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FREIGHT RATES AND MARITIME TRANSPORT COSTS

This chapter covers the development of freight rates and maritime transport costs. Section A encompasses some relevant developments in maritime freight rates in various market segments, namely containerized trade, and liquid-bulk and dry-bulk shipping in 2013 and early 2014. It highlights significant events leading to major price fluctuations, discusses recent industry trends and gives a selective outlook on future developments of freight markets.

The year 2013 was marked by another gloomy and volatile maritime freight rate market: all shipping segments suffered substantially; with freight rates in dry-bulk and tanker markets reaching a 10-year low in 2013 and similarly low levels in the liner market. The general causes of freight rates' low performance were mainly attributable to the poor world economic development, weak or hesitant demand and persistent supply overcapacity in the global shipping market.

Section B provides a brief overview of some relevant developments in shipping finance and in equity investment more specifically. In 2013, private equity investments continued to play a key role in the shipping industry as traditional bank financing remained very limited and available only to few solid transactions.

A. FREIGHT RATES

After five years of economic downturn, 2013 was marked by another gloomy and volatile maritime freight rate market. Indeed, all shipping segments suffered substantially, with freight rates in dry-bulk and tanker markets reaching a 10-year low in 2013 and similarly low levels in the container-liner market.

The general causes of freight rates' low performance remain, as in previous years, the result of a poor world economic development, weak or hesitant demand and persistent overcapacity from the supply side in the global shipping market.

1. Container freight rates

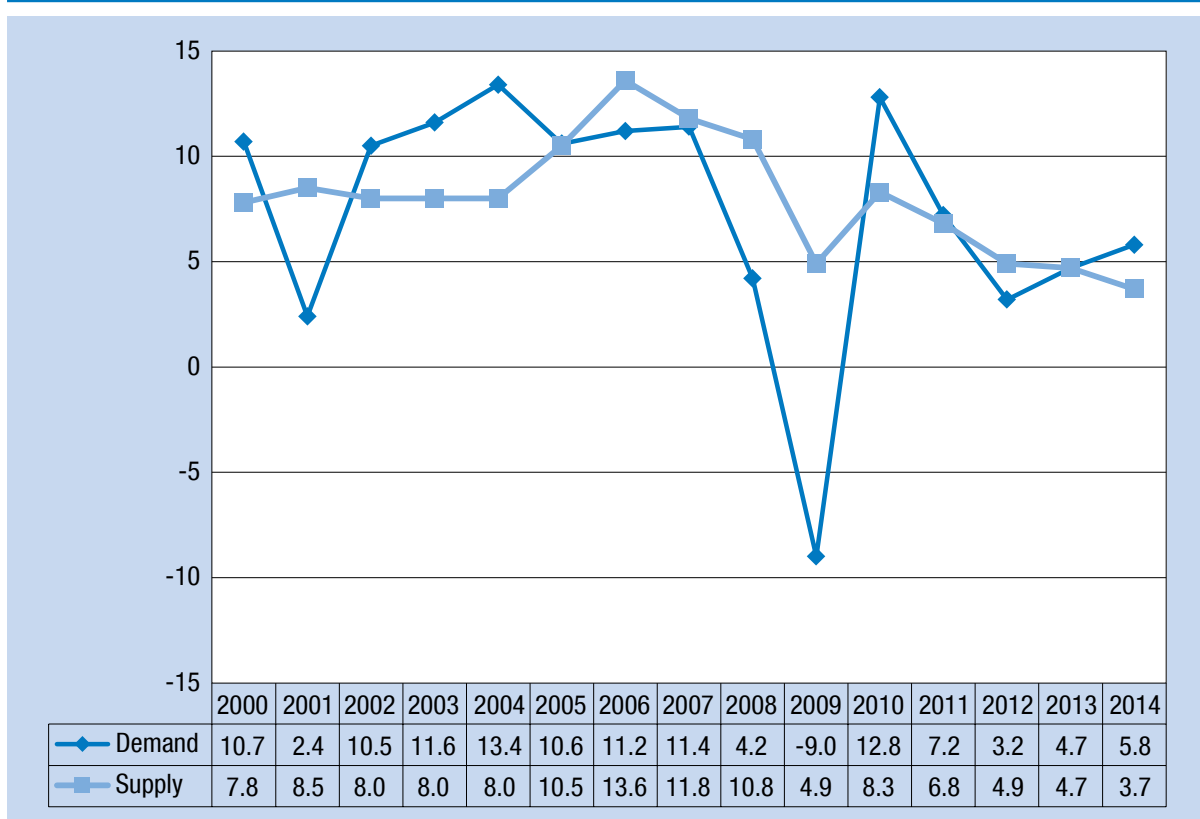
The container-ship market was tense throughout 2013, with freight rates remaining volatile and struggling to rise. Overall the sector fundamentals were slightly unbalanced, leading to low freight rates

and low returns with which carriers had to struggle throughout the year.

As illustrated in figure 3.1, overall global demand for containers transported by sea witnessed a growth estimated at 4.7 per cent in 2013 compared to 3.2 per cent in 2012. This global growth in demand was matched by a slight deceleration in growth of global container supply that was 4.7 per cent in 2013 compared to 4.9 per cent in 2012.

The growth in container demand, which was observed in most trade routes (see chapter 1), did not have an impact on freight rates as they remained historically weak and volatile. This is an indication that structural oversupply pertained, with the majority of trade lanes being oversupplied with tonnage. The delivery of new container ships in 2013, mainly dominated by large Post-panamax vessels of 8,000+ TEU capacities, did not help reverse the tendency (see chapter 2). Average freight rates on most trade lanes remained low and significantly below those of 2012, as reported in table 3.1 (Clarkson Research Services, 2014a).

Figure 3.1. Growth of demand and supply in container shipping, 2000–2014 (Annual growth rates)



Source: Compiled by the UNCTAD secretariat on the basis of data from Clarkson Container Intelligence Monthly, various issues.

