Baltic Dry Bulk Investor Indices

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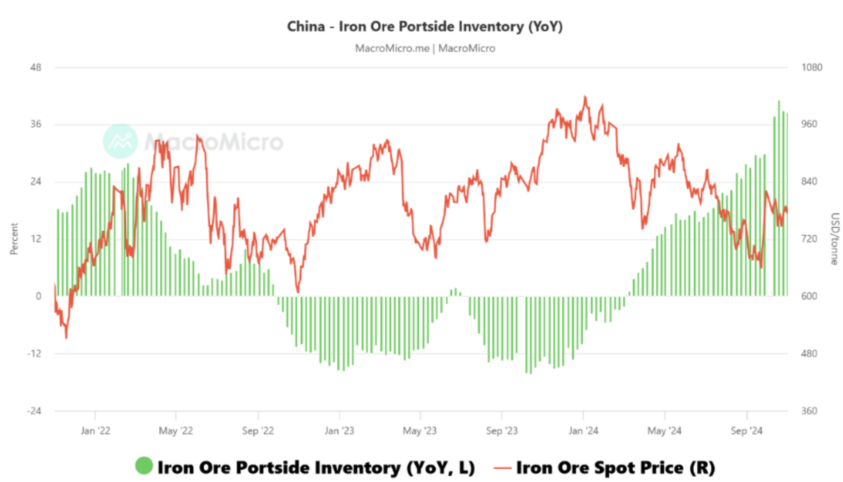
Dry Bulk: Without Better Demand, Asset Values Should Soften

From the beginning of September to the beginning of November, Capesize freight rates were down over 40%, only to recover in the last 10 days to $about $20,000/day, while Panamax rates remain low and cannot seem to get out of the doldrums. In the meantime, asset values as measured by Baltic Exchange have remained firm overall.

There are reasons that asset values have been firm (low orderbook, input cost inflation, changing emissions standards, evolving propulsion standards), yet all of these factors are supply side and very tangible. The outlook for dry bulk demand is more opaque and difficult to forecast.

There appears to be fundamental pressure on freight rates for the time being. Demand for seaborn iron ore and coal was firm for much of the year but both have faltered as of late as inventories have stockpiled on softer than anticipated demand. For example, China's portside iron ore inventory is at its highest since 2002 and, at about 154 million tonnes, are near a historic high. Furthermore, China's iron ore inventories at its ports are up 40% year-on-year.[1] This is a near-term damper on Capesize freight rates as we head toward Chinese New Year in February 2025. The outlook for the other major dry bulk goods is also modest. For 2025, Clarksons Research anticipates a 1% decline in seaborne demand for the major dry bulk commodities while they estimate the dry bulk shipping fleet to grow by 2.9%.

