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Offshore Vessel & Rig Connect Asia 2016

Facing Reality in the OSV Market – The Oversupply Issue

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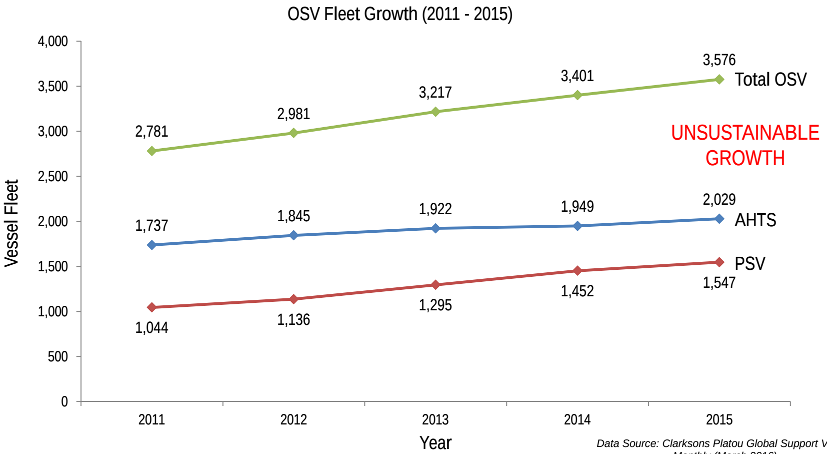
Current State of the OSV Market



Data Source: Clarksons Platou Global Support Vessel Monthly (March 2016)

<u>Staggering Growth of Global OSV Fleet</u>

- On average, PSV expanded by 10% and AHTS expanded by 6% every year for the last 5 years.
- Growth was most prevalent in the larger PSV (>750 sqm) & AHTS (>20,000 BHP) tonnage.
- 25% of the global AHTS fleet and 38% of the global PSV fleet was built only in the last 5 years.
- Current order book – 218 AHTS & 295 PSV newbuilds delivering over the next 3 years.

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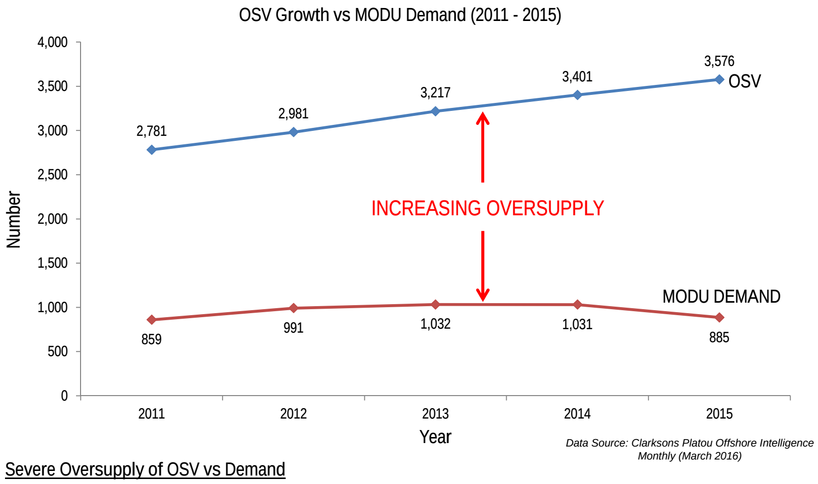


Severe Oversupply of OSV vs Demand

- Over the last 5 years while the OSV industry has expanded by 7.0% on average, demand growth averaged 0.6%.
- This means the OSV industry has outstripped demand by more than 10 times over the last 5 years.
- Clearest indication being 2015, where MODU demand fell by 14% but the OSV fleet continued to expand by 5%.

