



بنك الإمارات دبي الوطني
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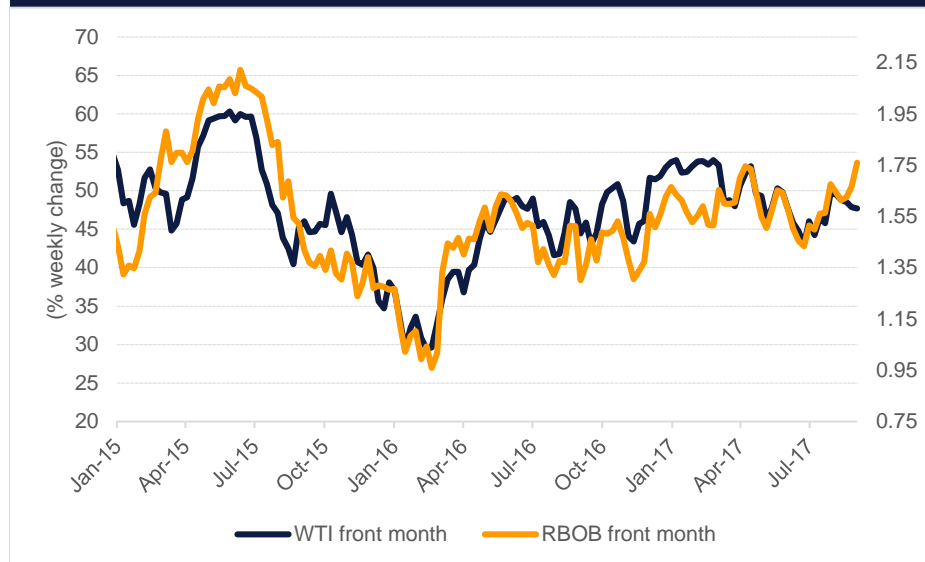
Commodities

28 August 2017

Crude oil update

Hurricane Harvey has made landfall on the Texas Gulf Coast, leading to serious flooding and affecting oil and gas production and refining infrastructure. The scale of damage will likely take several weeks to assess fully but in the near term the impact of the storm will have a multi-faceted impact on energy prices. In the week ahead of the storm, WTI and gasoline futures had already diverged with gasoline futures shooting to their highest level since 2015 while WTI closed lower.

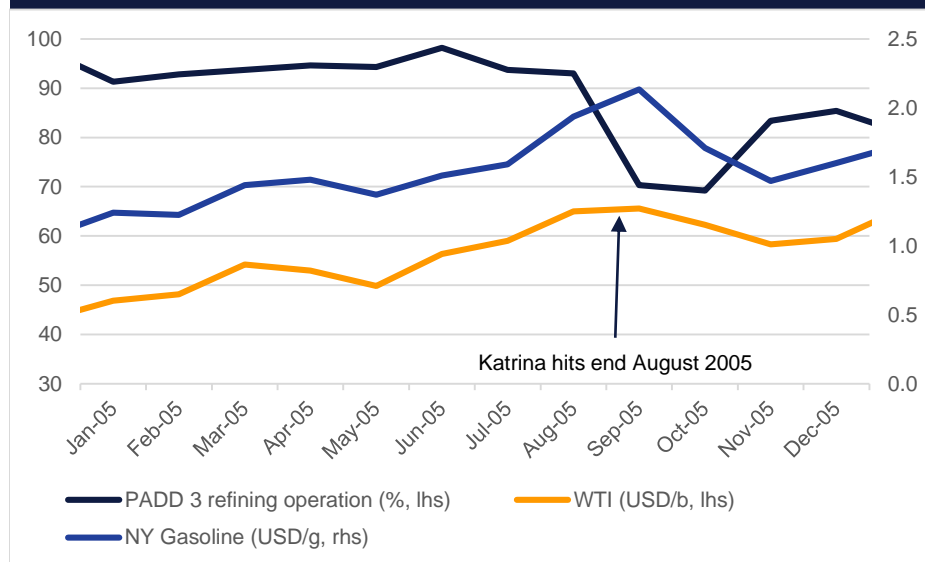
Upside risk to gasoline stronger than WTI



Source: EIKON, Emirates NBD Research.

