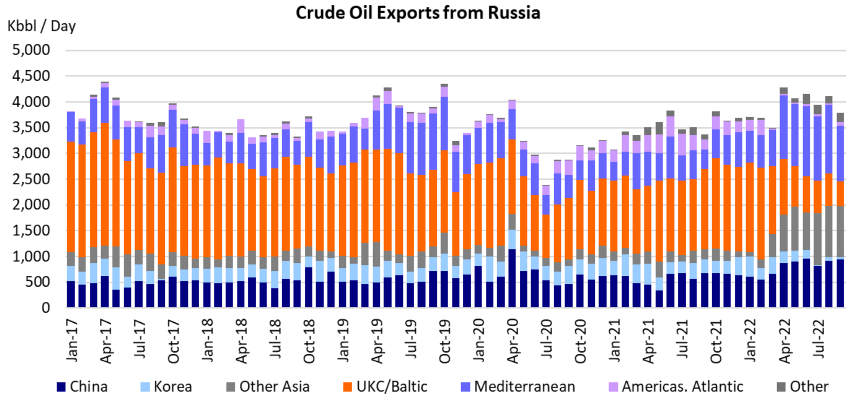
POTEN TANKER OPINION

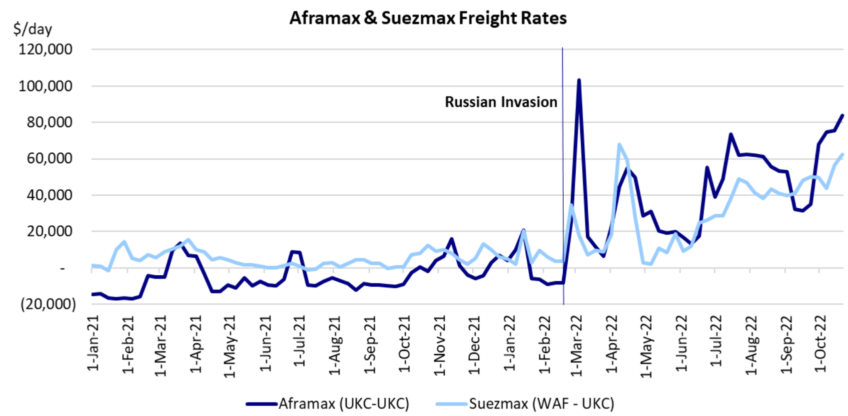
Putin's Rate Hike

There is a high level of uncertainty around Russian exports

According to the latest World Economic Outlook, published on October 11: "Global economic activity is experiencing a broad-based and sharper-than-expected slowdown, with inflation higher than seen in several decades." This has led to widespread worries about a global recession. The Chinese economy, which has been the main engine of global oil demand growth in recent decades has slowed recently and the future looks uncertain, partly due to the country's zero-Covid policy. OPEC+ has announced the biggest production cut since they throttled oil production by 10 Mb/d in May 2020 as a result of the global spread of Covid-19. At face value, these developments would not bode well for the tanker market. However, despite this, tanker rates have been on a roll in recent months. Why the disconnect? The answer is obviously the Russian invasion of Ukraine. This conflict has created massive geopolitical tension, triggered a wave of sanctions against Russia and it has caused a lot of dislocations, inefficiencies and uncertainty in the tanker market. Owners and charterers alike face a difficult choice: is this market set for further inefficiencies and rates increases as the EU ban on seaborne oil imports goes into effect (December 5th, 2022 for crude and February 5th, 2023 for products), or will the economic headwinds and possible cutbacks in Russian exports lead to a substantial decline in tanker demand? The latter could lead to a substantially weaker tanker market going forward.



Source: Lloyd's List Intelligence



Source: Poten & Partners

From a global perspective, it makes sense that ton-mile demand would increase when the EU starts to implement its import bans. Without restrictions, commodity flows are being optimized based on relative prices and shipping distances. Once restrictions such as sanctions or complex regulations (like the G7 price cap) are being factored in, the free flow of commodities will be compromised, and friction is introduced into the system. Regulatory uncertainty or geopolitical risks have a similar impact. Due to its geographical proximity, Russian crude oil and products have been ideal for European customers. Since the invasion of Ukraine, EU countries have started to wean themselves off Russian crude and products. This means that they have looked further afield for alternative supplies. This has increased the shipping distances. At the same time, Russia has been forced to look for alternative customers. They have sold additional barrels in India, China and Turkey. These shipments have also generated more ton-mile demand. This additional ton-mile demand has definitely contributed to the increase in tanker rates so far this year.

By December 5, tanker owners that fly any EU flag or carry P&I insurance from an EU club can no longer have crude oil onboard that originated in Russia, unless Russia has sold the crude to the buyer at or under the agreed price cap. However, the level of the price cap has not yet been agreed and/or disclosed. That means that any vessel that has recently loaded in Russia (or will do so in the next few weeks) has until December 5 to discharge its cargo. Considering the long sailing distances, recent shipments from the Baltic to China are already at risk of not arriving on time. How will the oil market treat Russian oil when the price cap is not (yet) settled? Does this mean there is the blanket insurance ban and a large portion of Russian barrels will be stranded?

How effective will the insurance ban be? The Russian government has had some time to prepare for the EU import ban and the associated restrictions on financial and maritime services, including cargo and vessel insurance. Will they have enough "alternative capacity" lined up to circumvent the ban? Will a growing portion of the "dark fleet" be allocated to Russian exports? What will the transit countries like Denmark (Danish Straits) and Turkey (Bosporus) do if a growing fleet of older, less well maintained, maybe underinsured tankers pass through their waters? Does the "dark fleet" have enough ice-class vessels to serve the Baltic Ports in the wintertime?

While the tanker industry usually finds a way to keep the oil flowing, despite the best efforts of sanctioning authorities, it seems that a meaningful reduction in Russian exports is in the cards (at least temporary). Will this put downward pressure on tanker rates? It is possible, but one could also argue that increased inefficiencies, more delays and heightened uncertainty will do the opposite.