Float, Rebalance and Flirt with Backwardation

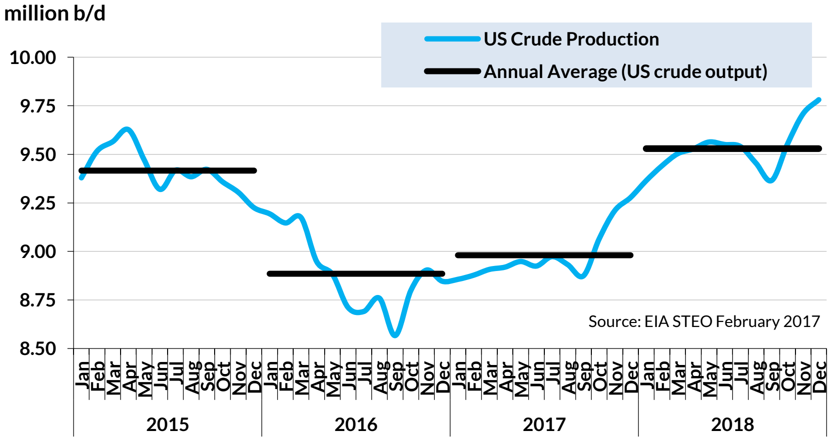
Weekly Tanker Market Report

The decision taken by OPEC in November 2016 to take back control is starting to have an effect. Promised production cuts of nearly 1.8 million b/d agreed between OPEC and a number of non-OPEC countries are primarily felt in the Middle East. According to the IEA, the Middle East OPEC crude production fell by a colossal 1 million b/d in January from December levels and initial Reuters estimates indicate that these cuts were somewhat further reinforced in February. As the Middle East is by far the largest market for VLCCs, the decline in crude exports at a time of rapid growth in fleet size is starting to hurt tanker owners. VLCC spot TCE earnings on the benchmark Middle East – Japan route started March at around $20,000/day, down gradually from $50,000/day in early January.

The oil markets are also changing. Shortly after production cuts were announced, oil prices firmed, fuelling optimism about the recovery in the US oil production. The latest EIA forecast for domestic output stands for notable increases in supply from October 2017 onwards, up by over 0.4 million b/d year-on-year in December 2017 and by another 0.5 million b/d in December 2018. However, independent industry observers speculate whether an even stronger and faster rebound is on the cards, as the rig count continues to rise, productivity per rig has increased around 20% over the past year and shale breakeven costs have on average fallen to just over $40/bbl (source: WSJ, Drillinginfo).

Despite the initial step up in oil prices in early December, very little volatility in prices has been observed thereafter. Yet, notable changes have been registered in the forward curve. Wide contango, which was a feature of the market in 2015/16, has narrowed substantially for near dated contracts; while pricing for longer dated contracts is moving towards backwardation. The front month of oil futures is being supported by production cutbacks, while the expectation of a stronger and faster rebound in US shale is applying downwards pressure further along the curve. There is also much debate for how long OPEC production will remain restrained.

Outlook for US Crude Oil Production



OPEC has stressed many times that the main reason behind its current policy is to rebalance the oil markets and to reduce massive oil inventories, accumulated in recent years. Although this strategy will support prompt oil prices, drawdown in stocks and easing forward oil prices threaten floating storage. Our analysis shows that the number of VLCCs in non-trading activities (primarily Iranian/non-Iranian crude storage and fuel oil storage) has started to slip. At the end of February 45 VLCCs were involved in various non-trading activities, down from an average of 52 units seen between July 2016 and January 2017. In fact, Iranian crude storage has started to decline rapidly a few months ago but up until February this was offset by robust non – Iranian crude storage.

Despite the latest drop, VLCC floating storage remains substantial, representing around 6.5% of the global VLCC fleet. However, the downward trend is likely to continue. Not only are the NITC ships finding their way back into the international trade, but also the anticipated drawdown in stocks and flirtation with backwardation makes it less attractive to use tankers for storage. This paints a bleak picture for VLCC owners in the short term…

Crude Oil

Middle East

As expected, an initially busier VLCC fixing pace merely accelerated the softening trend and rates re-set solidly into a lower range at down to the low ws 50's East and high ws 20's to the West. Availability still looks plentiful through the balance of March and Owners are likely to remain pressured over the next phase too. Suezmaxes dipped off a little, but then activity did pick up somewhat and rates returned to close to ws 85 to the East and low ws 40's to the West and delays in Singapore may provoke Charterers to keep shopping for the more clear cut positioned units. Aframaxes tightened further and rates took a step higher to 80,000 by ws 120+ to Singapore with perhaps a little more to come in the short term.

