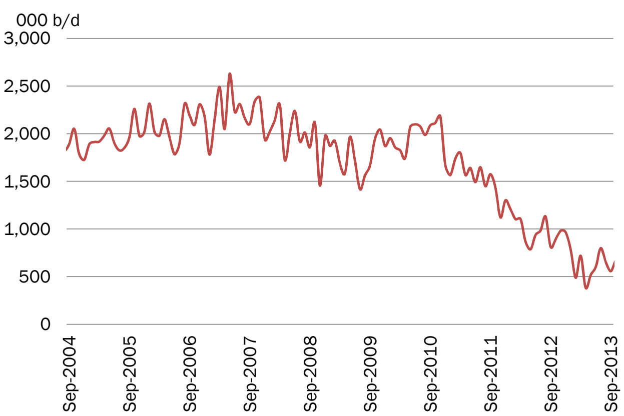
No. 23 – The Spot Market: A Year in Review

December 19, 2013

When looking back at the tanker spot market in 2013, a few keywords come to mind: oversupply, weak freight rates and continued poor earnings. Though these things were more prevalent in some sectors than others, overall, 2013 is not likely to be remembered fondly by owners.

The largest of the tanker classes, VLCCs, made little headway throughout the year as quite a few factors kept them from advancing. The biggest being oversupply, which stemmed from a decline in demand, a heavy refinery maintenance program and a consistent delivery profile. The increase in domestic crude oil production in the US has significantly limited its dependence on foreign sources, specifically from West Africa. Figure 1 shows the dramatic decline in US oil imports from West Africa over the past few years and as of September 2013, imports were as low as 618,000 b/d. Further supporting this, our proprietary data shows a decline in activity on the WAFR/USAC trade by nearly 31% year-on-year.

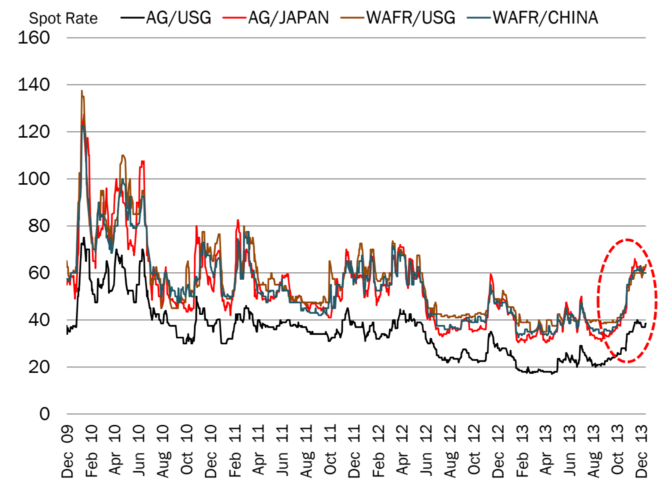
Figure 1: US Oil Imports from West Africa



Source: US Energy Information Administration

With respect to deliveries, as of November, there have been 31 VLCC newbuildings added to the fleet and less than half of that number sent to the breakers for demolition, bringing net fleet growth to 17 ships. With these factors combined, rates on the AG/Japan route traded between WS 32-40, on average, for the majority of the year, while AG/US Gulf traded between WS 18-27. In the Atlantic basin, WAFR/China traded between an average of WS 35-41. However, as we gear up to put 2013 behind us, the VLCC market has made a notable comeback. This has been due to a seasonal uptick in production of heating fuels ahead of peak winter demand and the rush to secure business ahead of the holidays. Additionally, there has been an increase in activity as China, the world's second largest consumer of crude oil, rushes to fill their Strategic Petroleum Reserve. Position lists have also been much tighter, which has given owners the room to push rates in their favor. As we close out the year, December rates on the AG/Japan route traded at an average of WS 62, while AG/USG traded at an average of WS 38. From WAFR/China, rates averaged WS 61 (Figure 2).

Figure 2: Historical-YTD VLCC Spot Rates



Source: McQuilling Services

The Suezmax sector was also no stranger to the issue of oversupply. Requirements out of West Africa for these sized vessels have been pressured by the previous year's East Coast refinery closures and the fact that US refiners are substituting foreign imports with domestic Bakken crude. This has caused rates to trade at an average of WS 57 for the year, down 5 WS points from last year's average. This route has closed the year on a more positive note on the back of a stronger VLCC market as rates reached their highest levels of the year at the WS 112 mark.

