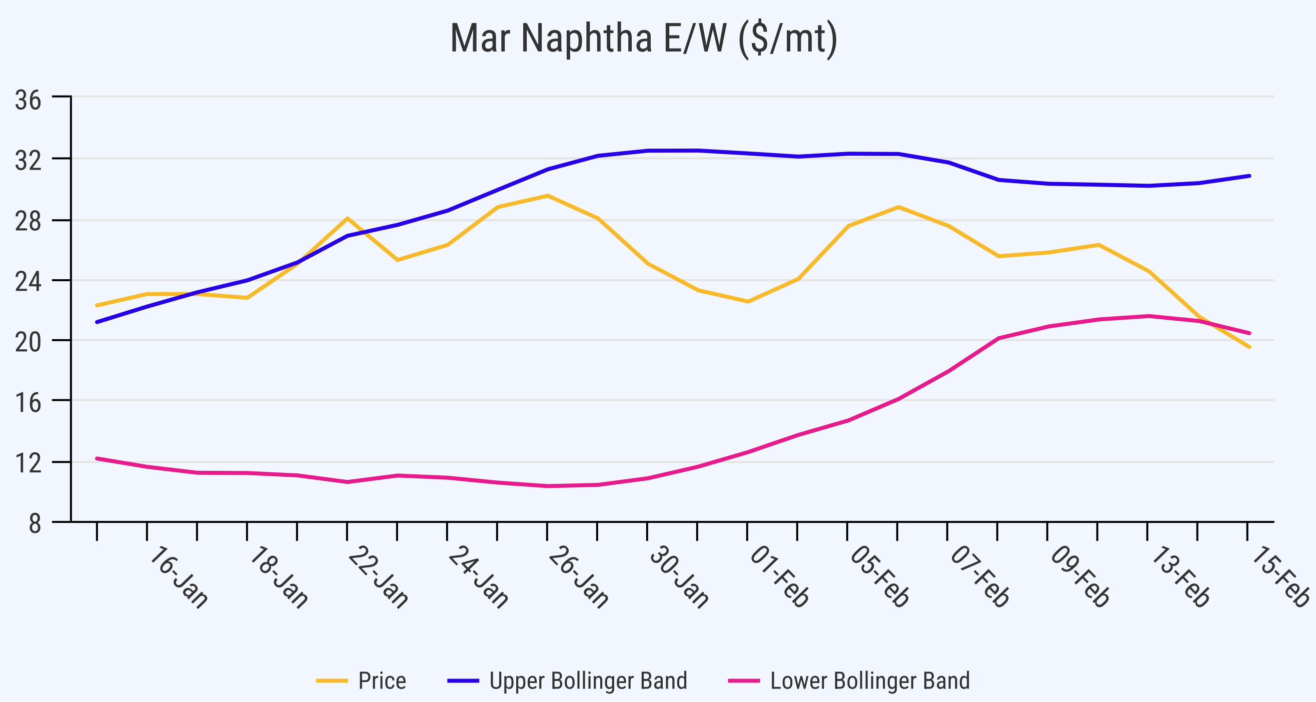
Logic: Short Mar Naphtha E/W

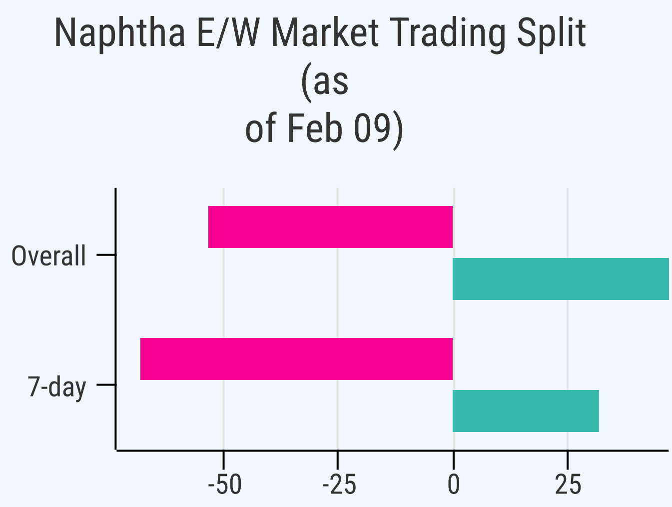
The Mar naphtha E/W contract has been an incredible contract to follow into this year. We first saw prices surge upwards on the back of attacks on ships by the Yemen-based Houthis in the Red Sea. Prices for the Mar E/W rallied from under $15/mt on Jan 10 to $23/mt in the following week. This strength intensified towards the end of January, on the back of drone attacks by Ukraine on Russian oil infrastructure, generating significant volatility surrounding the supply of Russian naphtha - which prices off the Eastern MOPJ benchmark.

