War risk exclusions by insurers heighten stakes in Red Sea attacks

Tanker rates spike as more ships forced to make costly reroute

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Crude tanker rates are rising due to Red Sea risks. (Photo: Jim Allen/FreightWaves)

In early February, oil markets were lulled by hope of a now-unlikely ceasefire in the Israel-Hamas war. But a recent string of Houthi attacks have reignited concerns about the Red Sea crisis, raising the floor for tanker rates.

The Iran-aligned Houthis claimed responsibility for Friday's attack on oil tanker M/T Pollux, which was bound for India. No injuries were reported.

This and other recent Houthi attacks, which followed a brief pause in early February, led major maritime insurer Steamship Mutual to issue an exclusion for all war risk claims in the Indian Ocean, Gulf of Aden and Southern Red Sea.

According to S&P Global Commodity Insights, any new insurance issued for Red Sea routes could impact oil prices by $1 or more per barrel. The alternative of rerouting around Africa's Cape of Good Hope is arguably less attractive, resulting in rising operational costs as well as higher vessel utilization.

Very large tankers see massive rate growth

While many tankers have already chosen the latter option, some have persisted in braving the Red Sea. Per data from Clarksons, Red Sea arrivals of crude tankers are currently 50% to 60% of where they were in the first half of December.

Clarksons also reported that the average rate on a very large crude carrier (VLCCs, or tankers that carry 2 million barrels of oil) going from the Middle East to China has risen to three-month highs at $66,600 per day. The average rate for VLCCs in Q1 thus far has tracked closer to $41,000 per day.

This growth has been incredible, given that VLCC rates averaged under $21,000 per day last quarter and a measly $8,700 per day in Q3.

Still, VLCC rates are not strangers to such extreme rate swings: In 2019, a series of attacks in the Middle East and U.S. sanctions on Chinese tanker owner Cosco spiked rates from $25,000 per day to over $150,000 per day over a six-month period.

Analysis from Bank of America reports that VLCC rates are expected to hold between $40,000 and $50,000 per day in March, before dropping to $35,000 to $40,000 over the second quarter.

Tanker demand could coast on oil market shakeup

Rising oil demand, however, might sustain tanker rates at current highs going forward.

Oil prices have been largely unmoved by developments in the Red Sea so far, as fears of weak fundamentals and the ever-looming threat of a recession have outweighed geopolitical risks. In late January, prices refused to budge in response to a Houthi strike on a product tanker.

But some analysts are arguing that pricing targets are skewed by seasonal weakness. Per data from Standard Chartered, January's global oil surplus weighing on prices is a natural occurrence. In fact, only three of the past 20 years have seen January report a net inventory draw.

StanChart notes that January's surplus is far less than in previous years: Compared to the average build of 1.2 million barrels per day — and certainly 2023's near-record build of 3.4 million — 2024 has seen only a meager build of 300,000 barrels per day.

In short, StanChart and the Energy Information Administration argue that February is headed for a considerable deficit that should shock markets back into bullishness.

When this deficit is recognized, it is unclear who will rush to rebalance it. U.S. exports of crude oil are already up 21.6% over 2023 in the year to date, shipping 24.6 million barrels per day. According to domestic producers, the rate of output growth is expected to slow in 2024 after a gangbusters 2023.

Saudi Arabia recently canceled plans to expand its oil production capacity, largely due to its discontent with stubbornly low prices but also because of a desire to withhold supply for future domestic demand.

The crackdown on Russia's shadow fleet continues, as the U.S. imposed sanctions on four entities in early February for violating the G7's price cap on Russian crude. Bank of America analysts note that such sanctions are likely to spur demand in the legal tanker market. A senior official in the U.K.'s price cap enforcement agency stated that "what we want to do is force volumes back into the G7 fleet."

So, while tanker rate growth is currently expected to be transitory, it would not be a surprise if these gains were here to stay longer term.