and accountants to name a few – to migrate eastwards.

So far, Fujairah's proven capabilities as the region's preeminent trading hub have triggered a wave of optimism, with 51% of survey respondents saying the Middle East can evolve its trading presence to rival Singapore and Rotterdam within 2-5 years. Others are less bullish, with over a third (37%) expecting it to take five years plus before the Middle East can near the podium hosting Rotterdam and Singapore, as governmental red tape, political quibbles and regional competition drag the timetable backwards.

The pace of the region's growth into a global trading hub remains to be seen, with many saying the responsibility to fulfil the vision lies in Fujairah's hands. As His Highness Sheikh Mohammed bin Rashid Al Maktoum said: "Opportunities are made – they do not just lie around waiting for someone to grab them."

What is the Most Urgent Recommendation Required to Establish a Liquid Trading Hub in the Gulf by 2020?



Abu Dhabi would benefit from a global trading hub in the UAE, according to 92% of GI Industry Survey respondents.

Rules & Format

The Chatham House Rule will be invoked at the meeting to encourage openness and the sharing of information: *When a meeting, or part thereof, is held under the Chatham House Rule, participants are free to use the information received, but neither the identity nor the affiliation of the speaker(s), nor that of any other participant, may be revealed.*

OPEN MIC: Following the Welcome Note and problem statement by the moderator and featured speakers, the breakout session discussion structure will follow an Open Floor format whereby all participants will be encouraged to proactively engage in the free-flowing conversation and not wait to be called upon to speak.

COME PREPARED WITH RECOMMENDATIONS: All Participants will be encouraged to come to the table with "Recommended Strategies" in answer to the Session's Critical Question.

In SESSION A:
SHORTLISTING 5 RECOMMENDATIONS
The 1 Hour Session will be broken into 3 parts:
- Commentary from facilitators
- Open mic with recommendations put forward
- Voting on recorded recommendations with final shortlist of 5

In SESSION B:
SHORTLISTING FROM 5 TO 3 RECOMMENDATIONS
The 1 Hour Session will be broken into 3 parts:
- Commentary from facilitators on shortlist of 5
- Author of each of the 5 shortlisted recommendations will get 5 minutes to promote & defend their recommendation
- Voting on Recommendations to reduce Shortlist to 3

WORKING LUNCH:
The Shortlist of 3 in each stream will be voted on to secure a ranking in order of importance (1-2-3).

Structure

APRIL 22nd 2018 | 8:00AM – 2:00PM

NETWORKING BREAKFAST	
PLENARY SESSION	
STREAM 1: TOP 5 RECOMMENDATIONS TO LEVERAGE IMO 2020 TO CREATE AN INDEPENDENT MIDDLE EAST BENCHMARK FOR OIL PRODUCTS?	**STREAM 2: TOP 5 RECOMMEND ACTIONS THAT MIDDLE EAST STAKEHOLDERS - TRADERS/REFINERS/SHIPPERS/PORTS - SHOULD ADOPT PRIOR TO 2020 TO SUPPORT THE REGIONAL PUSH FOR AN OIL PRODUCTS BENCHMARK?**
SESSION A Shortlist Top 5 Recommendations	SESSION A Shortlist Top 5 Recommendations
COFFEE BREAK	
SESSION B Top 5 Recommendations Shortlisted to 3	SESSION B Top 5 Recommendations Shortlisted to 3
WORKING LUNCH **POLL SURVEY on TOP 3 RECOMMENDATIONS in EACH STREAM**	
Final Declaration of Recommendations & Closing Comments	

The 2nd Middle East
Oil Markets Workshop 2018

Recent Workshops

Gulf Intelligence has produced a number of workshops to bring together industry, academia and government to deliver tangible intelligence and recommendations to address issues of critical importance.

Our recent projects include:

- Oman Energy Master Plan 2040
- Oil Markets Workshop: What is the Future Outlook for Middle East Oil Products Benchmarks?
- Gulf LNG Workshop
- Gulf EOR Workshop

Capturing recommendations between Participants at the Gulf EOR Workshop

H.E. Salim Al Aufi. Undersecretary, Ministry of Oil & Gas, at the Oman Energy Master Plan Industry Workshop

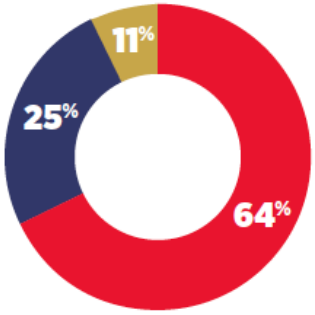
Participants at The First Gulf Intelligence Oil Markets Workshop discussing the future Outlook for a Middle East Oil Products Benchmark

Participants casting their recommendation votes at the Gulf LNG Workshop

Recent Interactive Survey Results

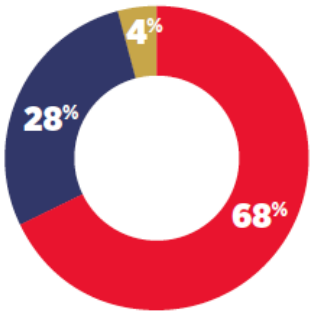
What are the Top 3 Steps to Facilitate an LNG Import Ecosystem in the Middle East?