The Mar E/W contract skyrocketed to a high of $35.50/mt on Jan 29 but ultimately settled at $28.75/mt the same day - recording the magnitude of volatility in the E/W during this period. Finally, despite easing off to $22/mt on Feb 01, the E/W rallied to levels flirting with the $29/mt handles on Feb 06 following a slew of further attacks on Russian refineries.



The Trade

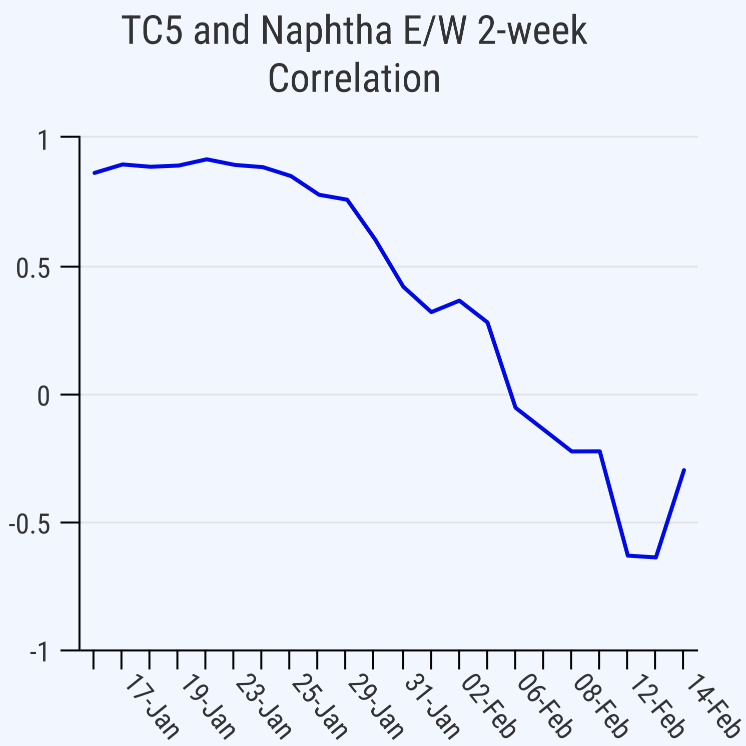
Despite the geopolitical risk premia buoying up the naphtha E/W, we recommended **shorting the Mar E/W** in our Feb 13 naphtha report. This was a contrarian trade considering the still-prevalent uncertainty surrounding Russian naphtha supply. Notwithstanding this, we expected the refinery attacks would be priced in by market participants considering news on the Ilsky refinery, which was attacked on Feb 09, expecting to be back online by Feb 18. Furthermore, we found this view corroborated by Onyx's market positioning on the Mar naphtha E/W, which highlighted a 7-day market trading split of 30:70 long:short.



Logic: Short Mar Naphtha E/W

Freight

Adding to this, the bullishness in the E/W was largely a function of freight becoming more expensive. However, the fortnight to Feb 12 highlighted an inverse correlation between the TC5 freight (from the Middle East to Japan) and the Mar E/W contract. This decline in correlation was perhaps a result of increasingly more cargo opting to make their journeys via the Cape of Good Hope rather than the TC5 route - which requires ships to pass by the Red Sea. This decrease in correlation was further evidenced considering the increase in TC5 freight rates, which surged from under $54/mt on Feb 07 to $59/mt on Feb 12. The Mar naphtha E/W declined from $27.50/mt to $26.25/mt in the same time frame.



Recent Data

Interestingly, we noticed a small rise in the two-week correlation between freight and the naphtha E/W between Feb 13 and Feb 15, however, we also observed the TC5 freight weaken from $55.40/mt to $55.20/mt in the same time. Despite this, we will continue to monitor this correlation for signs of shifting sentiment in the E/W.

In addition, the COT dashboard now highlights a 7-day long:short split of 55:45 for the naphtha E/W, highlighting a resurgence of bullish interest in the naphtha arb. However, it remains important to note that the E/W is made up of MOPJ and the NWE naphtha - both of which are more liquid than the naphtha E/W and are hence also important drivers of the E/W's price action. Despite the relatively bullish picture in the E/W, both MOPJ and the NWE naphtha now highlight a bearish 7-day skew with a 7-day market trading split of 40:60 long:short in both the prompt MOPJ and the NWE naphtha. Considering still weak petchem margins and the fact that naphtha prices remain high in both regions, we may see this bearish flip in sentiment worsen, adversely impacting the Mar E/W. Hence, we continue to hold this trade but we will continue to monitor how the recent buying in the E/W interacts with this bearishness across the naphtha complex.