Note: Supply data refer to the total capacity of the container-carrying fleet, including multi-purpose and other vessels with some degree of container carrying capacity. Demand growth is based on million TEU lifts. The data for 2014 are projected figures.

Table 3.1. Container freight markets and rates

Freight markets	2009	2010	2011	2012	2013
Trans-Pacific (\$ per FEU)*					
Shanghai–United States West Coast	1 372	2 308	1 667	2 287	2033
Percentage change		68.21	-27.77	37.19	-11.11
Shanghai–United States East Coast	2 367	3 499	3 008	3 416	3290
Percentage change		47.84	-14.03	13.56	-3.7
Far East–Europe (\$ per TEU)					
Shanghai–Northern Europe	1 395	1 789	881	1 353	1084
Percentage change		28.24	-50.75	53.58	-19.88
Shanghai–Mediterranean	1 397	1 739	973	1 336	1151
Percentage change		24.49	-44.05	37.31	-13.85
North–South (\$ per TEU)					
Shanghai–South America (Santos)	2 429	2 236	1 483	1 771	1380
Percentage change		-7.95	-33.68	19.42	-22.08
Shanghai–Australia/New Zealand (Melbourne)	1 500	1 189	772	925	818
Percentage change		-20.73	-35.07	19.82	-11.57
Shanghai–West Africa (Lagos)	2 247	2 305	1 908	2 092	1927
Percentage change		2.56	-17.22	9.64	-7.89
Shanghai–South Africa (Durban)	1 495	1 481	991	1 047	805
Percentage change		-0.96	-33.09	5.65	-23.11
Intra-Asian (\$ per TEU)					
Shanghai–South-East Asia (Singapore)		318	210	256	231
Percentage change			-33.96	21.84	-9.72
Shanghai–East Japan		316	337	345	346
Percentage change			6.65	2.37	0.29
Shanghai–Republic of Korea		193	198	183	197
Percentage change			2.59	-7.58	7.65
Shanghai–Hong Kong (China)		116	155	131	85
Percentage change			33.62	-15.48	-35.11
Shanghai–Persian Gulf (Dubai)	639	922	838	981	771
Percentage change		44.33	-9.11	17.06	-21.41

Source: Container Intelligence Monthly, Clarkson Research Services, various issues.

Note: Data based on yearly averages.

* FEU: 40-foot equivalent unit.

Mainlane freight rates suffered from the supply capacity brought by new very large container ships (VLCSSs), the majority of which were directly deployed on mainlane trades upon delivery. These new entries led to the redeployment of smaller Post-panamax vessels onto other routes and heightened the cascade effect. However, the cascading of TEU capacity from mainlane to non-mainlane routes was not sufficient to support freight rates on mainlanes. For instance, despite 10 general rates increase attempts over the course of 2013, struggling Far East–Europe trade route freight rates remained low and volatile, with full year rates averaging just \$1,084 per TEU, 20 per cent lower than the 2012 average (Clarkson Research Services, 2014b). Moreover, trans-Pacific freight rates were also saddled with oversupply. The Shanghai–United States West Coast annual rate averaged at \$2,033 per 40-foot-equivalent unit in 2013, 11 per cent below the full-year 2012 average. As to non-mainlanes, they also suffered from substantial capacity levels that have been cascaded down from the mainlanes since most of the added capacity was not needed. A number of non-mainlane freight rates have come under pressure. For instance, rates from China (Shanghai) to South America (Santos, Brazil), Australia/New Zealand (Melbourne) and South Africa (Durban) have all fallen to their lowest since 2009 (table 3.1). The channelling (or cascading) of tonnage capacity down the trade-lane hierarchy was also enough to put pressure on intra-Asian rates, despite the sustained robust regional trade growth (Clarkson Research Services, 2013).

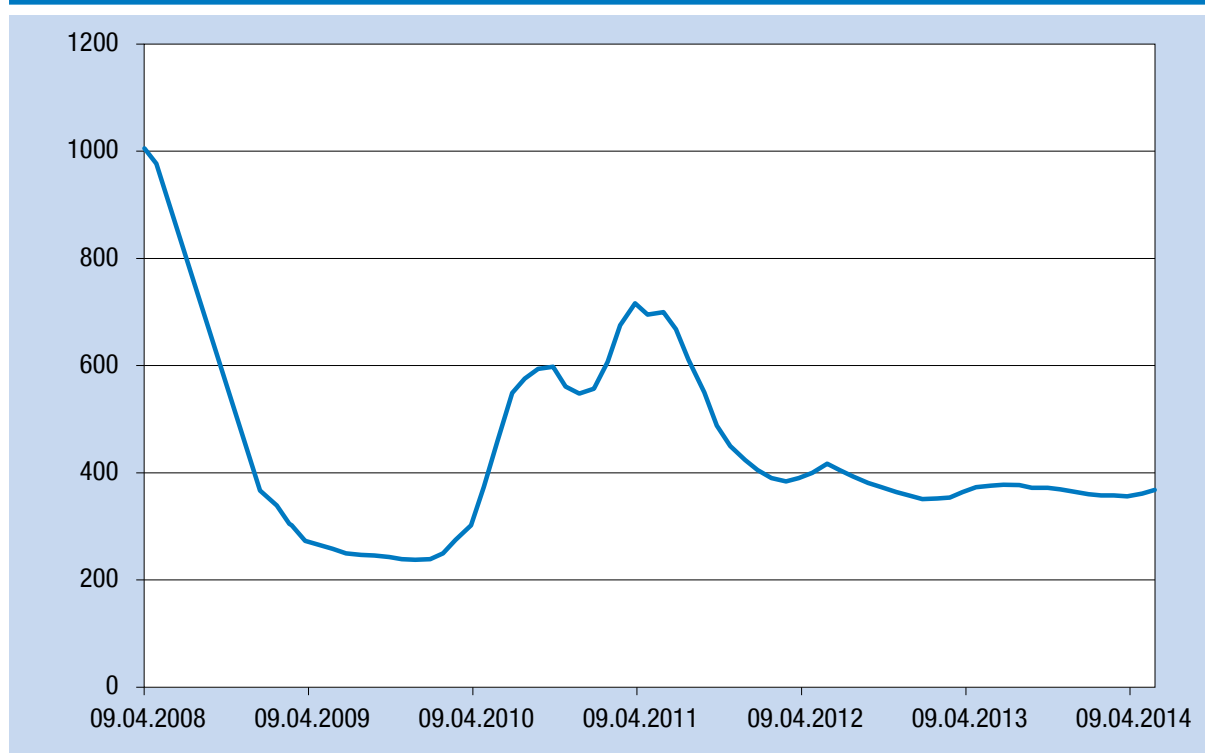
In an effort to deal with low freight rate levels and to leverage some earnings, carriers looked at measures to improve efficiency and optimize operations in order to reduce unit operating costs. Some of these measures involved operational consolidation, slow steaming, idling, and replacing smaller and older vessels with newer and more fuel-efficient ones. This was the case, for instance, of Maersk Line, which reported strong profits of \$1.5 billion in 2013, in contrast to generally poor figures posted by most carriers. Maersk claimed that the result derived from significant efficiency improvement per unit through network optimization, vessel retrofitting and the deployment of new, more fuel-efficient vessels, such as the new generation Triple-E 18,270 TEU ships, in addition to cost-cutting resulting from reduced fuel consumption and CO₂ emissions (*Lloyd's List Containerisation International*, 2014).³ It was reported that the

