Tankers Presenting A Buy-Low Opportunity

When I last wrote about crude oil tankers, in July 2011, I could talk about devoting excess shipping capacity to the purposes of floating storage. The crude oil futures market was in a deep contango then, meaning the crude oil could be sold forward at a price sufficient to cover the costs of storage.

Those days have come and gone; the crude oil futures market is backwardated, meaning the holder of floating inventory would have to sell the futures for less than the spot price, and refining margins are narrowing to the level where selling the refined product futures forward to lock in both the crude oil price and the refining margin no longer is the slam-dunk it once was. Tankers will have to earn their keep the old-fashioned way, by moving crude oil from Point A to Point B.

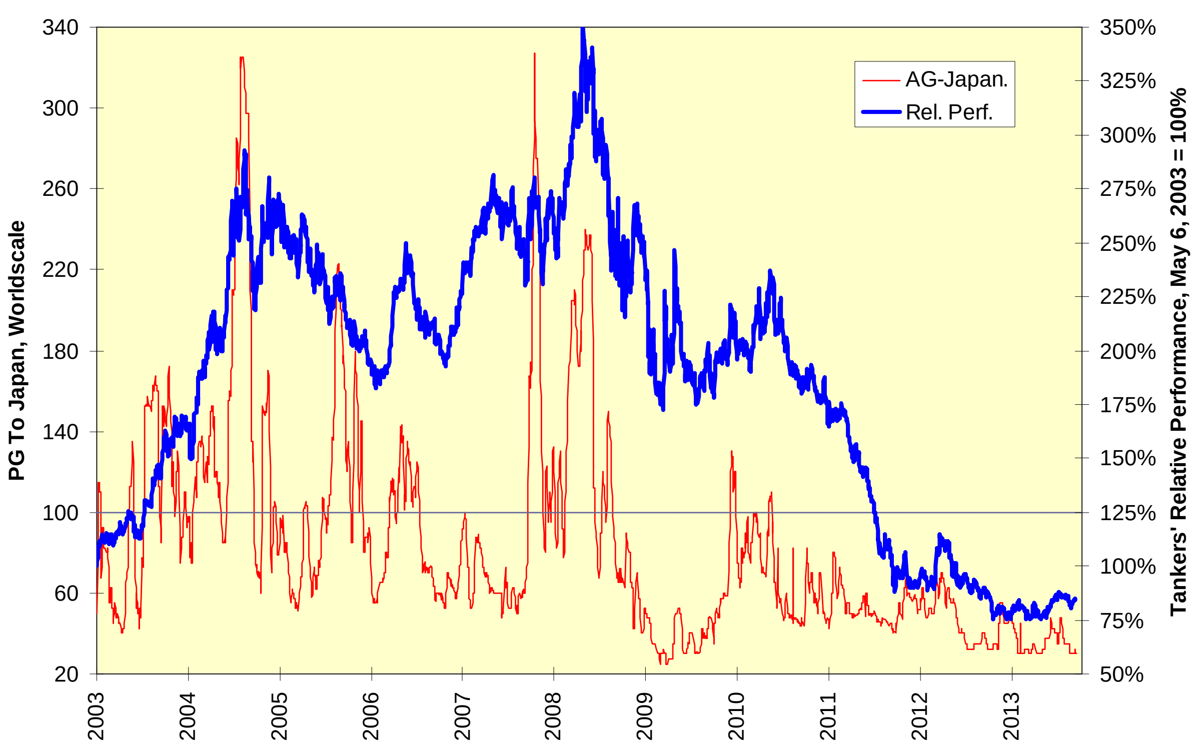
Tankers' Relative Performance

On the surface, which is where you hope your tanker remains en route, the industry remains in overcapacity. The supply overhang in the Persian Gulf for nominations over the next thirty days has remained more than 20% since the end of July; this is the highest level of overcapacity since March.

Moreover, tariffs between the Persian Gulf and Japan continue to scuttle along near their post-crisis lows. These tariffs are measured using the Worldscale index wherein 100 is set to industry's expected level. If reporting prices based on what an industry panel seems odd, it is.

The most certain sign of a market bottom is when stock prices refuse to fall on continued bad news. Let's compare the total return of the *Bloomberg* index of tankers, which includes Frontline (FRO), General Maritime (GMR), Nordic American Tankers (NAT), Overseas Shipholding (OSG), Teekay (TNK) and Tsakos Energy Navigation (TNP) to that of the MSCI-Barra World index. It stopped its rapid rate of decline in the fall of 2012 and has been moving higher since May.

Incremental Performance And The Persian Gulf-Japan Tariff



While some of this improvement in relative performance can be credited to the softness in the MSCI-Barra World index during the era of Federal Reserve policy confusion, some of this is in response to a much stronger market for crude oil itself. Dubai Fateh Blend, the key benchmark for Persian Gulf crude oil moving eastward into Asian markets, has increased almost 15% since April. Stronger prices in the absence of supply shocks are a function of rising demand, and this demand ultimately will reduce the tanker market's overcapacity.

Finally, the tanker market has some of that margin for error Benjamin Graham disciples love. It disconnected from the MSCI-Barra World index in 2010 and sat out the global bull market of 2012-2013. While no one should fall into the trap of thinking unloved stocks are a good buy simply because they are unloved, which index below has discounted three years of bad news and has outperformed the other since March by 17.3% to 7.4%?

Tankers Sat Out Most Of 2012-2013 Global Bull Market