CHINA AVIATION OIL SHUNS DIVERSIFICATION; JET FUEL FOCUS RETURNS

News / Airlines

China Aviation Oil is going back to basics -- its core aviation fuel business -- after pursuing an aggressive **diversification** strategy over the last two years.

Economic uncertainty in China and low commodity prices forced the company to rethink its strategy and it has concluded that focusing on expanding its jet fuel business is what will generate stable returns, CEO Meng Fanqiu said recently.

CAO is currently the largest physical jet fuel trader in the Asia Pacific region and the sole importer of the aviation fuel into China.

The company in 2012 launched a diversification strategy to cut its over-reliance on jet fuel and entered into gasoil, fuel oil and petrochemical trading, which contributed to its profits when the market was bullish and Chinese demand robust.

But trading margins have been thin or even negative at times since last year due to low prices and a slowdown in China's economy.

The company recently suspended petrochemical trading and is now planning to focus on jet fuel and globalize its jet fuel business, Meng said at the company's corporate briefing in Singapore last week.

INTEGRATED JET FUEL SUPPLY CHAIN

CAO plans to grow its international presence as an important aviation fuel service provider at international airports, Chief Operating Officer Jean Teo said at the briefing.

Meng said CAO will develop an integrated jet fuel supply chain. "The supply chain from procurement, transportation, marketing to fueling will bring synergy, while trading generates added value," he said.

The value chain works well at Shanghai Pudong Airport and CAO is developing the chain at the Hong Kong International Airport, Meng said.

CAO's associated company CNAF Hong Kong Refuelling Ltd. recently became one of three companies to get a refueling license at HKIA. The other two companies are Sinopec and PetroChina.

Winning the license for HKIA is proof of CAO's ability to provide refueling services at international airports, Meng said, adding that this will help the company to expand its refuelling business at more international airports.

The company is to globalize the model and extend its international supply network to more than 30 airports across the Asia Pacific, Europe and Americas in the next four years, Teo said.

CAO last year joined the Los Angeles-based LAXFUEL, the largest jet fuel consortium in the US, designed to create an open market and enable the sharing of fuel storage facilities at airports. The company sent its first jet fuel cargo to Los Angeles this year.

CAO supplied around 4 million mt of jet fuel in airports outside China in 2014, accounting for 40% of its total supply, Chief Financial Officer Wang Chunyan said.

The company will also invest more on infrastructure related to jet fuel supply, "which will bring more stable and long term returns" than trading, Meng said.

In 2014, the company registered a gross profit of $27.40 million from trading and fixed commission, down 47% from 2013 due to the negative impact of oil price volatility on trading profit.

Return on investment in associated companies fell 7% to $43.19 million. These companies include oil tanks in southern China and South Korea, pipelines linking Tianjin port with international airports in Beijing and Tianjian in northern China, as well as airport refueling facilities in Shanghai Pudong and Hong Kong airports.

ROBUST CHINA MARKET

To secure refueling contracts in the international markets, CAO plans to leverage its strategic alliances with major Chinese airlines, which are expected to add to their fleet and boost overseas refueling volumes, Teo said.

As the largest physical jet fuel trader in Asia Pacific and the sole importer of the fuel into China, CAO sees great potential in jet fuel demand growth from the civil aviation sector, driven by robust tourism, trading and logistics in the Asia Pacific region.

China's 'One Belt, One Road' scheme, which aims to connect the country with Europe, Central and Southeast Asia as well as Africa, will boost air traffic and eventually demand for jet fuel.

Total turnover of China's civil aviation industry is projected to reach 170 billion mt kilometer in 2020, at an average annual growth of 12.2%, Meng said, citing the Civil Aviation Administration of China, adding that air passenger traffic volume is expected to nearly double from 392 million in 2014 to 700 million.

China is expected to replace the US to become the top aviation market by 2030, Meng said.

Meng also expects to see a significant increase in jet fuel imports into China from 2020, when China's jet fuel demand growth outpaces the country's production capacity expansion.

It will result in higher importing profit for the fuel, Meng said. BUNKER AND CLEAN FUELS

In other areas, Meng said CAO will further develop its bunker fuel business since it follows a similar model as jet fuel.

CAO currently trades 4 million mt/year of bunker fuel, accounting for 10% of the market in Singapore -- the world's biggest bunkering port, according to Meng.

The company also plans to leverage global trends by supplying as well as trading future clean aviation and bunker fuels, COO Teo said.

In the clean transport fuels arena, CAO plans to expand its footprint in emerging markets such as Indonesia, with demand from agriculture, mining, tourism and air chartering industries.

The company is the importer of AvGas (aviation gas) into China and supplies the fuel internationally, with exclusive distribution rights in 14 Asia Pacific countries.

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