

LPG shipping rates have seen what can only be called a dramatic start to the year. The steep gains, followed by the freefall have dwarfed the volatility seen in 2020. As we move deeper into 1Q21, and China comes back into the picture after a long holiday, we do expect rates to find some floor. Meanwhile, the stock prices which are otherwise highly correlated, have shown remarkable resilience, seemingly immune to the recent fluctuations in the spot market.

**Figure 1** BLPG1 vs Drewry LPG stock price index



Source: Baltic exchange, Yahoo Finance, DMFR

### The rise

On 11 November 2021, the BLPG1 (representative of the Middle East Gulf to Japan route) was trading at 146.24 points. In November itself, before the start of winter, Japan's LPG stock had fallen by almost 6% month on month for the second month in a row, after logging gains for five consecutive months. However, as the winter kicked in and demand began to rise, imports skyrocketed, driven mainly by Japan, China and South Korea. On 18 January 2021, the CFR North Asia Propane prices jumped to a multi-year high of USD 687 per tonne from USD 482 per tonne on 25 November 2020. This was because January 2021 was on average 1% colder than the average of the January in the last decade for these three major OECD markets, which translated into a demand increase of roughly 1.25 mbpd of heating fuel over the same period in 2020.

This was further aided by shipping delays at the Panama Canal. Longer waiting times created a backlog for the Very Large Gas Carriers (VLGCs) waiting to transit the canal and subsequently disrupted the loadings in US Gulf. These delays coupled with a large number of dry-dockings (more on that later) propelled VLGC rates on the Persian Gulf-Japan route to USD 119 per tonne on 12 January 2021, the highest since 30 July 2014, when rates flirted with USD 120 per tonne levels.

**Table 1** LPG trade ('000 tonnes)

	Dec 19	YTD 2019	Aug 20	Sep 20	Oct 20	Nov 20	Dec 20	YTD 2020
<b>Imports</b>								
Japan	1,134	-	651	793	688	765	877	0
China	1,795	-	1,917	1,780	1,794	1,760	1,669	0
South Korea	834	-	598	697	650	621	659	0
India	1,227	-	1,240	1,643	1,428	1,396	1,510	0
US	537	-	347	443	442	477.9	-	0
<b>Exports</b>								
US	3,508	-	3,680	3,638	4,216	3,811	-	0

Source: Drewry Maritime Research

### The crash

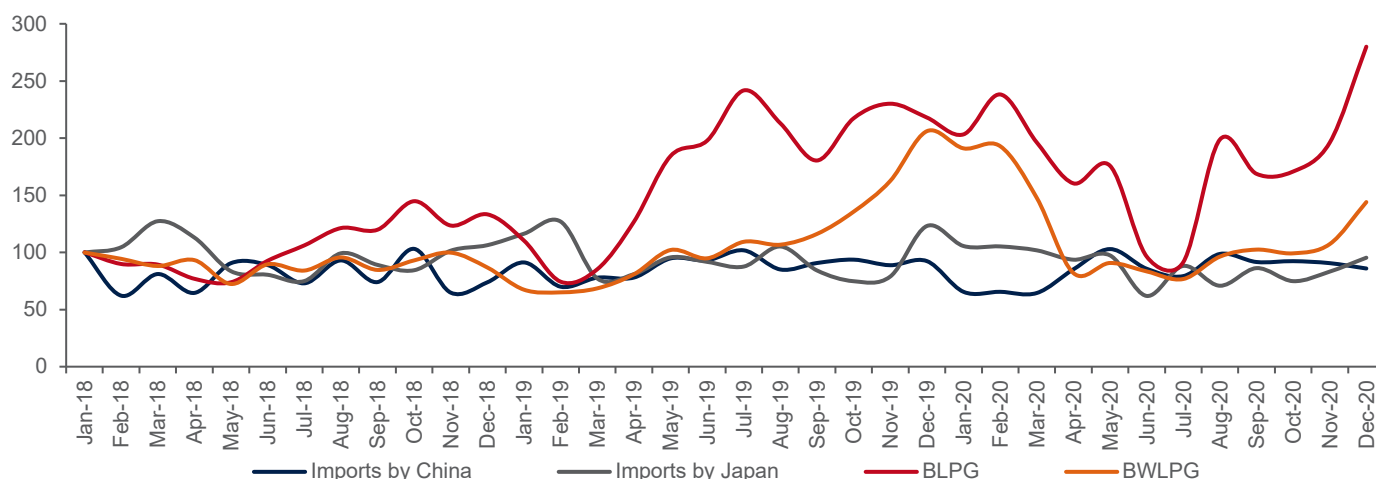
LPG shipping rates started the year with a bang, after a decent 2020 despite COVID-19 headwinds. The high rates could not be sustained as the VLGC rates extended their sharpest freefall in around two decades to USD 37 per tonne in mid-February. We may see further correction in the short term before a rebound or consolidation, primarily due to weak Asian demand, deferment of Saudi cargoes and bad weather conditions leading to the closure of the Houston ship channel. These factors led to arbitrage contraction as LPG prices fell in Asia, while they held their ground in the US and Algeria. The cancellations have led to better cargo availability, and subsequently, lesser fixtures on longer routes.

US LPG production has been resilient in the past couple of months. While data from local authorities shows that LPG production has almost normalised to pre-COVID levels in many parts of the country, US propane inventories are down year on year by an estimated 28%. Following this, approximately 10-11 LPG cargo loadings in February on US-Asia have been cancelled as the arbitrage has narrowed after a two-week retreat in Asian prices and disruptions caused by the closure of the Houston ship channel, which closed after 20 January 2021 due to fog and extreme weather conditions. The net impact was that US propane exports fell by 0.2 mbpd week on week to 1.26 mbpd in the week ending 22 January 2021. This translated to 13 VLGCs loading from US ports in the week, down from 20 vessels the week before. And the combined effect of these factors may continue into March, as US arrivals in Asia are expected to fall further to about 1.6mn tonnes in March from about 2.3mn tonnes expected in February.

