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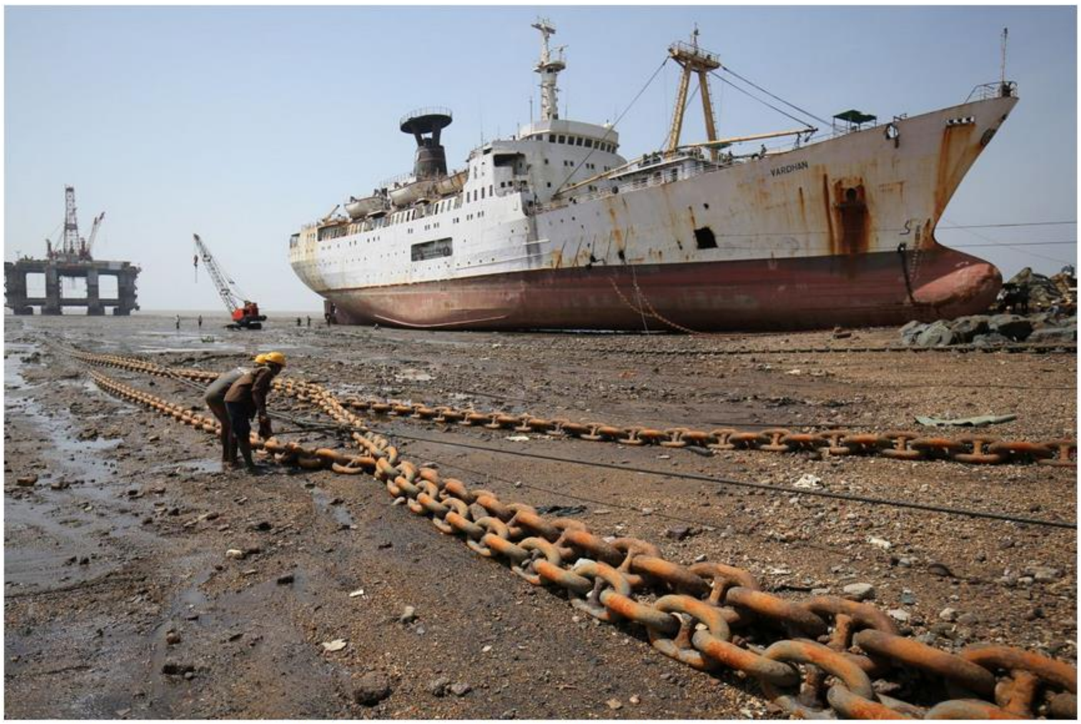
Shipowners on Pace to Scrap $1 Billion in Oil Tankers This Year

Dismal freight rates sending a record number of supertankers to recycling yards in South Asia



A decommissioned oil rig and ship stand ready to be scrapped at the Alang shipyard in western India in May 2018. PHOTO: AMIT DAVE/REUTERS

By Costas Paris

July 8, 2018 9:00 a.m. ET

ATHENS—Dire freight rates are pushing shipowners to scrap a record number of the biggest oil tankers this year, making it a bumper period for recycling yards in South Asia.

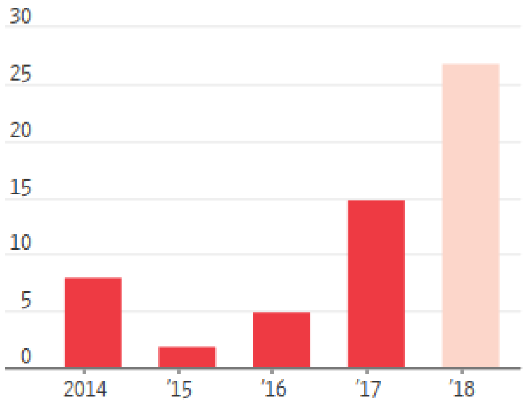
Very large crude carriers, or VLCCs, move much of the world's oil across the oceans. But there are far too many in operation in a shrinking market. Major oil producing countries have curbed production in recent years and the U.S. is importing less crude as it increasingly covers its needs with local oil.

The overcapacity is good business for ship-breaking yards in India, Pakistan and Bangladesh, which pay as much as $20 million for each VLCC sent to be taken apart for scrap. The industry is worth up to $5 billion a year, and tankers are among its top earners.

Heading For Scrap

Shipowners opt to recycle supertankers as demand for ocean oil transport falls.

Scrapped large crude carriers



Note: 2018 figure as of May 31
Source: GMS

"We expect $1 billion worth of VLCCs to be recycled this year," said Anil Sharma, chief executive of U.S.- and Dubai-based GMS, the biggest cash buyer of ships headed for scrap. "It's one of our best years overall."

Industry executives say the current global fleet of 720 VLCCs is about 20% bigger than needed to serve oil markets and that it will take until 2020 for VLCC supply to match demand, provided there are no orders for new ships.

Some 50 VLCCs are up for recycling this year, up from 15 in 2017, according to GMS data. Spot freight rates for those ships are hovering below $6,000 a day, according to brokers, in a business where $25,000 is generally considered a break-even rate.

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Greek owners, who have some of the biggest VLCC fleets, say if freight rates don't recover next year, smaller players will go out of business or be swallowed up by bigger peers. One owner with around 20 VLCCs said scrapping is expected to speed up unless there are clear signs of recovery, "which is unlikely."

"This year has been appalling for VLCC owners, to say the least," said Peter Sand, chief shipping analyst for Bimco, an association of shipping-industry executives. "There's been significant fleet growth while demand is low, and it doesn't look like it's going to get better until 2020, so you scrap to cut the bleeding."

A recovery in commodities markets, including the value of scrap metals, is making the hulls of tankers more valuable, changing the financial calculations for ship operators. Data from industry tracker VesselsValue show average scrap prices at around $425 per metric ton of steel in the last week of June, up from less than $300 per metric ton in 2016.

Some 1,000 vessels are broken up every year and their steel and other metals are melted or simply stacked up and sold to factories. PHOTO: KARAN DEEP SINGH/THE WALL STREET JOURNAL

Some 1,000 vessels are broken up every year and their steel and other metals are melted or simply stacked up and sold to factories. The yards in the Indian subcontinent recycle around 80% of all ships, with the remainder going to China and Turkey, although Beijing has said it will suspend scrapping starting next year.

The average age of VLCCs going to scrap this year is 18.8 years, the youngest since 2013, according to VesselsValue. A ship's average operational age is around 25 years, but after 15 years in the water, the vessel has to go through an extensive survey to determine if it is seaworthy. "An average survey costs about $2 million, and you have to do it again at 20 years, so a number of owners opt to scrap instead," Mr. Sharma said.

The oil glut is also sending offshore rigs to scrapyards. It is a relatively new business that has boomed over the past five years, as the cost of drilling at sea is much higher than inland exploration. At least 18 rigs have been broken up so far this year, compared with 46 last year, according to GMS.