



POTEN TANKER OPINION

Glass Half-Full Or Half-Empty?

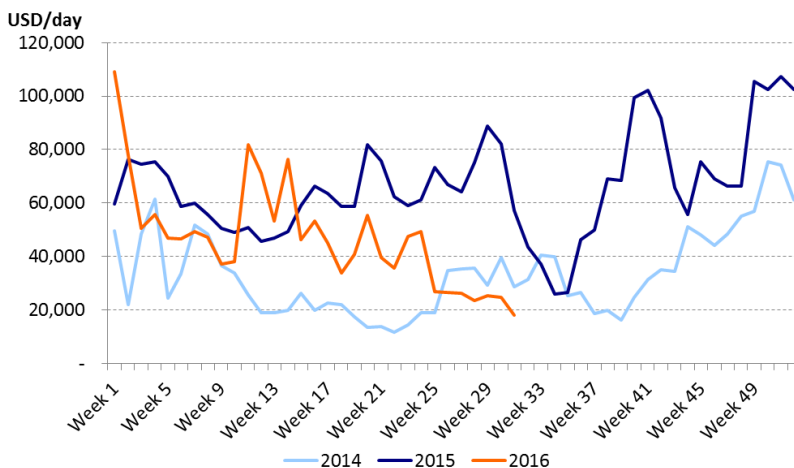
Factors that will drive tanker rates for second half 2016

The tanker market has been suffering from rather severe summer doldrums. Earnings across all tanker sectors, from VLCCs down to MRs are at levels not seen since September 2014, the period right before the most recent tanker bull market. While the summer period is historically a slow period of the year and tanker rates typically stage a recovery going into the northern hemisphere winter months, some people are concerned that this might not happen this year, at least not to the same extent. However, as is the case in almost every market, whether the glass is half-full or half-empty depends very much on your perspective and what you see as the main drivers of the market for the future. In today's opinion we will look at some of the factors that could shape the rate environment in the second half of 2016.

We will start with the supply side of the equation. Fleet growth in the first half of this year has contributed to the pressure on rates. In the first half of 2016, 23 VLCCs have been delivered, which is already equivalent to the full-year deliveries for each of 2014 and 2015. Another 37 vessels are scheduled for delivery in the second half of the year, so even taking into account customary delays and cancellations, VLCC fleet growth is expected to continue. The situation in the other tanker segments is similar, with 2016 deliveries outpacing recent years' additions and accelerating into the second half of the year. The main exception is the MR segment. This segment faced heavy deliveries in 2014-2015 and the inflow of new tonnage has started to slow. Can we count on significant scrapping in the coming years to offset some of these deliveries? Not likely. Only a handful of tankers have been scrapped so far this year and given the age distribution of the tanker fleet, we don't expect a significant pickup during the remainder of 2016. The tanker supply factor that could possibly drive rates higher is increased floating storage.

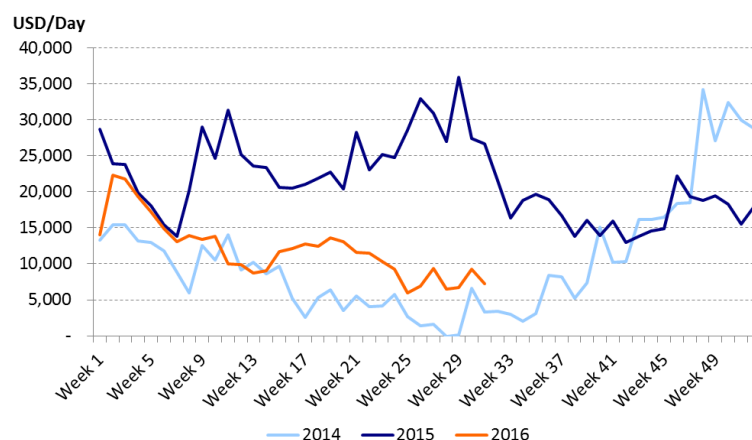
How about tanker demand? Here the situation looks slightly more positive. The year 2016 started well enough. Tanker trades were supported by the re-entry of Iran in the export market as well as growing U.S. crude oil imports. In the U.S., foreign barrels became more competitive when the Brent – WTI spread collapsed after the U.S. crude export ban was lifted. However, in the second quarter of 2016, several unforeseen events reduced oil flows worldwide. A combination of forest fires in Canada, severe drought in Venezuela, production outages in Nigeria and strikes in France led to higher prices and inventory drawdowns, with a negative impact on the oil and tanker markets. In addition to the usual suspects like seasonal field maintenance, these events have made it a particularly depressing summer so far.

Fig. 1: VLCC TCE Rates: AG-FE (270 Kt)



Source: Poten & Partners

Fig. 2: MR TCE Rates: UKC – USAC (37 Kt)



Source: Poten & Partners

However, many of these factors are likely to turn around in the second half of the year. Canadian production has been restored, for example, and outsized inventory draws in the U.S. are expected to come to an end as well. There are promising signs coming from Libya, where an agreement has been announced to reopen several export terminals, while U.S. airstrikes may reduce the threat of further oil disruptions. Analysts indicate that an additional 300,000 barrels/day of production and exports is possible in the near term. In the current oil environment, additional production will immediately enter the market and add to transportation demand. If oil production expansion exceeds demand growth, the additional barrels will end up in storage (mostly in consuming areas, occasionally on tankers). This will provide support for the tanker market.

In the longer term, world GDP growth and oil demand will be important drivers, but over the next 6 months, seasonal factors, weather, geopolitical developments and market psychology will probably be just as important as the fundamentals. So, is the glass half-full or half empty? Hard to say, time will tell. However, at this point in the cycle there is obviously a lot more upside potential than downside risk.