As the unusually cold weather retreats in Asia, heating demand has plummeted. South Korea, one of the countries driving LPG demand, is estimated to have imported 8.47mn barrels per month in 4Q20 which increased to about 10mn barrels in January. Come February, the estimate falls to 9.5mn barrels, and further to 8mn barrels in March.

Combined global imports have historically shown a strong correlation with spot rates and stock prices. Two of the major OECD importers, China and Japan, have influenced the shipping industry, driving the LPG shipping demand. In case of sustainable paradigm shifts in terms of demand, the imports by these two countries have even acted as leading indicators on stock prices of operators such as BW LPG, that are primarily into spot market operations.

**Figure 2 Monthly imports (China and Japan) against BLPG and BW LPG**



Source: Baltic Exchange, Yahoo Finance, DMR, DMFR

Note: All the securities in the above chart have been indexed to 100 as of 1 January 2018

### Light at the end of the tunnel

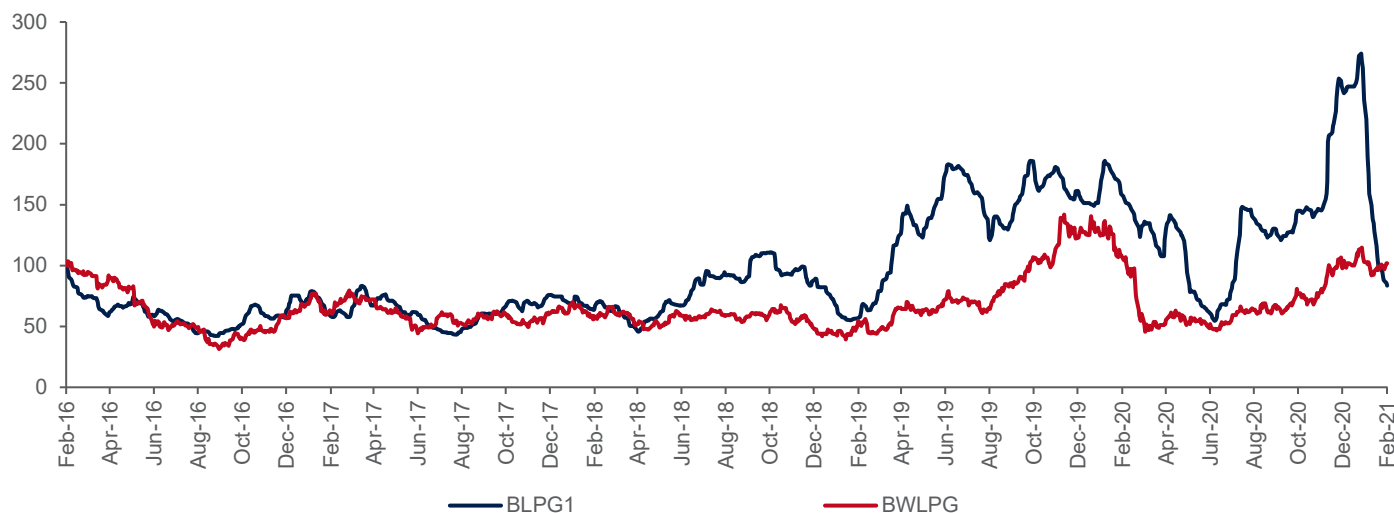
While there are several factors putting downward pressure on the LPG shipping market, it is not all that bad. The current freeze off is coinciding with China returning to the market after the Lunar New Year. Even if China draws down inventory in the short term, the country's 2021 demand for LPG is expected to rise by as much as 3.5mn tonnes over 2020. Therefore, even if China does not return to the import market immediately, LPG shipping has something to cheer from the world's largest importer.

The spot market also has something to look forward to from the supply perspective. As many as 90 VLGCs are slated for dry docking and special surveys in 2021. Of these, about 46 are scheduled in 1Q21 itself, according to some ship brokers. The packed dry-docking schedule can face certain delays as some of these ships are due for upgrades including dual-fuel LPG retrofitting.

### The unaffected, immune stock prices

The three stocks under our coverage, StealthGas (GASS), Navigator Holdings (NVGS) and BW LPG (BWLPG) have shown remarkable correlation with the spot market in the past. However, the recent rally barely made these stocks flinch; even BW LPG, which operates a spot market-dominated pure-play VLGC fleet, showed little movement.

**Figure 3** BLPG1 vs BWLPG



Source: Baltic exchange, Yahoo Finance, DMFR

The high correlation (0.90) in the last 52 weeks saw an unexceptional disconnect in December and January, during the steep rise and sharp fall. We believe this disconnect was mainly due to the two key factors behind the rise: inclement weather conditions at the Houston ship channel and strong winter demand. While these were two strong factors, they were temporary, not unprecedented, and too short-lived for most operators to take advantage of, as many ships are out of employment for dry-docking and dual-fuel LPG propulsion retrofits.

### Conclusion

All factors considered; the LPG shipping spot market has already had a turbulent year. The rise and fall of the spot market was unusual and short-lived, it was just driven by the usual factors all at once. As we move deeper into 1Q21, we do see some possible downside from current levels, depending on fixtures from China as it comes back after the long holiday. The downside however is limited, as vessel availability bottlenecks the supply. As we move further into March-April, we expect to see some consolidation, for both the shipping rates and stock prices.

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