Bright spots for tankers

Demand is depressed but there is hope for the refined products sector

The seasonal slump continues to bedevil owners in the tanker markets. In an Imarex comment, analyst Michael Reardon, wrote: "The Gulf market cannot get out of its own way, as too many ships are available for too few cargoes".

Reardon identified one temporary bright spot in the Suezmax market. "Rates in West Africa have moved to the upside as owners saw an opportunity to push back – but with limited September stems remaining, the upturn may have a short shelf life."

Attendees at Jefferies & Company's Shipping and Logistics conference in New York last week heard from senior executives of major listed tanker companies that the crude and product tanker markets continue to be soft, certainly in the near term. This was supported by OPEC which, in a statement, revealed its overall world oil demand projections for 2010 and 2011 were unchanged at 85.5M barrels/day and 86.6M barrels/day, respectively. Depressed economic growth could reduce this demand further, OPEC warned.

"In an oversupplied market characterised by depressed demand, refining operation levels are not expected to rise significantly in the coming months," OPEC said. It alluded to the sluggish products markets in the US and Europe and, particularly, where a historically large supply overhang kept upward pressure on gasoline prices well under control, at the tail end of the US summer driving season.

'Gasoline glut'

Poten Energy Services analyst Abe Glass backed up OPEC, describing a retrenchment in North American refining margins – as proxied by the '3-2-1' crack spread, at a Capital Link event. A recent *Wall Street Journal* article entitled 'Gasoline glut rides out the summer' noted that speculative inbound cargoes of gasoline (the '2' in 3-2-1) have actually added to the record inventories.

Nevertheless, experts from the investment side remain more optimistic about the prospects for oil movements and the tanker market several months in the future. Summarising his firm's event, Jefferies' top shipping analyst Doug Mavrinac told investors: "Crude oil tanker demand [is] expected to strengthen further in 2011 primarily due to developing economies' oil demand growth; global oil inventories continue to be depleted; OPEC [is] likely to increase production over next 12 months to balance oil markets; fleet growth remains benign."

Flattened crack spreads notwithstanding, smart shipping people are betting on an improvement in the refined products sector. In a presentation at the Jefferies event, Tsakos Energy Navigation, with a presence in both crude and products, emphasised that it was girding for greater participation in the products sector. At the same event, Overseas Shipholding Group CEO Morten Arntzen pointed out the highly favourable supply/demand dynamics of the product sector, where OSG maintains a large presence. His data indicated that hefty cancellations of orders translates into a decline in the available fleet at the time of an improved demand outlook – a projected 4% year-on-year growth in sector tonne-miles.

85.5M bpd

OPEC oil demand projection for 2010

86.6M bpd

OPEC projection for 2011

The OSG presentation delved into the specifics of the sector: on the supply side, Arntzen estimated 90 vessels would be delivered this year, blaming "cancellations and shipyard issues". For the first five months of 2010, there were 48 actual deliveries, he said.

According to the OSG presentation, demand in the sector will be enhanced by exports of low-sulphur diesel fuel from the expanded Total refinery at Port Arthur, Texas, and a seasonal increase in naphtha movements to Asian petrochemical facilities. Storage demand continues to be a factor in the refined product trades (unlike the crude arena); Arntzen said 27 ships are still providing clean storage, with Aframaxes comprising 70% of these. F

Regulatory reform to impact derivatives trading

EU legislation is likely to mirror that recently passed in the US

Freight derivatives were not the target of regulatory reforms passed in the US and which are now being drawn up in the EU. Yet several presentations at last week's Capital Link conference on freight derivatives held in New York indicate that a view is emerging that the contours of 'paper freight' (in the form of forward freight agreements) will indeed be affected, along with much bigger arenas where derivative contracts are traded.

London lawyer Declan McKeever, from Holman Fenwick Willan, explained that the EU ruling expected later this month is likely to mirror legislation (the Dodd-Frank bill) recently passed in Washington DC, so market participants would be less likely to engage in trans-Atlantic "regulatory arbitrage". McKeever also talked about a key tenet of the US legislation – that standardised over-the-counter derivative contracts must be cleared. He added that regulatory exemptions exist for non-financial market participants, but said "bespoke contracts will be tightly regulated."

Abe Glass from Poten Energy Services described one regulatory impact that is already apparent: the prohibition of proprietary trading activities by financial institutions. He pointed to the 2009 sale of Phibro Energy from Citibank to the energy group Occidental Petroleum (well known to tanker brokers), and to JP Morgan Chase shuttering a UK commodities trading desk in August.

Enforcement of the rules in the US will be phased in over a two-year period. F