November 2024

Shipping Market Review

Foreword

As we present our latest edition, Shipping Market Review – November 2024, we would first like to address a temporary change in its scope. This change is a direct consequence of the ongoing integration of the Sustainability department into our Research team. To ensure a seamless transition while maintaining the high standards of our output, we have found it necessary to refine the scope of our research temporarily. Consequently, we may give less coverage to some topics that we have previously explored in depth until the integration is complete.

This integration is more than a mere structural change; it represents a significant shift towards embedding sustainability at the core of all our activities. By combining our expertise in ship finance with cutting-edge shipping research and sustainability insights, we aim to offer our customers, investors and other stakeholders a comprehensive understanding of the industry's journey towards net zero while continuing to finance the transition.

We appreciate your understanding and patience as we undertake this important endeavour. The changes underway are designed to enhance the relevance and depth of our offerings, thereby providing greater value to all our stakeholders.

Thank you for your continued support.

Christopher Rex, Sustainability & Research, Danish Ship Finance

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Executive summary

Reaching the 2050 targets remains a formidable challenge

The shipping industry is struggling to scale the production of sustainable shipping fuels. However, we believe this approach is misguided. Instead, the industry should prioritise innovating the commercial drivers that influence value creation to effectively reduce fuel consumption. Various decarbonisation strategies are being explored across multiple sectors; it will not be the responsibility of the shipping industry to determine the outcome. By updating its commercial contracts, the shipping industry can facilitate further reductions in fuel consumption while simultaneously increasing investments in its crewing and technical management. The climate targets for 2030 are within reach, but achieving net zero by 2050 remains a formidable challenge.

The shipping industry is struggling to keep up with greenhouse gas emission reduction plans. The low-hanging fruit is being harvested, but accessing the larger abatement pools requires contractual and behavioural changes. The dominant business models currently prioritise short-term gains rather than investments in long-term potential. This chapter proposes critical changes that encourage large-scale investments in vessels, crews and technical management.

Introducing transparency and benchmarking to drive change

The industry's lack of transparency and benchmarking is currently hindering large-scale adoption of emission reduction tools with long repayment periods. These elements are crucial catalysts for improving environmental performance, because they allow stakeholders — e.g. customers, investors, banks and employees — to make choices aligned with sustainability goals. Benchmarking enables companies to compare their environmental performance against industry standards or peers. When competitive analyses are made public (e.g. improved Carbon Intensity Indicator (CII) ratings), it further motivates shipowners and operators to enhance their practices to meet or surpass benchmarks, fostering industry-wide improvements. Therefore, embracing transparency and benchmarking is essential for the industry to achieve significant environmental advancements.

Fuel budgeting on a voyage basis to increase returns

The next level is about commercialising best-in-class performance beyond lower fuel costs. In previous editions of this report, we have suggested introducing a voyage benchmarking tool that creates a fuel budget per voyage. The fuel budget is based on the median energy consumption across peers that have undertaken the same journey. The idea is to establish *what good looks like* while allowing top performers to earn more per dollar freight rate. The additional earnings stem from fuel not consumed under the fuel budget.

Fuel not consumed under the budget will become an equity kicker

Cargo customers are offered a fixed price for a voyage, although they still assume some risk from unpredictable weather conditions. The ship operator bears the risk of the operational implications of retrofits, new technologies, and fuel types. *Fuel not consumed* could become an equity kicker that rewards operational excellence. Such a simple mechanism may foster a changing mindset around value creation and eventually spark vessel ownership consolidation towards the most energy-efficient operators.

The future clean fuel choice needs to serve multiple sectors

The future choice of clean fuels for the shipping industry is widely debated. The IMO does not explicitly recommend any particular fuel pathway but provides a regulatory framework and sets targets to reduce greenhouse gas emissions. Multiple routes to decarbonisation are being explored, with parts of the industry examining options such as green ammonia. This chapter does not favour one clean fuel over another; however, it highlights that no alternative energy source has achieved global prominence without strong governmental support and widespread application across multiple sectors. It is uncertain whether green hydrogen will win out among decarbonisation technologies.

A route to energy efficiency and long-term partnerships

While the shipping industry awaits the introduction of new clean fuels, it could benefit from collaborating with cargo customers on a new contractual framework. By leveraging the fuel budget, such a framework would promote long-term collaboration and distribute financial risks and incentives more equitably. This approach would also encourage sustained improvements in energy efficiency. Fuel budgets should be reviewed and tightened annually to align with global climate targets.

Changing the commercial currents to drive down emissions

How the 2030 targets can facilitate a race to the top

For the shipping industry to meet the 2030 climate targets, it should create new commercial mechanisms that allow “fuel not used” to become an equity kicker that rewards energy efficiency beyond lower fuel costs. For this to play out, the shipping industry could introduce transparency and benchmarking through a voyage-based fuel budget that dictates what “good” looks like, from loading at terminal A to discharge at terminal B. Investments in upskilling of crewing teams and technical managers should come next. The ship operator that can compete on costs while earning more on the dollar freight rate is best positioned to participate in consolidating the shipping industry.

The shipping industry is maintaining course on its decarbonisation journey. Global and regional regulators are paving the way for continuous improvements in energy efficiency and increased uptake of alternative fuels. Industry pioneers are leading the way with green corridors and “book and claim” systems, while many shipowners are working to upgrade existing vessels. Still, few of these new initiatives have reached sufficient maturity where scale can begin to build. Sustainable shipping fuels are expensive and will be in limited supply. The shipping industry has not yet identified a winning pathway; multiple strategies are still being explored. The primary challenges are a fragile business case and a lack of differentiation.

It is possible to meet the 2030 targets…

There is much to indicate that the industry can meet its 2030 emission targets, but this will require a structural change in industry dynamics. Retrofits alone cannot unlock the world fleet’s full potential for energy efficiency. There is significant abatement potential encapsulated among business models, and unlocking it will require a systemic shift in value creation across the competitive landscape. The current model, whereby many shipowners profit most from speculating on ship price fluctuations, does not sit easily with climate targets that can only be met through long-term investments and behavioural changes.

…but transparency and benchmarking are required to change the commercial currents

Operational excellence cannot easily be identified among peers, since transparency and benchmarking have not been widely adopted. The IMO’s Carbon Intensity Indicator is not currently designed as a benchmarking tool that allows vessel performance to be compared on an apples-to-apples basis. It compares vessel performance across regions — apples to oranges — without adjusting for differences in operational conditions.

Establishing what good looks like

In previous editions of this report, we have suggested the introduction of a voyage benchmarking tool that creates a fuel budget per voyage. The fuel budget is based on the median energy consumption across peers that have undertaken the same journey. The idea is to establish what good looks like while allowing top performers to earn more per dollar freight rate. The additional earnings are generated from fuel not consumed under the fuel budget. For further information on fuel budgets, please refer to Shipping Market Review from November 2023 (pp. 7-8) and May 2024 (p. 10).

