

Ever Given

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Ships accumulating in
the Gulf of Suez

*Neither the Ever Given nor Covid
Can Stop the Flow of Goods
The Year in Review*

LINER BOOTY, BULKER BOOMS, EXPLODING GAS, CRUISE BLUES AND OTHER TALES OF 2021

The year just ending has demonstrated the resilience of the global economy and shipping industry, but the challenges are far from over, writes Niklas Carlen, Director, Maritime Strategies International

2 021 has been an extraordinary year. The pandemic has waxed and waned across the world, while approaches to dealing with it have become increasingly fractious and localised. The global economy has – at least superficially – emerged remarkably unscathed, but underlying fault lines have been exposed in supply chains and energy economics. This could also be considered the year that concern over climate change finally became real.

Containership markets moved into uncharted territory during 2021. A strong increase in containerised trade volumes, in particular from Asia to the US, has combined with a string of inefficiencies, shortages and bottlenecks across the containerised supply chain. The colossal pressure on supply chains has distorted the wider industry in a number of ways:

- the grounding of the Ever Given disrupted early attempts to ease backlogs;
- a lack of warehouse space has

meant that ports are being used to store goods packed into laden containers, and an apparent lack of outdoor space to stack empty containers means truck chassis are being used to store empty boxes, removing from circulation the very assets needed to unclog the ports;

- some Non-Vessel Operating Common Carriers (NVOCCs) have abandoned the ‘NVO’ part and chartered vessels from the market, whilst frustrated retailers are also wading in, chartering vessels and buying containers.

Meanwhile, secondhand prices soared as liner companies chose to buy tonnage outright rather than locking in all-time high charter rates for years to come. Until the flow of goods into the US from Asia slows, progress in unblocking the ports, and thereby freeing up containership tonnage, will be slow.

Looking forward, our overall position on the container market remains unchanged:

impairments to vessel productivity will be lower on average next year compared to this year, and further improvement will follow in 2023. With fleet growth ramping up from the middle of 2023 onwards, this will come to place pressure on market balances, freight and timecharter rates.

Many of the same issues relating to supply chain bottlenecks, port congestion and COVID-related operational disruptions have also had an impact on other shipping sectors, and there has inevitably been some spill-over of cargo from the container market to adjacent sectors.

For example, in the dry bulk market, container capacity shortfalls have prompted a partial reversal of containerisation trends for minor bulks, primarily lifting demand for geared tonnage, whilst some bulk carriers have even been pressed into service to reposition empty containers. Similarly, the multipurpose (MPP)

sector has also benefitted from the shift in minor bulks out of containers, whilst simultaneously seeing higher project cargo shipments on the back of increased infrastructure investment.

Indeed, government stimulus has traditionally been one of the levers used by policy makers to stimulate economic growth in times of crisis, and this year has been no exception. As a consequence, demand for construction-related materials has boomed, with seaborne trade of semi-finished steel products up by almost 6% yoy in 2021 and cement trade up by almost 7% year on year.

Iron ore trade began the year with a bang, buoyed by strong Chinese steel production – during the first six months of 2021 Chinese steel output was up 11.4% yoy. However, there has been a rapid slowdown in production from July onwards, driven by the emerging debt crisis in the property market alongside production limits

imposed by the government – Chinese construction accounts for approximately 30% of total Chinese steel demand.

Following the COP26 meeting in November 2021, the long-term outlook for global energy markets has come under intense scrutiny. The final communiqué gave some hope to coalminers, with a commitment only to ‘phase down’ the use of coal, rather than phase it out. Even so, there is no doubt that governments are increasingly adjusting energy policies away from the dirtiest fossil fuels (and coal in particular).

It is, therefore, a little ironic that, after declining by over 10% yoy in 2020, this year has seen a revival in seaborne coal trade, supported by the ongoing global energy crunch. A number of countries switched from gas to coal during Q3 in response to tighter gas supplies, and MSI expects coal trade to grow by 1.8% yoy in 2021 and by a further 3.1% next year.

