

# Transportation - Shipping

## 1Q Preview: Lower tanker ests on rates moderating; Focus remains on Product

Price Objective Change

### Lower 1Q estimates on rates moderating; returns in focus

We lower our 1Q23 EPS estimates for our product and crude tanker shipping coverage as we lower our rate forecasts, build in additional 1Q refinery maintenance downtime, and raise our operating cost estimates. We expect a slight moderation in rates and a step-up in vessel opex in 1Q to impact earnings, led by demand headwinds and inflationary pressure. However, given robust cash flow generation on historically elevated rates, we expect an increased focus on cash returns (buybacks, dividends) after carriers prioritized debt reductions in 2022. We reiterate our Buy on STNG and Neutral on TNK's shares, yet lower our POs to reflect a slightly more cautious outlook (STNG PO -4% to \$67 from \$70, and TNK PO -7% to \$43 from \$46). We lower our STNG 1Q23, 2023, and 2024 EPS estimates 31%, 13%, and 5%, to \$2.94, \$5.85, and \$2.05, from \$4.26, \$6.75, and \$2.15, respectively. We lower our TNK 1Q23, 2023, and 2024 EPS estimates 13%, 6%, and 5%, to \$3.65, \$10.05, and \$2.95, from \$4.21, \$10.70, and \$3.10, respectively.

### Refinery maintenance, OPEC+ cut a near-term overhang

Given an earlier and heavier US refinery maintenance cycle from February to May in 2023, Gulf Coast refinery runs were muted in 1Q with utilizations down to 85%-90% from upper 90s in 2022. This negatively impacted product tanker rates as LR2 (Long Range 2) time-charter equivalents (TCEs) declined to a \$40k/day range from \$80k-\$100k at 4Q22's peak. Scorpio Tankers, a Product carrier, sees rates as still highly favorable given the seasonal trough in demand compared to its \$17k/day TCE breakeven level. Alternatively, crude tanker rates held in better on a relative basis, as excess US crude production resulted in higher exports, given muted refinery activity. VLCC TCEs are in the \$60k/day range, down only slightly from 4Q22's \$65k/day average. However, we view OPEC+'s move to cut production by 1.16 mil barrels/day starting in May as an overhang, as lower volumes may consequently impact ton-miles. Middle East crude flows are primarily a VLCC focus, but we do see spillover rate impacts to smaller vessel classes (Suezmax, Aframax) given the addition of excess capacity to the market.

### Fundamentals intact; Focus remains on Product Tankers

Despite near-term demand challenges, tanker fundamentals remain favorable with record low orderbook-to-fleet ratios (3.9% as of April 7), as shipyards remain fully booked, and tougher emission standards. Tanker fleet growth is expected to average below 1% from '23-'24 according to Clarksons, while average speeds should continue to trend lower as carriers engage in slow steaming for older vessels to minimize environmental impact. As noted in our [Forum Takeaways \(see report\)](#), the increased demand for longer-term charters from counterparts such as Chevron, Exxon, and BP, is positive for tanker rate outlooks, and reflect shippers' desire to secure contracted freight capacity. We prefer the Product Tanker group given our view of its insulated demand drivers (refinery capacity dislocations, longer day-sailings given Russia export bans, US refinery capacity restarts) and a more constrained capacity view. Crude tankers should also benefit from China's 2H23 reopening and rising jet fuel demand. Nevertheless, crude tankers have a higher sensitivity to rising recession risks.

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### Abbreviations

STNG: Scorpio Tankers Inc.

TNK: Teekay Tankers Limited

VLCC: very large crude carrier

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**Refer to important disclosures on page 3 to 6. Analyst Certification on page 2. Price Objective Basis/Risk on page 2.**

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## Price objective basis & risk

### Scorpio Tankers Inc. (STNG; C-1-7; \$56.16)

Our \$67 price objective is based on an 6.2x EV/EBITDA multiple on our 2023 EBITDA estimate. Our valuation multiple is below the bottom of its 7x-14x historical trading range, as global mobility strengthens, pricing rebounds as inventories reach decade-lows, orderbook remains at historic-lows, and ton mile demand is rising. The negative impacts from COVID disruptions are fading (North America and Europe stronger, Asia stabilizing) though softening economic outlook may weaken demand for refined products. Our multiple is below the bottom end of its range as earnings are set to significantly compound.

Upside risks to our PO are volatile charter rates, better-than-expected spot product tanker rates in 2022-23, lower-than-expected vessel deliveries in 2022-24, a spike in global oil demand, and higher-than-expected levels of scrapping in the market.

Downside risks to our PO are drop off in mobility (return of lockdowns, war disruptions, which have shown to increase ton mile demand), liquidity risk given rolling debt through 2024 versus cash generation (which depends on day rates rising above the daily fixed cost base), a weaker-than-expected rate environment, overcapacity due to greater-than-expected vessel deliveries and lower-than-expected scrapping rates, and weaker global demand for refined products.

### Teekay Tankers Limited (TNK; C-2-9; \$40.82)

Our \$43 price objective is based on 3.2x our 2023E EBITDA. Our multiple is below Teekay's trading range (4.3x-8.1x) as crude tanker rate levels reach historic peaks as Russia's invasion of Ukraine drives longer-haul trade flows, inventories are at cycle lows, and orderbook remains at historic lows. The crude outlook looks to improve as mobility returns, though declining economic activity may weigh on demand.

Downside risks are: (1) Higher leverage levels, with exposure to cyclical and volatile spot market, (2) Risks to the global economy, (3) Risks of further OPEC production cuts and declining oil prices, (4) re-charter risk for vessels on charter.