Commercial decarbonisation can drive higher returns on invested capital

Such a fuel budget could reward energy-efficient operators (e.g. those that reduce their fuel consumption) with a higher return on invested capital. The value of the fuel not consumed under the fuel budget would serve as an equity kicker. Such a simple mechanism could help change the mindset around value creation and may eventually translate into a consolidation of vessel ownership favouring the most energy-efficient operators.

The competitive landscape of ship ownership

Operational excellence and energy efficiency are advanced not only by investments in energy-saving technologies and retrofits, but also by investments in upskilling crewing teams and technical managers of the vessels. When lower fuel consumption offers yields on invested capital beyond lower fuel costs, we could see a push towards more shipowners increasing their investments in crewing and technical management rather than treating these services as pure costs. Imagine what could happen if crew payments were linked to fuel efficiency. It could become a scale play, where larger and more advanced fleets of vessels with high-performing crews were allowed to increase their digital maturity beyond that of their competitors and further accelerate a consolidation push towards the largest and best-performing players. These players could compete on costs while earning more per dollar freight rates than their competitors.

The course for 2050 is set but the tactics remain unclear

The systemic dilemma for decarbonising the shipping industry

The IMO has given shipowners the flexibility to chart their own course towards 2050, provided they comply with regulations. However, this flexibility may misdirect parts of the industry onto pathways with little chance of success. The shipping industry is a niche sector that cannot dictate or single-handedly introduce a new energy source such as green hydrogen or green ammonia. While green hydrogen and ammonia represent potential energy carriers capable of decarbonising the shipping industry, shipowners will need to adopt fuel choices that benefit multiple sectors and industries to reap the benefits of global scale.

The International Maritime Organization (IMO) has been designated by countries worldwide to regulate international shipping emissions, ensuring that there is a unified set of standards. This global governance structure prevents the complications that would arise from attempts to impose national regulations on a transnational industry like shipping.

Global regulation guides the shipping industry

The IMO has formulated a broader strategy to reduce greenhouse gas emissions from international shipping and contribute to global efforts against climate change. While MARPOL Annex VI does not set explicit limits on CO_2 emissions, as it does for SO_x and NO_x emissions, it implements mandatory measures that effectively regulate CO_2 emissions by enhancing the energy efficiency of ships.

Navigating energy flexibility to reach destination targets

The IMO does not explicitly recommend any particular fuel pathway for the shipping industry. Instead, it provides a regulatory framework and sets targets to reduce greenhouse gas (GHG) emissions. It encourages the industry to explore various technological and operational solutions — including alternative fuels and energy sources — to achieve these goals. This approach allows for innovation and the adoption of a variety of solutions to meet the global targets for emission reductions.

Government support is crucial for the adoption of alternative energy sources

Historically, no alternative energy source has achieved global prominence without some form of strong governmental support. Governments play a pivotal role in mitigating risks, providing financial incentives, and creating a regulatory environment conducive to the adoption of new energy technologies. For emerging alternative energy sources — such as hydrogen, ammonia or advanced biofuels — to reach global scale, similar levels of government support will likely be necessary.

Solar and wind energy scaled because of government support

Take solar and wind energy as an example. Countries like Germany, China and the United States have heavily subsidised solar and wind energy through feed-in tariffs, tax credits, and renewable energy mandates. These policies have led to significant reductions in costs and increased global adoption, making solar and wind two of the fastest-growing sources of electricity generation worldwide.

Governments prioritise energy sources that serve multiple sectors

Governments often prioritise energy sources with broad applicability, because these can have a more substantial impact on national goals such as economic growth, energy security and environmental sustainability. They place significant importance on ensuring that the environmental benefits of new energy sources are realised domestically. Financial incentives such as subsidies or tax credits are more easily justified when the allocation of public funds broadly benefits the domestic economy.

Public-private partnerships help promote alternative energy sources

Private sector innovation and investment are crucial, but the scale and complexity of global energy systems make government involvement indispensable for the widespread adoption of alternative energy sources. This collaborative approach helps address the multifaceted challenges of transitioning to cleaner and more sustainable energy solutions.

What is hampering the green ammonia route to 2050?

The shipping industry cannot decarbonise alone

Limited global investments in hydrogen-based energy systems pose a challenge to the shipping industry's decarbonisation strategies. As the 2040 and 2050 IMO targets draw nearer, there is still no clear path forward to meet these goals. Green hydrogen is expensive and not competitive without a global carbon tax. The lack of a clear market direction across industries is discouraging large-scale investments in hydrogen-based energy systems. A cross-sectoral application is required for production and infrastructure to scale. Any hopes for political intervention outside the IMO may be misplaced; the industry's green ammonia route to decarbonisation demands an energy loss of 70-80% of the (renewable) energy invested in the transition.

New and more energy-efficient vessels are being ordered, many of which are at some stage of dual-fuel readiness. The industry will need these and other ships to meet the 2050 emission targets. However, enhancing engine capabilities does not, per se, make for a decarbonisation strategy. Investments in dual-fuel capabilities will not provide a yield until the sustainable fuels become available and cargo owners demand a decarbonised ocean offering. If other industries do not adopt hydrogen-based decarbonisation strategies, the shipping industry's transition could face several risks and challenges.

Competition from other decarbonisation strategies is severe

Global production of green methanol and green ammonia is struggling to scale. Green hydrogen has great potential as a clean energy carrier, but the global energy system has not yet seen significant uptake. Competition from other decarbonisation strategies is severe: many industries are working to identify bridge strategies that can postpone a switch to new fuels that would require the introduction of new infrastructures and new technologies. Take aviation as an example. This industry is currently focusing on biofuels and synthetic fuels as a bridge to decarbonisation. These fuels are seen as more compatible with existing infrastructure, reducing the need for new technologies. The shipping industry's bridge decarbonisation strategy seems centred around LNG and biofuels.

Green hydrogen is expensive and not competitive without a global carbon tax

Green hydrogen is currently significantly more expensive to produce than other forms of hydrogen and traditional fossil fuels. The global infrastructure for producing, storing, transporting and distributing green hydrogen is still in its infancy. Significant advancements in electrolyser efficiency, global policy frameworks, investment in hydrogen infrastructure, and increased renewable energy capacity will be essential for overcoming these barriers. In many countries, carbon pricing, subsidies and tax incentives have proved insufficient to make green hydrogen economically competitive with fossil fuels. A robust carbon pricing mechanism (such as a carbon tax or cap-and-trade system) is essential for green hydrogen to become more competitive. Green hydrogen could play a much larger role in the global energy mix as these factors improve.

The lack of a clear market direction is discouraging large-scale investments

There is significant uncertainty about which industries will ultimately adopt hydrogen-based energy systems, how quickly they will do so, and at what scale. Competing decarbonisation technologies, such as electrification, biofuels and synthetic fuels, are also advancing, making industries hesitant to commit to green hydrogen. This lack of a clear market direction is discouraging large-scale investments in green hydrogen projects. If other sectors do not adopt hydrogen at scale, there may be less incentive to develop the global infrastructure needed to supply green hydrogen.

