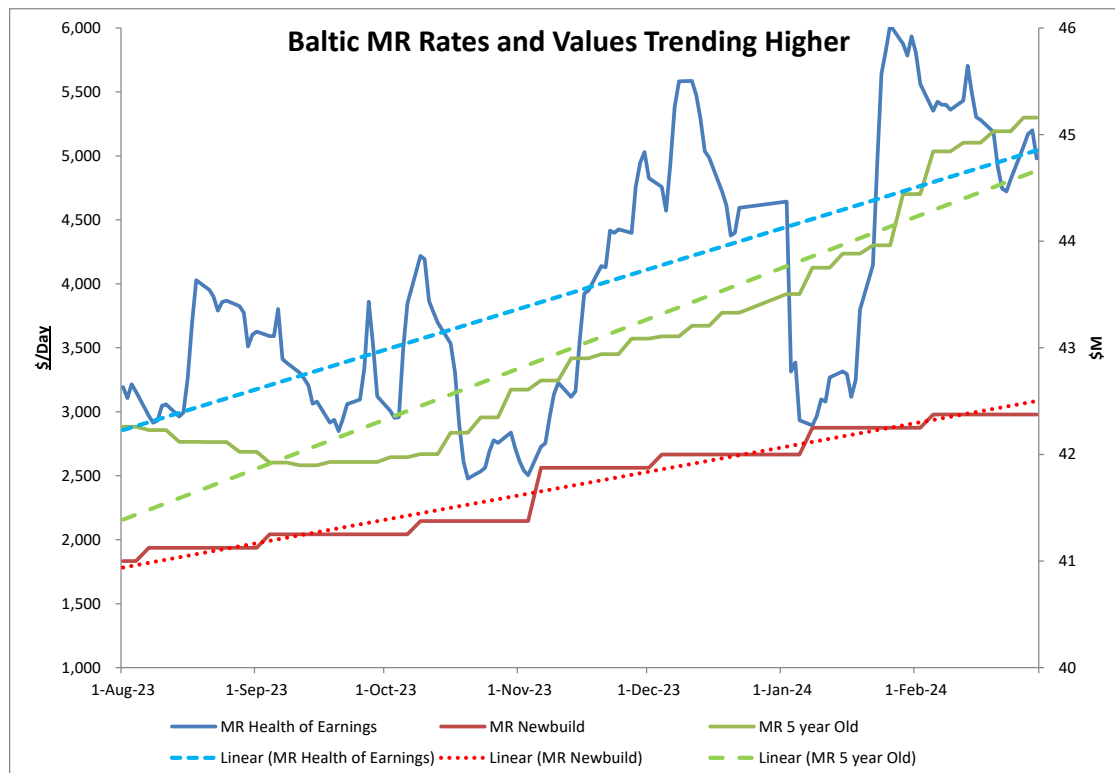


Baltic Tanker Investor Indices

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With MR Earnings Trending Firmly, Buy Secondhand or Order Newbuild?

Baltic Exchange Investor Indices (BII) have indicated an improving health of earnings trend for MR tankers since the middle of last year. In turn, asset values for MR tanker newbuilds and five-year old second-hand vessels have also trended steadily higher. With MR demand dynamics looking firm and fleet growth expected to be modest over the next 24 months, five-year old MR prices are, as measured by the BII, above those of newbuild order prices. Hence, what offers the better value: buying a second-hand tanker or ordering a newbuild? Well, it depends on several factors.



Buying second hand MR today; risks and rewards.

While it is not uncommon for second-hand “resale” (prompt newbuild) ship values to exceed newbuild order pricing, it is less common to see five-year old vessel values exceed newbuild order prices, as is the case today for MR tankers. Obviously, this is caused by the sustained health of the MR tanker markets over recent years, relative to the availability of MR second-hand tonnage.

Over the last 12 months, the Baltic MR implied spot timecharter earnings (MTTCEA) has averaged \$30,604. Currently, the Baltic MR tanker five-year-old value is about \$45.2 million.

Buying at that level and leveraging at 65%, we estimate that the cash breakeven for this five-year-old MR tanker is roughly \$19,600/day.¹ Given the favourable supply/demand outlook and that freight rates may meet or exceed the average seen over the last year for some time, this five-year old value appears justified. That said, the required breakeven is historically firm in our view and finding available high quality second-hand tonnage that is competitive amid tightening global emissions requirements is challenging. Still, from this simple perspective, if an investor can find it, the investor should buy it ... or should they?

Is ordering an MR more attractive than buying a second hand five year old?

As of the end of 2023, the Baltic MR newbuilding price is about \$42.4 million as compared to the five-year old price of roughly \$45.2 million. Naturally, this price difference has some attractions and risks.

With the newbuild order, the investor will have to wait, we assume, about 2.5 years for delivery. Also, while the supply/demand fundamentals are attractive, newbuild ordering has increased in recent months and predicting product tanker markets 30 months in the future is - beyond looking at the supply-side - guesswork at best and treacherous in general.

On the other hand, a newbuild may get a longer loan profile (about 20 years), so ordering an MR at roughly \$42.4 million implies an estimated cash breakeven of \$17,600/day², nearly \$2,000/day lower than the estimated cash breakeven noted above of a second-hand five-year old purchased and levered today. The lower breakeven is more modest risk as compared to historical freight markets, despite the need to wait 2.5 years.

Furthermore, given the strength in MR supply/demand fundamentals, ordering an MR tanker now means having a relatively early newbuild yard slot relative to the fundamentals. As such, the value of that order may well rise markedly over the build period. While novation of order contracts is not that common, it does happen. In addition, we estimate the price of a resale prompt newbuild MR today at

¹ Assumes purchase price of \$45.2 million, levered at 65%, 15-year loan profile, 8.75% interest, OPEX and G&A of about \$7,400 day.

² Assumes order price of \$42.2 million, levered at 65%, 20-year loan profile, 8.75% interest, OPEX and G&A of about \$7,400 day

about \$53 million, so the possibility of booking a solid gain on a newbuild order today upon its delivery towards the end of 2026 appears attractive.

The attractive technology advantages of a newbuild order today are also an important consideration. Ordering top specification vessels today offers lower risk/exposure to the ever tightening global emissions regimes and top charterers favour modern vessels.

Finally - and depreciation bores most people, we know - today's newbuild order at about \$42.4 million will have a five-year-old book value of an estimated \$32.7 million and \$23.1 million at 10 years of age. The five-year old second-hand MR tanker purchased today at about \$45.2 million will have a book value on her 10th anniversary of \$31.4 million. From a simple book "cost-to-replacement" perspective and the possibility of equity building profits, the newbuild order is more attractive than a second-hand vessel today.

In the end, the choice is simple: do both.

The core element not considered above is the investor's duration horizon against the risks. If the object is to make money in the near term, it still makes sense to buy a five-year-old MR tanker (if one can find one). However the price/risk dynamics, the technological advantages with the attractive supply/demand fundamentals indicates ordering an MR today makes sense if the investor holds a longer view.

All of the above is very broad-brush and there are variables likely not considered here. However, when five-year-old ship prices exceed newbuild prices, it is worth some *caveat emptor*, and worth considering the newbuild order.