Analysis: Asia's unquenchable thirst for oil to outpace 2017 refining growth

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Asia is gearing up to witness new refining capacity growth in at least four countries in 2017, but capacity reductions in some top consuming nations will pull down the net addition to a level that would be lower than the anticipated demand growth the region is likely to see this year.

While China, India, Taiwan and Vietnam are expected to add to their refining capacities this year, Japan will witness closures, while some independent refiners in China might be forced to give up capacity, analysts and market participants told S&P Global Platts.

"Oil demand growth in the Asian region is expected to exceed the net refining additions this year," said Sri Paravaikkarasu, Head of Oil, East of Suez, at Facts Global Energy. "And looking at the next five-year horizon, oil products demand growth should exceed net refining additions every single year, helping to clear product surplus somewhat."

Growth in India is set to be one of the strongest, with the rise in oil demand expected to outpace that of China's for the third year in a row this year, according to Platts Analytics. Indian demand is expected to grow by 7% year on year to 4.13 million b/d in 2017, while China's oil consumption is expected to rise by only 3% to 11.5 million b/d in the same period.

Looking at the overall oil products demand, FGE expects Asia's oil products demand to grow by 950,000 b/d in 2017, while Wood Mackenzie expects demand to grow by about 660,000 b/d in the same period.

"We expect a net capacity addition of 430,000 b/d in Asia Pacific for 2017. Oil products demand is expected to grow by 660,000 b/d in 2017. So demand growth will outpace capacity growth in Asia in 2017," Suresh Sivanandam, Senior Research Manager, Refining and Chemicals, at Wood Mackenzie, told Platts.

POCKETS OF EXPANSION

In China, CNPC's 260,000 b/d PetroChina Anning Refinery in landlocked Yunnan province is expected to come online in 2017, but despite this the net refining capacity addition is seen lower as independent refineries are expected to reduce capacities following government crackdowns.

"We expect at least about 100,000 b/d of refining capacity [at various Chinese] independent refiners to possibly disappear in 2017," Paravaikkarasu said. "Their crude volumes are getting squeezed."

In India, state-run Bharat Petroleum Corp. Ltd.'s Kochi refinery is expected to add about 113,000 b/d capacity to its existing 190,000 b/d, while capacity of the Bhatinda refinery of HPCL-Mittal Energy Ltd. is expected to rise by about 42,000 b/d from the existing 180,000 b/d.

In addition to India and China, Taiwan's Talin refinery is expected to see capacity expansions, while Vietnam will bring online its new Nghi Son refinery this year.

Taiwan's CPC Corp. expects to complete the construction of its new CDU, hydrotreaters and a condensate splitter at the Talin refinery in the first quarter of 2017, delayed from an initial schedule of end-2016.

The expansion will boost Talin's total capacity to 350,000 b/d -- or 400,000 including the new condensate splitter -- from 300,000 b/d currently. The plan includes the replacement an older 100,000 b/d CDU.

Vietnam's new Nghi Son refinery, with a capacity of around 185,000 b/d, is expected to be operational in early 2017.

"The expansions in India, China, Taiwan and Vietnam should take new refinery capacity additions to about 690,000 b/d in 2017. But we also expect capacity cuts to the tune of 447,000 b/d in Asia, including 347,000 b/d in Japan and 100,000 b/d in China. That should take the net refinery capacity additions in Asia to nearly 250,000 b/d," Paravaikkarasu said.

Japanese refiners are preparing to cut around 340,000-350,000 b/d of crude distillation capacity by the end of March 2017 to comply with current regulations, which require the refiners to raise their residue cracking ratio to an average of 50% by March 2017, from 45% at the end of March 2014.

Refiners can achieve this by either adding more secondary units or cutting their nameplate crude distillation capacity, with all expected to opt for the latter. This will bring Japan's refining capacity down to 3.44 million-3.45 million b/d at the end of March 2017, from around 3.79 million b/d currently.

REFINING LANDSCAPE

Despite an anticipated rise in oil products demand in Asia, ample supply from China was seen to be a key factor influencing refining margins in 2017.

In addition, rising crude prices would also keep margins under pressure.

"China's oversupply could be a game-changer for Pan-Asia refining," Nomura said in a recent research note. "We expect Asian refining margins to be under downward pressure until the inventory has been drawn down."

China in 2016 flooded the Asian markets with competitively priced oil products. Its diesel and gasoline exports in the first 11 months of 2016 grew by 112% and 74% year on year, respectively, to 303,000 b/d and 222,000 b/d, as the country aggressively pushed sales overseas amid weak demand at home, according to customs data.

Analysts expect the trend to continue this year.

"Margins are expected to remain positive through the first half of the year before turning slightly negative in the second half. Singapore complex margins should average $6/b," Paravaikkarasu said. "We should remember that crude oil prices are recovering too."

Asia witnessed wild swings in gross refining margins in 2016, with GRMs climbing to above $10/b in early 2016, but weakening to as low as $3/b in August before recovering to $5/b in October, Nomura said in the note. It expects crude oil prices to rise to $60/b in 2017 on the back of OPEC's decision to cut output.

"We may not see fantastic margins this year in Asia, which witnessed a golden period in 2015 and early 2016. But, still, there is room for margins to hold up well and be in the positive territory in 2017," said a senior Asia-based oil analyst.