company managed to save \$764 million in 2013 after cutting fuel consumption by 12.1 per cent. Maersk achieved these reductions despite having increased its fleet capacity by 0.2 per cent to 2.6 million TEU and shipping volume by 4.1 per cent to 8.8 million 40-foot-equivalent units (*Lloyd's List Containerisation International*, 2014).⁴

In another attempt to reduce costs, new alliances have also emerged. For instance, the G6 Alliance, which formed at the end of 2011 to bring members of the New World Alliance and the Grand Alliance together in the Asia–Europe and Mediterranean trade lanes, expanded cooperation to the Asia–North America East Coast trade lane in May 2013. This alliance is supposed to provide 30 per cent of total available capacity between the Far East and the United States Gulf Coast. Moreover, recognizing the emerging threat, Hapag-Lloyd, a key member of the G6 Alliance, and Chilean-based Compañía Sud Americana de Vapores (CSAV) announced their intention to merge and signed a binding contract in April 2014. This will form the fourth-largest global container shipping line, with some 200 vessels with a total transport capacity of around 1 million TEU and an annual transport volume of 7.5 million TEU (see press release: Hapag-Lloyd, 2014).⁵

Furthermore, the sale of non-core activities and the restructuring of portfolio management have been part of strategies applied by many liner shipping companies to minimize costs and to free up capital for new investment and cumulate cash reserves in a period of financial distress. These strategic measures have included the selling of freight terminal assets and other peripheral businesses, such as container manufacturing, inland logistics and customer services, which have affected shippers more directly. For example, CMA-CGM was able to increase its net profit by almost 23 per cent (or by \$200 million net gain) in 2013 from the sale of 49 per cent of its terminals link to China Merchants Holdings in June 2013, reaching a consolidated net profit of \$408 million against \$332 million in 2012 (*Journal of Commerce (JOC)*, 2014). On the other hand, the Republic of Korea-based Hanjin Shipping announced its plans to drop out of the transatlantic trade as of May 2014 in an effort to trim unprofitable activities (AlixPartners, 2014). The carrier plans also to divest parts of its dry-bulk fleet and container terminals as part of an effort to restore the company's finances, aiming to raise \$1.45 billion (*ShippingWatch*, 2013).

Figure 3.2. New ConTex Index, 2008–2014



Source: Compiled by the UNCTAD secretariat, using the New ConTex Index produced by the Hamburg Shipbrokers' Association. See <http://www.vhss.de> (accessed 26 September 2014).

Notes: The New ConTex Index is a container-ship time charter assessment index calculated as an equivalent weight of percentage change from six ConTex assessments, including the following ship sizes (TEU): 1,100; 1,700; 2,500; 2,700; 3,500 and 4,250. Index base: October 2007 = 1,000 points.

As to the charter market, the mismatch between centres of growing demand (non-mainlanes) and the new supply, dominated by VLCSs, had an impact on its rates, which remained depressed and under pressure throughout 2013. As shown in figure 3.2, the New ConTex Index⁶ remained low in 2013, averaging 367 points (compared to 388 points in 2012), reflecting the difficult situation the tonnage providers had to face. The reason for such low rate levels was mainly attributable to the effect of cascading and the large idle capacity (for which the total average volume amounted to 0.60 million TEU across 2013, and of which two thirds was charter-owned tonnage) (Barry Rogliano Salles, 2014),⁷ which maintained the downward pressure on the charter market. As a result, container-ship time charter rates remained low even when they appeared to have improved from previous yearly averages (table 3.2).

Despite better economic prospects and an increase in freight rates at the beginning of 2014, the market is expected to remain under pressure because of the

persistent mismatch between supply capacity and demand. The gap may actually grow in the coming years due to the increased order book of container ships in 2013. A wave of new orders of large vessels by most main carriers was noted in 2013 in a race to improve efficiency and reduce operational cost per TEU. The container-ship order book, which grew from 41 million dwt at the beginning of 2013 to 43 million at the beginning of 2014, represents about 20 per cent of the fleet in service (see chapter 2, figure. 2.8). The resulting overflow of orders may once again contribute to destabilizing freight rate recovery in general. Freight rates on individual routes will therefore continue to be determined by the way supply capacity management will be handled.

