



# POTEN TANKER OPINION



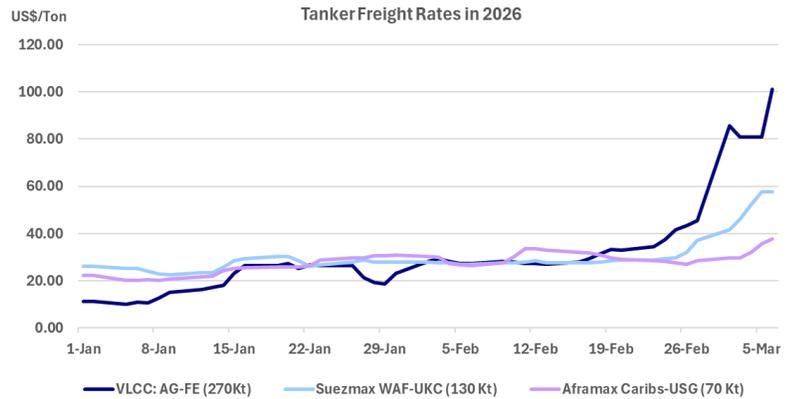
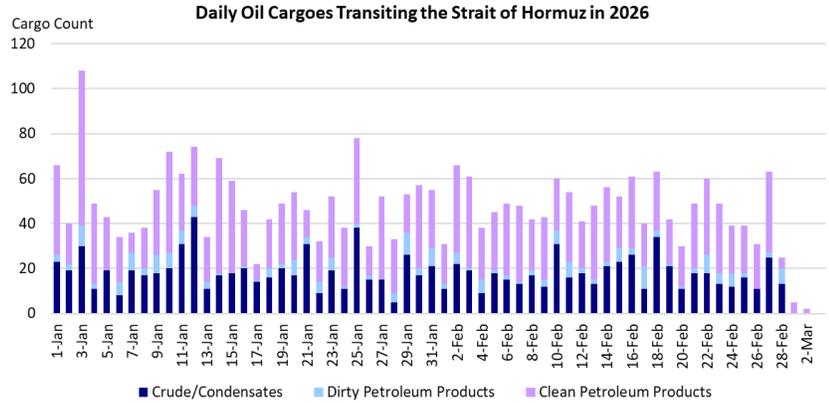
## Sailing Into The Unknown

### Iran conflict creates massive uncertainty

It is rare for us to cover the same topic two Tanker Opinions in a row, but these are unusual circumstances. Last Friday, we discussed several possible scenarios with respect to Iran in our Opinion titled “Will He Or Won’t He?”. On Saturday morning, the answer came. The U.S. and Israel launched airstrikes on Iran in what the U.S. military dubbed “Operation Epic Fury”. Iran responded with massive missile and drone barrages targeting U.S. interests and allies in the region. The outbreak of hostilities had an immediate impact on oil prices and tanker freight rates. The Strait of Hormuz has become key focus of the world, since 20-21 million barrels of crude oil, condensate and petroleum products pass through this chokepoint daily, representing about 20% of global oil consumption and approximately 30% of seaborne oil trade. In today’s tanker opinion we will try to give an overview of the current situation and see what could happen in the short to medium-term if the conflict persists.

After the start of the hostilities, traffic through the Strait of Hormuz slowed to a trickle, but it is important to note that it did not stop completely (see Chart 1). Some ships, including several tankers, do still sail through the Strait, even though the Iranian military stated on March 2<sup>nd</sup> that “The Strait is closed. If anyone tries to pass, the heroes of the Revolutionary Guard and the regular navy will set those ships ablaze”. One of the shipowners who seems unfazed by these threats is George Prokopiou, who’s company, Dynacom has sent at least five tankers through the Strait of Hormuz since the outbreak of the war according to reports in the Financial Times. Several dark fleet tankers are also continuing to use the narrow waterway to export Iranian crude oil from Kharg Island inside the Arabian Gulf. It should be noted that despite this, dark fleet tankers are not sailing risk free though the Strait of Hormuz. Several sanctioned tankers that have been linked to Iran were damaged in attacks this week.

Attacks on vessels in the Straits of Hormuz as well as in the Arabian Gulf have caused freight rates to increase dramatically, both in the Middle East as well as in other regions (see Chart 2). This has made trips from the Arabian Gulf extremely profitable, even considering the much higher insurance premiums that are now being charged. It is important to highlight that war risk insurance is still available for tanker owners (and charterers) that are willing to take the risk. It is just a lot more expensive. Prior to the conflict premiums for vessels sailing into the Arabian Gulf were typically in the range of 0.1 – 0.15% of the value of the vessel. According to various sources, rates have now increased to 1.0%, and, if a vessel is affiliated with the U.S. or Israel, premiums could go up to 3%. However, transiting the Strait of Hormuz poses severe physical security risks that insurance cannot solve. Against that backdrop, the shipping



Source: Vortexa, Poten

industry is not sure what to make of the U.S. offer of “risk insurance” and – if needed – U.S. Navy escorts. Some shipowners that are trapped in the Arabian Gulf now benefit from the unprecedented freight environment by offering their vessels for floating storage. There are reports of VLCCs earning \$400-500,000/day on short-term (30-90 day) floating storage contracts.

What will happen if the conflict drags on and oil supply from the Middle East is restricted for several weeks or months? We will see sharply escalating oil prices, prompting releases from Strategic Petroleum Reserves, lower refinery runs, fuel switching and stepped-up conservation efforts. Brent oil prices initially increased from \$72/barrel on the Friday before the war to \$76/barrel on Monday. At the time of this writing prices exceeded \$90/barrel, and further increases are expected. To allow more oil to flow in the global market, the U.S. has issued a 30-day waiver, allowing Indian refiners to purchase Russian crude from tankers — including sanctioned vessels — if they loaded before March 5<sup>th</sup>.

Tanker rates are at record highs due to a significant geopolitical risk premium in combination with a substantial reduction in effective vessel supply. Many ships remain stuck in the Arabian Gulf while others are waiting for cargoes in the Gulf of Oman. However, this situation is not sustainable. Eventually, the tankers waiting outside will leave the area to look for employment elsewhere. Middle Eastern producers will increasingly be forced to shut in production and lower global oil flows will dent ton-mile demand. Under this scenario, tanker rates will come under severe downward pressure.