In the first half of the year, Black Sea/Mediterranean rates traded at an average of WS 62 due to the lack of Libyan cargoes, but gained some momentum in the second half as rates averaged WS 66 through mid-December. The most recent uptick can be attributed to a slew of delays in the Bosporus.

The Aframax sector was quite volatile throughout the course of the year with temporary spikes brought on by weather delays in the US Gulf and seasonality factors in the Baltic. In the first half of 2013, rates from the Caribbean to the US Gulf averaged WS 97, down 13 WS year-on-year. However, as the rest of the year progressed, rates remained in the lower WS 100s (with the exception of October) and averaged WS 103, up 8 WS points year-on-year. The strongest levels of the year have been recorded in December, where rates have reached WS 175, the highest level recorded since 2010. Similar to the Suezmax class, Aframaxes trading in the Black Sea/Mediterranean were also pressured by the loss of Libyan cargoes. As a result, rates traded at an average of WS 79, down 5 WS points year-on-year.

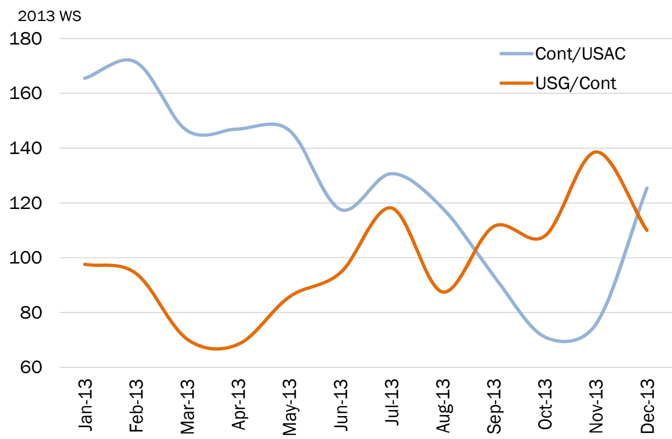
In the smallest of the crude oil tankers, Panamaxes also found themselves in a bit of an oversupply situation. This was brought on by reduced US imports from Caribbean nations due to rising supplies of Canadian crude. Despite this, rates in the Caribbean did not fare too bad in the first half of the year as delays in the US Gulf helped to support the market. However, as the year progressed, longer term effect were realized and rates dwindled, losing average of 9 WS points from the first six months of the year. Much like other sectors, rates have made a comeback in December and traded at an average of WS 122. This was again due to delays and the rush to secure tonnage ahead of end-year holidays.

On the opposite side of the spectrum, there was a bit more optimism in the clean products market in the beginning of the year. This sector, specifically MR tankers, captured the attention of market participants throughout the year. From time charter deals to newbuilding orders, it has been clear where confidence resides.

Beginning with the larger of the clean ships, LR2s and LR1s found support early in the year from the growing naphtha trade to the East. As demand waned and oversupply pressured the market, rates dropped on the benchmark trade mid-year and as the year progressed, rates gained some traction, but failed to meet the peaks that were recorded in February and March. Year-to-date rates for LR2s on the AG/Japan benchmark averaged WS 85, while LR1s on the same route averaged WS 103.

In the MR market, with strong demand in the beginning of the year due to regional product imbalances on the back of refinery maintenance, ships on the Cont/USAC route traded as high as WS 171. A weaker driving season put a damper on the market beginning in May/June and rates continued to fall throughout the rest of the year. This decline has also been due in part to the fact that US refiners are operating at high utilization rates and counteracting the need for European gasoline imports (Figure 3).

Figure 3: YTD MR Spot Rates



Source: McQuilling Services

What used to be the backhaul trade for clean product tankers, the USG/Cont route, gained quite a bit of traction and attention this year. This route averaged WS 99, up a staggering 21 WS points year-on-year due to increased exports to Europe and owners' desire to be compensated for the lack of barrels they would have on their trip back to the US Gulf (Figure 3).

So, as we close the door on one year and prepare for a fresh start, market participants can only hope for a prosperous 2014. Our assessment for DPP trades remain cautiously optimistic, while preliminary data indicates relatively bearish developments for CPP trades, specifically on MRs, in favor of LR sized ships.