

Certainty in uncertain

Duncan Jeffcock of Voyager Maritime Payment Systems explains how the current crisis in the financial markets and the lack of credit availability is affecting the bunker sector; and he offers a potential solution



Captain Duncan Jeffcock is global marketing director for Voyager Maritime Payment Systems, with responsibility for promoting the Voyager solution to the global bunker industry whilst building an international network of regional marketing managers.

Duncan's previous roles have included director of operations and commercial operations management within large shipping companies following a successful seagoing career spanning 28 years.

Contact:

Duncan Jeffcock
Voyager Maritime Payment Systems
Tel: +44 20 7790 0225
Email: Duncan.jeffcock@voyagermaritime.com
Web: www.voyagermaritime.com

A staggering \$14 trillion – or 90% – of international trade is handled on credit. That's a remarkable statistic in light of the current turmoil in the financial markets and a general decline in credit availability. International trade has felt the bite of the credit crunch in recent months as graphically demonstrated by the catastrophic collapse of the freight markets. According to London's Baltic Exchange, the dry bulk market has seen a drop of more than 80% in freight rates since June whilst the tanker market has fallen by 60%.

This is particularly relevant for the bunker industry, where fuel accounts for up to 70% of a vessel's operating costs. As freight rates fall, so does the profitability of charters. When daily charter rates were \$200,000 for a Capesize vessel and the bunker bill was a fraction of that, meeting the cost of the fuel caused no difficulty. Now charter rates have plummeted to \$10,000 or less a day, the bunker bill – and the ship operator's ability to pay – has become very significant.

Volatility and uncertainty over the cost of marine fuel has further exacerbated this problem. The recent fall in the crude oil price has, admittedly, been tracked by a lower bunker price, but the long term trend remains upward. Industry commentator Robin Meech of **Marine and Energy Consulting Ltd** believes that 'we must not think short-term, the underlying trend for bunker prices continues to be upwards with a reasonable expectation of reaching an average of \$900 a tonne by 2025. The requirement for lower sulphur emissions will force prices to rise, irrespective of the crude oil market'.

Higher bunker prices coupled with much lower freight rates have the potential to cripple the vessel operator. It is equally bad news for the fuel supplier who now runs the increasing risk of late or even non-payment. A credit survey recently conducted by **Petrospot Ltd** highlighted that the industry currently experiences bad debts approaching 18% and that is highly significant for an industry worth more than \$130 billion (see *Bunkerspot*, October/November, page 26). Late payment squeezes profit margins, reduces return on capital and increases the resource that needs to be applied to chase outstanding payments.

Even the traditional risk management

option of buying credit insurance is becoming much more difficult to achieve. Already this year, a leading supplier of industrial credit insurance claims to have withdrawn from the marine market and it is rumoured that others are following suit. The *Petrospot* credit survey concluded that around 22% of suppliers were credit insured but that this figure was likely to rise in the future. Meech agrees and believes that demand will increase dramatically as suppliers begin to lose confidence in their customers' ability to pay. But, he warns, in this climate adequate cover will be more scarce, premiums will rise rapidly and the conditions attached will be necessarily more onerous.

This volatile business environment makes it ever more important for vessel operators and fuel suppliers to identify new ways to manage costs, increase their available income and improve their access to capital.

Introducing a trusted and well-capitalised third-party into the bunker sector injects liquidity as well as reduces or eliminates the risks inherent in extending credit to facilitate a transaction. This may well be the solution suppliers and operators should be seeking. According to Greg Foust, Senior Vice President of Corporate Payment Systems Risk Management at **US Bank**: 'By providing credit directly to operators, a third-party financier would protect a supplier's credit portfolio and offer faster payment to the supplier. This would provide suppliers with additional liquidity allowing them to spend available funds on daily operations or to expand their business.'

A major Singapore-based supplier was quoted recently on *Reuters* newswire as saying: 'The main problem for us is getting money to do our trades, it's hard to get credit nowadays.' Unlike the oil majors and larger national oil companies, mid-tier bunker suppliers (who account for around 46% of all delivered fuel) rely on available credit to enable them to operate their business. If such a third-party facility could also guarantee that the supplier gets paid within a reasonable time – say 14 days or less – then the supplier's ability to attract and retain credit from its own financial backers would be more certain.

As credit becomes scarce, buyers too would benefit since they wouldn't need to rely on their suppliers' ability to extend them credit for their fuel transactions. With lending

times

criteria tightening up and evaluation reviews becoming more stringent, being able to offer generous credit terms is becoming more of a necessity than a luxury according to Michael Bandy, CEO of **Chemoil Energy**, who recently told *Dow Jones*: 'Many small players could find tightening credit lines and volatile prices are the final straw.' A lack of credit has the potential to place a ship operator in a very difficult place, particularly if low freight rates make cash-on-delivery arrangements impossible. Using a higher priced or lower quality supplier are not attractive alternatives but better than having no fuel at all.

Another advantage of using such an intermediary is that suppliers could extend credit terms to their customers whilst they themselves would be paid within a shorter period. For example, a supplier might be able to offer 36 or 40 days credit to a customer but take payment for the fuel they deliver within seven or 10 days. In an increasingly crowded and competitive market place that

could be an important differentiator. Those able to offer more flexible terms are likely to win customers over those who have no option but to restrict their payment options. Petrosport's credit survey revealed that 30 day credit terms continue to be the norm but that increasing prices might reduce those terms to assist with cash flow. With a continued long-term upward trend in bunker prices for the foreseeable future, it seems likely that we'll see suppliers reduce their credit terms.

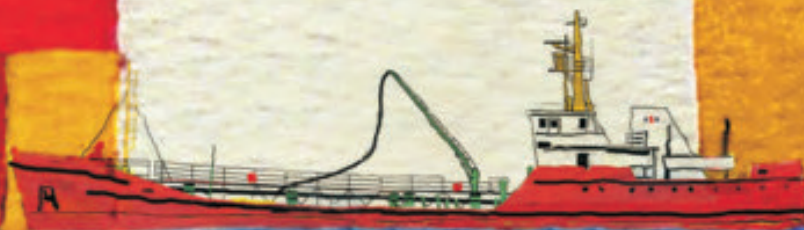
Introducing a third-party into the bunker transaction would also effectively remove the need for credit insurance to cover bunker fuel transactions. Aside from taking away the associated cost, the third-party system would eliminate the resources needed to handle these time-consuming activities. Risk management is often highlighted as a critical part of the business but managing risk and handling credit issues accounts for a significant portion of the working day for many in the industry – and that time could be better spent with

customers and on increasing sales.

It is unfortunate that the bunker industry is facing the double whammy of a credit freeze within a falling freight market. Without an available supply of credit offered on reasonable terms, many bunker buyers will soon find themselves unable to guarantee an adequate supply of fuel for their vessels. Similarly, suppliers who also rely on credit to run their businesses will face impossibly tough trading conditions. This will be exacerbated further when the flood of new building deliveries create their own tonnage crisis in a few months time. Sadly, some will not survive.

Having a new and independent market participant that is both trusted and well-funded would be a welcome and much needed addition to the marketplace. Acting as a clearing house, this intermediary would take on the credit risk and pay suppliers quickly whilst giving generous terms to buyers. And in these uncertain times this level of certainty could be a life-saver.

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