Cross-sectoral application is required for production to scale

Governments tend to offer stronger incentives and subsidies for technologies that benefit multiple sectors and generate substantial economic or environmental benefits. Many decarbonisation strategies rely on synergies between industries, such as shared infrastructure or supply chains, which can lower costs and improve efficiency. If hydrogen-based energy is adopted only by the shipping sector and not by others, policymakers may prioritise support for decarbonisation strategies with broader impacts, such as electrification or biofuels. Shipping alone may not generate sufficient demand to justify the high upfront costs.

Less political attention outside the IMO?

The shipping industry risks playing a relatively minor role in national decarbonisation efforts, despite being responsible for 2-3% of global emissions. This is due, in part, to the energy inefficiency of green ammonia as a propulsion method, which converts only 20-30% of renewable energy into usable power, resulting in 70-80% energy loss. To meet global climate goals, policymakers must prioritise sectors with the highest emissions reduction potential per kilowatt-hour of renewable electricity. Policymakers are often reluctant to support climate initiatives with a low-abatement return on investment, especially when the benefits of taxpayer funding are exported rather than kept within domestic or regional economies.

How to progress towards 2050?

The financial risks and incentives need to be shared out more equitably

Ocean transportation will continue to be the most environmentally friendly and economical way of moving cargo over long distances, even with higher sustainable shipping fuel prices. For the decarbonisation journey to become value-creating rather than value-destroying, however, shipping companies will need to rethink the conventional approach to carbon reduction. Moving beyond the abatement curve involves a combination of top-down and bottom-up activities: empowering frontline personnel (crew) to drive emissions reductions while making significant long-term investments in vessels and technologies.

Despite shipping being a niche customer within the global oil and gas industry, the ownership landscape in shipping is highly fragmented. However, some individual shipowners have begun exploring investments in dedicated fuel production to accelerate the adoption of sustainable shipping fuels. While this ambition is innovative, it may lack long-term viability. Shipowners should limit their fuel investments to pilot projects and testing facilities rather than committing to large-scale fuel production, as doing so would likely result in a misallocation of capital.

Sustainable shipping fuels present a weak abatement case for investors

From an investor's perspective, the shipping industry's green ammonia ambition presents a weak case for decarbonisation. The overall energy loss from green electricity to propeller efficiency can exceed 70%. In comparison, many other decarbonisation investments offer significantly better emissions reductions per dollar spent. Moreover, prematurely investing in a single fuel technology could lock investors onto a pathway that may not be viable in the long term. This risk includes potential technological failures or breakthroughs in other fuel types, rendering earlier investments obsolete. Additionally, the high cost of developing infrastructure for a dedicated fuel could put first movers at a disadvantage if more affordable or efficient technologies emerge later.

Introducing a fuel budget will increase transparency and reduce risks for cargo owners

Instead of focusing on establishing new fuel supplies, the shipping industry may benefit from innovating existing commercial dynamics, aiming for a future where sustainable shipping fuels are purchased on long-term contracts. Many of the existing frameworks for introducing new technology and sustainable fuels into the shipping market allocate a disproportionate share of the financial risks to the cargo owners. In many of the projects where new, more expensive vessels are presented to the market, the cargo owners are expected to cover most of the costs of onboard technology upgrades and pricier sustainable fuels without much certainty about fuel consumption or cost efficiency. This structure seems unattractive to many cargo owners, who are unlikely to engage in longer contracts if they bear most of the risk without much room for cost and risk management.

The contractual framework between shipowners and cargo owners must be revised

To encourage investment in energy-saving technologies and eventually increase the uptake of sustainable shipping fuels, the contractual framework between shipowners and cargo owners must be revised. The financial risks and incentives need to be shared out more equitably, ensuring that both parties benefit from the adoption of sustainable solutions. One solution could be the introduction of a voyage-based fuel budget, where shipowners assume full responsibility for retrofits and upgrades while benefiting directly from reduced fuel consumption.

Adopting a fuel budget will allow greater certainty when planning for transport expenses

Cost transparency and benchmarking only become more relevant in relation to more expensive fuels. Introducing a fuel budget per voyage can provide a clear understanding of fuel costs, offering the cargo owner greater certainty when budgeting for transportation expenses. Although the cargo owner would still assume some risk from unpredictable weather conditions, the fuel budget would mitigate concerns over the unknown cost implications of new technology and fuel types. The fuel budget should allow the cargo owner to engage in long commercial contracts, enabling investments with long repayment periods but greater abatement potential.

Annual tightening of fuel budgets

Fuel budgets should be reviewed and tightened annually to align with global decarbonisation goals. This will ensure that both parties contribute to meeting international emissions reduction targets. This gradual adjustment will allow both the shipowner and the cargo owner to plan for fuel efficiency improvements. ●

Shipping markets at a glance

Shipping Market Review – November 2024

Earnings and vessel prices

Earnings in the Tanker and Container segments are driving the ClarkSea Index

Longer travel distances and greater inefficiencies have managed to keep earnings and vessel prices in the top 30% observed since 2000. At the end of October 2024, the ClarkSea index was trading at around USD 25,000 per day.

Freight rates and secondhand prices are roaming in the top 30%

Secondhand prices and freight rates have been rather stable at high levels in the past six months. Similar to the ClarkSea Index (which measures average earnings across the main shipping segments), the Secondhand Price Index has grown by around 4-5% since April 2024. Both earnings and freight rates have been in the top 30% observed since 2000. Strong earnings in the Tanker markets helped sustain the ClarkSea Index at elevated levels until June 2024. This was soon replaced by even stronger freight rates in the Container market. While earnings in the Dry Bulk sector have also remained in the top 40%, they are lower than the ClarkSea Index.

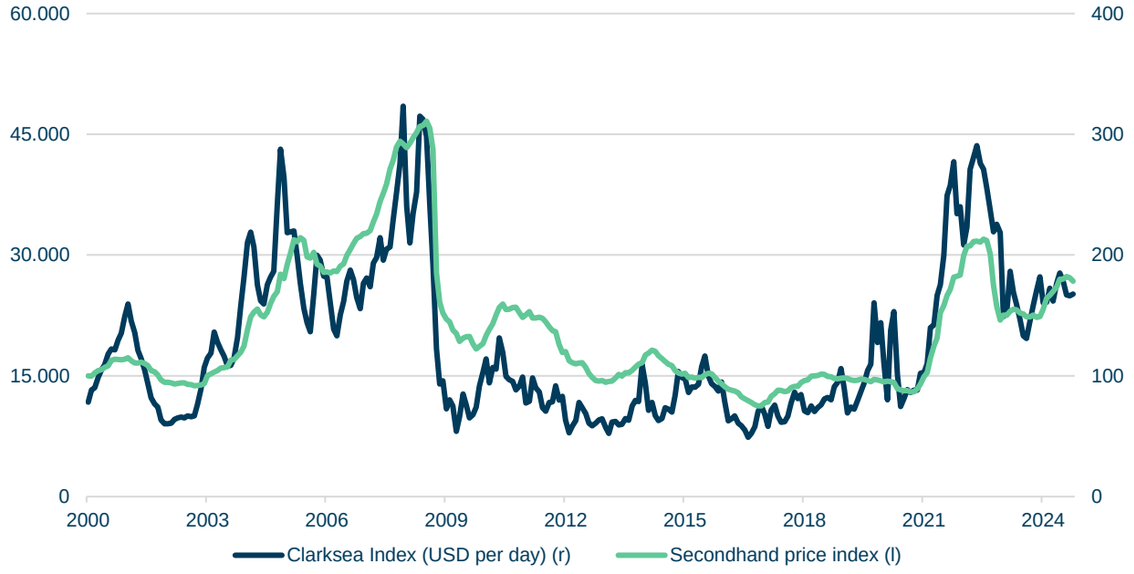
Newbuilding prices have hit a 16-year high

Newbuilding prices have continued to move upwards during 2024. The average newbuilding price index has increased by 3% in the past six months and is now close to the all-time high experienced during 2008 in nominal terms. Newbuilding prices for all major segments are roaming within the top 10% observed since 2000. It should be noted that prices are being settled among only a small subset of yards. Just 159 out of 300 yards globally have received new orders during 2024.

