What does a hard hit energy sector mean for platinum demand?

Last week, Royal Dutch Shell warned that it will slash the value of its oil and gas assets by up to $22bn after the coronavirus crisis hit demand for fuel and weakened the outlook for energy prices. This followed a similar announcement by other major energy companies, such as BP, which in early June announced plans to cut up to $17.5bn. These moves highlight the dramatic impact of COVID-19 on the energy sector in both the short and long-term. This creates both challenges and opportunities for platinum applications in this sector.

Oil refining output suffered a major pullback in Q2

Amid the global pandemic the oil industry was hit particularly hard. As fuel consumption slumped, a growing number of refiners have started to cut output since March, while some plants have also delayed planned maintenance work in an effort to slow the spread of the virus.

According to the International Energy Agency (IEA), global oil refinery intake plummeted by over 15% y/y in April. Despite a gradual lift of lockdown measures in most major economies, intake continued to weaken in May, as refinery storage bottlenecks saw several refineries in Europe, Asia and Africa reportedly closed for an indeterminate period. While a recovery in refinery operations is expected in H2, demand is expected to return only slowly as risks of a second wave of infections persist. The IEA currently expects that global oil refining output in 2021 will remain below the 2018 historical peak. The decline in refining activity, along with other supply-chain disruptions caused by COVID-19, is likely to weigh on platinum demand in this sector.

Gold

Spot gold breached $1,790 for the first time in eight years, as a further rise in COVID-19 cases globally boosted demand for safe haven assets.

Silver

Net Comex longs grew for the third week in a row, but net positions were still 46% below their late February high.

Platinum

The Italian Parliament gave the green light to a scrappage scheme to encourage sales of combustion engine cars as well as electric and hybrid vehicles.

Palladium

The Detroit Three posted sales declines of more than 30% y/y in Q2 in the US.
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Investment in oil and gas hit hard
Prior to the crisis, investment in global oil refining had posted healthy growth since 2015, with spending on new refinery builds and upgrades totalling some US$52bn in 2019 alone. As a result, a record amount of new refining capacity was added last year, including two mega refineries in China integrated with petrochemical operations, which boosted platinum catalysts in both petroleum and petrochemical sectors (the latter is a key component for our estimate for platinum chemical demand).

This growth, however, came to an abrupt halt in 2020, after the COVID-19 pandemic led to the largest drop in global energy investment on record. The IEA expects spending to plunge in every major sector this year – from fossil fuels to renewables and improved energy efficiency. Among these, investment in oil and gas is expected to record the largest decline, falling by almost one-third in 2020, with refining capacity inevitably being affected.

Transition to clean energy will help platinum demand
Alongside the short-term shock brought on by COVID-19, the global oil and gas industry has also seen efforts to shift away from fossil fuels to renewable energy sources that can help reduce carbon emissions. As governments rush to put together stimulus packages, there are arguments that they should also accelerate the transition to clean energy, as renewables (whose costs continue to fall rapidly) can stimulate job creation and economic development while reducing emissions and fostering further innovation. Among these, investment in hydrogen technologies should favour platinum. According to IEA, prior to the crisis, hydrogen technologies had already posted healthy gains in 2019 with increasing electrolysis capacity becoming operational and several notable investments announced for upcoming years. The fuel cell electric vehicle market is also set to grow, albeit from a low base.
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PGM consumption to benefit from continued expansion of oil refining and petrochemical capacity in China

While most oil (and petrochemical) producers have been negatively affected by the COVID-19 crisis, the impact on Chinese companies has been limited. Although Chinese platinum consumption in the petroleum and petrochemical sectors is also expected to weaken this year, this was largely due to a record 2019 performance, with volumes likely to remain elevated by historical standards. For palladium, net offtake is expected to remain buoyant. Looking further ahead, the continued expansion of oil refining and petrochemical units should continue to favour PGM consumption in the coming years.

In essence, this reflects the Chinese government’s desire to reduce their dependence on imported petrochemicals over the medium term, a wish amplified by the ongoing trade war with the US. Another major policy change in China saw the government (since 2015) giving more private refineries permission to directly import crude oil. This in turn has encouraged many private owned companies to invest in new oil refineries that would be more profitable through integrated downstream into the petrochemicals industry.

Against this backdrop, 2018-19 saw several new large oil-to-petrochemical complexes come on-line. While several areas of petrochemicals benefited from this policy, the impact on the paraxylene (PX) industry was one of the most pronounced, which helped to boost platinum demand. As the world’s largest PX consumer, China has historically been reliant on PX imports from neighbouring Asian markets. Palladium also benefited, although growth was more modest, given China’s already dominant share of global purified terephthalic acid (PTA) plants (which require installations of palladium bearing catalysts). To illustrate, Chinese PTA plants made up roughly 58% of the global total at the start of 2019, compared to a more modest 24% for PX. As PX is the preferred feedstock for the production of PTA, the gap between the two may also help to explain why the capacity expansion of the former has been faster over the last few years.

Turning to 2020, in spite of the pandemic, capacity expansions of key petrochemicals has continued so far this year, with several new plants under construction. In early June, it was reported that the central government approved a new mega petrochemical project as part of its efforts to boost infrastructure spending (to help support an economy struggling with the impact of the coronavirus pandemic). That said, as reported in our latest 5-Year PGM Forecast (published in June) the pace of PX capacity expansion is projected to moderate in China, as a repeat of last year’s record additions seems unlikely.

In the medium term though, the continued ramp-up of capacity in China will lead to a sharp fall in the country’s petrochemical imports and lower profit margins for many overseas manufacturers, some of which may be forced to contend with reduced operating rates and the risk of plant shutdowns.
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Gold

Source: Bloomberg

Silver

Source: Bloomberg

Platinum

Source: Bloomberg

Palladium

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Gold:Silver Ratio

Source: Bloomberg

Gold:Oil (Brent) Ratio

Source: Bloomberg

Platinum-Gold Discount, US$/oz

Source: Bloomberg

Platinum-Palladium Discount, US$/oz

Source: Bloomberg
Charts - CME Futures Net Positions*

Gold

*Managed money positions; Source: Bloomberg

Silver

*Managed money positions; Source: Bloomberg

Platinum

*Managed money positions; Source: Bloomberg

Palladium

*Managed money positions; Source: Bloomberg
Charts - ETP Holdings

Gold

Source: Bloomberg

Silver

Source: Bloomberg

Platinum

Source: Bloomberg

Palladium

Source: Bloomberg