Lloyd's List

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Printed By **Declan Bush**

From lay-up to order boom: Car carriers race to replace flagging fleet

Last year car carriers were in lay-up, having struggled through a decade of abysmal earnings. But with sky-rocketing rates and an orderbook worth about $4bn-$6bn, depending on how much of the hyperbole you are prepared to believe, the niche car carrier market is turning heads

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ONLY 12 MONTHS AGO THE SECTOR WAS IDLING VESSELS AS COVID SHUTDOWNS RAVAGED DEMAND.

FOLLOWING a decade of overcapacity and dire rates, the car carrier sector has collectively and simultaneously leapt at the opportunity to replace its ageing tonnage, spurred on by car manufacturers demanding eco-credentials and a rare window of profitable operations to justify investment.

The confirmed orderbook for this niche segment is approaching $4bn of largely liquefied natural gas dual-fuelled vessels due to start hitting the water from late 2023.

If the more hyperbolic assessments of orders that remain options, or unconfirmed and unfinanced letters of intent, are included, then the shopping spree gets nearer to $6bn.

Either way it is an impressive turnaround for a sector that anticipates at best modest long-term growth in demand, and only 12 months ago was idling vessels as Covid shutdowns ravaged demand.

Global auto sales are still hobbled by the current supply deficit in microchips, but even with such headwinds pent-up cargo demand from auto dealerships looking to replenish depleted stocks unfulfilled on top of their usual monthly seaborne import orders has turned the now undersupplied market on its head.

Global light vehicle sales forecast by reg

Source: Wards Intelligence/LMC Automotive

Vessels that were barely scraping time charter rates of $7,000 per day in the fourth quarter of 2020 are currently being fixed at $35,000 a day on three-year charters.

Firmed rates of $30,000 per day for even midsized 5,000 ceu vessels are yielding their owners earnings before interest, taxes, depreciation and amortisation of $8m-$10m a year after OPEX.

And the market is not cooling down any time soon. Based on the underlying lack of tonnage, current market conditions could last at least into 2024 when the majority of recent orders start delivering.

The car carrier sector entered the financial crisis in 2008 with an orderbook for more than 40% of capacity. Following a decade of surplus tonnage and lacklustre demand growth the market had just started to balance into growth at the point that Covid shut down the entire sector within a few weeks.

European car carrier operators idled entire fleets or drydocked early and by March 2020 companies were reporting that at least 60% of the market had effectively disappeared.

Companies that had tabled fleet replenishment plans eyeing the beginnings of a supply-demand realignment prior to Covid were forced to put plans on ice in the wake of the pandemic.

Despite an average age of nearly 13 years and a sizeable chunk of the market's 1990s-built fleet destined to be eliminated once the Energy Efficiency Design Index for existing ships kicks in in 2022, orders averaged just five vessels per year between 2016 and 2021.

On top of this, since the latest period of reasonable market earnings for which you would have to go back as far as 2011-15, the midsize fleet (4,000-6,000 ceu) has declined 27% and most other segments have declined by single-digit figures.

Global light vehicle sales forecast: Top 2 markets

So once the pure car and truck carriers (PCTCs) started breaking lay-up last year on improving demand, a good share of the panamaxes were quickly fixed for 12-24 months period and the upwards trend in the charter market has continued throughout the second quarter of 2021 with rate levels not seen in nearly 8 years.

Most of the major PCTC operators and tonnage providers including Eastern Pacific and Zodiac have already placed orders and although there is room for more to come, the lack of available newbuilding delivery slots before late 2024 will stagger the influx of tonnage. Short supply is set to drive rates for some time to come.

Despite the multi-billion dollar price tag on the current orderbook, once it is firmed up it will still only represent around 7% of the current fleet, which is firmly in the realms of necessary fleet renewal for a historically underbuilt and ageing sector.

Vehicle Carrier delivery schedule ($bn)

The other major dynamic shaping the market is the demand for more efficient tonnage from the auto manufacturers.

The fact that the vast majority of orders are for LNG dual-fuel is no coincidence. Tonnage providers report that their customers have made it clear that employment will be prioritised to dual-fuelled vessels which in most designs offer 25%-30% efficiency savings on the generation of ageing PCTCs operating today.

Once a handful of PCTC orders had been justified by increased earnings the reinvestment case was made and lemming-like the entire market piled in with orders. While that flurry of contracts has now slowed analysts agree there is potentially still room more further fleet replacements once those vessels facing the breakers yard due to class renewal, ballast water retrofits and the impact of EEXI in November next year force fleet removals.

If further orders do emerge it will be at a slowing rate squeezed by the midterm microchip shortage, which is holding back what would otherwise be an even more extraordinary period of sky-high rates to rival the container sector boom.

Most automakers have an inventory of completely built autos bar missing microchips. The chips deficit is partly caused by the auto industry itself cancelling orders during the Covid lockdowns in 2020, and that combined with a significant increase in demand for consumer electronics during the past year.

Some estimates indicate a loss in auto output in 2021 close to 4m units and while that production is forecast to improve mid-term, the bottlenecks are weakening demand, putting PCTC operators in a stronger negotiating position with shipyards.

Vehicle Carrier fleet age profile (number of vessels)

It is worth pointing out that the auto industry constitutes less than 9% of the global chips market while revenue is even lower so this is not considered a growth market for the chips industry and is therefore by no means a priority. Much of today's car production is still reliant on chips designs that are over 15 years old.

While auto analysts remain hopeful, some have already warned that the chip capacity challenge might create a cap on auto output well into 2022 and beyond.

The Association of European Vehicle Logistics meets in Brussels later this week for its annual conference where "strategies for survival" is the agenda topping topic.

"The industry is staring into the abyss as volumes continue to decline, demand fluctuates and forecasts are almost non-existent," read the uplifting agenda statement, which baldly states that the current microchip crisis "threatens the very existence of the logistics industry that moves new cars".

Beyond the chip shortage the long term forecast suggests that outside of the mature US and European markets where only the electric vehicle replacement offers limited growth, China will continue to rise in terms of seaborne trade volumes. It remains, however, the modest overall growth that will require the car carrier sectors to be mindful of previous cyclical misfires and keep the supply demand equilibrium firmly in sight this time round.