A Dreary Week for Rates, Could Chinese Macro Situation Spell Relief?

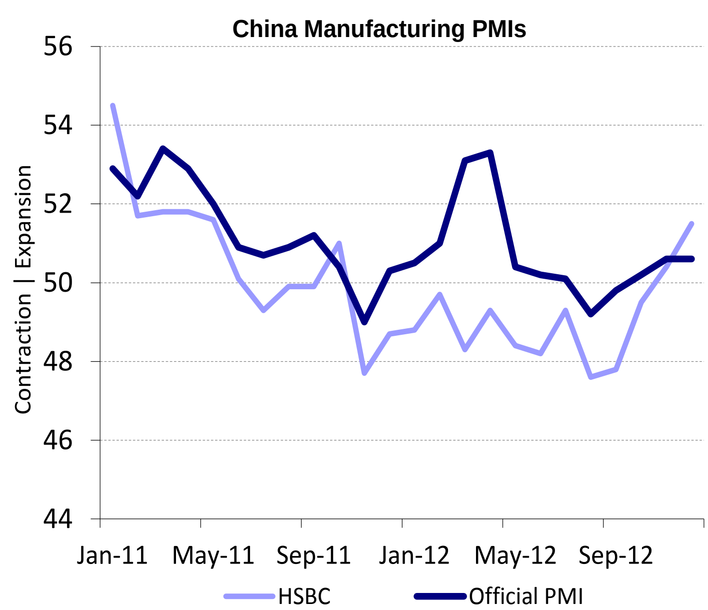
Extreme lows seen during generally strong rate season

This week saw fresh lows for several tanker routes, and the usual seasonal spike in earnings has largely failed to materialize. Limited demand has coupled with the oft-repeated fleet oversupply story to form an unwelcome combination for tanker owners. Indicators for macroeconomic growth coming out of China have been conversely upbeat. It is not clear that such metrics are indicative of a sustained pick-up in demand, though.

Mildly positive macroeconomic data coming out of China

Both major readings of Chinese PMI for December were released as of earlier this week, and the data were positive, pointing to continued – though modest – growth in manufacturing activity. Energy statistics mirror this positive, but muted, trend. Chinese power consumption has been up for most of the year, but is still nowhere near the double digit gains seen for most of the last decade. Indeed, this level of consumption growth is more consistent with continuing increases in residential living standards rather than breakneck industrial growth.

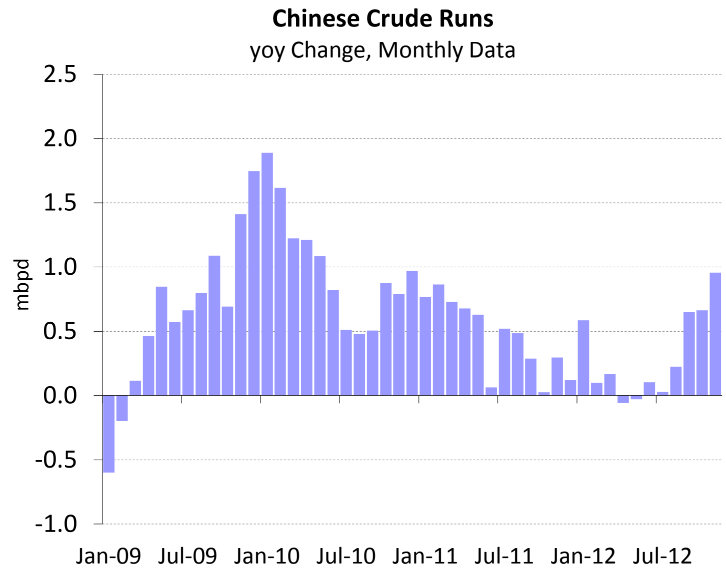
PMI readings continue to show growth in manufacturing sector



Source: Bloomberg, IEA, Poten

What is data really indicative of, though?

