



POTEN & PARTNERS

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POTEN TANKER OPINION



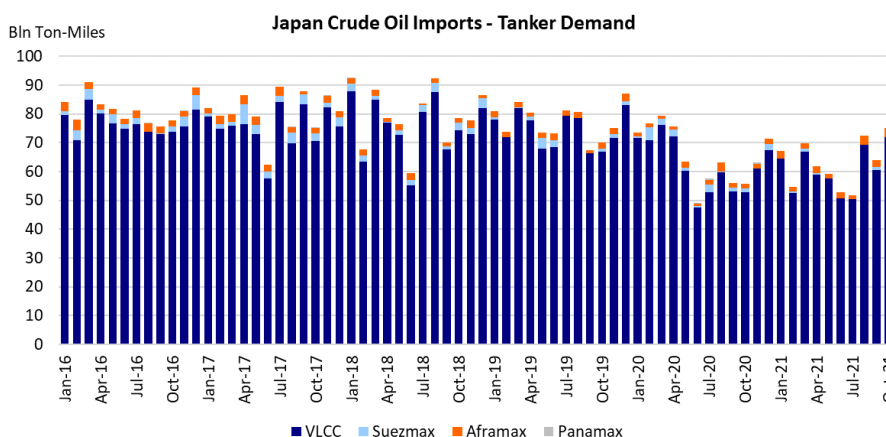
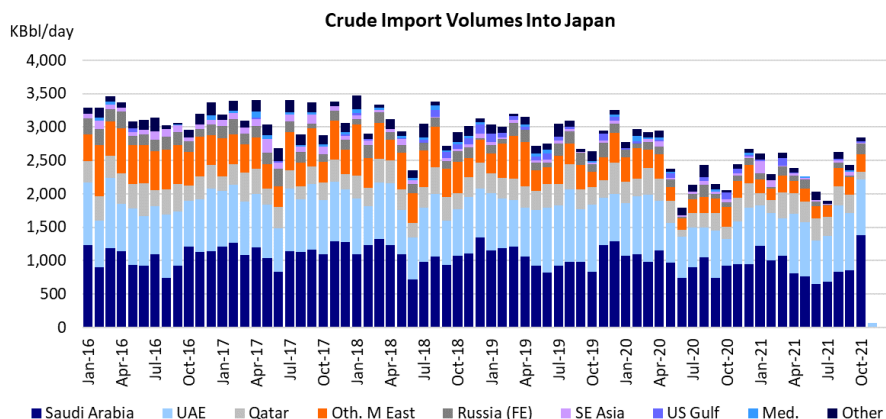
Under The Radar

Japan's oil demand is staging a strong recovery

For much of the 1970s and 1980s, Japan was a shipowners' dream. It was a rapidly growing economy that almost completely relied on imports of raw materials to fuel its expanding industrial base. Before China took over in the early 2000s, Japan was the key driver of ton-mile demand in Asia. For many years, it dominated the LNG, iron ore and crude trades in the region. Japan's GDP growth has slowed significantly in recent decades due to a maturing economy and an ageing population. The rise of China and India has overshadowed the land of the rising sun. However, the importance of Japan for the global tanker market is not to be underestimated. It still generates 8% of global crude oil ton-mile demand and after hitting a rough patch during the pandemic, Japan's oil demand has staged a strong recovery in recent months. Since Japan's imports are largely done on Japanese controlled tonnage, the increased activity is not immediately apparent in the tanker spot market. However, if this pickup in oil imports continues, it can be an important driver for overall tanker demand (and rates) in the coming months.

In recent months, the world is starting to recover from Covid-19 and the global economy is gathering steam. The resulting boost in energy demand, combined with disappointing renewable power generation (hydro and wind) in parts of the world, has created an acute shortage of natural gas, LNG and coal supplies. This supply crunch has created a run-up in energy prices and also triggered a massive switch to oil product and direct crude burn.

At 30 GW (GigaWatts) Japan is the world's largest user of oil-fired power capacity. On top of that, Japan has some 10 GW of dual-fired capacity that can switch from gas to oil and another 8-10 GW of deactivated powerplants which could use oil. Four of the seven largest oil-fired power plants in the world are located in Japan (the other three are in Saudi Arabia). In their October Oil Market Report, the IEA mentioned that "provisional August data already indicates that there is some unseasonably high demand for fuel oil, crude and middle distillates for power plants in a number of countries, including China, Japan and Pakistan in Asia." The APEX data from Lloyd's List Intelligence (Chart 1) seems to confirm the IEA observation, with a marked increase in Japanese oil imports in August, September, and October. Japanese imports in October are projected to reach almost 3.0 million barrels per day (Mb/d), the highest import volume since before the pandemic. If normal seasonal trends hold this year, November and December imports should be even higher. Since Japan sources about 80% of its crude oil from the Middle East (primarily Saudi Arabia and the United Arab Emirates), this bodes well for long-haul tanker demand.



Source: Lloyd's List Intelligence

While Japanese oil demand will be supportive for the tanker market in the short-term, what are the prospects for the medium to long-term? Over the last 20 years, Japan's oil demand has been gradually declining, from 5.48 Mb/d in 2000 to 3.74 Mb/d in 2019. Demand dropped to 3.33 Mb/d in 2020 due to the pandemic, but it is conceivable that future oil demand in Japan will never reach 2019 levels again.

As a country, Japan remains very dependent on fossil fuels and that seems unlikely to change in the short-term. In 2019, about 6% of Japan's energy supply came from renewable sources, a small percentage compared to some European countries like Germany (13%) and the U.K. (12%), but more than the U.S. (4.3%). Renewable output is growing, but Japan's mountainous geography makes it difficult to build large-scale solar and wind farms. Nuclear energy remains deeply unpopular in Japan after the Fukushima accident and importing large volumes of renewable fuels such as ammonia and hydrogen, which could use Japan's existing energy infrastructure is not (yet) a realistic option.

Japan will remain an important market for crude oil tankers (in particular VLCCs). In the winter months demand could receive a 70,000 b/d boost from the power sector. In the longer term, tanker ton-miles will be underpinned by continued strong demand for oil in Japan.