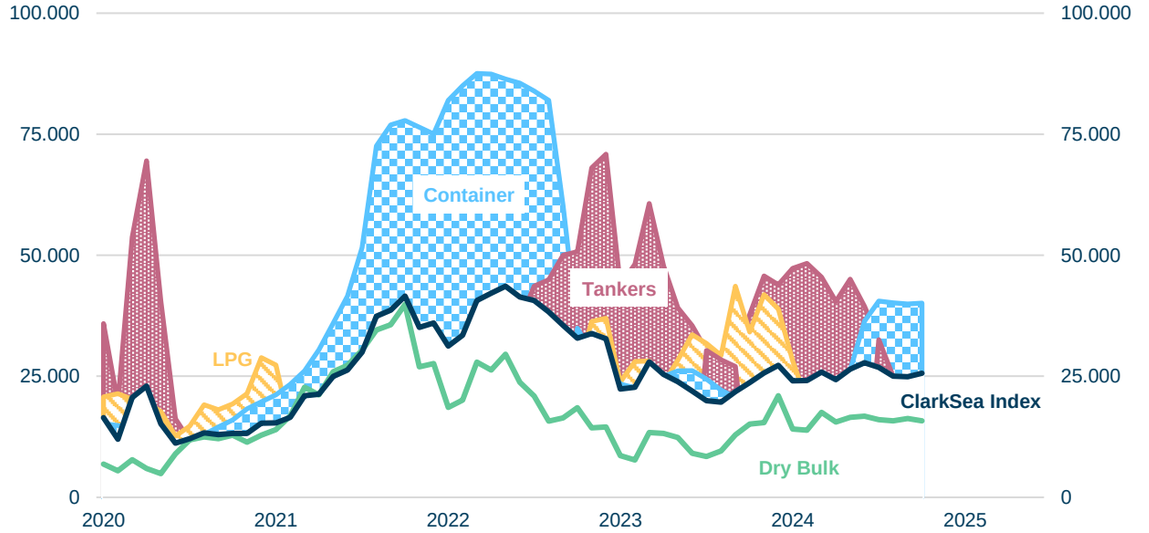
Scrap values are softening along with demolition activity

Demolition activity in the first nine months of 2024 dropped by more than 30% compared to the same period last year. Apart from 2022, demolition activity has not been this low since 2008. Reduced activity, particularly in the Dry Bulk and Container segments, has pushed scrap prices down by around 10% on average throughout 2024.

Rates and values (USD per day and index)



ClarkSea Index (USD per day)



Source: Clarksons, Danish Ship Finance

Supply outlook

Resilient fleet growth in 2025 despite uncertain regulatory and market conditions

Fleet growth is set to remain strong in 2025, at 3.9%, driven by a large inflow of new vessels and historically low scrapping levels. Despite uncertainty around future fuel choices, owners are continuing to place orders.

Steady growth in the orderbook

The orderbook, now accounting for 14% of the fleet, has increased steadily since October 2020, reflecting continued appetite for fleet expansion, especially in the Tanker, Gas and Container segments. In 2025, a large inflow of vessels is expected, with 88 million DWT scheduled for delivery—a 5-year high. This will rise further in 2026, with 93 million DWT expected. The concentration of these deliveries in the next two years suggests a somewhat front-loaded orderbook. Fleet growth is projected at 3.9% annually in 2025 and 2026.

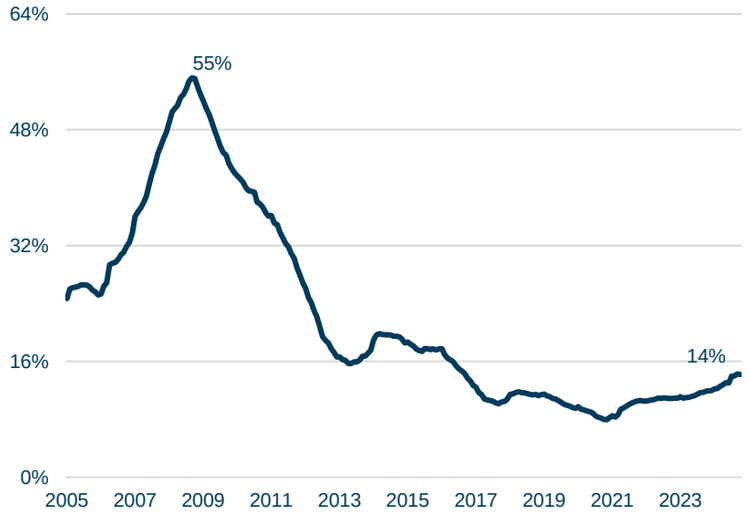
Historically low scrapping amid a booming resale market

Scrapping activity has hit historical lows in 2024, as high resale values for older vessels have shifted owners' incentives. Older tonnage, particularly in the shadow fleet market, has fetched high prices, delaying scrapping plans. However, as supply is expected to outpace demand in the short to medium term, scrapping is likely to increase. Weakening fleet utilisation, along with regulatory pressures and excess capacity, could drive more vessels to recycling yards.

