Effect and aftermath of global crisis on vlcc market in nigeria essay example

Countries, United States

Introduction

The term financial crisis has been used broadly to several situations whereby some financial institutions or assets face a sudden loss in a huge part of their value. The 19th and 20th centuries have encountered bank panics and recessions (Kindleberger & Aliber, 2005). Other situations related to financial crises include stock market crashes as earlier witnessed in the United States and bursting of financial bubbles, sovereign defaults and currency crises. What has been considered as the global financial crisis began in the United Kingdom and the United States of America following a significant standstill in the global credit market in July 2007. However, the effects of the crisis started showing in different countries in the mid of 2008 (Baker, 2008). Currently, stock markets have fallen, huge financial institutions have failed or sold out, and some governments in even the most developed nations have developed rescue packages to overcome the effects of this financial crisis. The United States is considered one of the root causes of this global financial crisis (Abubakar, 2008). It contributes about 25% of the world output, with an estimated gross domestic product of about $14 trillion. Economic analysts argue that even a 1% contraction in the United States economy would lead to approximately 140 billion, which is equivalent to the gross domestic product of many of the developing countries such as Pakistan.

However, the effects of the global financial crisis has been felt in all countries of the world including Africa and some of its stable countries such as Nigeria with huge crude oil deposits. The economic analysts further believe that the initial response of the policy makers in Nigeria to the global financial crisis were mild. This could be due to the fact that they underestimated the magnitude of the crisis as a mild economic turmoil. For instance, when the market capitalization dropped from N12 to about N9 or less, the Minister of Planning stated, rather insensitively, ‘ there is no problem in the Nation’s capital market. What we have presently is just corrections and adjustments. shareholders are getting dividends and bonuses and they are happy’ (DT October 6, quoting the Minister of State, Finance). When the government finally accepted the crisis as a genuine challenge, it sought measures to evade it. The nation’s dependence on the export is very important with 99% of foreign exchange, and 85% local revenues derived from export related to a single commodity – oil. Estimations reveal indicate that about 58. 4 percent of the Nigerian exports are United States bound, and about 25 percent to the Eurozone.

The Variables

The effects and aftermath of the global financial crisis on very large crude carriers (VLCC) markets in Nigeria have been felt in different aspects of the nation’s economy. The dependent variable in this paper is the freight rate, which refers to the rate at which a specific cargo is delivered from one point to the next; probably the sender to the receiver (Mtango, 2008). The freight rate depends on the mode of transport, the form of the cargo, its weight, and the distance between the freight points. However, the independent variables in this research study include deliveries, the United States gulf route to Nigeria, new buildings, and order book. These variables are as discussed bellow.

Freight Rate

Following the global financial crisis, freight rates have reached a level that no longer covers the costs of running a vessel, thereby forcing very large crude carriers' managements to resort to cost-focused managements of the freight. The costs of running these freights include operation costs, periodic costs, capital costs, voyage costs, and cargo handling costs. Before the global financial crisis, the freight rates from Nigeria to different destinations were sufficient to cover the running costs thereby making the freight business unreliable. These freight rates depend on other factors such as tariffs and barriers imposed on the freight handlers in the transportation process.

United States Gulf Route to Nigeria

The Gulf of Guinea on the Atlantic Ocean provides a shipping route between Nigeria and the United States. Commodities move from either directions through the Gulf of Guinea. Over the past decade, the area has been marked with criminal activities such as piracy, which has seen about 300 American sailors held hostage by the pirate criminals seeking ransom. The United States engages in foreign direct investment and equity investment in the United States – Nigeria gulf shipping. However, despite the 2007 boom in the foreign direct investment, equity finance, corporate, and project finance is already weakening. These have led to the downward trend in oil prices. The countries that have been hit by the financial crises are the primary markets for the oil, thereby threatening the gulf shipping of the oil, which also faces failing to meet the expenses as witnessed in freight rates. The shipping of oil containers through the gulf has become expensive since some of the former oil destinations have become unable to procure more oil as they did in the past. Therefore, shipping tankers have travelling longer distances without stopovers face spillage challenges alongside theft threats.

Deliveries

Most of the oil deliveries in Nigeria depend on pipelines for the supply of the commodity. These pipelines have faced attacks that interrupt the deliveries of crude oil to the destinations. Following the global economic crisis, the cost of assets such as brass used in the manufacture of barrels used for transporting the oil to different destinations fell drastically. However, banks and financial institutions also face financial challenges. Nevertheless, the interest rates have become favorable to the borrowers, thereby allowing the acquisition of financial aid to develop delivery lines. For instance, in Nigeria, the interest rates have remained at averagely 9% and the lending rates at about 16 percent, which are lower than the interest rates before the financial crisis that at times went up to 12% and 18 percent respectively. Considering the shipping costs of the commodity, most companies have resorted to piping the oil to different delivery destinations. The environmental hazards of the pipelines also make the latter a favorable method of transport for the commodity.

Order Book

Considering the order book in different shipping and freight handlers, there have been increased unshipped orders. However, considering the previous trends prior to the global economic crisis, the margin and profitability analysis indicate that most of the present orders have not matched the same margins in the former. Customer orders have been associated with the reduced liquidity of the potential buyers.

Demolition

The global economic crisis has led to the demolition of inactive oil pipelines, and tankers, which have become useless to the shipping companies.

New Buildings

However, the rate at which new buildings are being put up ensures that the replacements meet the shipping needs of these companies.

Conclusion

Following the global financial crisis, all nations of the world have either suffered directly or indirectly through interdependence. The crisis began in the developed nations such as the United States and the United Kingdom. Nevertheless, developing nations have also faced similar circumstances. Nigeria, being one of the financially stable African countries depends on the developed nations such as the United States for its oil exports. The financial crisis ensured that the freight rates reduced significantly to sustain the operations, making the business unprofitable, thereby forcing investors to seek other means of deliveries such as piping.

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