POTEN & PARTNERS

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POTEN TANKER OPINION

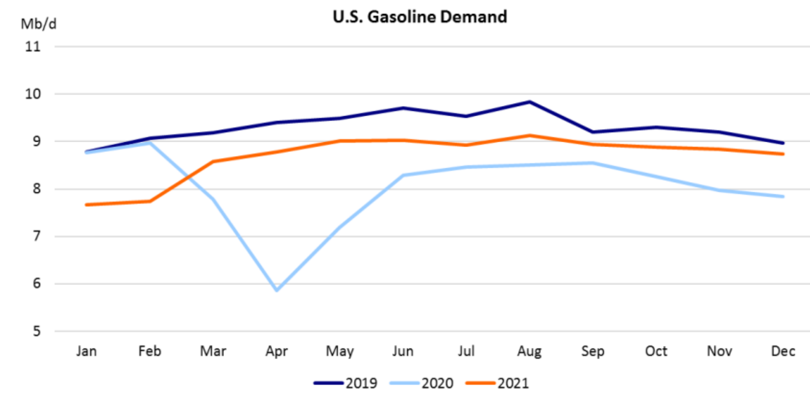
Are We There Yet?

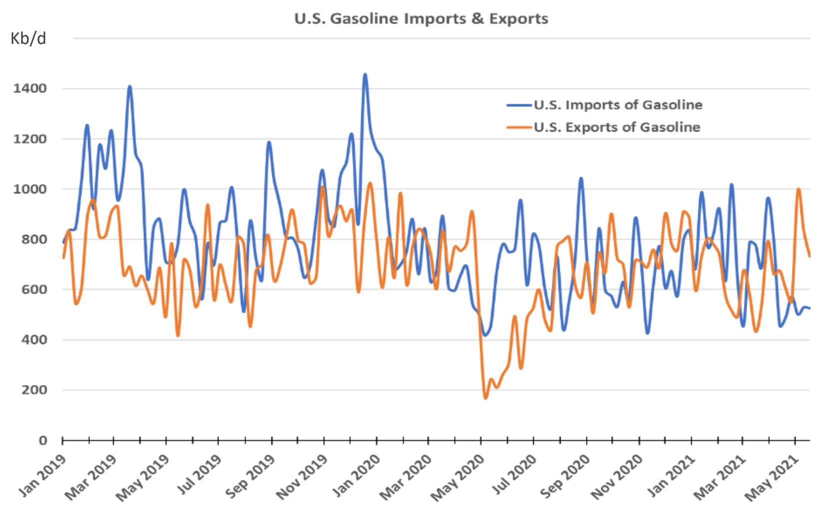
The summer driving season in the U.S. is about to start

Traditionally, the upcoming Memorial Day weekend marks the beginning of the summer driving season in the U.S. For a variety of reasons (weather, summer road trips, school vacations, etc.), Americans tend to drive more in the summer than in the winter, and this year, we have the added dimension of the country coming out of the Covid-19 pandemic. Most of the movement restrictions and mask requirements have been lifted across the United States in recent weeks (in particular for the people that are vaccinated) and the expectation is that it is going to be busy on the road. Many American will be travelling this weekend (and this summer) to take the trips that they postponed during the pandemic. A lingering impact of Covid-19 is that the overwhelming majority of people will drive their own car this weekend, rather than use more "public" modes of transportation such as planes or trains. The growth in Vehicle Miles Travelled (VMT) over the summer will closely match the growth in gasoline demand rather than electricity demand, because, despite the continued growth in sales of electric vehicles, they still only represent less than 2% of passenger cars in the U.S. Will all this driving and associated gasoline demand have any impact on the tanker market?

The American Automobile Association (AAA) expects that 37 million people will take trips (50 miles or more) this Memorial Day weekend, an increase of 52% from last year. However, travel will still be down 10% from 2019 and, even in the longer term, gasoline demand is not expected to fully recover to their previous highs due to the increasing penetration of electric vehicles. In the first quarter of 2021, sales of battery only electric vehicles (EV's) reached nearly 100,000 units, a record, representing a 44.8% increase compared to Q1 2020. Combined with the 200,000 hybrid electric cars, the total electrified market was more than 300,000 vehicles, which is a little under 8% of total U.S. car and light vehicle sales. It is expected that the growth of EV's will accelerate as more models become available and government policies make them more attractive relative to gasoline powered cars. Another factor that could lead more drivers to consider electric cars is the increasing price of gasoline. Earlier this week, the average retail price for regular gasoline in the U.S. was $3.02 per gallon, the highest since 2014.

The impact of the summer driving season on the tanker market has diminished over the years. Under normal circumstances, the U.S. has abundant refining capacity and gasoline inventories as well as ample pipeline capacity to distribute the products to consumers, so the market should be well supplied. However, the last 16 months were not "normal circumstances". As can be seen in figure 1, U.S. gasoline demand cratered in March/April





Source: DOE Energy Information Administration

2020 as a result of the pandemic lockdowns. For the first few months of 2021, gasoline demand remained below year-ago levels, but we have seen a strong recovery since March 2021. Further demand increases are expected throughout the summer as U.S. economic activity accelerates post Covid. However, so far this year, gasoline supply has been lagging demand growth. The cold snap that affected Texas in mid-February temporarily shut down refining infrastructure in the U.S. Gulf area and the recent cyberattack on the Colonial Pipeline disrupted critical refined product flows from the U.S. Gulf to the U.S. Atlantic Coast. This tightened the market and pushed up prices.

The way gasoline demand influences the tanker market is through imports and exports, since these movements are predominantly seaborne. There is a Jones Act fleet, moving refined products between U.S. ports, but the U.S. cabotage market is small relative to the international product trade. As can be seen in figure 2, both imports and exports of gasoline were negatively affected by Covid-19 in April/May 2020, but U.S. exports were initially hit much harder. Since the third quarter of 2020, both import and exports of gasoline have been averaging around 700,000 b/d, even though they show significant weekly volatility. The average for 2019 was around 735,000 b/d, so there is some upside potential. A further recovery of U.S. gasoline exports will be closely tied to when and how the Latin American economies recover from Covid-19, since those are the most important export destinations for U.S. refiners.

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