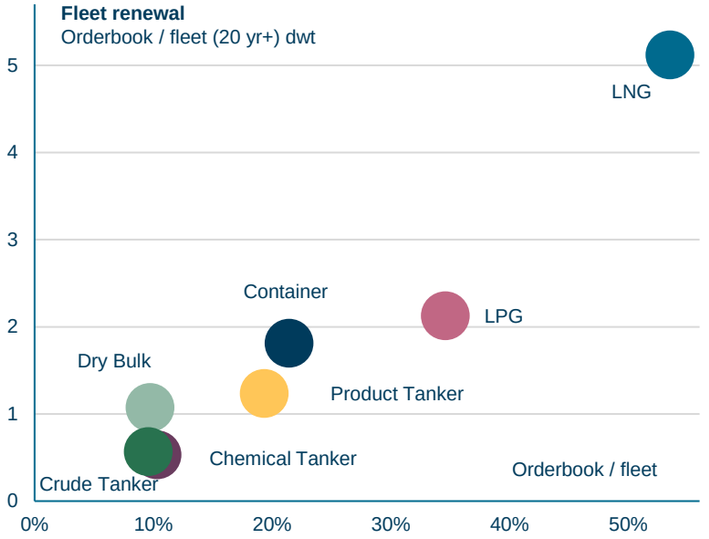
Regulatory pressures and fuel uncertainty

Regulatory changes such as the EU Emissions Trading System (ETS) are widening the market divide. Rising costs for operating older vessels are pushing many owners into renewing fleets, while uncertainty over future fuel choices makes dual-fuel investments a risky bet. This has led to an emerging two-tier market. The top 50 owners, who control 38% of the fleet in the main segments, are investing heavily in dual-fuel technology, with 60% of their orderbooks dual-fuelled or dual-fuel ready, versus 23% for the rest. While these owners are positioning for flexibility, it is uncertain whether these vessels' full potential will be realised, as it is unclear which future fuel type will be available. Meanwhile, those delaying fleet renewal could face higher costs and operational challenges. This disparity may lead to increased consolidation as smaller or less adaptive players struggle to compete in a more regulated market.

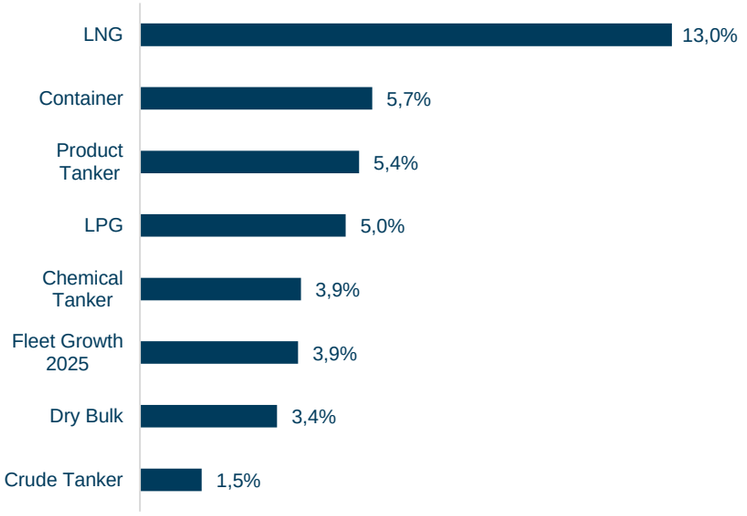
Global orderbook-to-fleet ratio



Orderbook-to-fleet ratio (%)



Fleet expansion in 2025 (before scrapping)



Source: Clarksons, Danish Ship Finance

Fleet utilisation outlook

The disruption-driven shipping markets may be facing a tough period ahead when markets normalise

Since 2020, shipping markets have been powered by one disruption after another. However, fleet growth is expected to outpace demand in 2025, assuming markets normalise, which may not be the case. Nearly all major shipping segments are expected to see fleet utilisation decline, with some facing a rather tough period ahead.

Shipping markets have been powered by disruptions...

The shipping industry has been structurally oversupplied for prolonged periods since 2008. Freight rates and vessel prices fell steadily from 2008 to 2019 due to surplus vessel capacity. However, extraordinary events since 2020 have masked the underlying supply surplus. The COVID-19 pandemic caused major disruptions to supply chains, leading to increased port congestion and logistical bottlenecks. As shipping markets began to recover, these disruptions were replaced by inefficiencies caused by longer travel distances due to the Ukraine-Russia war and, more recently, the Israel-Hamas conflict.

…but fleet growth is set to outpace demand in 2025

Seaborne demand volumes are expected to grow by 1.8% in 2025. However, the market disruptions are likely to abate somewhat, which is expected to reduce travel distances by 0.9%, leading to distance-adjusted demand growth of 0.9% for the year. The merchant fleet is projected to grow by 3.9%. Consequently, supply is expected to outpace demand, which will likely pressure freight rates and vessel prices. Nearly all major shipping segments are expected to see declines in fleet utilisation.

A tough period ahead for Container vessels

The wave of disruptions has masked the underlying supply surplus in the Container segment and kept freight rates and vessel prices at high levels. However, when the situation in the Red Sea normalises, we may see the market flooded with a vast amount of capacity in addition to the usual delivery schedule of the orderbook. This will weaken fleet utilisation and pressure freight rates.

China outlook is weighing on the Dry Bulk segment

China imports around 40% of global seaborne Dry Bulk trade. The Chinese economy has continued to struggle, with the property sector being the biggest drag on economic growth. So far, there has not been any impact on imports while demand has been weakening. Demand for Dry Bulk vessels could be significantly impacted if weakening demand begins to reduce imports, c.f. demand deep dive on page 16.

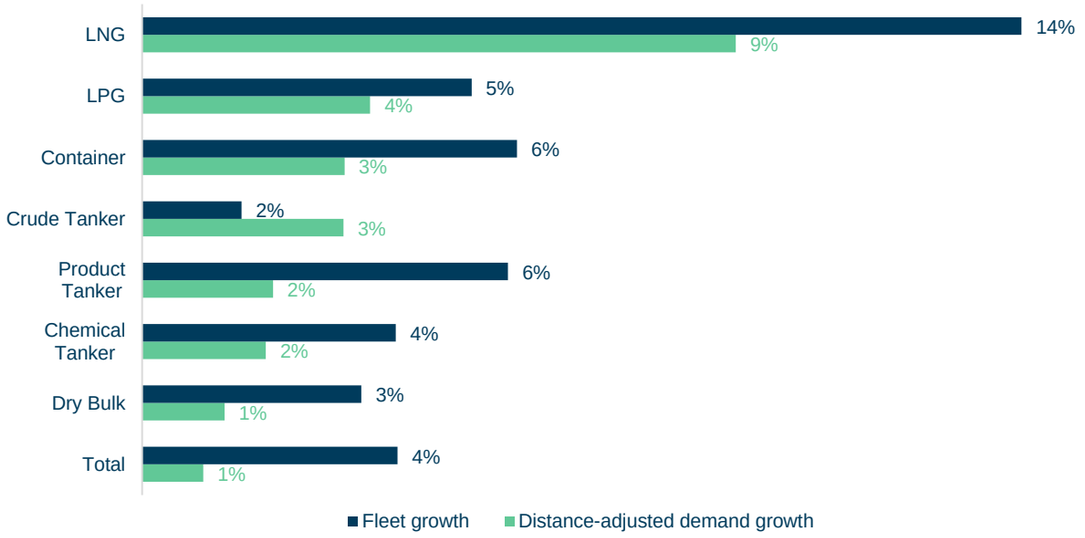
Tankers are in a comfortable position, but increased scrapping may be needed

Seaborne demand in the Crude and Product Tanker segments are projected to be solely driven by volumes in 2025. While fleet growth for the Crude Tanker segment seems fairly manageable, the Product Tanker fleet is set to expand ahead of demand, along with the Gas Carrier fleet. This may require increased demolition of older vessels to balance the market. These segments are currently also thriving on longer travel distances due to the geopolitical situation, but the risks of these issues escalating or deescalating could burden the outlook, c.f. demand deep dive on page 17.

