



A CLASSIC PARADOX:

A Positive Outlook Despite a Weakening Market

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Undoubtedly, the burning shipping issue being discussed by all those related to the shipping industry is when and how deep will the next shipping recession be. Will history repeat itself?

It is immensely difficult to attempt any forecast in a notoriously volatile industry such as shipping. However, having been asked the question, I will provide my strictly personal view of the market and its outlook.

The recent softening of the market has provided grounds for concern among the international shipping community. After all, we are experiencing the classic symptoms of a declining market, namely:

- *Falling vessel prices.*
- *A predominance of sellers over buyers.*
- *Falling freight rates and level of enquiries.*
- *Hardening of lending criteria by Banks.*
- *Reduction of market credit extended to shipping groups by suppliers.*
- *Recent notable failures to float shipping funds and a slowdown of shipping fund related investments.*

- *Crystallization of the expectation by most shipping market participants that the market should drift lower in 1990.*
- *Technical supporting evidence that the market has broken through previous support levels and should now head lower.*

With so much evidence supporting a further fall in the market together with an expected cyclical downturn, why is there still such a lot of controversy over future freight and vessel value levels?

I suspect the main reason is the undoubted long-term bullish fundamental position of the industry, which is at odds with the above short-term view. The previous recession was so deep and long that its structural effects, especially on the supply side of the industry (namely, newbuildings), should be long lasting. As such, the scene was set for a long-term recovery in shipping because of the reduction (permanent or temporary) of the shipbuilding industry. True, recently Japan has recovered strongly in shipbuilding terms. However, the supply side is still supportive of the industry. In addition, newbuilding prices have already risen to levels that cannot be justified by current freight rates unless the market improves – and indeed substantially- over the 1990's. Lastly, some smaller vessels sectors have been totally ignored in newbuilding terms and as such, represent attractive areas for concentrating investments by secondhand-minded owners.

On the demand side, too, although world economic acting growth seems to have slowed down, it is still positive and the sociopolitical developments in East Europe and the softening of international tension should result in increased international trade and demand for customer goods by developing and newly liberalised countries, as well as, the building-up of their capital sectors.

The above brief review does point out to a short-term recession with the fundamental long-term prospects of the industry intact. However, I do not believe in the "correction" theory and that this mini recession will be more than a simple correction. The main reasons, in my view, lie with the "herd or psychological effect" as seen so often in the shipping industry, as well as, the still wide differential between vessel values and those that most secondhand tonnage has been acquired for a few years ago. As such, owners still have substantial equity to protect, even at vessel values 20% - 30% below today's levels.

This may lead to their placing the vessels for sale in the market and this may further depress the market. Banks have an important role to play in the shaping of the future recession by their collective reaction to the weakening market. As long as they remain broadly supportive of their existing clients and cautiously still support new entrants to the market, their contribution will continue to help the market overcome its short-term weakness.

It is also notoriously difficult to make predictions of the duration of a forthcoming recession but if I had to take a view, this would support a recession over a 12 to 18 month period before a sustained market recovery.

As a broad conclusion, I believe that history will not repeat itself in the same way as the early to mid 1980's crisis. The next months should be a period of consolidation by most shipowners whereby they should pay particular attention to maintain their liquidity position and identify more promising shipping sectors in anticipation of the undoubted opportunities that lie ahead in the shipping industry when the market once again turns positive.

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