West Africa

Suezmax sentiment had already hardened and there were some mild rate gains posted early week, though the big breakthrough never quite materialised. Owners are still positioned to make a more significant push and Charterers may well have to give further ground next week. VLCCs saw reasonable volumes, but the main feedstock came from Eastern ballasters and rates therefore fell off in tandem with the AGulf, plus a small 'insurance' premium for the longer voyage duration. Currently levels hold at a steady low ws 60 mark to the Far East and at around $2.75 million for runs to West Coast India.

Mediterranean

Aframax Owners ended last week with a degree of expectation that they could engineer further improvement, but lists never tightened sufficiently and rates remained stuck at no better than 80,000 by ws 120 cross Med accordingly. The balance is now just a little finer and any replacement needs could provide a positive catalyst into next week. Suezmaxes didn't find enough local volume to force rates higher than 140,000 by ws 85 for European destinations, but if West Africa does make a more noticeable move, then sentiment and rates, here will also inflate.

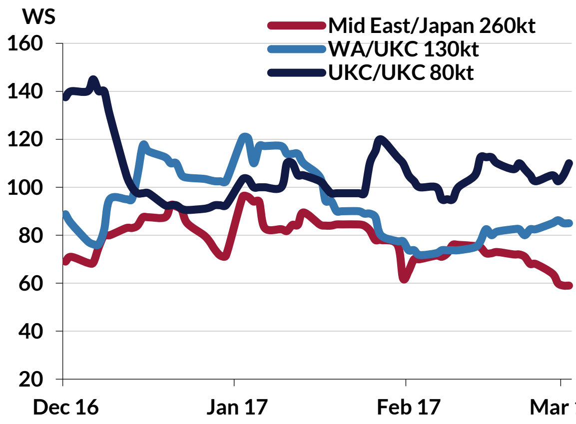
Caribbean

Aframaxes see-sawed through the week - highs of 70,000 by ws 155 upcoast and lows of ws 120, with the end point being somewhere in the middle. Every day a slightly different supply/demand mix and that looks set to remain the case over the near term. VLCCs were occasionally picked off and to some extent performed better than elsewhere at no less than $4.2 million to Singapore and $3.3 million to West Coast India, but forward availability still threatens for rates to break lower.

North Sea

A mild improvement in Aframax fortunes but 80,000 by max ws 105 cross North Sea couldn't really excite, though ice class units from the Baltic did manage to squeeze up to 100,000 by ws 110 before the week's end on busier interest. 'Arb' economics for VLCCs to the East were fairly flat line with some making sense of $4.5 million for crude oil from Hound Point to China, but a deal for fuel oil at $3.7 million to Singapore failed to make it past the 'subjects post' with pricing the reasoning.

Crude Tanker Spot Rates



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Clean Products

East

An active week on the MRs, which has seen a solid movement of ships going on subs and fully fixed away. A couple of headline rates have given a slightly inflated sense of the market, which Charterers will be keen to correct in the new week. For example, ws185 on subs to SAF would suggest that EAF runs have come up 25 points – however, when considered that last UMS ships were unsuitable, these numbers are not market representative. Ws165 seems the correct market level, but will need a fresh test early next week. Westbound voyages have also firmed slightly, with $1.03 million on subs ex-Kuwait, and rumours of a repeat number also on subs. The fact that these were market cargoes reflects the fact that higher numbers are needed to entice Owners into repositioning West of the canal. Naphtha East has remained relatively untested ws132.5 is in theory still the market level, but this is for sure one of the routes which needs testing next week. Shorthaul rates are still plagued by the fact that LR1s are picking them up, tiding themselves over for potential longer haul post discharge. These have been trading around the $175k level - but with the MRs and the LR1s looking active, Owners may be tempted to do cheap numbers to capitalise on what they feel is a moving market in a week or so.

A stabilising week for the LRs with rates drifting slightly on LR2s, but holding firm on LR1s. 75,000 mt naphtha AG/Japan is now flat at ws 105 and 90,000 mt jet AG/UKCont is at $1.45 million, but both rates could see improvements in the coming week with a slightly shorter list and a few stems in the market. 55,000 mt naphtha AG/Japan is at ws 117.5 and has been all week, with 65,000 jet AG/UKCont at $1.20 million with maybe a little more to come next week.