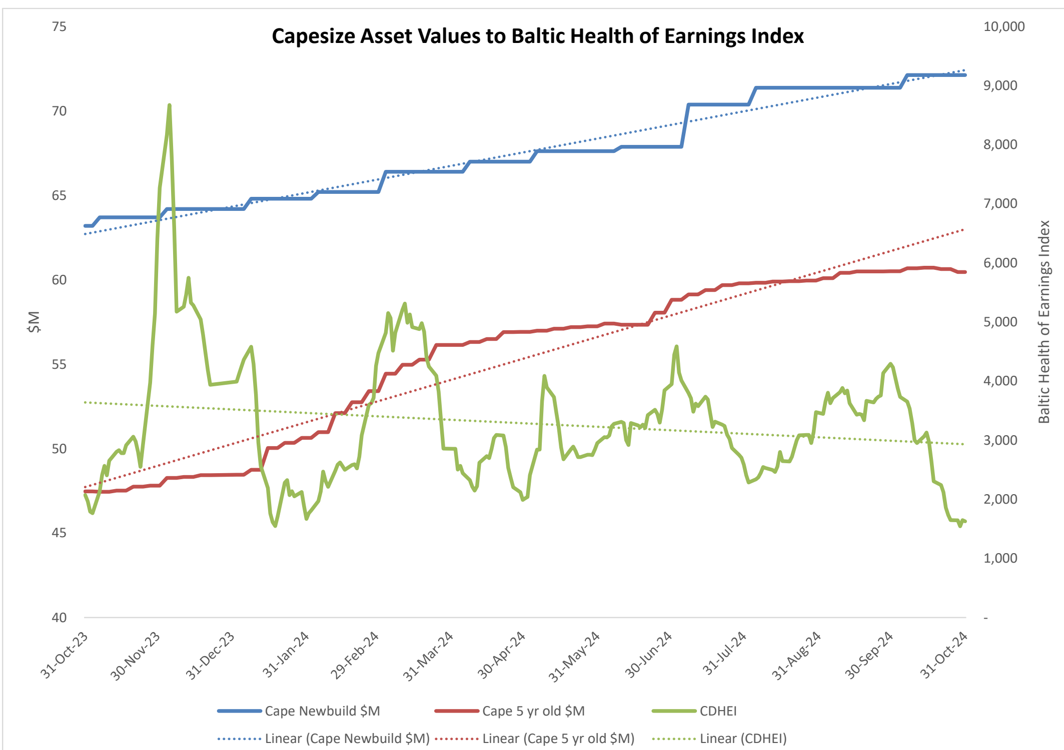


[1] MacroMicro, Dalian Commodity Exchange

Freight Rates Pressuring Asset Values

As measured by Baltic Exchange Investor Indices, the Capesize and Panamax Health of Earnings Indices do not currently justify the five-year-old asset values for the respective sectors.[2]

Over the last 12 months, Capesize spot rates averaged $24,487/day, five-year-old Cape asset values increased 27% and we estimate cash breakeven increased 15%. If an investor purchased a five-year-old Capesize today, we estimate the cash breakeven would be $21,776/day while the average spot earnings of Capes today is $15,311.[3] In addition, although the Cape CAL2025 FFA at time of writing at $19,737 is better than today's freight rates, it remains below our estimated cash breakeven. As such it does not make fundamental sense to sense to purchase a five-year-old Cape at today's asset values.



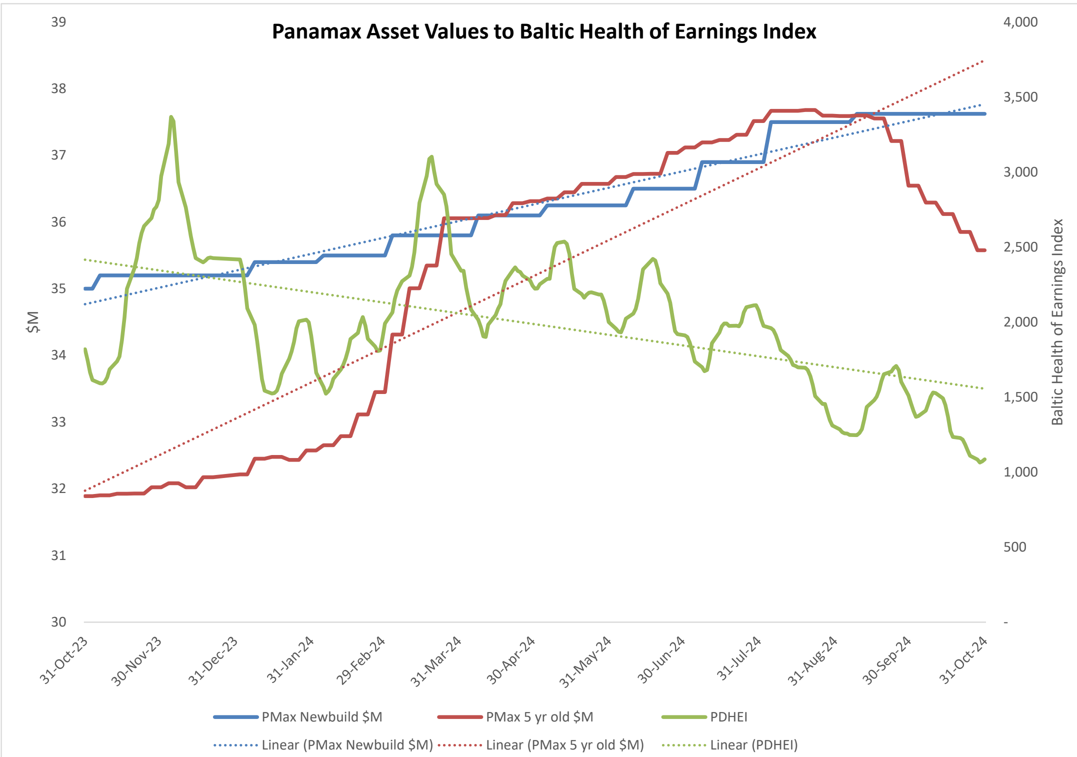
The Panamax picture is different. Over the last 12 months, Panamax spot rates averaged $15,221/day, five-year-old Panamax asset values increased 12% and our estimated cash breakeven increased 4.5%. If an investor purchased a five-year-old Panamax today, we estimate the cash breakeven would be $14,306/day while the average spot Panamax time charter equivalent today is $10,891.[4] Unlike the Capes, five-year-old Panamax values have declined in recent months.

