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Shipping confidence up on expectation of rate increases but new investment appetite wanes

Overall confidence levels in the shipping industry increased slightly in the three months ended February 2012, to reach their highest level since May 2011, according to the latest Shipping Confidence Survey from international accountant and shipping adviser Moore Stephens. This is the third successive quarter in which there has been a small uptick in confidence. Rates are expected to increase over the coming year in the three main tonnage sectors covered by the survey. But the number of respondents expecting to make a major new investment over the next twelve months fell to its lowest figure for three years, despite a fall in the number of those anticipating an increase in finance costs.

In February 2012, the average confidence level expressed by respondents in the markets in which they operate was 5.5 on a scale of 1 (low) to 10 (high). This is marginally up on the figure of 5.4 recorded in the previous survey in November 2011. It compares to the 5.8 recorded one year previously, in February 2011, and to the 5.9 figure posted in February 2010. The survey was launched in May 2008 with a confidence rating of 6.8.

Confidence was up among owners (rising from 5.3 last time to 5.6), charterers (4.9 to 5.0) and brokers (5.2 to 5.6). But managers (down from 5.6 to 5.2) were alone among all respondents in being less confident about the market this time, having been the most optimistic in the previous survey. Confidence was up in Europe, from 5.1 to 5.3, although the region remained the least optimistic of all geographic sectors covered by the survey. Meanwhile, confidence was down in Asia, from 5.8 to 5.7, and in both North America and Latin America (from 5.8 to 5.6 and from 6.4 to 5.7 respectively).

Although confidence levels improved marginally over the three-month period covered by the survey, a number of respondents expressed concern about the current state of the industry. “There are too many ships,” said one. “Freight levels cannot go much lower and we will be bumping along the bottom for a while. Apart from owners causing their own malaise by over-ordering ships, structural changes - such as China subsidising its own maritime industry - will keep a lid on developments in certain sectors.”

A number of respondents counselled patience. “Some market sectors are very depressed,” said one, “but a re-balancing is already under way. We have to be patient. It will be at least three-to-five years until margins become reasonable.”

A number of respondents, however, saw reasons for greater optimism. “We firmly believe that the markets will pick up over the next twelve months, although the gains will be quite low,” said one, while another insisted, “We think fourth-quarter 2012 will signal a turning-point for the industry.”

The role of the banks was uppermost in the minds of a number of respondents. One emphasised, "Numerous owners are unable to make their mortgage payments, and a large majority will be unable to keep up just the interest payments. The banks may be ready to announce further rounds of write-offs to avoid tax and to please the markets. It's only a matter of time before more shipowners are drawn into the firing line. We are seeing operators dropping out of the market or vessels being handed over or taken back due to non-payment of hire. The margins have gone for speculators, and charterers can now be very selective and are driving rates down. It is amazing that we haven't seen more established names affected already. Owners are managing to keep the banks at bay with the book value of ship assets, but if the assets were written down to true market values then we would see another story."

In common with previous surveys, a high percentage of respondents expressed concern about overtonnaging. One remarked, "It is unbelievable that some owners are still ordering new ships, given the current economic problems and the general perception that rates will remain low when the vessels now on order eventually enter service."

Predictably, political and economic factors – and their likely impact on the industry - continued to occupy the thoughts of respondents. One felt that, "The upcoming US elections in November will act as a catalyst in allowing new money to flow into the system," while another said, "The continued inability of western governments to either control their spending or exit the euro makes bad times more likely."

The overall number of respondents expecting to make a major investment or significant development over the next twelve months fell, on a scale of 1 to 10, from 5.2 to 4.9, the lowest figure since the 4.8 recorded in February 2009. All categories of respondent were less confident than in the previous survey, most notably charterers, whose expectation rating in respect of major investments was down from 5.8 to 4.9, the lowest figure recorded by this category of respondent since the 4.8 returned in May 2008. This reverses a trend whereby charterers had emerged over the life of the survey as the category of respondent most confident of making a major investment. This time, the rating for owners was down from 5.5 to 5.2 and, for managers, from 5.4 to 5.2. Over the life of the survey, the highest overall expectation rating is the 6.0 recorded in August 2010.

Expectations of major investments were down in all geographic areas covered by the survey. In Asia, the fall was from 5.2 to 5.0 (the lowest figure since November 2009), while in Europe it was from 5.1 to 4.8, the lowest figure for that region for three years and equal to its lowest rating in the life of the survey. The figures for Latin America (6.6 to 5.2) and North America (5.1 to 5.0) were also down.

Demand trends, competition and finance costs continue to dominate the top three factors cited by respondents overall as those likely to influence performance most significantly over the coming twelve months. Overall, 22% of respondents (down from 24% last time) cited demands trends as the most significant performance-affecting factor, with 20% (up from 17% last time) identifying competition. Finance costs (unchanged at 17%) featured in third place, followed by fuel costs (up 3 percentage points to 12%).

Fuel costs were in fact the second most significant factor for charterers, despite being cited by fewer respondents in this category (23%) than last time (26%). Demand trends (unchanged at 24 cent) was the leading performance-influencing factor for charterers, with competition - up significantly from 15% to 23% - in third place.

Although demand trends remained the number one performance-affecting factor for owners, it was cited by only 21% of such respondents, as opposed to 26% last time. Finance costs (up one percentage point to 18%) were in second place, followed by competition, at 17%. For managers, meanwhile, competition and demand trends (both up 2 percentage points on last time to 19%) occupied the top two places, with finance costs in third place at 16%.

