November 2017 www.nautinst.org

Seaways

The International Journal of The Nautical Institute

Heading south

Are relations between ship and shore on the rocks? **p14**

The Nautical Institute

Overtonnage – a recurring nightmare

Overordering and underuse of tonnage is a familiar cycle in the shipping industry – with serious safety and environmental implications. Is it time for a radical solution?

Capt Naveen Singhal
MNI

A ship is built over a period of many months, utilising huge amounts of resources, and resulting in the emission of millions of tonnes of CO_2, both directly and indirectly. Demolishing that vessel well before the end of its life cycle for want of a charter is a pitiable situation. It is also against the fundamentals of environment and sustainable development. But how can we expect a shipowner to be concerned about the environment if the survival of the business is at stake? The same applies to vessels which are put in cold lay-up, which deteriorates the condition of a vessel and accelerates the aging process as well.

On the one hand, IMO has a number of environmental initiatives aimed at reducing the overall carbon footprint of the maritime industry. On the other hand, these initiatives are nullified by demolishing ships well before they reach their planned 'recyclable age'. Can't shipbuilding be planned in a manner which is consistent with tonnage demand? If regulators can intelligently work out an 'out of the box' solution, since there is no solution within the box, then owners will not need to resort to demolishing their assets in such an untimely and environmentally unfriendly manner.

Sustainable development and the UN

The UN's Millennium Development goals aim to make poverty history though pressing for sustainable development of humanity and conservation of resources. Interestingly, just the reverse seems to be happening in the shipping industry.

If we look at the maritime industry in terms of an Environmental Impact Assessment (EIA), the significant environmental aspects which would emerge are:

- Resource damage (Ships being demolished at half the expected age);
- Resource depletion (Ships lying idle subject to aging, corrosion);
- Damage to seafarer health and welfare through joblessness.

These environmental impacts contradict the fundamentals of growth and sustainable development as established by the UN Millennium Development goals, the UN Framework Convention on Climate Change (UNFCC), GRI's sustainable development principles, the World Bank Group's Global Environment Facility Program, the triple bottom line framework and, last but not least, common sense.

The situation in figures

According to BIMCO figures, average fleet growth from 2007 to 2015 was 8.6% (45 million dwt) per year. Demand growth for the same period was just 4.5% per year. During the period January to November 2016, demolition figures were 841 vessels or 41.3m dwt. This exceeded the 2015 total of 38.9m dwt.

In 2016, Rickmers demolished two Panamax container vessels, built in 2007 and 2008, after less than ten years of service. On the basis of back of the envelope calculations, a Panamax in 2007 would have cost about USD 70 million, with a sale price in 2016 of about USD 5.6 million. This is just one case where prominent ship owners are dealing with severe volatility.

Maritime Strategies International (MSI), an independent research firm, has forecast a stormy road to recovery for the shipping sector due to excess tonnage. In the tanker sector, for example, high supply of ships leads to a VLCC daily charter rate of USD 5000, which does not even cover operational expenses. On the other hand the same VLCC in a low vessel supply market could command USD 100,000 per day – which does not make economic sense to the charterer. This extreme volatility attracts fly by night 'investors' (who might perhaps be better termed 'intelligent gamblers'). They enter the market at rock bottom, make their money on the rising market and sell the asset just short of the recession, leaving the sound, committed and traditional ship owner in a quandary.

According to Bjorn Højgaard, CEO of Anglo Eastern Group: 'From a point of view of management of the asset, it is detrimental to have wildly fluctuating vessel values and thereby also fluctuating life spans of ships depending on market conditions. Many people think that a surplus of tonnage is good for a ship manager (as there are more ships to manage) but as a ship manager, much of how we create value is by taking good care of the asset over the long haul. This purpose is at odds with a situation in which one year, a shipowner wishes to starve the maintenance budget and the next year he wishes to upgrade the condition of the ship, based on volatility of freight markets. For us, who try to manage ships and their human resources through the ups and downs of shipping, it would be much preferable if the earnings were positive and stable and not as volatile as it is in this over supply of tonnage.'

