Baltic Dry Bulk Investor Indices

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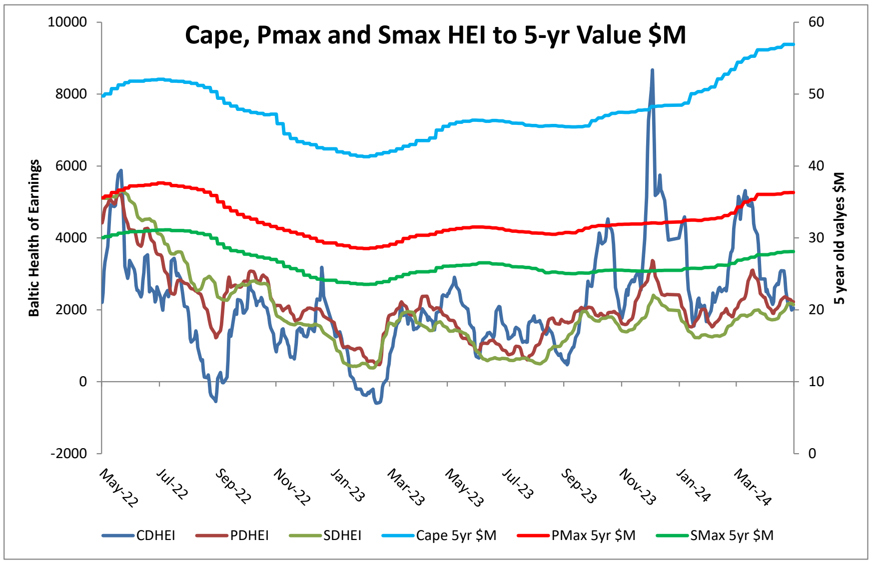
The Dry Bulk Good Times, on Hold or Holding-on?

There is the old adage: "The two happiest days in a yacht-owner's life are the day the yacht has been purchased and the day it has been sold". This saying is also applicable to dry bulk ship owners. In between those two happiest of days of dry bulk shipowning are the highs, lows and mediocrities of the market, with mediocrities being the most prevalent of conditions in recent months. Since the introduction of the Baltic Investor Indices, and generally for the last 24 months, dry bulk ship asset values have been relatively stable (on average across sectors) yet freight rates have only offered a few whimpers of support for the asset values and in some cases have been pretty mute.

With the dry bulk orderbook remaining historically low, asset values have remained relatively firm. Shipowners with healthy balance sheets are patiently "on-hold" and looking to buy dry bulk assets in recent months. Those with weaker balance sheets are "holding-on" as long as possible with the clear hope that the dry bulk market will firm as demand growth exceeds supply growth in the coming years, or so it is hoped.

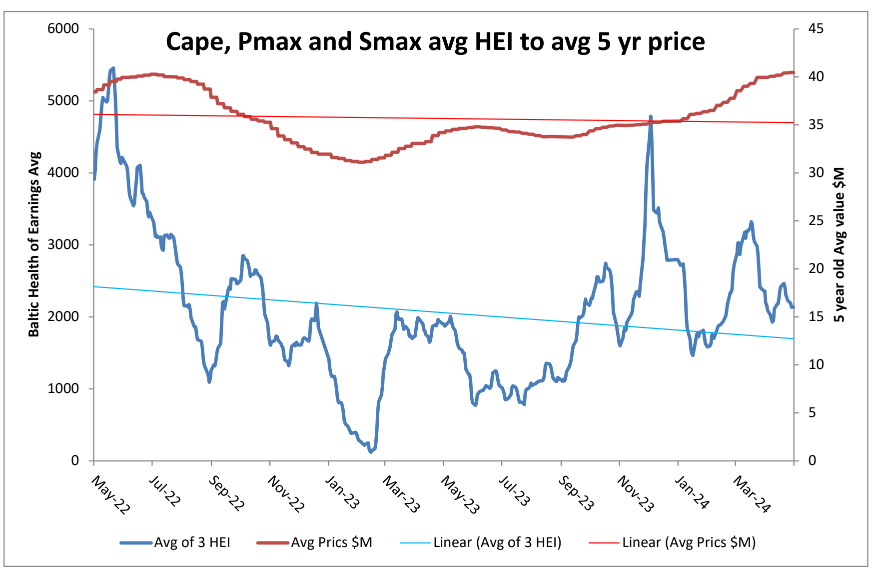
Over two years, health of earnings keeping asset values in check…

The Baltic Exchange produces a Health of Earnings Index (HEI) for each of the four major dry bulk ship types. HEI shows the ratio of earnings against cost, with a negative result indicating that earnings are below operating costs In addition, the Baltic Exchanges publishes estimated five-year-old asset values. We look here at the Capesize, Panamax and Supramax HEI to five-year-old asset values over time.