It has also been a positive year for the grains/soybean trade, with growth of over 5% yoy in 2021 — the strongest rate of growth for five years. Improved trade this year has come despite rising prices, rising farm input costs, and tighter stocks that will need to be replenished. Next year, MSI forecasts an annual growth of 3.9% for seaborne grains/soybean trade. However, a developing La Nina weather pattern could present challenges to near-term production, with the Northern Hemisphere winter harvest likely to

see some disruption.

At its peak, it is expected to be a ‘moderate’ strength event, with drier conditions in the Southern half of Latin America threatening production, and wetter conditions in Australia encouraging for yields there. As for the outlook for the first half of next year, Brazil’s soybean crop is yet to be impacted by La Nina (indeed, weather conditions have been favourable so far), and the area of planting has increased. High prices have incentivized farmers to plant more, with acreages expected to grow by 4.5%, compared to 2-3% average growth rate over the last 5 years.

Although global dry bulk seaborne trade declined by 1.6% yoy in 2020, this year has seen a strong bounce back, with total cargo volumes set to grow by 4.0% and 2.1% respectively in 2021 and 2022. After hitting their highest level in over ten years, bulk carrier earnings are expected to witness a correction in 2022 on the back of weaker trade growth and easing Chinese port congestion.

Stronger sectoral demand within construction, mining and agriculture has also been positive for other shipping sectors. Within the car carrier market, demand for construction equipment has been buoyed by government stimulus, with global equipment sales hitting a new record level in 2021.

Similarly, within both the mining and agricultural sectors,

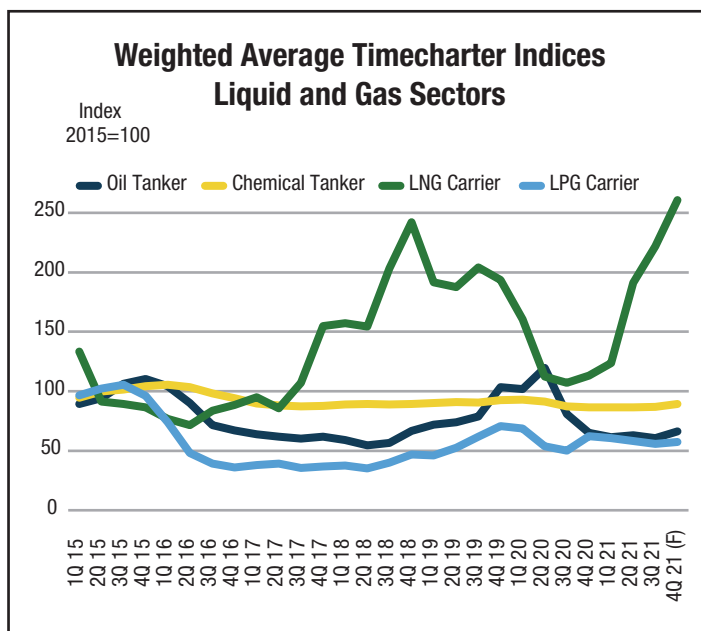
capital expenditure took off again in 2021 on the back of much firmer commodity demand and prices, with replacement requirements for the ageing equipment fleet and the need to replenish equipment inventories adding further impetus to demand.

New car sales also increased during 2021, but fell short of MSI’s initial forecast due to supply disruptions brought on by microchip shortages – production of an estimated 10 million cars was lost during 2021, and the automotive industry still remains firmly in crisis mode today. Microchip supplies are not expected to normalise before H2 2022 at the earliest and, as a consequence, finished vehicle inventories have been largely depleted in key sales markets.

The combination of pent-up demand and inventory rebuilding requirements should see sector momentum carrying through into 2023. Although charter rate increases for car

carriers have failed to match the exponential developments in the container sector, they will remain comfortably above long term average levels through 2023 on the back of solid demand fundamentals and benign near-term fleet growth.