The divergence between crude and gasoline is down to the enormous share of refining capacity held in the Gulf region that has been affected by the storm and will remain disrupted owing to flooding. The Gulf Coast of Texas holds more than 26% of the total refining capacity in the US and the entire Gulf region (PADD 3) represents more than 50% of total refining infrastructure. In August 2005 during Hurricane Katrina, a stronger hurricane with bigger storm surge, refining capacity in PADD 3 collapsed quickly, sending gasoline and WTI futures higher, albeit only for a few months before they settled back into pre-hurricane levels. Since then refining infrastructure has been beefed up and reinforced but heavy rainfall could still cause damage in the days ahead.

Hurricane Katrina saw similar effects

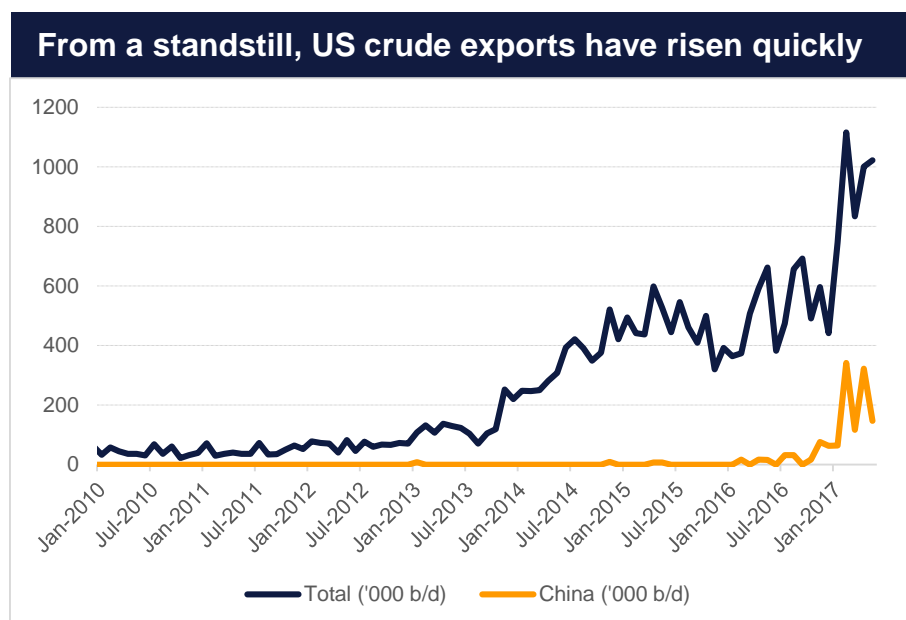


Source: EIA, Emirates NBD Research.

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The hurricane season historically has had an outsized impact on US energy markets but as the US has become both a much larger producer and exporter of crude oil the reverberations of Hurricane Harvey will be felt further afield. Singapore gasoline cracks over Brent futures have already shot higher and a prolonged disruption of US cargoes to Asia will send regional buyers in search of comparable light grades, hence why Brent futures have pushed higher today while WTI is weaker. Supply outages in Libya will also support Brent futures in the short term.



Source: EIA, Emirates NBD Research.

Is this the shot in the arm that the oil market has been looking for and that OPEC has so far failed to deliver? As we noted last year when wildfires impacted Canadian production, relying on one-off variables is not a sustainable strategy for rebalancing markets. A sustained boost to prices will only be apparent if indeed damage is significant in onshore oil fields, particularly in the Eagle Ford region which is less likely to be inured to hurricane conditions compared with offshore Gulf of Mexico fields.

The weekly EIA data will likely send some conflicting signals over the next few weeks—lower production, lower refinery demand with a likely build in stocks as oil produced further inland is unaffected and dumped into stocks—and could result in prices whipsawing as we enter a seasonal refinery downturn. Further, if the WTI curve eventually follows suit and pushes higher as well as a result of the tighter US market, then we would expect to see further hedging activity undertaken by producers in the US.

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