Five commodity themes for 2020

What will be the biggest drivers and concerns for global energy and commodity markets in 2020? S&P Global Platts president Martin Fraenkel shares his outlook

This year has been marked by a tug of war between geopolitical tensions and macroeconomic concerns, rangebound commodity prices and – perhaps most importantly – rising consumer awareness of climate change. As we look ahead to 2020, we think the year will bring some of these themes into even sharper focus.

The upcoming US presidential election, a decelerating Chinese economy and rapidly evolving technology will once again keep commodity markets unpredictable, even for the most seasoned observer.

Here are my personal five commodity themes to watch during the coming year.

Energy transition

Energy transition is going to be ever-present, driving discussions and strategic planning in 2020. World leaders in both politics and industry are under mounting pressure from consumers – particularly in the West – to deliver increased energy produced with dramatically lower emissions and in more sustainable ways.

Heightened awareness by the Extinction Rebellion movement and the activist Greta Thunberg has put both governments and companies on notice of people's expectations that action must be taken to keep the global average temperature rise at no more than 2 degrees Celsius.

While it is certain that this shift will require huge investment, the way forward is still emerging. Numerous technologies and solutions are vying for the same investment dollars that are already shifting away from traditional higher-carbon intensity industries. There will likely be a heavy reliance on subsidies, which in turn are dependent on policy. No one single approach is likely to win out, at least in the short term.

In terms of transportation, the focus has been predominantly on electric vehicles, while there is also increased investment and research into the use of hydrogen for heavy duty and long-distance transportation. But biofuels look set to take center stage in 2020, as favorable economics and the consumer-led call for immediate action have revitalized support for the fuel, particularly in Europe.

Biofuel blending looks to be the fastest route to reducing emissions, with consumption expected to increase in 2020, eating into gasoline and diesel's share of the market and adding renewed pressure on oil refiners.

With more than 1 billion conventional cars in the global fleet, road transport currently accounts for 20% of global carbon emissions, a number that is not likely to fall without a bigger solution for infrastructure. Based on this trend, S&P Global Platts Analytics forecasts that global oil production will need to increase to meet rising demand from road transport over the coming years.

In the US, the situation is more complex, with tensions apparent between federal and regional policies. At the same time, natural gas is cheap, putting pressure not only on coal use for electricity production, but also on cleaner nuclear, renewables and energy storage.

Of course, the race to renewables alone will not be enough to meet aggressive carbon reduction targets. To deliver these significantly lower emissions, every type of energy and product needs to reduce its carbon intensity – we will need carbon capture and storage and consumers will need to be more energy efficient.

Economic slowdown in China

Tariffs and trade wars will continue to dictate global pricing and trade flows for multiple commodities in 2020, but the consequences of the ongoing dispute between China and the US, particularly, are now rippling out into the economy, sparking fears of another recession.

The dispute – now in its 21st month – has exacerbated a change in local Chinese policy that aims to wean state-owned enterprises and banks off stimulus packages. The combined effect is that the rate of China's economic growth has slowed to a pace not seen since 1992.

The effects of this domestic slowdown and weaker fuel demand growth have resulted in increased gasoil, gasoline and jet fuel exports, putting pressure on Asian commodity prices and refinery margins.

Platts Analytics expects that exports of gasoline, gasoil and kerosene in 2019 will reach an estimated 54.5 million mt (1.17 million b/d) if no more rounds of export quotas are released by the year end. This is nearly a tenth of the country's crude imports, which is roughly equivalent to Saudi Arabia or India's refined exports – both regions where refineries also cater heavily to export markets.

This figure is likely to rise in 2020, with the significant growth in new refineries resulting in total capacity reaching 18.71 million b/d, with another 320,000 b/d still under construction.

China's crude imports have remained robust in 2019 as a result, surging 17% year on year to hit a historical high of 10.76 million b/d, or 45.51 million mt in October. Sinopec, the largest refiner in the country, forecasts that imports could reach 500 million mt in 2019.

The rise of new markets

Despite strong electric vehicle production, the slowdown in Chinese demand following the government's decision to reduce state subsidies on EVs in July is weighing heavily on the market (with sales down 50% year on year).

While many are hopeful that EV sales could be poised to rebound in 2020, significant costs associated with buying an EV and limited infrastructure remain a barrier to entry for many. Although leading manufacturer Tesla has moved back into the black this year, costs in the sector as a whole are expected to come into parity around 2022-23, while 2025 is widely touted as the year when sales may take off globally.

Similarly in the petrochemicals market, the transition from virgin to recycled plastics is under way, with many brand owners making global commitments on the back of European policies. However, virgin polymers and feedstock monomers are expected to remain more competitively priced into the mid-2020s, and this is challenging traditional discounts for recycled material. It remains to be seen whether the consumer push can be sustained despite unfavorable economics, and manufacturers will have to test consumer appetite to bear the cost of increasingly recycled packaging.

Investments are under way globally, but as with all nascent markets, infrastructure that makes industries truly scalable and markets commoditized will take time to develop.

Weather-driven market events

Weather-related demand swings have always been a feature of commodity markets, particularly natural gas and electricity, but the cycle of significant climate events is increasing.

In the spring of 2019, US farmers were unable to plant crops on 19.4 million acres in the Midwest. This was the largest number of so-called “prevent plant” acres since the government began tracking this type of data in 2007. In 2018, the number was 1.9 million acres.

The cause of this was flooding due to an accelerated snow melt in the spring, which was caused by record rainfall at the time. Over 14 million acres that were intended for corn, soybeans and wheat went unplanted, sending corn and soybean prices to multi-year highs.

As agriculture and biofuel demand grows, these swings in demand will get larger as will the demand for heating fuels, as growing populations get access to domestic gas or LPG, making the demand for these commodities increasingly vulnerable to weather conditions.

Beyond blockchain

2020 could be the year of the centralized ledger, but potentially without Blockchain technology itself.

Blockchain has huge advantages for security and encryption, with some early adopters using the software in North Sea oil contracts. But speed, cost and energy intensity mean it is currently difficult to scale for many players in the commodity markets.

Smart contracts that offer a similar level of security are already a reality, albeit with centralized ledgers using the similar reconciliation and physical documentation of trade but without the need for simultaneous record keeping, thereby reducing the energy, latency and cost. These efforts could significantly reduce costs and lower barriers to entry across commodities markets.

Platts has already leveraged this technology, launching Platts Trade Vision in November 2019, a cutting-edge tool that allows price submissions into Platts US Natural Gas benchmark indices. Already nearly half of our data is being submitted through Trade Vision after just a few weeks.

Data automation and artificial intelligence will play an increasingly transformative role in 2020. Successful trading has always been focused on nimble operations and scale, but tighter margins and increased competition have made participants look at accessing faster, broader datasets to gain an advantage.

In a world where data is now more valuable than oil, the seriousness of efforts by companies – including Platts – to harness the power of data and technology cannot be underestimated. ■

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