A Better access to the LNG market through developed infrastructure, which serves the whole system.
B Stronger regional cooperation.
C Removal of subsidies.



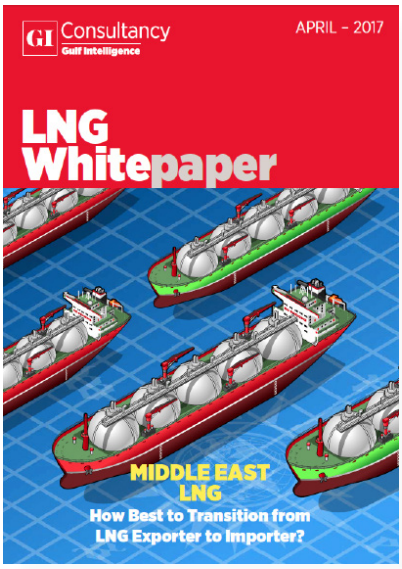
What are the Top 3 Steps to Maximize the Value of Middle Eastern LNG Exports?

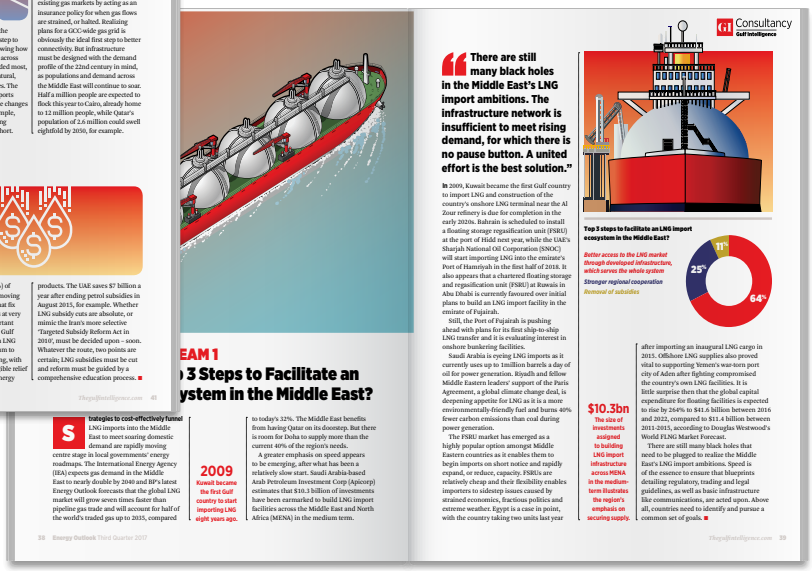
A Flexibility delivery.
B Trusted supplier.
C LNG as a bunker fuel.



The Post-Workshop Report

Gulf Intelligence will harvest the content from the workshop into a Oil Markets Workshop Report, which will be distributed to the relevant and wider stakeholders.





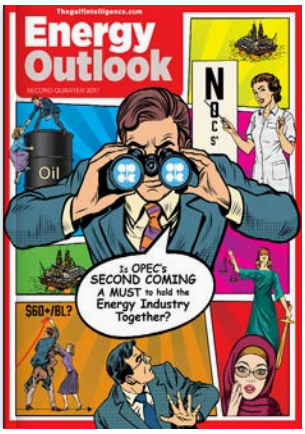
Gulf Intelligence

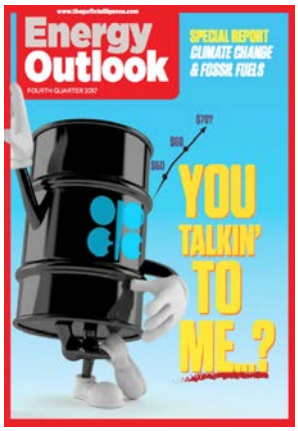
'We Facilitate Knowledge Exchange'

Gulf Intelligence is a strategic communications & research firm effective across the full value-chain of the Middle East Energy Sector. We facilitate knowledge exchange and advance the business interests of national and international stakeholders operational in the regional industry.

The Gulf Intelligence Publications

Energy Outlook harvests content from the Gulf Intelligence forums into a series of white papers and editorials, as well as exclusive interviews, speeches and articles by leading figures in the MENA and International Energy Industry, including H.E. Abdalla Salem El-Badri, Former OPEC Secretary General, H.E. Mohamed Suhail Al-Mazrouei, UAE Minister of Energy and H.E. Khalid Al Falih, Minister of Energy, Industry & Mineral Resources, Saudi Arabia





The Gulf Intelligence Middle East Energy Series: 2009-2018

Gulf Intelligence has been humbled over the years to host many of the world's recognized energy leaders, including the ministers of most OPEC member states, the heads of international multilateral energy institutions including IEA, OPEC and the IEF, who have all provided timely, relevant and useful intelligence for our international energy industry partners.

Consultancy
Intelligence
Publishing