Tankers- decorum upstairs, hoopla below decks

Contributed by

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The shipping markets don't always take vacations- the tanker market continues to show a great surge of optimism. Low oil prices and resultant changes seaborne tanker flows caused ton miles to spike upward, with inefficient routings leading to a stretch of existing vessel supply. The jury is still out on the longevity of the rally; investors- who sit on the upper decks, have been very cautious on accumulating tanker shares. But we can say that the stronger spot market, like here and now, has led to expectations of a stronger hire environment going forward, like in the future. Investors are aware of the hoopla down on the lower decks- and are still studying it. As always, there are legitimate differences of opinion on where we are in the cycle, and, therefore, whether early cycle valuations (which are more generous than mid cycle multipliers) might be applied to the tanker shares. The oil price structure adds another wild-card- will the "contango", which could now support floating storage in tankers (taking supply out of the market) become an ongoing factor, as it did in 2009 and 2010?

From down on those decks populated by shipping people and freight traders, the dramatic shifts in expectations reflects real optimism that can be readily bench-marked. The settle prices for "paper" FFA transactions which I follow closely don't move in a vacuum; across the sectors, they will exhibit a correspondence, albeit not following dollar for dollar, with the respective forward physical (period time charter) hires- discounted below the FFA prices.

The newfound market optimism was visible in the estimated hires for a one year period charter on a modern VLCC. At mid-year, a time of a lengthy doldrums for VLCCs, most analysts would have pegged such charters at around $22,000/day- a level based on cost recovery, ie one reflecting a breakeven (operating cost plus a capital component) that owners could lock into. Fast forward to end December, when the spot equivalent for notional TD3 (AG to Japan) VLCC voyages stood above $60,000/day, after having peaked above $90,000/day TCE (by some analysts reckonings) in mid December- the forward rate- for physical time one year time charters was estimated variously between $33,000/day and $35,000/day. The period rate mirrors, with a discount, the daily TCEs for 2015 of $37,000 (Q2), $35,000 (Q3), $43,000 (Q4) and $32,000 (2016, Q1- with the precise equivalent subject to estimates of fuel prices throughout much of 2015).

The Suezmaxes, which had also seen strength throughout the year as voyage lengths increased (as TD5- Nigeria to the US Northeast, evaporated); at year-end, one year period charters were worth roughly $27,000/day, compared to $18,000/day in mid year physical period time charters. The time charter equivalent (TCE) of the spot TD20 (West Africa to Rotterdam, rather than Philadelphia), which had soared in November only to back off in early December, ended the year an upward thrust- reaching up to nearly $60,000/day at the year end. The period rate- less volatile than spot, is reflective of optimistic TCE's (similarly to the larger VLCCs) of $32,000 (Q2), $29,000 (Q3), $32,000 (Q4) and a very cautious $20,000 (with Q1 of 2016's TCE being subject to fuel price estimates).

The Aframaxes have also gone from strength to strength; the optimism surrounding this sector was evident at end 2014, when one year period hires were estimated to be around $21,000/day for such units- in contrast to the $14,000/day levels (slightly above financial and operating breakevens) prevailing earlier in the year. Spot rates in this sector are volatile and trade-specific- by late December, the TD7 (North Sea to Continent) and TD17 (Baltic to Continent) were exhibiting a seasonal firming with spot TCE's reaching $47,000/day and $74,000/day- respectively. The forward hires were discounted below the volatile spot equivalents- but strength in the minds of paper traders could be seen from the $27,000/day and $38,000/day equivalencies for the "Calendar 2015" FFA positions. The TD9 Aframax run, indicative of shifting trades in the Caribbean, was showing a very healthy line-up of quarterly prices- all around $30,000/day for the remainder of 2015 (still well above the $21,000/day for physical deals of comparable tenor).

The product trades in the Atlantic continue to be strong- arbitrages are supporting increased tonnages of middle distillates from U.S. refineries, to Europe and to burgeoning markets in South America. After a mid December flirtation with trans-Atlantic time charter equivalents, for a basket of voyages on MR (50,000 dwt) product tankers, reaching $44,000/day (compared to a breakeven of circa $12,000/day), the measure has backed off to a hire equivalency around $33,000/day- still very firm (and above all of 2014 up until late November). Still, there is an element of caution in the market. Assessments from the forward paper ("swap") markets are several thousand dollars a day higher; traders have put values around $18,000/day on the trans-Atlantic market equivalencies Brokers estimate that a modern MR ship is worth around $15,000/day for a one year physical deal- reflecting some art mixed with broker science, but undeniably discounted from the swaps.

During the past weeks, chatter heated up as the Obama Administration seemed to be opening up the marketplace for further exports of condensates- there's not a lot of fresh news here, really, and there are still ambiguities about exact processes that qualify. But, nevertheless, the trend towards U.S. exports of crude oil, or at least high-API gravity (light) crude oils, is clear. The big beneficiaries here will likely be LR (long range 70,000 dwt up to around 100,000 dwt) product tankers on long haul trades to Asia- especially when (not "if") the widened Panama Canal opens up. As with all shifts in tanker trades, a holistic look at ton-mile impacts is needed- barrels from someplace else will be backed out. There's been considerable tension surrounding the impact of such exports on the Jones Act- tankers serving U.S. intra-coastal trades (for example Corpus/ Aransas to Philadelphia). However, with elevated foreign hires, it's not like Jones Act tonnage (feeding a smallish portion of refinery inputs) would suddenly be priced out of the market. Neither the investors upstairs, nor the shipping people below decks, have a real clear handle on this one, at least not yet.