Bahri is booking VLCCs owned by Maran Tankers. Photo credit: MTM

Saudi Arabia was not bluffing when it said it would focus on crude-oil market share. New tanker charter contracts at extremely high rates confirm that a large wave of Saudi oil is definitely en route.

Rates for VLCCs (very large crude carriers; tankers that carry 2 million barrels of crude oil) spiked to nearly $200,000 per day in October 2019, propelled by a confluence of events ranging from security threats to U.S. sanctions on Chinese tankers. VLCCs rates are now surging back towards those earlier peaks, this time driven by the chartering of Bahri, the shipping arm of the oil company Saudi Aramco.

VLCC rate spike

According to Frode Mørkedal, managing director of research at Clarksons Platou Securities, “Average VLCC rates surged to $85,000 per day yesterday [Tuesday] on one of the busiest days recorded out of the Middle East Gulf, led by Bahri on the back of the increased Saudi export announcement for April. Our brokers saw Bahri taking nine vessels from the market, pushing Middle East Gulf-East [Asia] rates from $28,000 per day all the way to $105,000 per day for the last fixed ship seen this morning [Wednesday]. Our brokers see further support in the market pushing for higher earnings on the day.”

The Tankers International commercial pool is reporting multiple VLCCs on subjects at around

$140,000-$160,000 per day, and one VLCC on subjects for a short-haul trip for Bahri from the Middle East Gulf to the Red Sea at $205,707 per day. When a ship is “on subjects,” the contract is non-finalized and more of an option; when it is “fully fixed,” the deal is done. During the October 2019 spike, VLCCs were on subjects at over $300,000 per day, but cooler heads prevailed and the highest fully fixed rate was around $190,000 per day.

As of noon EST on Wednesday, Tankers International listed a last-done rate on the Middle East Gulf-Asia run at $170,500 per day, and a last-done rate on the Middle East Gulf-U.S. Gulf route at $142,000 per day. VLCC owners who have ships either on subjects or fixed to Bahri in the past two days include DHT (NYSE: DHT), Frontline (NYSE: FRO) and privately held Maran Tankers, among others.

What’s different this time?

Two factors underscore the scale of the coming Saudi crude wave: first, multiple tanker contracts have been signed to carry oil from the Middle East Gulf to the U.S. Gulf; and second, Bahri has its own VLCC fleet and yet it’s chartering from outsiders.

“The discount now priced into Saudi Arabian crude has seen more bookings going west, and it has been a very long time since we have seen Bahri itself book VLCCs to carry Saudi crude to the U.S. Gulf, which was a common occurrence prior to the shale revolution,” said Mørkedal.

Before this week, there was an average of three VLCCs doing Middle East-U.S. Gulf runs per month. Back in 2015, prior to the shale revolution reaching full steam, there were around 15 a month, he noted. This has a major effect on the VLCC supply-demand balance. The trip to the U.S. Gulf is around 1.8 times as long as the voyage to Asia, so it soaks up almost twice the vessel capacity for the same cargo volume.

“Bahri owns its own ships and rarely comes to the spot market for more vessels,” continued Mørkedal. “This is therefore a good indication that the taps are opening again on the long-haul Middle East Gulf-U.S. Gulf trade and that Saudi Arabia, now looking to export above its max production capacity, is likely to need more ships to cater to its own transportation.”

In response to a query from FreightWaves, Evercore ISI analyst Jon Chappell made a similar point. “Aramco is chartering ships from third parties, not Bahri, for the first time in a long time. Talk is of eight VLCCs, or 16 million barrels, just for the first 10 days of April. Rates for VLCCs doubled Monday to Tuesday and it looks like they’re doubling again today [Wednesday].”

How long will the rate surge last?

Asked whether VLCC rates could stay above $100,000 for an extended period, as they did in the fourth quarter of 2019, Chappell replied, “It all depends how long Saudi Arabia plans to pump 12 million-plus barrels per day.”

According to Randy Giveans, the shipping analyst at Jefferies, told FreightWaves, “Rates are unlikely to be sustainable above $100,000 per day for multiple months, but they certainly could stay above this level for a couple of weeks.

“Current fixtures are closer to $145,000 per day. We expect rates to pull back from these levels, but should be supported above $60,000 per day, which is well above our current second-quarter rate assumption.

“Huge surges are usually short-lived, but the pullback usually settles much higher than where it started,” explained Giveans. He added, “Beyond the next few months, the two points of focus will be inventory levels and U.S. production and export levels. Those will determine the market strength in the second half of this year and 2021.”

Stock-market effect

As the rest of the stock market is crashing this week, stocks of VLCC owners are up by double digits. Since Friday, shares of Frontline are up around 33% and the stock price of Euronav (NYSE: EURN) is up around 20% (including a pullback for all crude-tanker stocks in the early hours of trading on Wednesday).

“Tankers had their best one-day gains ever yesterday, and Monday was an up day as well despite crude falling 25%,” said Giveans. “Much of this was short-covering, but some of it was energy investors looking for ways to play the increased Saudi volumes as opposed to U.S. domestic oil producers, who are being negatively impacted.”

Tanker stocks could be driven even higher if investors who don’t traditionally invest in these stocks are attracted by their “hedge” potential amidst the Wall Street carnage.

“They absolutely should be,” said Chappell. “In this price war, tankers are the perfect hedge.”

Giveans confirmed, “I have been getting lots of inquiries from larger investors regarding tankers, earnings upside, and dividend payout potential. First-quarter earnings will almost certainly be higher than fourth-quarter 2019 earnings based on company guidance and quarter-to-date rates. And if VLCCs average $80,000/day and Suezmaxes [tankers that carry 1 million barrels of crude oil] average $50,000/day in the second quarter, that quarter could — surprisingly — be even better than the first quarter.”