Geopolitical tensions are the primary concern

As mentioned, geopolitical tensions have broadly benefited shipping markets so far. However, possible trade wars between the west and China are also a growing concern for shipowners. In 2018, a trade war broke out between the US and China, which had major implications for Container trade. The US and EU have recently imposed tariffs on certain goods (such as EVs) in order to protect domestic industries.

Expected fleet utilisation, 2025



Source: Clarksons, Danish Ship Finance

A deteriorating outlook for the Chinese economy

One of the key drivers for shipping markets is losing momentum

The Chinese economy is one of the key drivers for shipping markets. However, the economy is slowly losing momentum because of a combination of cyclical and structural challenges. Seaborne demand will be impacted negatively if the weakening economy begins to reduce imports.

Around 26% of world seaborne trade goes to China

The Chinese economy plays a vital role in global seaborne demand. The economy imports a staggering 25% of global seaborne trade, while also exporting a significant amount of manufactured and refined goods. For certain ship segments, the influence of China is even more pronounced. For instance, Chinese imports account for around 39% of global seaborne Dry Bulk trade. Consequently, any fluctuations in the Chinese economy will have a significant impact on global seaborne demand.

The Chinese economy continues to struggle…

In the third quarter of 2024, annual GDP growth reached 4.6%, falling short of the government's target of "around 5%" for the year. A combination of slowing growth, declining confidence, and households withholding spending and investment has weakened domestic demand and dampened economic momentum. This is also reflected in consumer prices, with the CPI Index increasing by a mere 0.4% year-on-year in September 2024, following a prolonged period of deflation in 2023.

…with investments in the property sector declining by 30% since 2021

Unsurprisingly, the property sector, which accounts for about a fifth of the economy, remains the biggest drag on China's growth. Real estate investments have already decreased by almost 30% since hitting their peak in 2021. Residential property prices have likewise experienced negative growth.

Challenges may require structural changes to the economy

The Chinese economy is facing structural challenges. Despite decades of growth being driven through investments and exports, making China one of the world's largest economies, this strategy has left Chinese households on the sidelines and weakened domestic demand. Moreover, the population is declining and ageing. Stimulus packages may only provide a short-term boost to the economy. Addressing these structural challenges will require a transformation of the economy to stimulate private consumption and redistribute wealth. This will take time and may come at the expense of rapid, yet short-lived, investment-driven growth and not positive for seaborne demand.

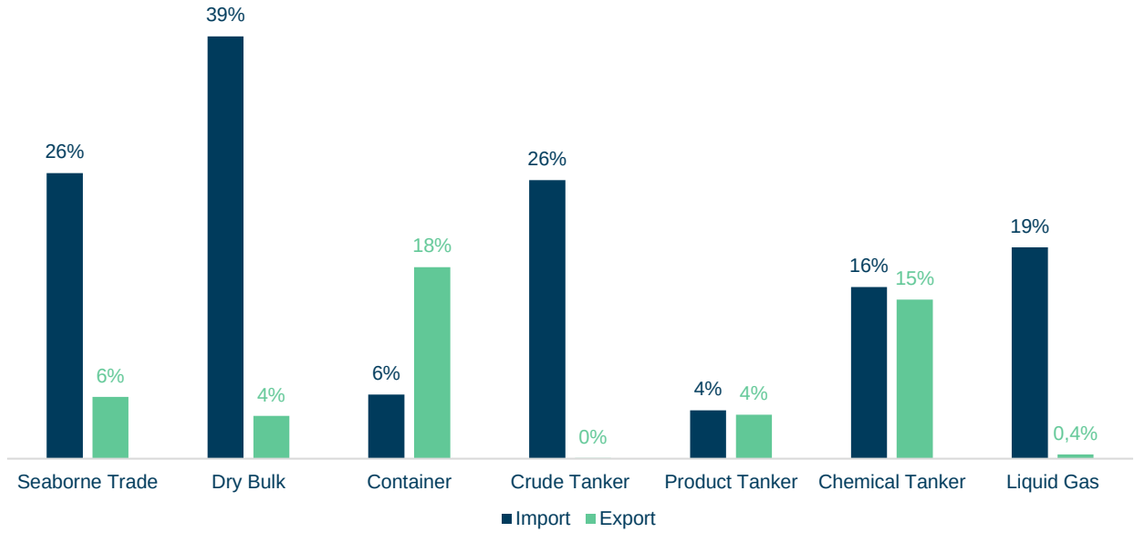
Commodity imports continue to rise while demand weakens

Remarkably, while economic growth has been slowing, we have not seen any impact on shipping demand. Chinese seaborne imports increased by over 4% in the first eight months of 2024 compared to the same period last year. The continued imports coupled with lower domestic demand have led to a buildup of commodity inventories. Coal inventories have more than quadrupled since 2021, while iron ore inventories are also close to hitting all-time highs. Likewise, crude oil inventories have increased significantly. This might also be a strategic effort to bolster domestic reserves of various commodities.

Seaborne trade may be impacted across the board

Seaborne demand could be significantly impacted if weakening demand begins to reduce imports and trigger drawdowns of the accumulated inventories. Some segments, namely Dry Bulk, Crude Tanker and LNG, seem more exposed, since China accounts for a large part of their trade. Furthermore, a structural transition away from investment- and export-driven growth will further reduce demand.

Share of seaborne trade imported and exported by China (%)



Source: Clarksons, National Bureau of Statistics of China, S&P Global, KKR, Rhodium Group, China Coal Resource, Vortexa, Danish Ship Finance

Tipping point for global tonne-mile demand

Geopolitical events have increased shipping distances and driven freight rates and ship prices to record highs, but what happens when the disruptions reach a tipping point?

The shipping industry has thrived in recent years due to geopolitical disruptions, with longer routes driving up freight rates and vessel prices. However, these gains rest on fragile foundations, as they are largely attributable to geopolitical shocks. The ongoing Middle East crisis is jeopardising market stability, with potential volume losses that could alter market dynamics. This geopolitical situation, involving countries like Iran and Israel, poses multiple risks – including the closure of chokepoints such as the Strait of Hormuz. While such a scenario is considered unlikely by most, the industry must remain alert to the shifting dynamics that could quickly turn a tight market into one facing serious demand challenges.

The tipping point: potential disruption at the Strait of Hormuz

The Strait of Hormuz is a vital artery for global energy trade. Approximately 20% of the global oil and LNG supply passes through this chokepoint, making it a critical linchpin for the shipping industry. Any disruption here – whether caused by military conflict, sanctions or geopolitical brinkmanship – would have far-reaching consequences for oil and gas cargo volumes, triggering a sharp decline in tonne-mile demand. The current boost to freight rates from extended voyages could evaporate quickly if shipping lanes are blocked or cargoes become unavailable.

