THE LOADSTAR

LongRead

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Project Cargo

Project cargo rides on the success of the oil and gas sector; without it, the project operators starve. Certainly, there are growing opportunities in the renewables sector and these should not be, and nor are they, sniffed at. But after three years of weak oil prices, project cargo has been left a little emaciated.

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Fortunately, the "sideways slide" appears to be moving upwards once more. Oil prices have recently hit their highest level in three years. Consultancy Rystad Energy noted in its latest Oil Service Report its expectations that this boom in crude prices was likely to propel the greenlighting of 100 new offshore projects, globally, by the end of 2018.

"The offshore suppliers have created their own comeback," says Audun Martinsen, VP of Oilfield Service Research at Rystad Energy. "Their constant search for cost reductions and streamlining of operations has enabled them to cut offshore project costs by almost 50% compared with the heights of the last cycle."

Rystad claims offshore suppliers had reduced the prices they charge by as much as 30% compared with what they were quoting back in 2014. This plummeting price is linked to a seismic drop in offshore drilling contractor day rates – down between 50% and 70% in the same period.

"Not only are the suppliers charging less for their services, they have also improved the efficiencies of their operations, thus shortening lead times from project sanctioning to first oil," says Martinsen.

"As an example, the time required to drill and complete a well has fallen by 30% in the North Sea, the Gulf of Mexico and Brazil over the past four years."

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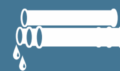
Volga Dnepr

At the heart of **unique logistics.**



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This is one of the positive, underlying trends that senior analyst for multipurpose and breakbulk shipping at Drewry, Susan Oatway, has seen. While some of these projects, such as the offshore Libra Field in Brazil may grab the headlines – it is expected to cost some $91bn and produce up to 12bn barrels of crude – it helps that the predicted surge in project confirmations covers a good geographical spread.

About 30 are expected across Asia, including the Pegaga field in Malaysia – which is expected to be developed at a relative snip at just $1bn – while Rystad expects 30 in Europe and 20 in Africa and the Americas each.

"Companies have more free cash flow at hand in 2018 than they did during the recent peak years of 2008 and 2011," Martinsen continues.

"In fact, 60% of the companies looking to finance their project development costs can do so through their cash flow. Supported by strong oil prices, we see a very small risk of these projects not materialising."

Commercial manager of Antonov Airlines Martin Griffiths says that despite a supposed weakness in the sector, energy was one of the carrier's strongest in 2017. It accounts for some 11% of Antonov's total output, he says.

"We saw a record 139% increase in freight tonne km (FTK) of energy cargo carried, which also included four flights from Slovenia to Mexico providing more than 60 megawatts of power," Griffiths continues. "As well as 41 flights from the US to Puerto Rico, with over 80% of cargo carried being energy related."

Oatway also sees benefits arising from the renewable sector. She goes so far as to say that they have provided a steady source of income throughout weak oil times. In recent years project operators have seen the traditional oil region of Saudi Arabia join the likes of Egypt as a "renewables hotspot".

At the start of the year, *Bloomberg* quoted the head of Saudi's renewable energy project development office, Turki Mohammed Al Shehri, stating that as much as $7bn would be spent on domestic renewable energy projects over the course of 2018. Solar, he said, would be the leading light.

By the end of 2023, Saudi Arabia wants 9.5 gigawatts of solar and wind capacity installed. Why is an oil-rich country doing this? According to *Bloomberg*, it is to feed domestic consumption, freeing up greater quantities of crude to export.

Oil and gas company Mubadala Petroleum hired Sapura Energy to deliver a platform for the Pegaga gas field development offshore Malaysia

"We are continuing to see growth in the number of renewable energy projects being undertaken," Oatway continues. "Importantly, though, we have also seen some improvement in the oil and gas markets. This pick up has come in the last 12 months, or so, although it's worth cautioning that the market remains very slow – with growth mainly driven by improving oil prices.

'Recovery and stabilisation of the oil and gas market has increased demand for equipment, and Volga-Dnepr has performed more than 100 deliveries of oil and gas equipment'

Robert van de Weg, vice-president for sales and marketing, Volga-Dnepr Group

To these words of caution, Oatway also adds that as a sector, project is "very difficult" to assess on a short-term basis. Particularly as it is a market that loves a good lead time. In general, project lead times can be anything from 12-18 months. Which means operators know that they have the work lined up – but first they have to get through a year of prep.

Chief executive of Agility Project Logistics Grant Wattman – who described the industry in recent years as "sideways sliding" – believes the activation of Final Investment Decisions and Notices to Proceed has been pivotal in bolstering optimism.

"It is expected there will be major projects awarded this year, which bodes well for 2019," says Wattman. "Going forward, though, there are challenges to be faced, namely talent resourcing that has thinned as a result of the downturn over the last couple of years."