[2] The Baltic Exchange publishes the Baltic Health of Earnings index on every trading day for each major cargo vessel type. It shows the ratio of earnings against cost with a negative number indicating that earnings are below operating costs. The Health of Earnings Index is highly correlated to freight rates, however takes in to account increases in OPEX over time.

[3] Cash breakeven is computed as OPEX, plus G&A expense, debt amortization, interest and fees. On a five-year-old Capesize we assume 65% leverage with a 17-year profile, SOFR of 4.86% Margin of 3%. Increasing asset values offset by a declining SOFR has led to the 15% increase in cash breakevens.

[4] Cash breakeven is computed as OPEX, plus G&A expense, debt amortization, interest and fees. On a five-year-old Panamax we assume 65% leverage with a 17-year profile, SOFR of 4.86% Margin of 3%. Increasing asset values offset by a declining SOFR has led to the 4.5% increase in cash breakevens.

However, we can assume there is little fundamental support to purchase a five-year-old Panamax at today's prices. While not the most liquid, FFAs are one proxy for the forward market and the Panamax CAL25 FFA is at $12,545 at time of writing. Again, this is not promising for asset values maintaining their current levels despite their recent adjustment downwards.



Reasons for Demand Driven Optimism May Take Time to Transpire...

According to the World Bank, global consumption accounts for roughly 75% of gross domestic product (GDP), with the remaining 25% driven by investment. However, consumption in China is 54% of GDP, while investment accounts for 43%.[5] The Chinese economy is, therefore, still maturing. While China has been loosening monetary policy for a number of months, in order to make their stated target of 5% GDP growth, they need the Chinese consumer to pick up some more of the tab.

The recent announcement by the National People's Congress of $1.4 trillion of regional debt support and forgiveness has received only muted applause from markets, with some large foreign corporations in fact cutting their business outlook in China.[6] There is thinking that China is waiting on further stimulus measures to see how the new Trump Administration will proceed with its trade policy, particularly tariffs. If there is more stimulus supporting not only Chinese investment but also the Chinese consumer, then that should be beneficial for freight rates.

On a more micro-level, the Simandou Mine in Guinea should be complete by 2025. The project has anticipated production of 120 million tonnes per annum, which is equivalent to approximately 650

[5] World Bank and Carnegie Endowment for International Peace
[6] CNBC: China's $1.4 trillion stimulus disappoints: Here's what to know 12 November 2024

Capesize loads per year. This could significantly increase Capesize tonne-mile demand over 2026, outpacing anticipated fleet growth in 2026 and 2027. Better rates for Capes are generally supportive for rates in other dry bulk sectors.

All said, however, over the next quarter at least, we would expect some softening in Cape and Panamax asset values until such time that freight rates can provide a better investment justification.