Strategic risks surrounding the Strait of Hormuz

The use of energy supply as a geopolitical weapon has been evident in past conflicts. Historically, the Strait of Hormuz has been a flashpoint for conflict. During the Iran-Iraq War in the 1980s, the so-called Tanker War saw vessels targeted as part of the conflict, significantly impacting oil flows through the region. Beyond the immediate impact on shipping, any significant disruption at Hormuz would likely cause a spike in global oil and gas prices, exacerbating already high fuel costs. Such price hikes would ripple through global energy markets, contributing to inflationary pressures and increasing transportation costs for goods shipped by sea. While countries such as the US and China may temporarily stabilise markets by drawing from their strategic petroleum reserves, this would only provide short-term relief.

Limited spare capacity puts pressure on global supply

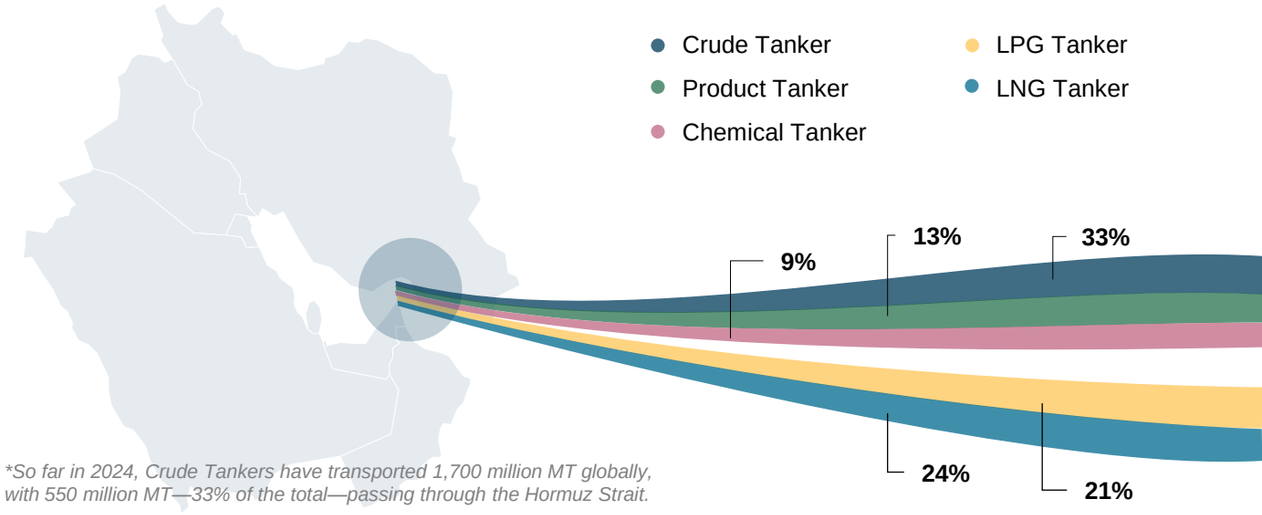
This vulnerability raises the question of whether other producers, such as the US, Brazil or Nigeria, could step in to fill the gap in the event of a major disruption in the Strait of Hormuz. However, spare capacity outside the Middle East is limited. The US, despite being the largest producer, is facing infrastructure constraints that limit its short-term flexibility, while Brazil and Nigeria are already operating near capacity.

Current estimates place spare capacity in global crude oil production at around 6 million barrels per day — far below the 20 million barrels that pass through the Strait of Hormuz daily. Adding to this challenge, much of the world's available spare capacity is located within the Gulf region, which would also be affected by a disruption in the Strait of Hormuz.

Wider economic impacts on the shipping industry

If a disruption in the Strait of Hormuz were to sharply reduce global oil volumes, the effects on the shipping industry would be profound. A sudden decline in available cargoes would cause tonne-mile demand to plummet, severely impacting the profitability of Oil and Gas Tankers. Additionally, rising oil prices would increase fuel costs across the board. This would ripple through the broader global economy, driving up the cost of transported goods and exacerbating inflation. A likely economic downturn would shrink demand for commodities and goods, further reducing seaborne trade. Shipowners would face higher costs and declining volumes – creating a challenging outlook for the industry.

Share of seaborne trade out of Strait of Hormuz*



*So far in 2024, Crude Tankers have transported 1,700 million MT globally, with 550 million MT—33% of the total—passing through the Hormuz Strait.

Source: Danish Ship Finance, IEA. Clarksons, EIA

Shipbuilding

Shipping Market Review – November 2024

Shipbuilding

Strong demand growth and high newbuilding prices – but not for all

The outlook for the global shipbuilding industry is being shaped by massive yard output, strong yard utilisation, and an unremitting appetite for ordering new vessels. Newbuilding prices are close to record-high levels. Most yards appear to be sold out until 2027. Still, many yards are set to run out of orders before 2027. There is a group of 170 second-tier yards, representing 27% of global yard capacity but only 5% of the orderbook, that are steadily running out of orders. In 2024 and 2025, these yards are only expected to utilise 38% and 23% of their capacity, while the smaller group of first-tier yards will be operating at close to maximum capacity until the end of 2026.

Newbuilding prices are settled between yards that secure new orders

The average newbuilding price index stood at Index 125 in November 2020. Strong contracting activity sent the index up, and by October 2024 it had risen to Index 190 (+51%). The group of 130 first-tier yards, controlling 73% of yard capacity and 95% of orders, have benefited most. The remaining group of 170 yards are running low on orders. These yards have benefited little from higher newbuilding prices.

China is building most vessels on order

China controls 42% (24 million CGT) of the global yard capacity, distributed between 140 yards, and has secured 57% of vessel capacity currently on order. A group of 70 first-tier yards control 34% (19 million CGT) of the global yard capacity and 55% of the orderbook. These yards have an order cover (i.e. orderbook/yard capacity) of more than four years, while the remaining yards have orders to keep them occupied for approximately another six months.

South Korea is losing ground to China

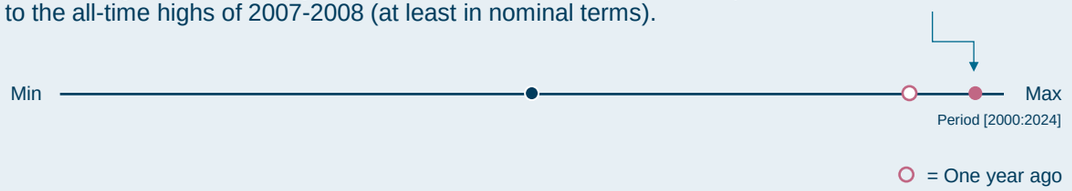
Eight South Korean first-tier yards control 22% (13 million CGT) of global yard capacity and have secured 26% of vessel capacity on order. These yards are running an order cover of three years.

Japan is struggling to keep up

Japan controls 17% (10 million CGT) of global yard capacity, distributed between 48 yards, and has secured 9% (13 million CGT) of the orderbook. A group of 31 first-tier yards, controlling 11% of global yard capacity and 7% of the orderbook, are running an order cover of almost two years.

Market cycle position – November 2024

The average newbuilding price index has increased by 3% in the past six months and is close to the all-time highs of 2007-2008 (at least in nominal terms).



Global demand for shipbuilding capacity has been high since 2021. Annual contracting has outpaced annual deliveries, meaning the global orderbook has increased for 16 consecutive quarters. A total of 144 million CGT is currently on order, distributed between 300 yards.

