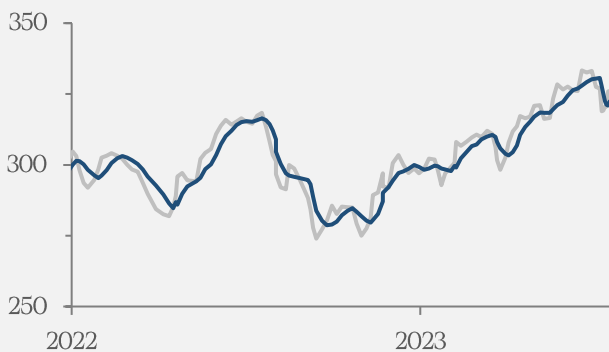


Daily Thought

What Drives the Draws? – August 24th, 2023

An important inventory distinction to make, that isn't often done – are commercial stockpiles (both refinery, and ex-refinery), and strategic stockpiles. While strategic stockpiles are much less price sensitive (typically event sensitive, like the 2005 release during Hurricane Karina) and released at the will of the governing body (like, Joe Biden, or Xi Jinping), commercial stockpiles, especially those held in tanks at refineries are much more *fluid*, and highly price sensitive. While strategic inventory is controlled by the government, commercial inventories are controlled by price sensitive, profit oriented organizations, like refineries, and holding a barrel in storage, vs. buying in the market presents an opportunity cost. When the forward curve is highly backwarddated (i.e. you need to pay up to buy a barrel in the market today, vs. waiting for the next contract) the incentive to draw inventory is much higher. Over the past weeks, time spreads have eased strongly, signaling that we may see the pace of refinery inventory draw slow. In China, commercial inventories (ex-refinery, shown in fig. 1) began to sharply draw at the beginning of August, along with refinery inventories (shown in fig. 2). Recall, we believe that it's OPEC's goal to keep

(Fig. 1) China Commercial Inventory (mb)



(Fig. 2) China Refinery Inventories (mb)



Source: Kpler, HTM Analysis

inventories drawing to a point where they remain the marginal barrel, and while growth to meet y/y consumer demand will come from ex-OPEC countries, and carefully supplemented by the cartel. To execute on this plan, they need to draw commercial inventories (less so strategic, as they have never been a strongly correlated factor). While West of Suez inventories are the strongest correlation (i.e. OECD), and those have (according to high frequency data) drawn ~20mb since mid-July, but China has been more stubborn, with inventories all higher YTD. Higher cracks will push runs as high as the market can support (throughput wise), though there's incremental east refining capacity coming online/back online through year end that may counter cracks. So OPEC is in a tough spot, needing to drain Chinese inventories while keeping prices in check. Additional cuts may do just that,

Daily Pricing & Week on Week Benchmark Chg.

CAD Priced Liquids

Condy | \$103.73 (+0.5%)

Synthetic | \$110.96 (-0.8%)

WCS | \$79.92 (-6.5%)

USD Priced Liquids

Bonny Lt. | \$88.39 (-0.4%)

LLS | \$81.99 (-0.4%)

MEH | \$81.24 (+0.1%)

NYMEX | \$78.89 (-0.6%)

WTI FOB | \$80.71 (+1.7%)

CAD Priced Gas

AECO | \$2.72 (-6.6%)

Alliance | \$2.61 (+1.5%)

Empress | \$2.71 (-6.4%)

Station 2 | \$2.63 (+41.0%)

USD Priced Gas

Dawn | \$2.33 (-4.5%)

Houston | \$2.46 (-2.0%)

Malin | \$2.93 (-36.6%)

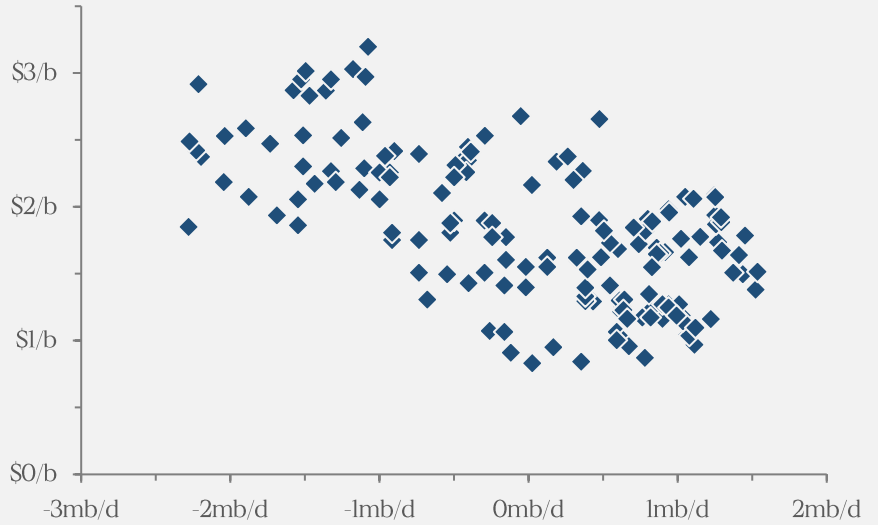
PG&E | \$4.45 (-29.2%)