Even more pronounced growth has manifested itself in the way of almost one mbpd year-over-year growth of Chinese crude runs in December. Is the totality of these data points indicative of foundation building before a booming expansion, of merely tepid growth, or of a situation where the numbers simply do not match reality?



Source: National Bureau of Statistics of China

Crude run data supports Chinese bull case…

…while notable analysts call data integrity into question

Although initial reactions to these macroeconomic data were positive, Bloomberg notes that analysts at Goldman Sachs, UBS, and Mizuho were, among others, quick to call the accuracy of the data into question, reportedly citing a divergence from the recent China New Export Orders PMI subset, which has begun to reverse gains seen in the second half of 2012 and teeters on the border of expansion and contraction.

Is there a new growth dynamic in China?

Such a difference needs not be incongruous, though. The combination of Manufacturing PMI, New Export Orders PMI, crude runs, and power consumption paints a picture in which it is alternatively possible that domestic demand is in fact a driver of a still-perceived-as-tenuous Chinese recovery. Concurrent with rising wages for domestic workers and a slowly strengthening Renminbi, China's current account surplus has indeed continued to fall while still seeing a recovery in GDP growth over the same time period. The confluence of years of rapid export-driven growth and domestic infrastructure investments has created stronger levels of domestic demand, buoyed by a burgeoning middle class.

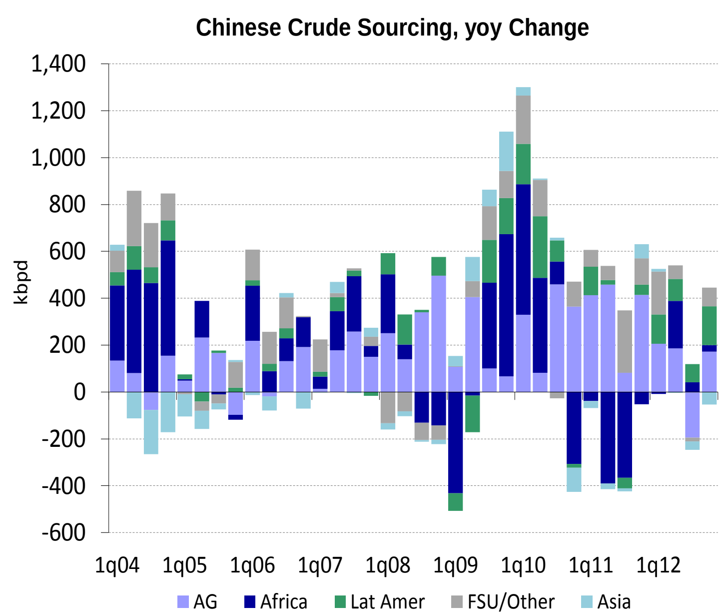
Domestic demand becoming a reliable growth engine?

Source: Bloomberg

Crude imports remain strong...

Seaborne crude imports to China have not surprisingly been strong of late as well, in part due to aforementioned Chinese domestic demand. After a drop off in African imports coinciding with unrest in Libya, Latin American and AG imports have both picked up over the past year. Growth in FSU imports, which have been partially land based, should be largely seaborne in the near term, driven by exports out of Kozmino.

...as mix of importers continues to shift



Source: Bloomberg, IEA, Poten

Tanker markets, of course, are agnostic to the reasons underpinning the strength of demand for their capacity. It does not take much imagination, however, to recognize the

Could have been worse without maturation of Chinese domestic economy

much more severe rate environment that would have resulted without strengthening Chinese domestic demand.

Will this be foundation of tanker demand rebound?

We maintain a bearish view for tanker rates into the spring on continuing deliveries and concerns over production. On the other hand, the Chinese economy appears to be on solid footing. With this foundation in place, rebounding growth elsewhere could spur export growth from Asian emerging markets. Coupled with a more reasonably sized fleet – perhaps induced by the recent extension of weak earnings and their potential resulting insolvencies – economic strength in China would provide the underpinnings for a way out of the current rate doldrums.

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