2. Tanker freight rates

Freight rates in the tanker segment remained weak in 2013, reaching historically low levels in both crude and products sectors. As reflected in table 3.3, the

Table 3.2. Container-ship time charter rates (\$ per 14-ton TEU per day)

Ship type and sailing speed (TEUs)	Yearly averages												Yearly average percentage change 2013/2012
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Gearless													
200–299 (min 14 knots)	16.9	19.6	25.0	31.7	26.7	27.2	26.0	12.5	12.4	12.4	12.6	13.0	3.24
300–500 (min 15 knots)	15.1	17.5	21.7	28.3	21.7	22.3	20.0	8.8	9.9	12.8	10.0	10.9	9.00
Gearled/gearless													
2 000–2 299 (min 22 knots)	4.9	9.8	13.8	16.4	10.5	11.7	10.0	2.7	4.8	6.3	3.3	3.4	1.77
2 300–3 400 (min 22.5 knots)	6.0	9.3	13.2	13.0	10.2	10.7	10.7	4.9	4.7	6.2			
Gearled													
200–299 (min 14 knots)	17.0	18.9	27.0	35.4	28.0	29.8	32.1	16.7	18.3	22.1	18.1	21.1	16.53
300–500 (min 15 knots)	13.4	15.6	22.2	28.8	22.0	21.3	21.4	9.8	11.7	15.4	13.5	14.9	10.49
600–799 (min 17–17.9 knots)	9.3	12.3	19.6	23.7	16.6	16.1	15.6	6.6	8.4	11.2	7.7	8.7	12.34
700–999 (min 18 knots)	9.1	12.1	18.4	22.0	16.7	16.9	15.4	6.0	8.5	11.5	7.6	8.7	14.91
1 000–1 299 (min 19 knots)	6.9	11.6	19.1	22.6	14.3	13.7	12.2	4.0	5.9	8.7	5.7	6.6	15.50
1 600–1 999 (min 20 knots)	5.7	10.0	16.1	15.8	11.8	12.8	10.8	3.5	5.0	6.8	3.9	4.1	5.77
Ship type and sailing speed (TEUs)	Monthly averages for 2013												
	Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.	
Gearless													
200–299 (min 14 knots)	12.1	13.4	10.0	12.6	13.3	13.1	13.5	13.5	13.5	14.4	13.0	13.7	
300–500 (min 15 knots)	10.2	10.5	10.7	10.5	11.3	11.3	10.1	10.3	9.9	11.3	11.2	13.5	
Gearled/gearless													
2 000–2 299 (min 22 knots)	3.2	3.0	3.1	3.3	3.3	3.4	3.5	3.6	3.5	3.5	3.5	3.4	
Gearled													
200–299 (min 14 knots)	20.2	20.6	19.7	19.7	23.4	23.4	20.9	19.6	19.6	23.4	20.7	21.9	
300–500 (min 15 knots)	13.8	13.8	14.0	14.2	14.1	16.5	17.7	14.6	14.3	15.6	16.9	13.5	
600–799 (min 17–17.9 knots)	8.0	7.4	7.4	9.0	9.0	10.0	8.7	8.7	8.7	9.0	8.9	9	
700–999 (min 18 knots)	8.1	8.6	8.4	9.1	9.0	8.5	8.5	9.1	9.4	8.9	8.8	8.4	
1 000–1 299 (min 19 knots)	5.3	5.7	5.8	6.0	6.2	6.4	6.3	6.3	6.9	8.1	8.2	7.8	
1 600–1 999 (min 20 knots)	3.7	3.8	3.9	4.0	4.1	4.2	4.2	4.3	4.2	4.2	4.4	4.5	

Source: Compiled by the UNCTAD secretariat based on Hamburg Index data from Shipping Statistics and Market Review, various issues, 2002–2014, produced by the Institute of Shipping Economics and Logistics, Bremen, Germany. See also www.isl.org (accessed 26 September 2014).

Abbreviation: min = minimum.

Table 3.3. Baltic Exchange Tanker Indices

	2008	2009	2010	2011	2012	2013	Percentage change (2013/2012)	2014 (first half year)
Dirty Tanker Index	1 510	581	896	782	720	645	-10.42	774
Clean Tanker Index	1 155	485	732	721	643	607	-5.6	574

Source: Clarkson Research Services, Shipping intelligence network – Timeseries, 2014.

Baltic Exchange Tanker Indices maintained their downtrend since 2009. The average Dirty Tanker Index declined to 645 points in 2013 compared to 720 in 2012, representing a drop of 10.42 per cent. The average Baltic Clean Tanker Index reached 607 points in 2013 compared to 643 in 2012, a 5.6 per cent drop compared to the 2012 annual average.⁸

This decline was mainly due to the lack of equilibrium in the tanker market conditions, which continued to suffer from a relatively soft demand (see chapter 1) and a massive oversupply of vessels (see chapter 2).

Freight rates and earnings for the different tanker markets

For the first 10 months of 2013, the tanker market reached its weakest performance in 20 years, with rates dropping below the level of operating costs. The VLCC, Suezmax and Aframax segments of the tanker markets saw their average daily returns dropping by 15 to 20 per cent compared to 2012 (Barry Rogliano Salles, 2014). Despite increases in Chinese imports, the lower demand from the United States due to increasing self-sufficiency and the transfer of the oil-refining industry from West to East regions affected rates, which were also challenged by the growing supply of tonnage which affected fleet utilization negatively. However, towards the end of the year, a combination of winter demand, higher Chinese demand, weather-related delays in the Turkish Straits and a slower fleet growth caused rates to soar and the Baltic Dirty Tanker Index surged above 1,000 in early 2014. Despite the sudden upturn in rates, the returns recorded were short-lived. Oversupply of capacity still remains a concern that needs to be cleared before a sustained rates recovery can take place.