Geographically, demand trends remained the most significant factor for respondents in Asia and Europe (both 22%, compared to 18% and 26%, respectively, in November 2011). In Asia, competition assumed increasing importance for respondents (up from 17% last time to 21%), with finance costs in third place at 15%. In Europe, competition (up 2 percentage points to 18%) shared second place with finance costs, down from 19% last time. In North America, meanwhile, demand trends (up from 25% to 28%) pushed competition (down from 26% to 25%) into second place, with finance costs in third place with 15%.

There was an 8 percentage-point drop (from 57% to 49%) in the number of respondents overall who expected finance costs to increase over the next twelve months – the lowest figure since November 2010. There was also a 2 percentage-point increase, from 6 to 8%, in the number of respondents who thought that finance costs would come down during the coming year – still some way short of the 25% who thought likewise three years ago, in February 2009. The numbers of owners and managers expecting finance costs to rise was down (from 57% to 46%, and from 56% to 45%, respectively), but 48% of charterers were expecting increases as opposed to 46% last time.

Fewer respondents in both Asia and Europe were anticipating an increase in finance costs compared to last time (down from 54% to 49% and from 61% to 48%, respectively). The same was true of North America (down from 47% to 38%).

According to one respondent, “Never before have we been confronted with a situation where the banks appear not to understand the industry, seemingly preferring statistics above a clear understanding of the business. If they stopped providing billions of dollars for even more unnecessary fleet expansions on the part of certain companies, the financing of other small, medium-size and niche operators would be assured.”

The survey revealed that respondents are now more confident of rate increases than they were three months previously. In the tanker sector, the number of respondents expecting rates to increase over the coming year was up from 30% to 35%. Charterers were alone in recording a fall (from 40% to 35%) in expectation of higher rates, against an 8 percentage-point increase, to 15%, in their numbers who thought that tanker rates would fall.

In the dry bulk sector, meanwhile, all the indicators pointed upward. There was a 15 percentage-point increase, from the all-time survey low of 23% to a more optimistic 38%, in the overall number of respondents who thought that dry bulk rates would rise over the next twelve months. Even charterers were looking up rather than down, with 44% of their number (the highest since August 2010) anticipating higher rates, as opposed to just 33% in the previous survey. In August 2011, jut 8% of charterers expected dry bulk rates to increase. The number of owners anticipating higher bulk rates, meanwhile, was up from 20% (another all-time low) to 35%, while 38% of managers thought that rates were on the way up, as opposed to 31% last time.

In the container ship market, 31% of respondents overall expected rates to increase over the next twelve months, as opposed to 23% last time. Charterers led the way, with a 13 percentage-point increase to 26%, which nevertheless still left them trailing managers (up from 23% to 30%), and owners, up 5 percentage-points to 28%. All these figures, however, were well down on those for one year ago. In February 2011, 56% of owners, 47% of managers, and 40% of charterers said they thought containers ship rates were likely to increase.

Moore Stephens shipping partner, Richard Greiner, says, "Nobody could accuse the shipping industry of being faint-hearted. Despite public confirmation that an increasing number of big industry names are in financial difficulty; despite there being too many ships to carry the cargo available to them for the foreseeable future; despite the prohibitive cost of fuel; and despite an ailing world economy, confidence in the shipping industry still increased slightly over the past three months. In fact, confidence today is higher than it was three years ago, in February 2009.

"Confidence is contagious, as is the lack of it. Although confidence in the shipping industry is significantly down compared to what it was when we launched our survey in May 2008, it is still holding up better than many had predicted. In part, that is due to a belief in the product and the service on offer. Shipping people know their industry. Although it is possible to carry anything from pins to elephants by other means of transportation, ships remain the only viable option for an overwhelming amount of the cargo that has to be carried on global routes. So, even if the supply-demand equation is currently out of kilter, there is both a need and a demand for shipping, and that is ultimately good for confidence.

"Almost without exception, owners, managers, charterers and brokers expect rates to go up over the coming twelve months, albeit starting from a chronically low base point. Improving rates may be too late for some, but could be the saviour of others as they seek to demonstrate to the banks and other investors that there is a genuine prospect of more money coming in.

"Shipping is not the only industry which has lost some of its household names. There may be more casualties to come. But higher rates are what is needed, particularly in an industry which, historically, has been accused of under-selling itself. Respondents to our survey this time exhibited a reduced appetite for finding money to spend on new investments over the coming year, but that may change if there is more money to spend – particularly if the cost of borrowing comes down.

"Meanwhile, there have been encouraging signs in the past couple of months in connection with efforts to address the worldwide economic downturn. Europe's plan for bailing out Greece may be more of a short-term palliative than a long-term solution, and there remain serious doubts about other euro economies such as those of Italy, Portugal and Spain. But it is a start, and one that coincides with indications that the beginnings of a recovery may be under way in the US economy.

"Shipping has a long way to go before it returns to the rude health which made it such an attractive investment opportunity for so many just a few years ago. Given the way that environmental and safety regulations are driving up the cost of operating in today's industry, it is unlikely to attract, for the foreseeable future, those looking to make a quick killing before exiting the market. They will not be missed. Shipping prides itself on its competitiveness, but the last thing it needs at the moment is more transient competition.

"Sometimes, the circulation of confidence is better than the circulation of money. The shipping industry is managing to maintain the former, but will need more of the latter in order to take the next step towards recovery."

● The Moore Stephens Shipping Confidence Survey includes responses from key players worldwide in the international shipping industry to a targeted, web-based survey by the Moore Stephens Shipping Industry Group. Responses were received from owners, charterers, brokers, advisers, managers and others. Editors can apply for a copy of the survey by emailing chris@merlinco.com

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