Other negative consequences of excessive tonnage include low freight rates, which may even result in earnings below operational expenses. In some cases, budget constraints will have further consequences for the safe operation of a vessel.

- Safety standards and safety are put on the back burner;
- Training budgets are frozen;
- Machinery maintenance takes a hit, resulting in more incidents and breakdowns;
- Seafarers' wages suffer, which could lead to dissatisfied seafarers and below par performance.

Ultimately, we could see more maritime accidents, leading to more severe environmental consequences.

Setting a precedent

In a BIMCO market analysis published in May 2016, BIMCO President Phillippe Louis-Dreyfus said 'We really need to demolish an enormous number of ships and refrain as much as possible from

building new ships.' He went further, saying 'Buy one, scrap one'. Brilliant! But could it be done?

In the 1970s and 1980s it was common practice to flood the market with cadets. This led to an oversupply of seafarers, excessive unemployment, and low wages. If during those years someone had suggested the need to balance the supply of seafarers entering the industry with the demand (based on number of ships in operation), the industry would have laughed. This would not have favoured owners, since an oversupply of seafarers gives them the means to control 'seafarer wages'.

Today, this approach is against the ILO-MLC 2006 guidelines. Section B 1.4.1 (3)e of the ILO MLC 2006 code recommends that flag states monitor the supply and demand of seafarers and maintain a balance to ensure fair and sustainable development of seafarer numbers.

In a similar manner, IMO needs to control tonnage growth, or the shipping industry will become synonymous with recession due to excessive tonnage. This would become a self-perpetuating cycle, deterring young people from choosing the sea as a career, and diverting potential investment to other industries.

Why IMO?

While IMO does not have a role in providing business solutions to ship owners, controlling and ensuring a balance between the 'supply' and 'demand' of vessels will quite certainly improve the industry for all interested parties, and for society as a whole.

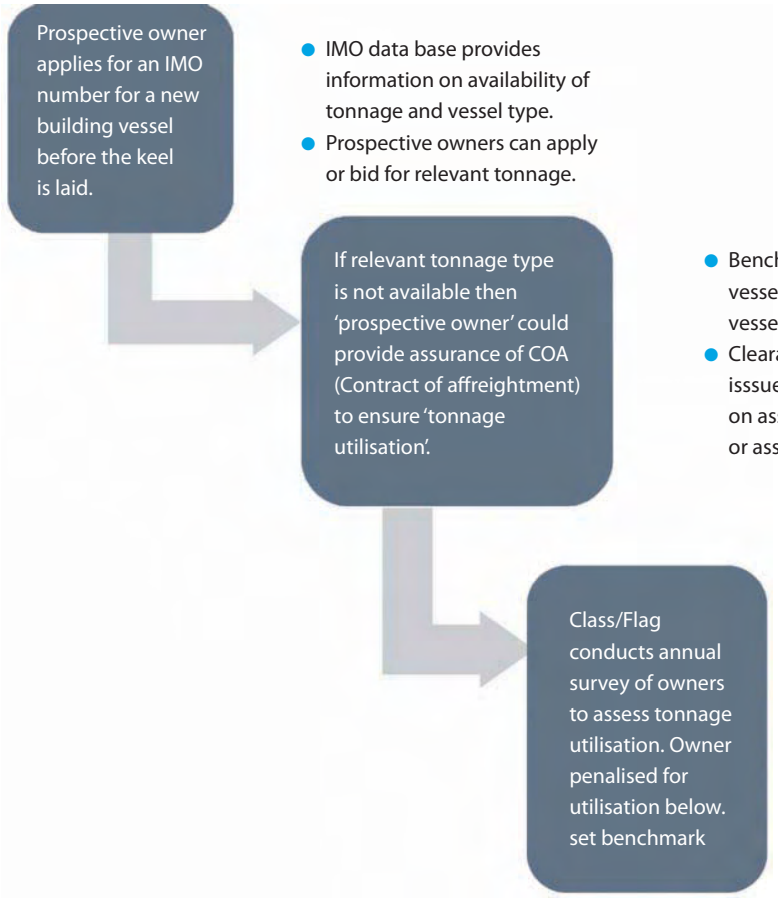
The negative impact of an imbalance in the supply/demand of ships and cargo has a direct impact on five of the 17 Sustainable Development Goals (SDGs) of the United Nations. As a UN body, the IMO cannot shy away from the responsibility of supervising how the 17 SDGs will be implemented. The five relevant goals are as follows:

