

August 2019

Pay to pollute or be creative and comply?

By Chris Chatterton, COO, The Methanol Institute

For an industry that counts every dollar and cent, why are some shipowners apparently prepared to risk money on non-compliance with IMO2020 and at the same time distance themselves from the funds they will need to build ships in future?

A mere six months before the start of the global sulphur cap, shipping is undergoing a bout of introspection rarely seen before. If the cap itself is cause for concern, then the unwillingness of some owners to take a proactive view on the changes necessary is surely an alarm bell.

Recently a record fine of USD\$80,000 was assessed against a cruise ferry after it entered two fjords in Norway with sulphur values far beyond the legal limits. A leading cruise brand has been targeted for 2017 emissions of SO_x in European seas that were 10 times more than all of Europe's passenger vehicles.

The need to future proof investments in clean technology is understandable; it's for this reason that waiting until the 11th hour before complying proves so tempting and why for a few it is worth taking the risk of non-compliance.

But when the cost of non-compliance by a polluting ship is higher than the costs of switching to a clean alternative it goes against financial logic, as well as negating the benefits to the environment of IMO2020.

Reports from the EU's Environment Commissioner state that low-sulphur non-compliance in the Baltic SECA averages 5% and 8.5% in the North Sea; broadly in line with the IMO's official 6% estimate.

With total 'at risk' non-compliant fuel of approximately 4.5m tonnes annually, based on a conservative 1.5% non-compliance rate, it suggests that total global fines in 2020 could amount to almost \$1.5bn or higher.

This sizeable amount could be put to better use by operators working towards compliance. The fine in the above incident would certainly be enough to retrofit the vessel to both bunker and burn methanol, a fuel that is already compliant with IMO2020.

It seems unthinkable that some shipowners should prefer paying fines for violations rather than making strategic investments that will secure the next 10-20 years of their business. Of course, plenty will comply; using a scrubber-based business case or a hike in their fuel bills which they will try to pass on to customers.

Despite their limited availability until comparatively recently, alternative fuels cannot be discounted. They present an opportunity for owners to emit less SO_x and NO_x after 2020 and present options for a low carbon shipping environment.

Ignoring alternatives also fails to take into account the trend towards green finance, which is growing just as traditional liquidity decreases. Oil refiners have already responded as Government policy increasingly swings behind clean fuels; the next stage is greater use of renewables, funded by investors focussed on sustainability.

The cost of shipping capital is likely to continue rising as banks and other finance sources demand a sustainable strategy as the price of doing business; the announcement of the Poseidon Principles, with 11 banks representing 20% of the \$450bn ship finance market signing on, confirms that.

They are in large measure a response to the UN's "Principles for Responsible Banking", which prompt banks to begin stepping up their commitment to meeting the Paris climate agreement as well as working to integrate the UN's Sustainable Development Goals into their business models. Of the 28 original signatories, a number have also signed on to support the Poseidon Principles.

The increased use of green bonds and other non-traditional sources for ship finance means that shipowners need to be more flexible and creative. This will not merely be an option: the banks themselves have environmental, social and governance targets to meet.

It is true that some alternative fuels are expensive, not just in upfront investment terms but also because without massive subsidies they cannot be competitive. This might not matter provided the industry is prepared to accept an uneven playing field, though this would overturn decades of regulatory precedent.

Others lack the necessary infrastructure and a regulatory pathway for their use within a timescale that permits the design, construction and operation of ships before 2030 and well ahead of 2050.

Even so, the industry should already be taking steps to define its post-2020 transition to clean fuel. It could be that ability to continue operating in the long term will depend on it, if social and political pressures on shipping continue to grow.

It's very likely that we will see more companies and organisations from Japan, Korea and China sign up to the Poseidon Principles, as well as Asian export guarantee agencies. For now, they are the best instrument we have, despite some suggestions of greenwashing. We think this is an approach that will become embedded and as it does, the industry will have to swing behind it.

Until then - and because we need both sticks and carrots - 2020 enforcement must be the priority; fines need to act as a genuine deterrent and not represent the cost of doing business. As is obvious to anyone with an eye on the sustainability of the industry, that cost will continue to rise – in the process making alternatives and renewables cost effective - until not just compliance, but a sustainability mindset becomes second nature.

Ends