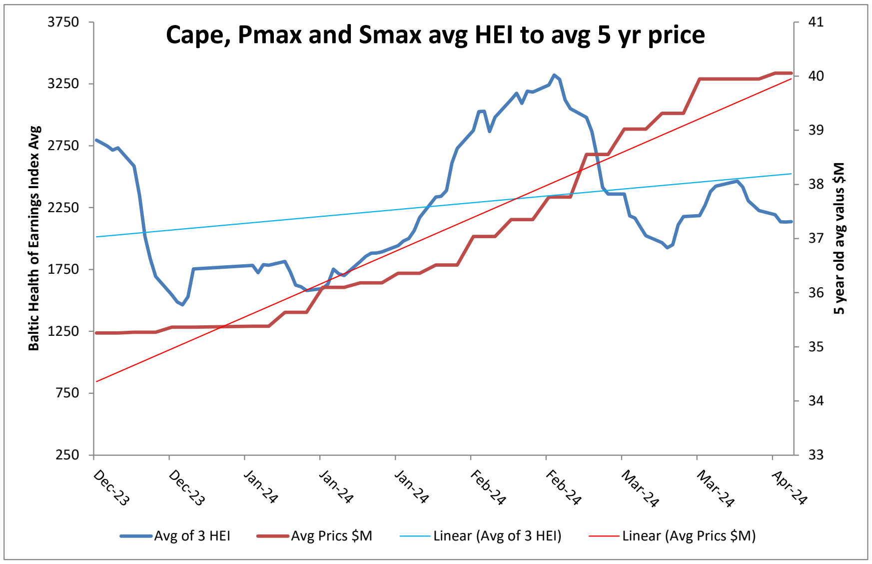


We believe that the above graphic does not tell the investor much. For the most part, over the last two years, earnings have been uninspiring while asset values have trended up of late. In the above, as one might expect due to the size and trades of the vessels, the Supramax asset values are the most correlated to HIE at 0.83x and Capesize the least correlated at 0.48x.

When we zoom out and look at the industry from "thirty-thousand feet", the investor can glean more information. We took the liberty to take the average of the Capesize, Panamax and Supramax HEI and compare that average to the average Capesize, Panamax and Supramax five-year-old asset value over the last two years. HEI has been trending softer, while five-year old asset values were basically stable over the period. This means that had an investor bought a five-year old dry bulk asset in May 2022, the results were largely uninspiring.



Despite the uninspiring results over two years as noted above, when we look at this broad average result over the last six months, the picture is quite different. Over the last six months, average asset values have been steadily increasing. Freight rates have fared better as well, but have been outpaced by increasing asset values. The correlation between asset values and HEI has been negative overall and a remarkable -0.29x for Capesize bulkers.



Dry Bulk Supply/Demand, on balance, is attractive.

Over the last six months, it has been good to be an owner of dry bulk assets generally and the larger ship types in particular. The Capesize orderbook, for example, is at just 6.2% of the fleet, which is nearly at the 25-year-low seen in July 2023 according to Clarksons. The overall dry bulk fleet orderbook is at 9.3%, which is above the 7.2% 25-year-low seen in February 2021, but still historically low. Meanwhile, the dry bulk orderbook has been under 10% of the fleet for over four years since early 2020, the longest streak below 10% since 1996.

The current spot cape market is about $22,100/day. The near-term Capesize FFA market for the remainder of the available periods for 2024 are approximately $30,000/day. We understand the FFA market is not necessarily the best way to predict the market, but it is, indeed, a market. Cape FFA's for June 2024 are at $30,125 (Braemar, 2 May 2024).

Capes are not the entire market but they are a segment that creates market gravity for the other segments. In our experience, when Capesize freight rates rise, it helps other segments. Iron ore, coal and grains are the three largest dry bulk cargo types. Most iron ore is carried on Capesize bulkers and China is, by far, the single largest importer. Over the first quarter of 2024, Chinese iron ore inventories rose, as is seasonally typical, but not to record highs. In addition, during the first quarter of 2024, Chinese iron ore prices dropped and inventory at Chinese steel mills dropped to a four-year low (Arrow Research) as mills await even lower prices. Chinese data is notoriously opaque, slow and we all await fresh data. However, possibly in anticipation of Chinese steel mills taking advantage of low priced iron ore, Capesize rates today are improving slowly and the FFA market is indicating an improving market.

Finally, the S&P Global Manufacturing PMI (sponsored by JP Morgan) was at 50.4 in April (a number above 50 indicates an expanding global economy while below five means a contracting global economy). Inclusive of China, this was the third straight month of expansion coming off of a 20-month high of 50.6 in March.

On balance, therefore, the fact that asset values are increasing ahead of freight rates over the last six months, should not be a surprise.