Agility has focused on developing innovative customer solutions and, as a result, it has managed to win business and grow market share in capital projects, oil and gas, and marine services.

"Our most active projects are in LNG and petrochemical projects, conversion of existing facilities for lower cost gas inputs, and upgrading processing equipment for higher grade and quality outputs," he continues.

"These projects are taking place primarily in North America and the Middle East. We anticipate an uptick in the mining sector, which has been one of the sectors performing worse than the oil and gas sector over the past couple of years."

Robert van de Weg, Volga-Dnepr group's vice president for sales and marketing, tells *The Loadstar* that from 2017 onwards, the Russian airline has "witnessed persistent demand" from the project sector.

"This demand has come from among such industries as aerospace, oil and gas, and energy, with Volga-Dnepr continuing its operations under long-term partnerships with existing customers and responding proactively to urgent requests.

"Recovery and stabilisation of the oil

and gas market has increased demand for equipment and Volga-Dnepr has performed more than 100 deliveries of oil and gas equipment including transportations in Russia and to the Middle East sites."

Likewise, manager of products at Cargolux Eric Reisch says its "core offering" has been "pretty well" received by both its customers and the wider industry. According to Reisch, the carrier's tailored services and solutions have seen a "particularly consistent" upturn in popularity.

"They have performed extremely well," he says. "For the project cargo sector, we are looking to consistently deliver the same type of air cargo expertise while heavily relying on our shoring and engineering specialists' contribution for optimal planning and guidance."

Over the course of 2017, Reisch says Cargolux (CV) witnessed near-20% growth in demand for outsized and heavy shipments. He cited the carrier's own internal initiatives as the fuel behind this "unprecedented" performance.

But he also credited a "strong overall market", which the carrier has been experiencing since the closing days of 2016. "Our specialised products, CV Jumbo and CV Power, generate around 9% of CV's overall volumes," he continues.

"It was a busy and challenging year for everyone, but all divisions stood strong together, found their rhythm early in the year and met all the expectations, which paid off in the peak season."

Industry feels powerless in tit-for-tat trade spat

Photo: © Florin Seitan | Dreamstime.com

Supply chain concerns hit the oil and gas industry in mid-June when the US announced the imposition of $50bn of tariffs on Chinese goods. This followed an earlier imposition of 25% tariffs on steel imports from not only China, but also Canada, Mexico and the European Union.

Trade attorney at Bracewell, Josh Zive, told S&P Platts that the earlier set of tariffs were bad news for any sector heavily dependent on steel.

With reports of new offshore sites expected, the need for steel could not have been greater for oil and gas. And some companies are already reporting not only prices rises, but longer lead times in accessing steel.

Zive said he found it difficult to perceive any scenario in which costs and lead times did not increase at an accelerated pace, now that tariffs had been expanded to additional trading partners.

Ed Longanecker, president of the Texas Independent Producers and Royalty Association – which represents the state's oil industry – issued his own rebuke of the move, in which he said he was extremely disappointed by the imposition of tariffs.

"This decision will cause slowdown in exploration and production activity for an industry that is still in recovery mode, which will result in job loss, decreased production and related tax revenue that supports all levels of our economy," he said in a statement.

"This is a net loss for the United States with repercussions that will only build over time."

Cargolux's manager of products, Eric Reisch tells *The Loadstar* that the airline has been monitoring the political developments coming out of Washington, as well as the response from the wider international community.

"Although we can't do much to influence these decisions and/or threats, we must ensure compliance is adhered to at all times," he says. "In the event trade war threats develop, the impact would of course not be limited to the project sector, but affect many others."

Project cargo manager at Maurice Ward Europe, Bogdan Dima, feels powerless: "There will always be 'government attitudes' that will impact all the sectors – not only ours as project forwarders – but we cannot control these factors, as they are 'untouchable'."

With Texas the home of US oil and gas, Longanecker adds that he is expecting a "significant increase" in the cost of materials used for both exploration and production.

"Our members, who are responsible for producing more than 85% of the oil and natural gas within Texas, and thousands of additional operators and service-oriented companies in the state, would bear an inordinate financial burden," he notes. "[This] will reverberate throughout the state and country."

Vice president of sales and marketing at Volga-Dnepr Robert van de Weg warns that protectionism "will not be a good thing for global trade".

Ripples from a wave of consolidation

A wave of consolidation has swept across the logistics industry – in fact across industry in general.

But these changes can often prove negative for customers who find themselves left with just a few parties dominating an industry, and therefore pricing.

In the past 12 months, a ripple from that wave graced the bow of the project sector. Several core players saw themselves under new management. Perhaps the biggest of these came when German-headquartered Zeaborn Group announced it had acquired the breakbulk side of the sinking Rickmers operation.