Mediterranean

The main driver this week has been Black Sea enquiry which has been plentiful and steady from Monday onwards leaving rates trading around the 30 x ws 170 mark with anything prompt likely to pay more. This helped the East Med rates as the Black Sea drew tonnage away meaning Owners for looking at 30 x ws 147.5 for East Med whilst the less active and better supplied West Med was trading around 30 x ws 142.5-145. The market look to be fairly steady at the close of play with these rates likely to hold into next week whilst the sentiment for the market is defined.

MR activity has picked up in the Med this week as cargo volumes increased as in NWE. As a result, rates are now drawing sentiment from the North, although perhaps not quite at the same levels just yet. 37 x ws 135 for Med/Transatlantic runs whilst Med/Red Sea seems to have steadied around the $700k mark despite dipping below earlier in the week. Some forward dates mean there is some hope for Owners moving into next week although cargo volumes will need to increase a bit before we see any substantial gains.

UK Continent

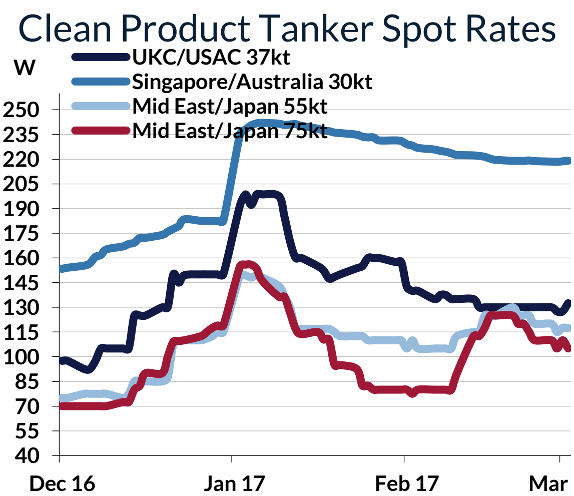
Week 9 has brought some unexpected fortune for the MRs in NWE. Despite a somewhat slow start, the middle of the week saw a flurry of activity leaving the tonnage list looking tight. With plenty of enquiry on the Friday, Owners are now bullish with their rate ideas on all routes. 37 x ws 140 on subs TC2 leaves WAF runs needing a fresh test, but likely to be around 37 x ws 155-160. Mixed aromatics seem to be working to the East as well with Owners likely to try and improve on the $1.2 million last done. With plenty of cargo left to cover and tonnage still on the tight side the outlook remains positive heading into early next week.

Ice requirement in the Baltic has been the saving grace in the last week for the Handies by maintaining last done levels of 30 x ws 180 with occasional gains for anything slightly prompt or replacing. The non-ice X-UKCont business has been plagued by slow enquiry at low volumes and a fairly lengthy tonnage list meaning rates have gradually softened as the week has progressed with last done 30 x ws 160 starting to come under pressure.

Flexi action has picked up a touch this week, although as has been the case recently, the majority of spot fixing has been done behind closed doors meaning 22 x ws 210 is more of a guideline level with individual cargoes likely to achieve differing rates depending on dates.

LRs

Week 9 has provided a steady level of LR activity in the West. LR1 rates have remained flat, meanwhile and as suspected LR2 rates have slipped a touch given the slightly heavier tonnage list. TC 16 has hardly moved holding at 60 x ws 120, but with Owners preferring to keep their vessels in the West and few outstanding cargoes this side of the weekend, Charterers might attempt to shave a few points away from this level at the beginning of next week. Having said that, MRs are looking pretty active which might help Owners hold the line. As mentioned Owners are reluctant to go East on the LR1s, but as a guide today one Owner is willing $1.2 million for ARA/AG. Subsequently, a touch less could be achieved in the end. A mixture of LR2 rates have been reported this week for varying runs to the East, but the general trend for rates has been southbound. Levels have slipped down to $1.85 million for ARA/Singapore and arguably $50k less depending how one views things. The Med/Japan number has naturally fallen as well with a ballaster from New York on subs for a Skikda/Japan run at $1.975 million. There is a chance levels could rebound if the handful of vessels on subs are cleared away, yet with further visible options on the horizon and a generally bearish naphtha market, it is hard to see where the upside will be triggered from at present.



Dirty Products

Handy

The five D's; Dodge, dip, dive, duck and…dodge is the best way to sum this week's contest between Owners and Charterers in the continent as momentum has yoyo'd back and forth in a riveting weeks trading. As the week developed Owners managed to keep the position list off prompt dates tight forcing rates to once again pop back up above the 30 x ws 190 levels. Owners will be keen to build on this momentum on Monday, but Charterers will be grateful for the two day weekend where tonnage has time to replenish and dodge any further hype.

