Late August slouch takes tanker toll

The tanker market remains gloomy – but prospects seem more promising for larger vessels

For Frontline, the cost of a VLCC waiting 10 days at Fujairah would be absorbed if it meant capturing an additional 10 Worldscale points on a rebound
[Photo: Dietmar Hasenpusch]

Late August has followed an established pattern, shaping up as a sluggish stretch in the tanker market calendar. This time, the doldrums have come around with a vengeance – and against the backdrop of active management of output by OPEC members across the entire spectrum of the tanker markets.

In the larger vessels, the undercurrent of optimism regarding the traditional strength later in the year continues to percolate. The upward sloping structure of the FFA curves illustrate this clearly; where spot VLCCs quoted at W49, for the Gulf/East route, equate to less than $11,000/day, the December position is pegged at W75, which calculates back to more than $37,000/day.

Imarex's tanker specialist Michael Reardon summed up the feelings in a client memo, saying: "Optimism can be found, however, on hopes of a relatively impressive fourth quarter – though the current supply function will remain an obstacle until demand can chip away at the position list." In another memo to his clients, he wrote: "Both VLCCs and Suezmaxes are running near opex levels on benchmark routes as supply has overwhelmed demand." Bloomberg News, which conducts an informal survey of VLCCs that are available to load cargo in the Gulf, estimated the magnitude of the surplus at 20%.

Frontline, in its 2Q10 results presentation, likened the tanker market to a sleeping bull, saying: "It's not dead, only resting." Management suggested that the cost of VLCC waiting 10 days at Fujairah would be absorbed if it meant capturing an additional 10 Worldscale points on a rebound.

Although the bigger ships attract more attention, smaller product carriers have been mired in similarly difficult market conditions. Traditionally, trades such motor gasoline and diesel in the North Atlantic, or naphtha in Southeast Asia, have been driven by arbitrage differentials, usually catalysed by a jump in demand (or a sudden tightening, or other disruption, in supply).

Analysts at Lorentzen & Stemoco (LS), lamenting the low returns seen by owners of product tankers, commented: "Arbitrage opportunities remain few and far between at the moment and any opening windows, offering owners some hope of rate increases, have promptly been shut."

The closely watched 3-2-1 crack spread on NYMEX crude oil, a proxy for refining margins, has lately been hovering around $6/barrel, a differential (price for outputs less cost of the input) near the low end of its recent range.

Rates remain low

The weakness has been tied to reports of continued US economic malaise (based on snippets garnered from the Federal Reserve, and from disappointing reports regarding housing). In the US, stockpiles of crude and refined products are at historically high levels.

The result has been less need to bring in clean product; owners of MR product tankers are seeing rate quotes of W134 in the North Atlantic TC2 (Rotterdam into New York harbour) trades, working back to less than $5,000/day – a level insufficient to fully cover most owners' operating expenses.

In the East, the situation is not much better on the smaller ships; the TC4 (Singapore-Japan) rate of W150 was yielding less than $4,000/day. LS analysts have said: "Markets in the East have had more activity compared to the West, however, rates remain at low levels." One bright spot, amid the dismal market canvas, could be found in the LR tankers trading from refineries in the Gulf out to Japan (the TC5 route), where the prevailing 165 rate worked back to nearly $15,000/day. But analysts sensed the fragility of this situation, as receivers of feedstocks in Asia were holding back on their purchases.

In spite of the weak nearby returns, owners of product tankers, and investors in equities such as Torm, Omega and d'Amico have pictured a future where Asian refineries will export increasing surpluses of products.

An analysis by Bloomberg has suggested that rising refining capacity, at a time of a Chinese economic slowdown, will generate growing surpluses of refined material. With weak margins at home, but with a need to amortise fixed costs by keeping the refineries in operation, it is postulated that refined products will then be exported. F