Upside risks are: (1) a rapid upturn in spot rates, (2) continued debt paydown, or (3) M&A improving valuation for its assets and therefore NAV.

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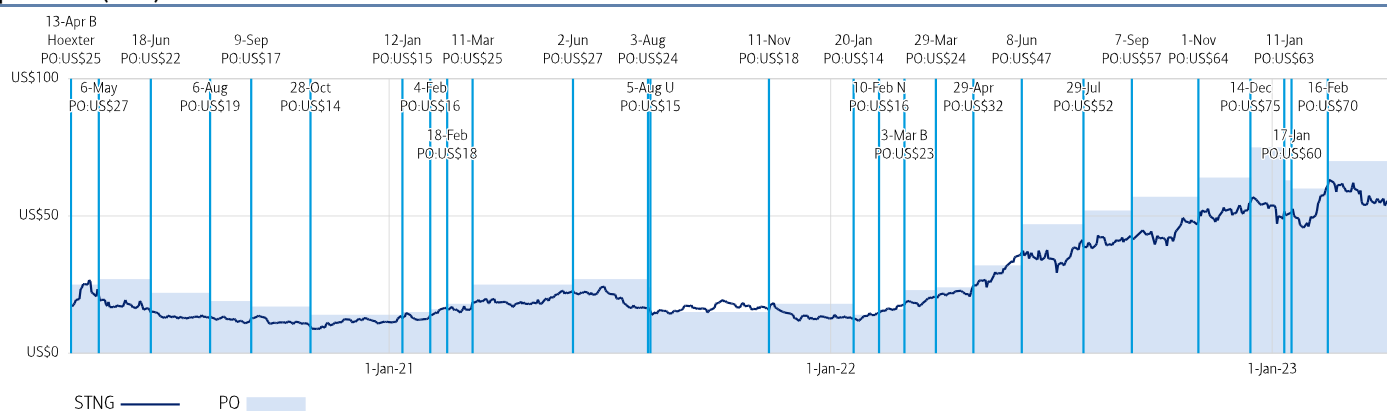
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Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
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	J.B. Hunt Transport Services	JBHT	JBHT US	Ken Hoexter
	Kirby Corp	KEX	KEX US	Ken Hoexter
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	Norfolk Southern	NSC	NSC US	Ken Hoexter
	RXO, Inc.	RXO	RXO US	Ken Hoexter
	Schneider National	SNDR	SNDR US	Ken Hoexter
	Scorpio Tankers Inc.	STNG	STNG US	Ken Hoexter
	Union Pacific	UNP	UNP US	Ken Hoexter
	Werner Enterprises	WERN	WERN US	Ken Hoexter
	World Fuel Services	INT	INT US	Ken Hoexter
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	Teekay Tankers Limited	TNK	TNK US	Ken Hoexter
	TFI International	TFII	TFII US	Ken Hoexter
	TFI International	YTFII	TFII CN	Ken Hoexter
	UPS	UPS	UPS US	Ken Hoexter
	Wabtec Corp.	WAB	WAB US	Ken Hoexter
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	TuSimple	TSP	TSP US	Ken Hoexter
	XPO, Inc.	XPO	XPO US	Ken Hoexter
<b>RSTR</b>				
	Triton International, Ltd	TRTN	TRTN US	Ken Hoexter

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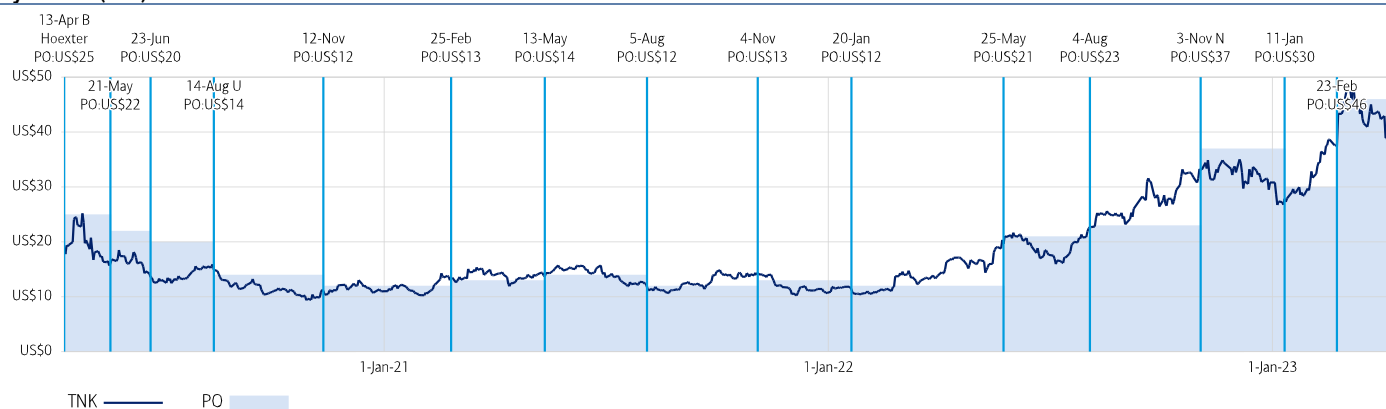
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## Scorpio Tankers (STNG) Price Chart



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## Teekay Tankers (TNK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	68	51.52%	Buy	38	55.88%
Hold	28	21.21%	Hold	15	53.57%
Sell	36	27.27%	Sell	18	50.00%

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