- **SDG Goal 1 – No Poverty:** Seafarers will be in poverty if they do not get jobs;
- **SGD Goal 3 – Good health and wellbeing:** Shipowners will find it difficult to adequately support the good health and wellbeing of seafarers if they are not financially sound;
- **SGD Goal 8 – Decent work and economic growth:** Shipowners must make adequate profits if they are to ensure decent work and conditions. Economic growth is only possible if we can prevent the deflation of the shipping industry;
- **SGD Goal 12 – Responsible consumption and production:** Irresponsible 'production' (ordering and building of ships), unconnected with 'consumption' (cargo carriage requirements) is the 'root cause' of this cyclic recession;
- **SGD Goal 13 – Climate Action:** The untimely demolishing of vessels is leading to a significant amount of carbon emissions.

Oversupply of tonnage has a direct impact on the earnings of a ship owner, and thus their ability to implement safety and environmental protection. Hence it is an essential responsibility of IMO to set the rules of the game, and ensure that flag states monitor them and industry follows them.

It is difficult to imagine another international body able to undertake a role of such immense significance to the maritime industry. IMO does not stand as a policeman, but establishes the law in collaboration with flag states. It cannot put its head in the sand and believe that ships will remain safe and the oceans will remain clean while merely recovering operational expenses is itself a herculean task. In such times, safety and good environmental practices go out of the window.

Flag states, which are the pillars of IMO, have to get together to figure out the 'tonnage available', 'tonnage required', 'cargo available', then agree on some form of regulation to control and monitor ship building – a process that might look something like the diagram below.



The process would be as follows:

A-Conduct an assessment of cargo:

1. Assess estimated global movement of different cargoes:
a. Oil, LPG and LNG
b. Bulk cargo
c. Container cargo
d. Offshore Vessels
e. Other ships (Reefer, livestock, etc.)
2. Assess the estimated growth in cargo movement.

B-Conduct an assessment of tonnage:

1. Assess available tonnage basis cargo/vessel type
2. Assess expected demand of tonnage based on cargo growth
3. Assess tonnage and type of vessels which are being demolished.

Based on A and B, the vessel type and tonnage required can be determined.

Regulating tonnage:

Following this assessment, the model shown on the previous page could be applied (All ships below GRT 500 exempted).

Perhaps it would be possible to create a forum involving IACS and Class to monitor the implementation of the regulations.

This would create a win-win situation:

- Owners would be able to earn a reasonable value for the money they invest;
- Operators would be able to maintain and sustain basic minimum safety and environmental standards;
- Freight rates paid by the shipper would fluctuate within reasonable inflationary limits;
- Seafarers can expect reasonably good salary and service conditions for the service they provide in harsh and unsafe conditions.

We have to think out of the box if we are to ensure a steady market as opposed to a highly volatile market full of uncertainties.

Is anyone listening on the Albert Embankment?

Historically, the IMO has acted on the environment under pressure from the international community. It is now time that, as the international marine body of the UN, it does something concrete to control tonnage. Only this can prevent the vicious recessionary circle which might otherwise jeopardise the usefulness of the maritime industry and the very existence of responsible shipowners. We have seen several big names in the shipping industry vanish in the last few years, and some of those who are still flying the flag are considering turning away from their 'shipowning' status. The shipping community – shipowners, seafarers, shippers, manning agents and others – looks to IMO for its survival. The author hopes that IMO will not disappoint them.

Blue sky thinking is needed to ensure a safe, environmentally responsible – and profitable – future