

CHARTERING MADE EASY

By George Margaronis Managing Director of Clarkson Hellas Ltd.

The Basics

Chartering quite simply is defined as the hiring of ships. When an agreement is reached on the terms and condition of carriage between the parties involved, namely the owner of the ship and the charterer (cargo interest), a contract stipulating those terms and conditions agreed is drawn up and signed. The contract is called a charter party. The two most common types of employment for ships are voyage charters and time charters. Frequently intermediaries are involved in the process called shipbrokers. Voyage charters involve the payment of freight per ton of cargo transported on terms set out in the charter party which specify amongst others the precise nature and quantity of the cargo (exact or within a range), the port(s) of loading and discharging, the lay time (the time available to the charterer for cargo operations) and demurrage (liquidated damages payable by the charterer to the owner in the case of delays beyond the lay time agreed). All costs associated with and incidental to the performance of the voyage are borne by the owners and include bunker costs, port charges, canal dues and cargo handling costs where applicable. These costs are known as voyage costs. Time charters can be broken down into two broad categories namely time charter trips and period time charters. The time charter trip involves the hiring of a ship for a specific voyage of a specific cargo. Owners will at regular pre-agreed intervals (usually every 15 days) be paid hire, which is in most cases expressed in United States dollars per day. A period time charter would involve the hiring of the ship to perform multiple voyages and could be as short as a few months or as long several years in tenure. The voyage expenses mentioned above are borne by the charterers in the case of time charters. The operating costs that include such things as crew costs, insurance, repairs and maintenance, etc in both the case of voyage and time charter are borne by the owners.

Present Freight Markets

The demand for ships is a derived demand. The demand is not for the ships themselves but rather for the services that they are able to provide. The nature of the demand and supply curve is such whereby small incremental changes in demand or supply yield more than proportional changes in freight rates. This inelastic nature of the demand and supply curve explains the volatility that is so characteristic of freight markets. This volatility is more profound the further up we move on the supply curve as we approach full capacity utilization of the fleet with increasing demand, and a demand curve shifting ever outwards. There are two very simple reasons that explain the inelastic nature of the demand curve. The first is the lack of substitution for ocean transportation by other viable alternatives. The second is the relatively small portion that ocean transportations costs account for of the total price of the goods the commodities transported produce. On the supply side at any given moment in time the amount of available ships is given. The supply can change only very slowly as new buildings as delivered to their owners. The time from ordering a vessel until taking delivery would normally not be less than two years. Quantity is expressed in terms of million ton-miles, a function of tons and distance carried. As growth in industrializing China increased in momentum so did their demand for raw materials. Raw materials were necessary for the building of infrastructure and manufacturing units necessary to provide goods for domestic consumption but at the same time for export while they capitalized on the very low labor costs and consequently low cost of production. The net result was a huge increase in demand. Consequently freight rates reached levels unprecedented in the past and more importantly lasting thus far for the best part of four years. Chinese port infrastructure was unprepared for the huge influx of raw material arriving for discharge at their doorstep. At the same time the exporting countries in particular Australia were also struggling to cope with the sheer volume of quantities of coal and iron ore that needed to be exported. The result of the build up of tonnage on both sides (loading and discharging) lead to congestion, which in turn placed a constraint on the supply side, further increasing freight rates as a result. Looking ahead it seems that we will be experiencing high and volatile freight markets for some time to come and even though the growth rates in China may at some stage cool off and the world fleet has been growing at a healthy pace with minimal scrapping there is a very large proportion of overage tonnage that are potential scrap candidates. These will act as a safety valve relieving the market for any excessive downward pressure that may be experienced. All in all a new plateau substantially higher than that of past years will be established that will act as a support level for the market in the foreseeable future. Estimated to be twenty percent of the world's commercial shipping. Not bad for a little country on the periphery of Europe. Our initial commitment started when did the first of several special issues that coincided with the bi-annual Posidonia Shipping event, the industry's premier networking opportunity. We wanted foreign visitors to the event to get some insight into the workings of Posidonia while having a

practical guide on what to do and see while in Athens. Since the beginning Insider has maintained close ties to the shipping community in Greece and abroad. Many of our regular readers are engaged in the industry and tend to be dynamic, well-educated, well-traveled and internationally-minded Greeks, Greek somethings or just philhellenes. Insider is distributed each month at the Marine Club in Piraeus, a veritable beehive of shipping activity. Even though it is already the largest single industry in Greece shipping still has tremendous potential to benefit the country in so many ways. As the saying goes, a rising tide lifts all ships. Not only does shipping create wealth, employment and national economic well being but the fact that a small country like Greece, on the edge of Europe, could have such a profound impact on this global industry is striking. The tradition of shipping raises the international profile of Greece in a way that no advertising campaign, regardless of budget, could ever achieve. The image of Greece as a dominant player in the industry is based on accomplishments in the past and present. Achievements cannot be easily dismissed since being Number 1 requires an industry that is competitive, shrewd and visionary. That is why Insider accepted the invitation to be communications sponsors for the Shipping Forum and to help Capital Link in its efforts to promote the further development and competitiveness of the shipping sector through the event and hopefully to continue setting standards for the industry world-wide.