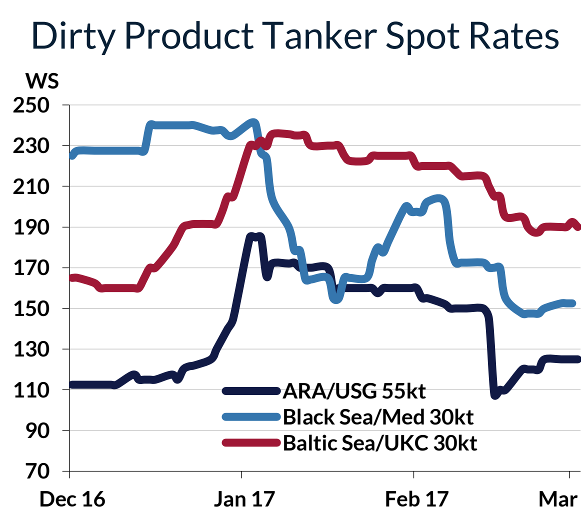
There has been more of a buzz around the Mediterranean this week with activity noticeably firming. Similarly, to the UKCont there has been an ongoing battle on which direction this market is heading. In fairness, Charterers have done well at keeping a lid on Owner's aspirations given that the week seemed to flow in their favour. Looking ahead into next week, weather delays and potential late running units could add more fuel to the fire so it will be interesting to see if Charterers move early Monday morning or wait for the dust to settle.

MR

Rinse, wash, repeat for the MR's in the Continent as levels continue to trade sideways and approved tonnage availability remains thin on the ground. Depending on what restrictions are required one might need to look ahead and pull vessels from further afield if necessary. We have seen a busier side to the Mediterranean this week with a number Owners maximising bigger cargo opportunity and with it rates have ticked over. We expect little change looking ahead however, we might see charterers utilise the Handies bigger companions where availability restricts.

Panamax

We started this week reporting on Monday with 55 x ws 125 being confirmed from this side of the Atlantic, but gradually as we've moved through this week the hand brake has been lifted and firmly applied when it comes to fresh enquiry. The Caribs market has followed a similar fate as inactivity has put further pressure on last done level within the region. The outlook for next week for both sides of the pond is leaning to be one where fresh tests on last done levels could be seen.



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Dirty Tanker Spot Market Developments - Spot Worldscale

			wk on wk change	Mar 2nd	Feb 23rd	Last Month	FFA Q3
TD3	VLCC	AG-Japan	**-11**	59	70	82	58
TD20	Suezmax	WAF-UKC	**+4**	85	81	112	88
TD7	Aframax	N.Sea-UKC	**+5**	106	101	101	105

Dirty Tanker Spot Market Developments - $/day tce (a)

			wk on wk change	Mar 2nd	Feb 23rd	Last Month	FFA Q3
TD3	VLCC	AG-Japan	**-8,750**	20,500	29,250	40,250	19,750
TD20	Suezmax	WAF-UKC	**+1,750**	17,250	15,500	28,750	18,250
TD7	Aframax	N.Sea-UKC	**+4,000**	14,500	10,500	12,500	14,000

Clean Tanker Spot Market Developments - Spot Worldscale

			wk on wk change	Mar 2nd	Feb 23rd	Last Month	FFA Q3
TC1	LR2	AG-Japan	**-10**	105	115	118	
TC2	MR - west	UKC-USAC	**-1**	129	130	174	139
TC5	LR1	AG-Japan	**-10**	116	126	118	118
TC7	MR - east	Singapore-EC Aus	**+0**	219	219	241	

Clean Tanker Spot Market Developments - $/day tce (a)

			wk on wk change	Mar 2nd	Feb 23rd	Last Month	FFA Q3
TC1	LR2	AG-Japan	**-2,250**	9,250	11,500	12,250	
TC2	MR - west	UKC-USAC	**+0**	6,750	6,750	13,500	8,000
TC5	LR1	AG-Japan	**-1,250**	7,750	9,000	7,750	8,000
TC7	MR - east	Singapore-EC Aus	**+250**	11,000	10,750	13,000	

(a) based on round voyage economics at 'market' speed

ClearView Bunker Price (Rotterdam HSFO 380)	**-1**	305	306	308
ClearView Bunker Price (Fujairah 380 HSFO)	**-6**	328	334	336
ClearView Bunker Price (Singapore 380 HSFO)	**-7**	323	330	340
ClearView Bunker Price (Rotterdam LSMGO)	**-7**	476	483	463

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