SoCal | \$3.82 (-52.6%)

Waha | \$2.06 (-14.3%)

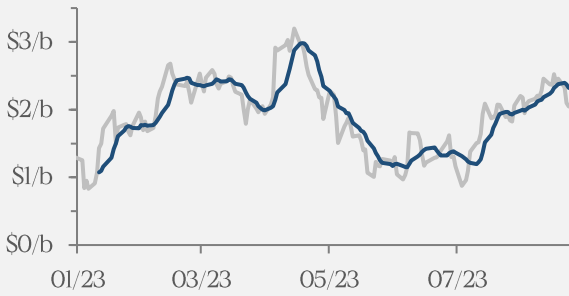
to some extent, but risks moving the flat price. Spreads are the most important part of their toolbox. Not only does it discourage US supply (as down strip isn't moving materially), but it encourages destocking. In the past weeks, cash Dubai (as assessed by Platts) has seen a softening of time spreads - not as extreme as the Brent, or WTI softening, which moved close to YTD lows last week but the Dubai cash curve has undeniably become less steep over the past weeks. The correlation between Dubai spreads, and YTD inventory draws has been relatively positive (as in, the higher the spread, the quicker the draw, and mostly driven by China, the swing 'destocker') and

(Fig. 3) Dubai Cash Spread vs. Global Crude Draws (mb/d)



Source: Argus Media, Kpler, S&P Platts, HTM Analysis

(Fig. 4) Dubai co2 to co5 Cash Spread

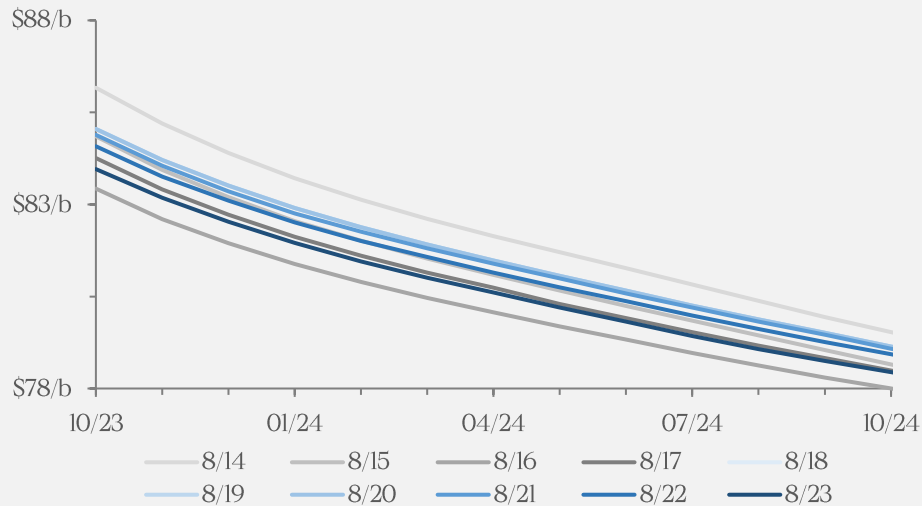


Source: Argus Media, S&P Platts, HTM Analysis

see heavy differentials easing (including South American, and Canadian grades), and time spreads easing - which should result in Chinese commercial, and refining inventories beginning to flatten. On the other hand, we still expect (as discussed) OPEC to do everything to keep the curve as backward as possible. With cheaper South American heavy sour barrels and time spreads that are stagnating, we would expect Chinese underwhelm on draws at current in favor of taking cargos which would be slightly bullish crude prices now, though less healthy for a future price spike's longevity.

with the softening in Dubai spreads, along with the softening in differential on heavy crudes, we think that China commercial inventories start to flatten, as the incentive to draw from inventories fades. We know that Chinese refining capacity (post-maintenance) has been strong, but actual refining runs weaker due to the lack of domestic demand (and see August 19th 'Weekend Flows' for our outlook on Chinese refining). While we think runs could increase if export quotas do in the coming months, maintenance, and a lazy economy should keep general feedstock demand in check (fuel oil has also made up a large portion of feedstock demand thanks to tightening import quotas, which we believe are now relaxed). So, we

(Fig. 5) Platts Dubai Cash Forward Curve



Source: Argus Media, Bloomberg, S&P Platts, HTM Analysis