The VLCC/ultralarge crude carrier (ULCC) segment, following a weak start to the year, encountered the strongest growth in freight rates towards the end of 2013. The weak freight rates were largely driven by low demand (mainly from United States crude imports) and the impact of rapid fleet growth in recent years. However, improved Chinese crude imports towards the end of the year and a lack of tonnage availability – the lowest seen for some time – in the two main VLCC loading regions (the Persian Gulf and West Africa) caused the rates to improve significantly by the end of 2013. Another important element that impacted VLCC rates was the increased level of demolition that the segment witnessed, the highest since 2003 (some 22 VLCCs went to scrap as opposed to 14 VLCCs in 2012). As seen in table 3.4, VLCC/ULCC spot tanker

freight rates exhibited an increase of more than 40 per cent on average in November and December 2013 compared to previous months. This in turn supported shipowners' margins which had reached an all-time low. In the first 10 months of the year, average earnings for VLCC/ULCC were around \$10,000 per day (equal to operating expenses estimated also around \$10,000 per day); this was then topped to more than \$40,000 per day in November and December 2013, representing a three-year record high. Rates have since fallen back to lower levels due to structural challenges in supply and demand (Clarkson Research Services, 2014b).

Similarly, Suezmax spot freight rates remained relatively weak throughout the year, with a slight increase towards the end. The low levels were also largely attributable to supply-side pressure on the market and to low demand, mainly due to the withdrawal of United States crude imports from West Africa and the absence of Libyan cargoes during most of the year. As with other tanker segments, improvement in market conditions towards the end of 2013, particularly in the Mediterranean, the Black Sea and West Africa (Clarkson Research Services, 2014b), and partially because of VLCC higher freight rates that pushed some shippers to split their cargoes (Organization of the Petroleum Exporting Countries, 2013), helped rate recovery. As such, rates for tankers operating on the West Africa–Caribbean/East Coast of North America route increased by 25 per cent in November to stand at WS 60 points, and rates on the West Africa–North West Europe route gained 24 per cent to stand at WS 62 points. As to earnings, they averaged around \$12,755 per day in the first three quarters of the year, down 30 per cent compared to the same period in 2012. However, a notable surge in earnings was recorded at an average of \$50,323 per day in December 2013. Earnings have since declined, falling back to \$14,463 per day in February 2014 (Clarkson Research Services, 2014b).

Aframax spot freight rates also remained weak with a slight improvement towards the end of year. The increase was mainly due to large delays in the Turkish Straits limiting available tonnage and the increased demand in the Caribbean and Mediterranean. The healthiest increase was registered on spot freight rates for Aframax trading on the Caribbean–Caribbean/East Coast of North America route as it increased by 50 per cent in December 2013 with WS 155 points, and by 70 per cent from December

2012. As to spot earnings, they remained low in the first three quarters of 2013, averaging around \$10,395 per day and not changing much from 2012 levels in the same period. Conversely, average earnings rose to \$34,000 per day in December and exceeded \$50,000 per day in January 2014. However, the higher rate environment could not be maintained, and earnings fell back to around \$13,000 per day in February 2014 (Clarkson Research Services, 2014b).

A positive point was the drop in bunker prices throughout the year, averaging \$593 in Rotterdam compared to \$638 in 2012, which supported daily returns of most tanker markets. These were also sustained by scrapping (8 million dwt was scrapped in 2013, the highest level since 2003), delaying or cancelling delivery of new vessels (which amounted to approximately 50 per cent of orders scheduled for delivery in 2013) (Danish Ship Finance, 2014), removal of vessels, together with slow steaming, which became the norm as part of cost-cutting efforts and control of supply.

During the first quarter of 2014, the crude tanker market continued to suffer from massive oversupply. However, crude tanker spot rates strengthened significantly, with Aframax and Suezmax rates achieving one of their highest quarterly averages since 2008. A combination of stronger fundamentals (increased demand of crude oil imports by China and a greater volume of long-haul Asian crude imports from West Africa) and seasonal factors (weather delays, particularly in the Atlantic basin) led to a significant spike in crude tanker rates during the early part of the first quarter. These strong rates were not sustained and dissipated during March 2014, as seasonal factors decreased and Chinese crude imports slowed. This weakness has extended into the early part of the second quarter of 2014 (Danish Ship Finance, 2014).

The clean market, on the other hand, continued to outperform the crude market that began in 2012. This was mainly noticeable in the first part of the year with an increase in clean trade, led by Asian oil demand (R.S. Platou, 2014). Medium-range tanker rates increased with an average at \$16,000 per day, a strong improvement from the 2012 rate of \$12,000 per day. However, there continued to be an oversupply of tonnage in the product tanker market, which held back time charter rates.

In the near foreseeable future, as for container shipping, it is likely that the tanker market rates will remain threatened by the imbalance between supply

and demand. Changing trade dynamics, longer travel distances and scrapping could potentially absorb the increasing inflow of vessels. However, fleet growth is still expected to outpace tonnage demand. Consequently, the market will remain under pressure in 2014 as a result of overcapacity, whereas 2015 may see some market balance improvement.

3. Dry-bulk freight rates

Similar to other shipping segments, a weak demand, the depressed world economic situation, and oversupply of tonnage continue to control the dry-bulk freight rates.⁹ Nevertheless, the year was divided into two phases. As shown in figure 3.3, the Baltic Dry Index, which started the year at 771 points, remained very low during the first six months with a six-month average of 843 points and reaching its lowest level at 745 points in February. However, over the second half of the year, as for oil tankers, the bulk market witnessed noticeable increases in freight rates with the December index reaching 2178 points, leading to an average index of 1214 points for the year compared to an average of 918 points for 2012. The peak December level had not been seen since November 2010. The improvement of the market was due to an increase in demand that outpaced the increase in available vessels and was primarily led by the Capesize segment, as China began to restock coal and increase iron-ore imports (Danish Ship Finance, 2014). The rates in the smaller segments increased too, but at a slower and more constant pace. However, these high rate levels were not maintained and by June 2014 the index was down to 915 points.