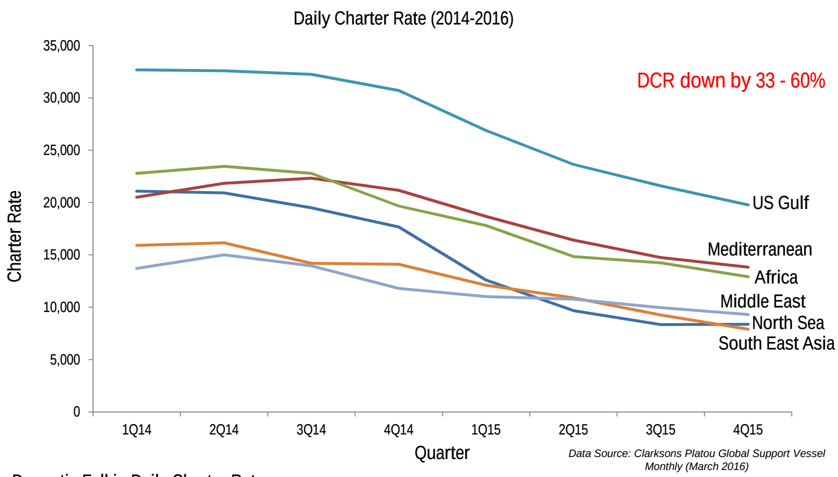
Current State of the OSV Market

Dealing with the OSV Oversupply Issue

There are three ways the industry can deal with this oversupply issue:

- Temporarily reducing supply (warmstacking & coldstacking)
- Shifting the oversupply issue (sale & purchase)
- Permanently reducing supply (scrapping / recycling)

Short Term: Stacking Vessels



Dramatic Fall in Daily Charter Rates

- Daily charter rates have been falling fast across all regions, anywhere between 33 to 60% drop.
- Regions with the worst DCR hit is North Sea (60%) and South East Asia (50%).
- Number of charters have also decreased significantly, giving rise to idle vessels and those able to find work are committed at much lower rates, insufficient to sustain operations.

Short Term: Stacking Vessels

Operating Costs Across Different Modes of Operations		
Active Operations	Warmstacking	Coldstacking
Crewing Payroll	Reduced Crewing Payroll	No Crewing Costs
Ship Stores	Ship Stores	No Ship Stores
Logistics	Logistics	No Logistics
Maintenance	Maintenance	No Maintenance
Fuel / Lubes / Water	Fuel / Lubes / Water	No Fuel / Lubes / Water
Insurance	Insurance	Reduced Insurance
Agency	Agency	Increased Agency (Layup)
Overhead	Overhead	Overhead
Depreciation	Depreciation	Depreciation
		One-Time Costs
		Vessel Reactivation Cost
		Crew Retraining Cost

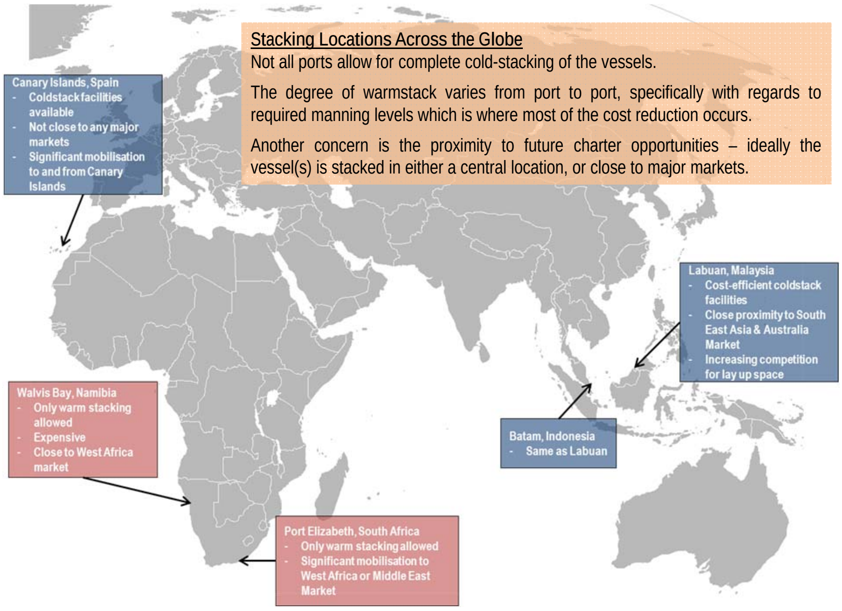
Warm vs Cold Stacking

Charter rates and utilisation have fallen to the point where it may no longer be financially viable to actively operate vessels.

Warm & coldstacking of vessels can bring about different cost saving opportunities. One-time costs associated with coldstacking strengthens the argument for a longer stacking period (6-12 months), so that these fixed costs can be spread over a longer period of time.

Clarksons reports that more than 600 OSVs have already been laid up globally, however this figure is believed to be closer to 1,000.