Massive yard output

Annual deliveries reached a seven-year high in 2023, when 35 million CGT was added to the world fleet. An astonishing 43 million CGT is scheduled to be delivered in 2024. Annual deliveries have only been above 40 million CGT in the five years between 2008 and 2012.

Large appetite for new vessels

Annual contracting activity has also been high between 2021 and 2024, with a four-year average above 50 million CGT. Contracting has not been as high since before 2013.

Stable yard capacity at 56 million CGT

Yard capacity remains fairly stable at around 56 million CGT distributed between 300 yards. If orders were distributed evenly, every yard would have employment for the next 2.5 years. The average capacity utilisation at yards is 76% in 2024, but there is considerable variation between yards.

Uneven access to new orders

A group of 130 first-tier yards have attracted 95% of current orders (CGT) while controlling 73% of the global yard capacity. These yards are running at a utilisation rate of 90%, whereas the remaining group of 170 second-tier yards are utilising 38% of their capacity in 2024.

Source: Clarksons, Danish Ship Finance

Shipbuilding outlook

First-tier yards are set to operate at maximum capacity until the end of 2026

Global yard utilisation is expected to remain high at close to 70% or above until the end of 2026. In 2027, yard utilisation will dip below 60%, but new orders are likely to fill vacant slots.

A clear two-tier market

The bifurcation of the global yard industry between first- and second-tier yards is clearly visible. The group of 130 first-tier yards, which control 73% of global yard capacity but 95% of the orderbook, are scheduled to utilise more than 90% of their capacity until the end of 2026. The 170 second-tier yards are expected to utilise 38% of their capacity in 2024 but will soon run out of orders.

China's first-tier yards are running at full capacity

Chinese yards are expected to use 90% of their annual capacity until the end of 2026. The group of first-tier yards, representing 70 of the 140 Chinese yards but 79 of the 81 million CGT in capacity, are scheduled to run at maximum capacity until the end of 2027. The 70 second-tier yards are expected to utilise 72% of their capacity in 2024 but will run low on orders (26%) as early as 2025.

South Korea seems to be falling behind

The South Korean yards are expected to fully utilise their 13 million CGT capacity in 2024 and 2025, but utilisation is already expected to drop to 85% in 2026 and 64% in 2027.

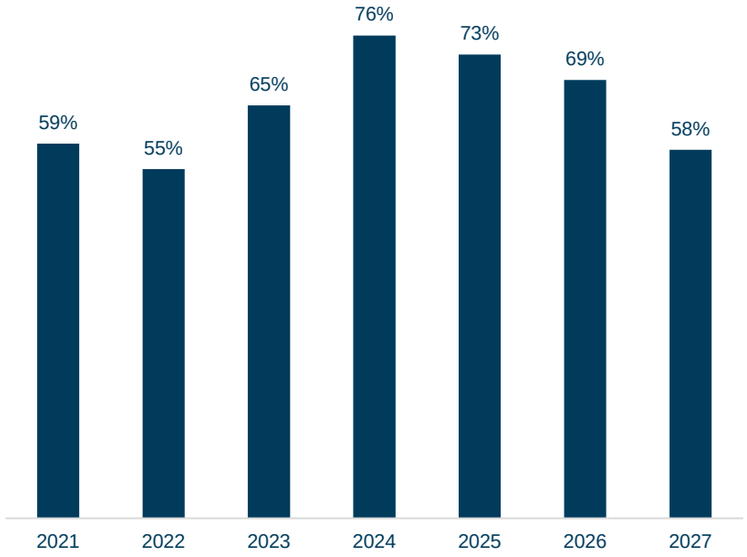
Sluggish demand for Japanese newbuildings

Japan controls 10 million CGT in yard capacity but will struggle to use more than 50% in 2024 and 2025. The 31 first-tier yards, which control 6 million of the 10 million CGT, are faring better than the 17 second-tier yards. The first-tier yards are expected to use 65% of their capacity until the end of 2026, while utilisation for the second-tier group will be 30% in 2024 and 2025, dropping further in 2026.

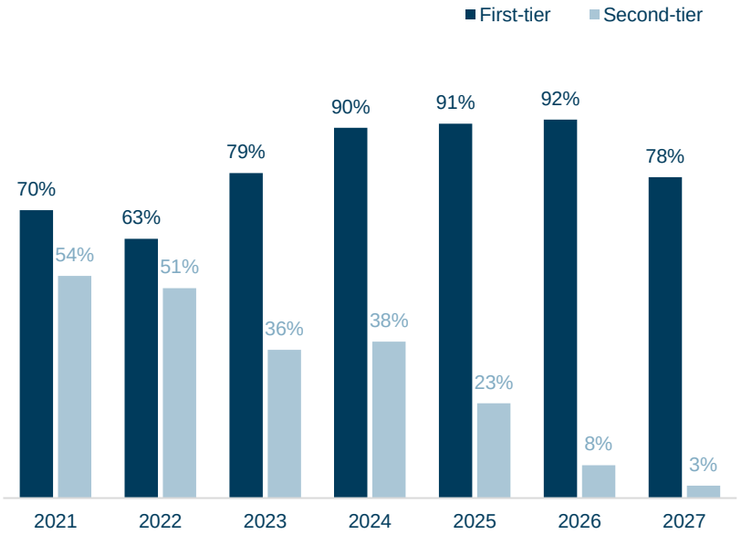
Vacant yard capacity

The group of 170 second-tier yards, representing 27% (15 million CGT) of global yard capacity, are running low on orders. 40 yards will deliver their last order this year, and another 90 yards in 2025.

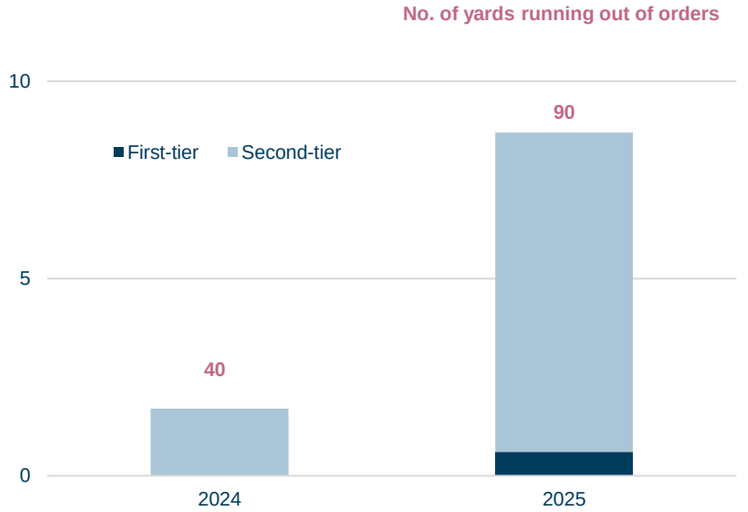
Global yard utilisation



Yard utilisation by tier



Capacity of yards running out of orders (million CGT)



Source: Clarksons, Danish Ship Finance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