For the emotional, the salvage of at least some of Rickmers was a blessing. The move came almost 150 years after the launch of the carrier's first sailing vessel.

From Zeaborn's side, the move saw its multipurpose vessel (MPV) fleet expand to 50 as it took control of the 15 Rickmers MPVs. It now offers capacities ranging from 7,500 to 30,000 tonnes.

Chief executive of Agility Project Logistics Grant Wattman echoes a familiar line: that consolidation is not good for the industry. He says its main effect is that it limits options for customers. But he recognises that for some carriers it has been important.

"It has been a necessary step by the industry because profitability has been impacted," says Wattman. "We are seeing consolidation in the engineering contractor community as well. We anticipate this to continue in both the carrier and service sectors."

Business development manager of Mexican forwarder Multitraslados Alexa Iruegas says the consolidation so far experienced in shipping has led to an "inevitable" increase in project rates. Even so, this was expected, and Iruegas and his team have sought to offset the effects.

"We've worked on route forecast and consolidation since last year, as we had meetings with our preferred shipping lines to know how Mexico's overseas routes would be affected by it," he says.

"So, we had time to prepare and find a different carrier for our top tradelanes. The rates were indeed

Photo: © Designer491 | Dreamstime.com

affected and it's something we have been working on with our customers."

Despite the changes Iruegas has seen, this is not a picture shared by the senior analyst for multipurpose and breakbulk

> **'I'm not sure why they're not consolidating fleets, though. Economically, you'd think the older vessels must be worth much more in scrap than operating'**
>
> **Drewry analyst Susan Otway**

shipping at Drewry, Susan Oatway. She believes that, unlike rate hikes that have been seen in other consolidated sectors, they do not seem to have followed in project cargo.

This, she says, is because unlike in container shipping, consolidation has not limited fleet supply. In fact, she says, in project cargo it seems to have spurred carriers to build more ships. A point that was brought sharply into focus with the announcement that Zeaborn and Intermarine had formed a joint-venture, Zeamarine.

Under the JV, fleets, staff, customers and offices will be consolidated. But the number of vessels in the fleet is set to rise from 75 to 100 by the end of the year.

Managing partner of Zeaborn – which will be the majority shareholder – Ove Meyer says each "respective entity" brings its own "unique" value to the partnership.

He adds that Zeaborn is particularly interested in Intermarine's strong US and South American presence in the project sector. But is bringing more vessels onto the water a wise idea?

"The issue is that consolidation within project cargo has at no point improved the fleet supply front," says Oatway. "Some operators have even used it as an excuse to build more ships. The effect of this on cost is more linked to levels of competition and demand.

"Due to the fragmented nature of the market, the competition is so fierce, which is what is keeping the rates so low. When you look at the small fleet and reasonable demand, it should be good for the carriers. But it is the competition that's affecting prices – keeping rates low – as opposed to consolidation bumping prices up."

When you have the same number of ships, prices won't be pushed up. Oatway says this has been an interesting aspect of the project consolidation. The companies doing the

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buying are either going for a formal takeover or forming a joint-venture.

"But they are not consolidating the fleet," she continues. "It is all much more fragmented than what we have seen on the container side. There are around 20 major operators in MPV operations, and the top 10 [based on Drewry ratings] control less than 30% of [deadweight] tonnage.

"I'm not sure why they're not consolidating fleets, though. Economically, you'd think the older vessels must be worth much more in scrap than operating. The owners are saying they are running on fumes, but this clearly isn't the case as they'd have scrapped them."

Of course, not all operators are running old ships. Intermarine, for one, has a relatively modern fleet, so scrapping ships would be a financial nonsense. And on the smaller operator side, they often run small trades, which can make use of older vessels. Even so, Oatway notes, changes in legislation will probably have some impact.

"When the sulphur cap comes in [in 2020] you'll see more scrapping as the financial viability fades," she predicts. "Also, demolition prices for these ships have fallen over the past five years along with the market, so we have to get a bit further down the line to make it worth it."

'Consolidation bolsters the available options for forwarders and shippers'

Keyur Gandhi
Express Global director

Project cargo unit manager of Maurice Ward Europe Bogdan Dima believes the purpose of mergers between carriers is not only to reduce their costs, but to improve the footprint offered.

"I don't see any big issue on that as all the mergers between carries are done in order to reduce their costs and to cover more areas than were previously available to customers," says Dima. "From our side, we see this as a 'one-stop shop' movement in respect of controlling the vendors."

Dima's comments mirror those of Express Global's director, Keyur Gandhi, who sees nothing but benefit from consolidation. He says it bolsters the available options for forwarders and shippers.

"This in turn does affect the profit margins," Gandhi adds, "but at the same time, we are seeing many container carriers enhancing their capabilities to carry breakbulk cargo on their containerships. This increases the options of ships for certain categories of cargo."

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