Although coal has benefitted from the ongoing energy crunch, the real winner in 2021 was natural gas. As the year draws to a close, MSI estimates that global LNG trade expanded by 5.9% yoy in 2021, and next year looks even stronger with trade growth forecast to grow by over 7% yoy. Robust natural gas demand in 2021 has been supported by the post-COVID economic recovery in key importing regions, but also by the trailing impact of last year’s winter inventory depletions, which resulted from lower-than-average temperatures in Asia and Europe. The subsequent hot weather during the Northern Hemisphere summer prevented the typical cyclical restock of volumes due to



increased demand for cooling.

Political tensions between Russia and the EU have added to market tightness – Europe has traditionally relied on Russia for over 30% of its natural gas imports, but lower than expected pipeline flows from Russia have increased the pressure on European importers to secure supplies from other sources, with the EU reluctant to request increased supplies from Russia. Charter rates are expected to remain at elevated levels in 2022 as stronger demand coincides with slowing fleet growth to tighten LNG carrier availability.

After declining by almost 7% yoy in 2020, global oil demand expanded by an estimated 6% yoy in 2021, with growth forecast to slow to 3.1% yoy in 2022. From a trade perspective, H2 21 has been characterised by major declines in Chinese crude imports in response to rising crude prices, as well as import quota limitations for

independent refiners. The change in China's crude import profile is critical for the market.

Prior to 2021, it had provided a consistent and strong driver for crude import growth, even when other regions contributed next to nothing. This year, the reversal means global crude imports are effectively flat from 2020, despite positive contributions from OECD regions and India. However, Asia is — and will remain — the driver for crude import growth, with the shortfall in Chinese imports expected to be temporary.

Despite positive moves in the West, Asia's recovery has been much stronger, with pre-pandemic oil demand levels likely to be exceeded this year. The composition of demand has changed significantly, though, with strong gasoline demand in major consumer regions. Diesel consumption has also been firm, supported by power generation demand with higher use by off-grid

generators. The “energy crunch” that emerged in Q3 21 has been a support to this sector.

Tightness in global gas markets is helping support power generation demand — the ability to switch to oil for power generation is most prominent in Asia, particularly China, India and Japan. These countries are likely to account for about half of the potential increase in oil demand for power generation usage that could persist through Q1 22, largely comprising fuel oil and gasoil.

In contrast, jet fuel demand is still well below pre-pandemic levels, with Asia Pacific and Europe the most prominent components of this “gap.” Globally, jet fuel demand in Q4 21 was about 2 Mn b/d lower than pre-pandemic levels. This element of oil demand is likely to take the longest time to recover, and remains most at risk to travel restrictions and other measures which are — and could be — put in place to prevent the spread of new variants. Clearly though, this element of oil demand is also most at risk of new restrictions emerging in response to the Omicron variant of COVID.

The supply-side increase in 2021 far outweighs demand, driven by a strong growth in the available fleet as the floating storage dynamic reverses. However, the dearth of contracting seen in the latter part of 2021 should be positive for fundamentals, providing

support for higher rate levels in the future.

Finally, at this seasonal time of year, spare a thought for the beleaguered cruise lines. Whilst air travel and jet fuel demand have taken a hit during the pandemic, nothing compares to the destruction witnessed in the cruise sector. After more or less grinding to a halt during the first half of 2020, cruise line operators have struggled to resume operations with any sort of consistency. Global cruise passenger volumes declined by 75% yoy in 2020 to 7.5 million passengers and, though this year has seen a partial recovery to grow by 10% yoy, this still means that passenger numbers remain over 70% below pre-pandemic levels.

Although MSI expects over 20 million passengers to cruise during 2022, the sector remains at the mercy of government actions to combat the pandemic, as well as fluctuating public opinion about their safety from the virus and the potential dangers of international travel. The net revenue losses experienced by the industry during the last two years exceed the net aggregated revenue gains over the preceding five-year period.

With mega cruise ships routinely costing in excess of \$1 billion to construct, and a large newbuilding orderbook scheduled for delivery over the next three or more years, sector profitability is likely to remain under pressure for some time to come.