Average earnings in all bulk carrier sectors remained relatively weak in 2013 although slightly higher than in 2012, due mainly to the improvements in Capesize spot earnings in the second half of the year. With earnings averaging \$7,731 per day in 2013, bulk carriers in general had to struggle to cover typical operating expenses. The overall low earnings continued to push owners to keep operating their fleets at slower speeds.

Capesize

After a weak beginning in 2013, with average earnings of about \$6,435 per day, the Capesize market improved towards the end of the year with average spot earnings exceeding \$40,000 per day. This

increase was mainly due to a strong demand for iron-ore import by China and lower growth in Capesize fleet supply.

The end of 2013 witnessed an increase in the Capesize order book, influenced by historically low newbuilding prices and improved freight rates. However, in the short term and for the first time in several years global iron-ore trade is expected to grow faster than the Capesize fleet, which is likely to improve rates and earnings in the Capesize sector.

Panamax

In 2013, average Panamax spot earnings remained at historically weak levels, reaching \$6,600 per day – although levels were 25 per cent up on a year-over-year basis, they were still 71 per cent less than average earnings over the previous 10-year period (\$22,934 per day). The low spot earnings were largely due to sustained strong supply growth and fairly limited

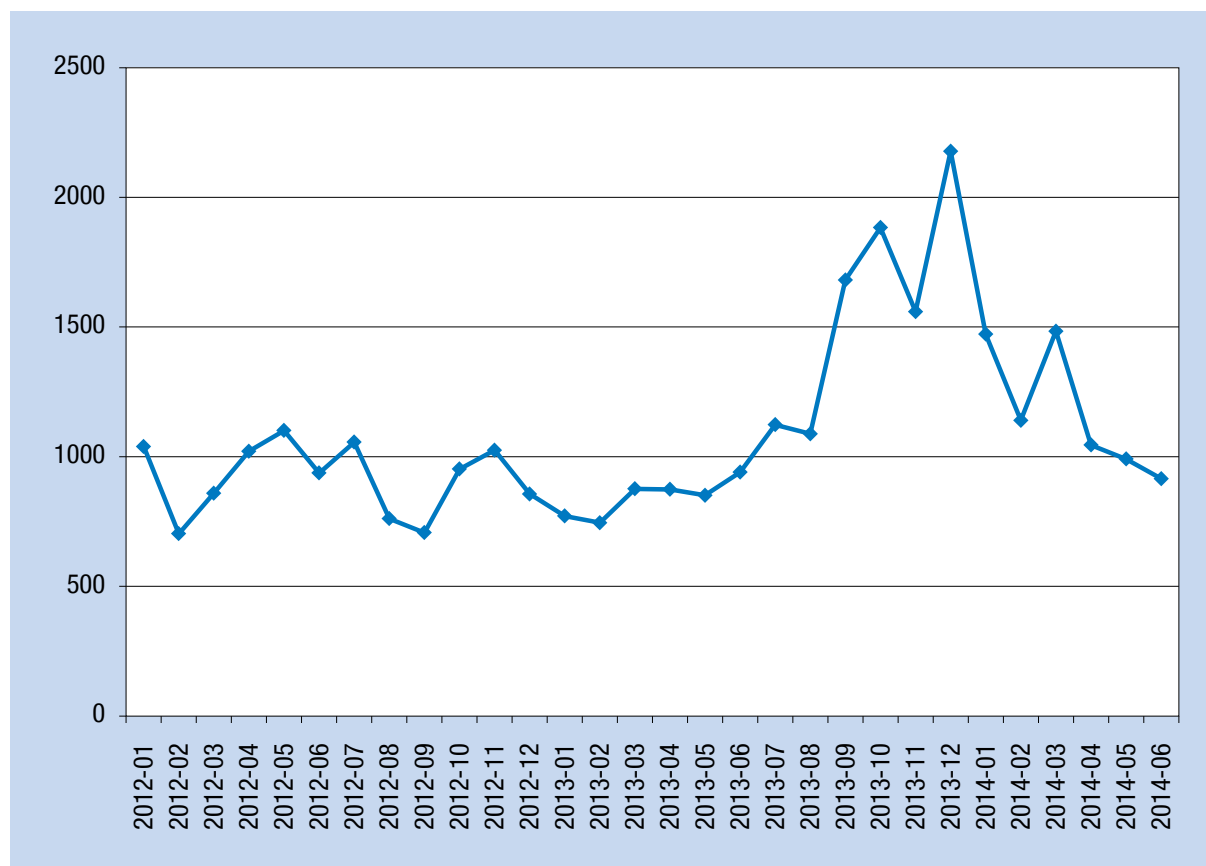
scrapping. Panamax fleet growth was the fastest out of all bulk carrier sectors in 2013, increasing by 9 per cent.

Panamax time charter rates also improved marginally in 2013 with earnings averaging \$10,099 per day. This compares to an average of \$9,706 per day in 2012 and \$14,662 per day in 2011.

Handymax and Supramax

Oversupply continued to affect the Handymax market in 2013, as deliveries continued and exceeded scrapping. Average earnings remained below the historical 10-year average of \$23,118 per day. Although still historically weak, freight rates in the Handymax sector have been supported to some extent by strong mineral import demand, particularly as China has been building up stocks of bauxite and nickel ore, as well as by firm growth of the intra-Asian coal trade.