Short Term: Stacking Vessels



Medium Term: Sale & Purchase

Geographic MODU Demand Trend					
	2012	2013	2014	2015	4-year Average
North America	15%	10%	-3%	-19%	0%
South / Central America	-4%	-1%	-8%	-11%	-6%
West Africa	3%	2%	-3%	-18%	-4%
North Sea	6%	3%	4%	-13%	0%
Mediterranean	7%	14%	-4%	-4%	+3%
Middle East + India	13%	12%	-4%	-6%	+3%
Asia Pacific	-2%	11%	1%	-18%	-2%

Data Source: Clarksons Platou Offshore Intelligence Monthly (March 2016)

Vessel Second-hand Market

- Regions like Mediterranean, Middle East & India are showing less drop off for MODU demand than other regions.
- Despite the depressed market, flexible charterer requirements in these regions allow for absorption of older tonnage in offshore activities, making them prime second-hand markets.
- Buyers from these regions are taking advantage of depressed prices to buy low cost vessels, often on the back of contract commitments.
- Some of the regions identified often have restrictive cabotage regulations which will preclude a foreign vessel operator from working there in the first instance, ensuring less of a "crossing of interests" between the Buyers and Sellers.
- By selling vessels into these regions, Sellers are removing supply out of their normal operating regions, possibly on a medium to long term basis.

Medium Term: Sale & Purchase

Fierce Competition Within S&P Market		
Availability for Sale	Newbuilding Resales	Second Hand
PSV (<600 sqm)	14	39
PSV (600 - 850 sqm)	85	47
PSV (>850 sqm)	13	26
AHTS (4,000 - 8,000 bhp)	58	85
AHTS (8,000 - 12,000 bhp)	9	39
AHTS (>12,000 bhp)	19	66

Data Source: Clarksons Platou (March 2016)

<u>Competition within S&P</u>

- Oversupply is also depressing sale values.
- Newbuilds' resale predominately built in low cost Chinese shipyards is putting pressure on S&P values of older tonnage.
- This also presents a cautionary tale against new building fervour & speculative building during the upturn.

<u>Challenges to Selling Older Vessels</u>

- Less Interest / Appeal to Buyers – Charterers across regions are setting increasingly stricter age mandates (10/15/20 yrs) in their tenders, which make older vessels a lot less marketable.
- Newbuilding Competition – Currently, there are a large number of newbuilds for resale in Chinese yards, as a result of speculative building during the last upturn. These can be available for a fraction of their build price and comparable to second-hand sale prices.
- Large Write Down – As the older vessels are sold at a substantially reduced price, companies end up having to take a large write down on book values of these vessels or incur losses on disposal. This is particularly true for vessels built during the boom period at inflated prices.

Long Term: Recycling / Scrapping

Scrapping of OSV vs MODU					
	2011	2012	2013	2014	2015
MODU	14	25	10	31	46
% of Total MODU	1.5%	2.6%	1.0%	3.0%	4.5%
OSV	18	26	29	40	37
% of Total OSV	0.6%	0.9%	0.9%	1.2%	1.0%

Data Source: Clarksons Platou Offshore Intelligence Monthly (March 2016)

<u>Recycling / Scrapping</u>

Only way to lower supply in the market is to take vessels out of circulation by recycling / scrapping them;

- Number of OSVs being scrapped has been very low over the last 5 years, thereby contributing to the oversupply issue.
- Scrapping of MODUs, on average has been around 2.5 times more than that of OSVs in recent years.
- Fall in demand is thus 2.5 times greater than the fall in supply.
- With 30% of the OSV fleet 20 years and older, there is a huge potential for scrapping in the OSV market.
- The important takeaway is that the only way for day rates to rise is for there to be a continuous removal of supply, mainly through scrapping of older / obsolete tonnage.

Recap: OSV Oversupply Issue

SHORT TERM

LONG TERM

MEDIUM TERM

<u>Future Outlook of OSV industry</u>

- Oil prices still in the doldrums, widely believed to be another couple of years before market recovers.
- The issues of oversupply means the industry will not be able to tap into the increase in oil prices even when it rebounds, and charter rates will remain low as there will still be too many vessels competing for work.
- This represents a secondary lag, resulting in Owners having to wait another couple of years after the oil price recovers for the supply / demand dynamics in the OSV industry to normalise.
- Therefore, it is important that we act now to tackle this oversupply issue.
- By reducing the oversupply issue in the interim, we will be able to keep charter rates at a respectable level while we wait for the storm of this oil crisis to pass.
- In the long run, this will better position our industry for the eventual recovery of the oil market, which may not necessarily rebound to the last upturn levels.