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No. 2 – Tanker Demand Outlook

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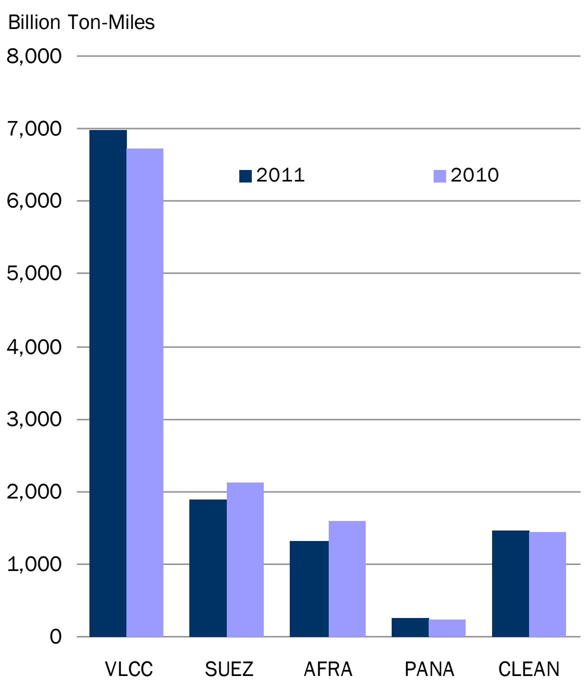
In our recently published 2012-2016 Tanker Market Outlook we noted that demand to transport crude oil and residual fuels contracted by roughly 2% from 2010 to 2011. The market for clean petroleum products posted slightly better results, rising by around 1.5% during the same time period (Figure 1).

In addition to oversupply stemming from robust contracting in 2006, the tanker market has been negatively impacted by several events. The Arab Spring acted as a double edged sword as it slashed Libyan crude oil production for the majority of the year and prompted members of the International Energy Agency to release 60 million barrels of oil from the Strategic Petroleum Reserves in June 2011. This reduced demand for loadings and discharge from the global tanker fleet. Oil demand was further pressured throughout the year as a solution to the European financial crisis remained elusive and signs of an improving US economy were clouded by political wrangling. As the year came to an end, rising concerns over inflation in emerging economies further lowered oil demand and economic forecasts.

Figure 1: Ton-Mile Demand 2011 vs 2010



Source: McQuilling Services

For the transportation of crude and residual products, the VLCC class remains the most consolidated of all sectors with eight trades making up 77% of demand. On a regional basis, the Far East made up the largest portion of demand as its expanding economy and downstream sector continuously require new sources of hydro-carbons. The opposite has been occurring in OECD North America and Europe as weak petroleum product demand reduced refinery utilization rates and crude-oil imports via pipeline have altered supply sources. This trend can be observed as ton-mile demand from the Middle East to the US Gulf declined by 4% throughout the year.

In recent editions of our Tanker Market Outlook, McQuilling Services noted the trend of increased trade between loading regions in the West with cargoes destined to the East. The load regions are defined as the Americas, West Africa and Europe and discharge regions include the Far East, South East Asia and India. We expect this trend to continue materializing in the future despite demand being slightly lower in 2011 compared to previous years. The contraction was largely influenced by reduced Libyan production which had a significant influence in widening the price differential between light and heavy crudes. This raised the price of West African crudes in comparison to oil supplies from the Middle East, lowering ton-mile demand from our loading zones in the West.

The West-to-East trades are also largely influenced by fuel oil arbitrage into the Asian market as Singapore is the world's largest bunkering hub. In 2011, data shows that bunker sales hit another record high of 43 million tons, with sales averaging 3.5 million tons per month. This strong demand helped limit the fall in West-to-East fixtures last year [1].

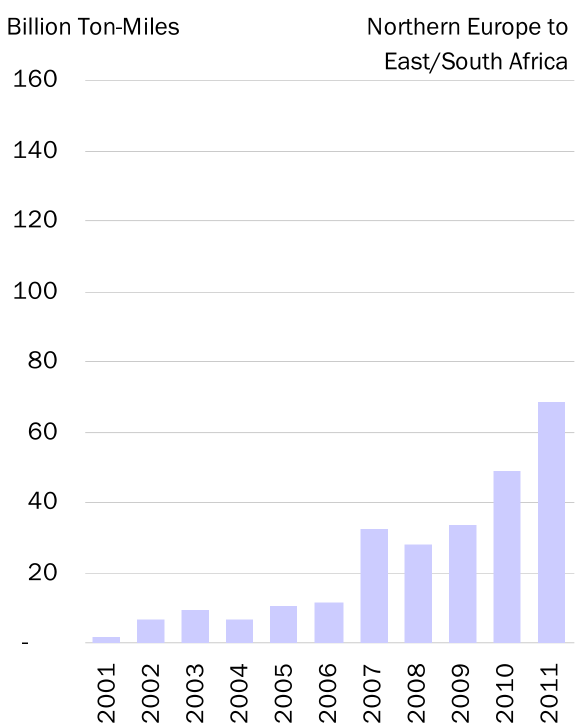
Ton-mile demand for the Aframax class sector fell by 18% throughout the year. Despite its greater flexibility compared to VLCC and Suezmax vessels, regional factors negatively influenced demand. In the Western Hemisphere reduced throughput rates at refiners located on the US East Coast lowered import requirements from load ports in the Caribbean and northern South America. Data published by the EIA put refinery utilization on the East Coast at 70% of capacity in 2011 compared to a national average of 85% [2]. Ton-mile demand was further pressured from the reduction in Libyan supplies, the economic situation in Southern Europe and, to a lesser extent, recent events in Syria and Iran.

During the next five years, we expect ton-mile demand for crude and residual products to rise by an average of 1.5% per year. Ton-mile demand for the Suezmax class is forecast to rise by 9% during the forecast period but its overall share will remain stable at about 18% of demand.

With only one exception, trade volumes on the top 15 CPP trade routes increased by approximately 13% from 2010 to 2011 even though the total sector only expanded by 1.5%. Trade in clean petroleum products posted a noticeable shift towards larger tankers on trade between the Far East and the Caribbean, EC Mexico, Venezuela and Colombia. Overall, LR1's share of ton-mile demand rose by almost 15% throughout the year as the downstream industry has begun undergoing structural changes.

A steady rise in trade from Northern Europe to South/East Africa has been observed over recent years. These volumes are mainly comprised of gasoline and gas oil. The boost in trade can be attributed to the region's healthy economic outlook with GDP growth forecast at 5% this year [3].

Figure 2: CPP Trade Northern Europe to East/South Africa *2001-2011*



Source: McQuilling Services

Over the next five years, McQuilling Services forecasts that CPP ton-mile demand will rise by an average of about 2% per year. We expect the MR2 class will remain the work horse of the clean petroleum products trade but will slowly cede some tonnage to larger vessels. Trade in petroleum products will continue evolving as weak margins are consolidating the refining industry in OECD countries. These closures have totaled just over 1 million b/d in the US Atlantic Basin since the second half of 2011.

The McQuilling Services 2012-2016 Tanker Market Outlook is currently available in PDF and hard copy formats. This report includes a detailed discussion of tanker market demand, asset markets, orderbooks and several other aspects impacting the industry.

For more information please contact McQuilling Services at: +1 516.227.5700 or services@mcquilling.com

References

[1] The Maritime and Port Authority of Singapore, http://www.mpa.gov.sg/sites/pdf/bunker-sales.pdf

[2] "Weekly Petroleum Status Report", EIA, 1983-2011

[3] "The World in 2012" The Economist, December 2012