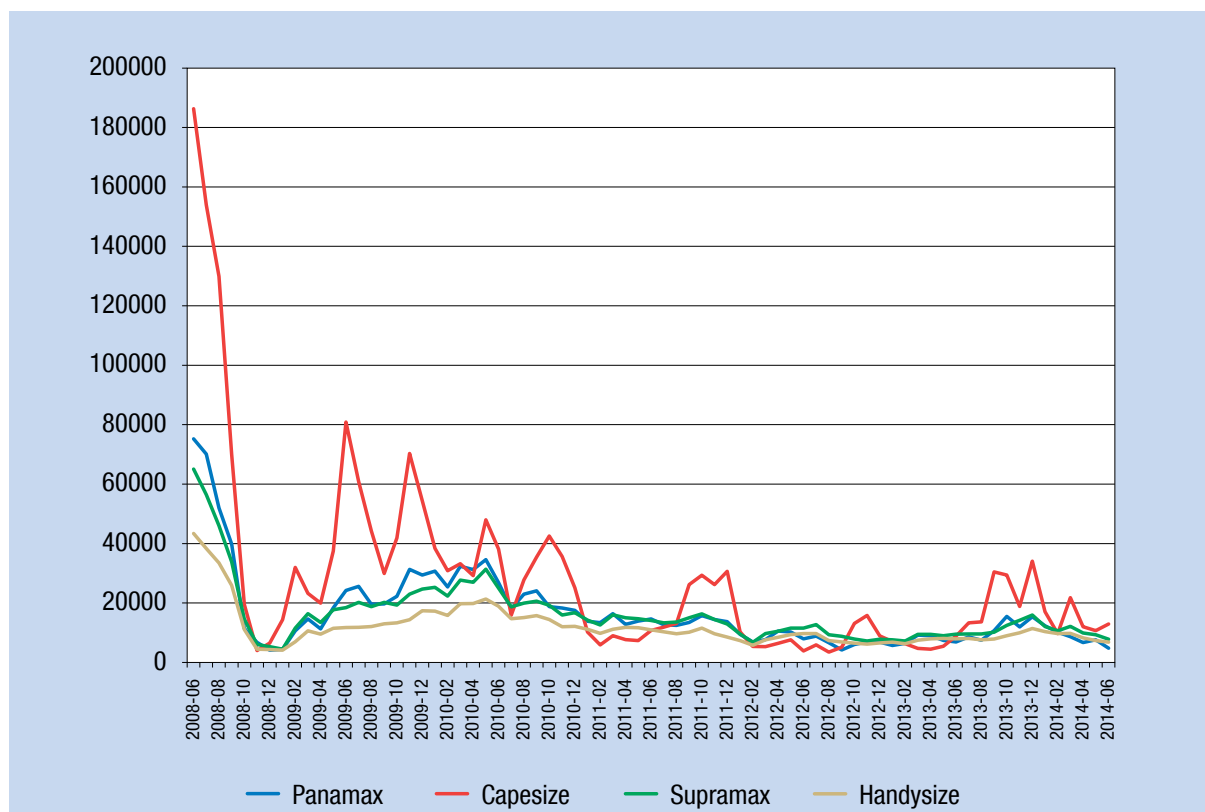
Figure 3.3. Baltic Exchange Dry Index, 2012–2014 (Index base year 1985 = 1,000 points)



Source: UNCTAD, based on London Baltic Exchange data.

Note: The index is made up of 20 key dry-bulk routes measured on a time charter basis. The index covers Handysize, Supramax, Panamax and Capesize dry-bulk carriers, carrying commodities such as coal, iron ore and grain.

Figure 3.4. Daily earnings of bulk carrier vessels, 2008–2014 (\$ per day)



Source: UNCTAD, based on data from Clarkson Shipping Intelligence Network; figures published by the London Baltic Exchange.
 Note: Supramax – average of the six time charter routes; Handysize – average of the six time charter routes; Panamax – average of the four time charter routes; Capesize – average of the four time charter routes.

Average Supramax earnings increased by 9 per cent but remained relatively weak at \$9,468 per day in 2013 due to persistent supply growth. The current levels of oversupply in the market and the growing order book suggest that market fundamentals are likely to remain imbalanced in the short term.

The dry-bulk market rates for 2014 and beyond are still dominated by a large order book and uncertainties with the Chinese demand for dry-bulk commodities. Even though market balance seems to have improved, long-term prospects and freight rate recovery remain unclear.

B. SOME RELEVANT DEVELOPMENTS IN SHIPPING FINANCE: PRIVATE EQUITY EXPANSION

The year 2013 witnessed another important time in terms of institutional investor (such as private equity and hedge funds) participation in the shipping sector.

As discussed in the previous issue of the *Review of Maritime Transport*, over recent years, private equity funds have been paying particular attention to the shipping sector by taking advantage of the opportunities created by tight credit markets and investing in shipping companies, as well as vessels that, since the global economic downturn, have reached historically low prices (vessel value collapsed as much as 71 per cent in five years) (Arnsdorf and Brautlecht, 2014). From the perspective of these funds, the main objective of investments in the shipping sector is to sell or float their investments once the market rebounds.

In 2013, private equity investments continued to play a key role in the shipping industry as traditional bank financing remained very limited and available only to a few solid transactions. Private equity investments have been very active in buying shipping loan books from banks, accounting for about \$5 billion in 2013 (Arnsdorf and Brautlecht, 2014). One example is the Royal Bank of Scotland, which sold hundreds

of millions of dollars of shipping loans to hedge fund Davidson Kempner Capital Management and private equity firms Oaktree Capital Management and Centerbridge Partners, all in the United States (*Financial News*, 2014). Similarly, in December 2013, Commerzbank AG, Germany's second-biggest bank, sold 14 chemical tankers to a fund managed by Oaktree Capital Management, eliminating \$383 million in non-performing shipping loans (Arnsdorf and Brautlecht, 2014). The investment approach for private equity and hedge funds has been to buy vessels directly as well as through joint ventures with shipping specialists. For example, Oaktree Capital Management partnered with Navig8 to form a joint venture and order new vessels, seeing the low prices for modern and fuel-efficient ships as an opportunity and a worthwhile investment. The company ordered six chemical tankers from a shipyard in the Republic of Korea for delivery in 2015. Other examples of equity investments include Apollo Global Management, which teamed up with Hamburg-based ship manager Rickmers Group to invest as much as \$500 million in container vessels,¹⁰ and York Capital Management, which formed a joint venture with Greek shipowner Costamare Inc. to buy five container ships for more than \$190 million (Arnsdorf and Brautlecht, 2014). Further examples of recent private equity investments in shipping are given in table 3.5.

