

FIS Baltic Dry Index

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Is the pullback too deep?

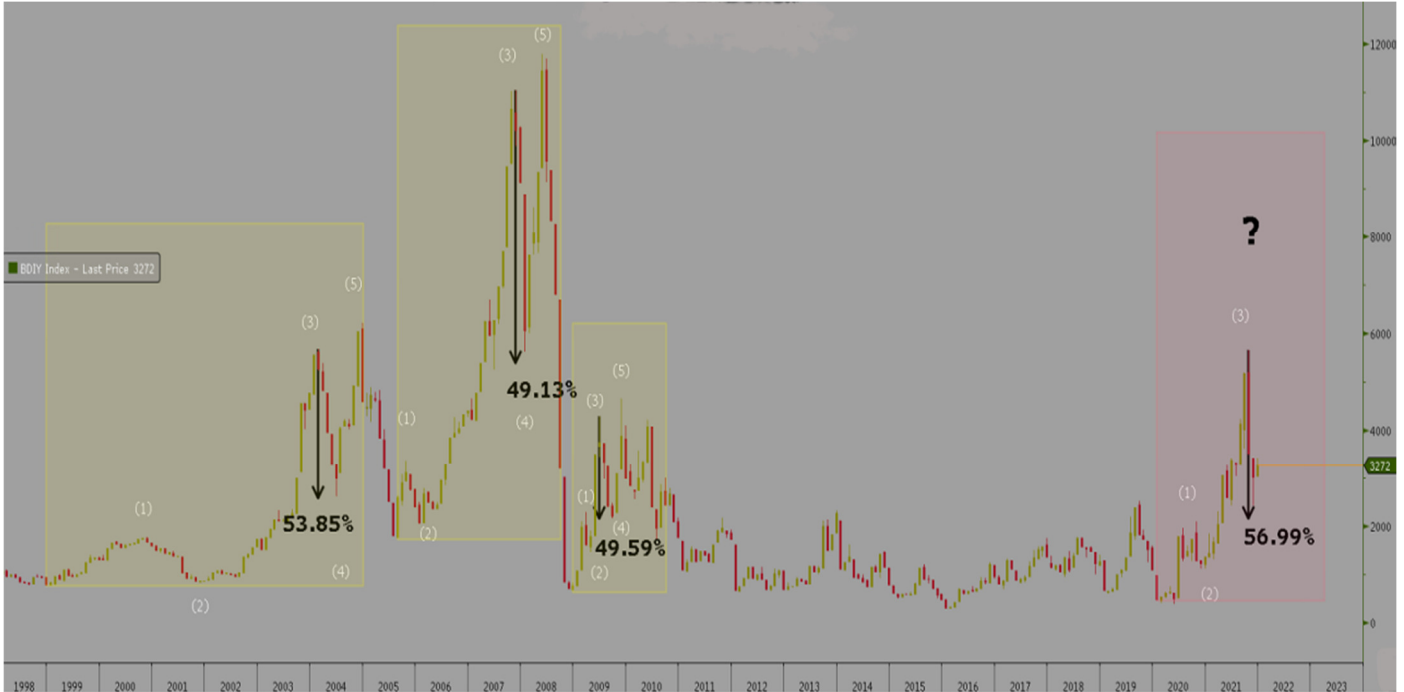


Chart source Bloomberg

Super cycle is a word that we have heard brandished around a lot the in 2021, as we enter 2022 the Chinese year of the Tiger the question being asked by ship owners is, will we see higher pricing in 2022, are we still in the bull cycle?

Fundamentally we have seen questions being asked about the health of the Chinese economy on the back of bond defaults in the real estate sector. A cut in the RRR this week would suggest the government are prepared to act swiftly to stabilize the sector and add further stimulus to the economy if needed. If this is a case and steel production curbs are eased, then we have the potential to see further support in the Baltic Dry Index next year.

With the index reaching its highest levels in 13 years, we have looked at 3 previous cycles over the last 25 years, specifically at their shape. There is a clear pattern that consists of 5-waves within the 3 cycles highlighted, all of which saw their valuations halved between the point 3 and point 4, before rallying to a new high.

We can see between 2020-2021 that we have a 3-wave pattern higher, which as we know has created excited chatter from owners due to the increased valuations. The bull argument is straight forward, we have a very clear 4-wave pattern that would suggest that there is one final upside move within this cycle, if this is the case then the FFA market is likely to make new highs in 2022.

The bear argument is the tricky one, if the cut in the required reserve ratio fails to stimulate the Chinese economy, then market sellers will also have a legitimate question to ask the market bulls:

Is the market pullback too deep at 56.99%?

We have seen pullbacks at 53.85%, but this is the deepest one yet, logically the deeper the wound the slower the recovery. As an optimist I want to say that we have a bull wave to come, history repeats itself, they are self-fulfilling. In any normal year I would be beating the bull drum hard, I still lean in this direction. However, this same pattern failed spectacularly in the Iron ore market after government intervention to reduce iron ore prices worked.

For this reason, we will call ourselves an optimistic bull, rather than a nailed to the wall bull!

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