However, the interest of equity funds in the maritime sector may have serious repercussions on the sector. The new influx of finance is creating new opportunities

for shipowners, shipyards and trade generally, but at the same time it is destabilizing its market fundamentals. As noted above, and bearing in mind the discussion in chapter 2, the year 2013 witnessed a surge in world order books. Backed by private equity and hedge-fund financing and driven by the low price of newbuilding vessels and the arrival of more efficient and economical ships, shipping companies have placed a large number of orders. This additional capacity, once delivered, may disturb the demand–supply equilibrium and threaten the future prospects of the industry, in view of the current fragile economic recovery and persistent oversupply in ship capacity. A deepening in the imbalance between supply and demand would in turn impact freight rates and raise volatility, as the shipping companies would have to manage the new supply capacity with trade demand on various routes, which consequently would strain their earnings. This was observed during the ship-ordering spur of the mid-2000s that eventually led to overcapacity after the global financial crisis severely hit demand and depressed trade flows. On the other hand, private equity may find it difficult to exit the shipping sector once it becomes less profitable and gloomy. Nevertheless, private equity investments, if targeted properly, remains a good opportunity for the shipping sector to improve its efficiency and for shipping companies to become more financially sound, especially at a time when cash is scarce or expensive.

Table 3.5. Selected recent private equity investments in shipping**December 2013**

- Oaktree Capital Management buys 14 chemical tankers from Commerzbank for \$383 million.
- Davidson Kempner Capital Management reportedly pays \$500 million for part of Lloyd's Banking Group shipping portfolio.
- Undisclosed buyers purchase loans made by DNB to Genco Shipping and Trading; price not revealed.
- Kinder Morgan Energy Partners enters into an agreement to buy American Petroleum Tankers and State Class Tankers from an affiliate of the Blackstone Group and Cerberus Capital Management for \$962 million.
- Citi Bank buys \$11.8 million in TMT loans from Chang Hwa Bank; SC Lowy and Deutsche Bank buy TMT loans from First Commercial Bank for a total of \$96.7 million; JP Morgan buys TMT loans from FCB for \$34.2 million.

November 2013

- Global Maritime Investments orders six ships, financed by a large United States institutional fund; price not revealed.

October 2013

- Blackstone Group set up a partnership with Eletson Holdings to establish a liquefied petroleum gas shipping company worth \$700 million.
- Oaktree announces a partnership with Navig8 Group to form Navig8 Chemical Tankers, and places orders for six 37,000-dwt fuel-efficient vessels.

September 2013

- Funds affiliated with Apollo Global Management enter into a joint venture with Rickmers Group to invest in container ships, which will initially focus on second-hand vessels; the joint venture has a capacity to invest up to \$500 million.

August 2013

- Kohlberg, Kravis and Roberts (KKR) sets up Maritime Finance Company, with \$580 million in equity, with the purpose of originating, structuring, investing in and distributing debt financing; the venture is funded by KKR, KKR Financial Holdings, and MerchCap Solutions.
- Blackstone buys nine refined product tankers from Germany's Hartmann for an undisclosed price.

May 2013

- Delos and Tennenbaum Capital Partners buy 80 per cent stake in Konig and Cie, the first time that United States investors take control of a major German Kommanditgesellschaft house.

March 2013

- WL Ross/Astrup Fearnley announces plans to raise \$500 million in new private equity for a fund that will target distressed shipping and transportation assets.

February 2013

- The Arab Petroleum Investment Corp (Apicorp) joins Tufton Oceanic to establish a \$150 million fund that acquires five medium-range tankers.

January 2013

- SC Lowy provides \$85 million of debtor-in-possession financing for Korea Line, after serving as the line's sole restructuring advisor and taking a stake in the company.

Source: Lloyd's List, based on Marine Money, Lloyd's List, Bloomberg and Reuters company filings. See <http://www.lloydslist.com/ll/static/classified/article440167.ece/BINARY/privateequity-timeline> (accessed 10 June 2014).

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ENDNOTES

- ³ Based on Maersk *Sustainability Report 2013*, available at <http://www.maersk.com/en/the-maersk-group/sustainability/~media/97169B32CA46458897FAE47C780CF69F.ashx> (accessed 15 October 2014).
- ⁴ The measures also reduced CO₂ emission by 3.8 million tons, SO_x by 67,000 tons, NO_x by 95,000 tons and particulate matters by 8,000 tons.
- ⁵ Compañía Sud Americana de Vapores will become a new Hapag-Lloyd core shareholder besides HGV (City of Hamburg) and Kühne Maritime. The company will initially hold a 30 per cent stake in the combined entity. The partners have agreed on a capital increase of €370 million once the transaction has been concluded, to which CSAV will contribute €259 million. This will then increase the CSAV share of Hapag-Lloyd to 34 per cent. A second capital increase of €370 million will be linked to Hapag-Lloyd's planned stock exchange listing.
- ⁶ ConTex stands for "container-ship time charter assessment".
- ⁷ The number of container ships laid up, which had reached almost 11 per cent in 2009, was about 3.4 per cent at the end of 2013.
- ⁸ "Dirty tankers" typically carry heavier oils such as heavy fuel oils or crude oil. "Clean tankers" typically carry refined petroleum products such as gasoline, kerosene or jet fuels, or chemicals.
- ⁹ Data extracted from Clarkson Research Services *Shipping Review and Outlook*, spring 2014 and autumn 2013.
- ¹⁰ The venture bought six container vessels from Hamburg Süd for €176 million (\$240 million).