GOLDEN DESTINY

This Week's News: A snapshot on the economic and shipping environment

Week ending 5th October 2012

ECONOMIC ENVIRONMENT

The risk of eurozone meltdown is being reflected in the high unemployment ratios, slow manufacturing activity and inflationary pressures all over the world.

EU statistics agency showed that unemployment in the eurozone hit a fresh high of 18.2million in August with the highest unemployment rate being recorded in Spain, where 25.1% of the workforce is out of a job and the lowest level of 4.5% was recorded in Austria, while the unemployment rate in Germany was 5.5%. In addition, annual inflation in the OECD region rose by 2.0% in the year to August 2012, up from 1.9% in the year to July 2012. Annual inflation increased in Germany to 2.1% in August from 1.7% in July and the United States to 1.7% from 1.4%, while more moderately in France to 2.1% from 1.9% and Italy to 3.2% from 3.1%. Annual inflation slowed in Canada to 1.2% from 1.3% and in the United Kingdom to 2.5% from 2.6%.

Outside the OECD region, annual inflation accelerated in India to 10.3% in August from 9.8% in July and the Russian Federation to 5.9% from 5.6%, while more moderately in China to 2.0% from 1.8% and South Africa to 5.1% from 5.0%. Annual inflation stayed stable in Brazil at 5.2% and Indonesia at 4.6%.

Even the negative outlook of euro region and its effects worldwide, the European Central Bank kept its main refinancing rate unchanged at 0.75%, stating that for now there is no need to cut rates below what are already historic lows.

In Greece, there seems to be a dispute with troika on the austerity package of EUR 13.5 billion proposed by the government for 2013-2014, but Greek Finance Minister reassures that an agreement could be reached by Monday's Eurogroup meeting for the country to receive the next tranche of aid by the end of October. Troika estimates that 2013 GDP contraction could be at 5% versus 3.8% of Greek government's estimations in the 2013 draft budget. According to two German magazines, Greece will receive its next tranche of international aid despite budget shortfalls and slow progress on reforms because Eurozone does not wish the country to exit from euro.

In the meantime, Greek banking sector is under some restructuring with Alpha Bank announcing that it has entered into exclusive negotiations with Credit Agricole S.A. to acquire the entire share capital of Emporiki Bank. The transaction is expected to be completed b December 31st 2012 and is subject to applicable regulatory approvals and procedures as to work councils and employment representative bodies of Credit Agricole S.A. In addition, Piraeus Bank is in advanced negotiations for the acquisition of Geniki Bank, the Greek subsidiary of Societe Generale and National Bank with Eurobank are closely monitoring the developments of Hellenic Postbank.

Asian and US factories are still struggling from eurozone recession. In China, manufacturing activity is still in the doldrums with September recording again slowdown even some signs of stabilization from the lows reached in August. The official Purchasing Mangers' Index, released by the National Bureau of Statistics and China Federation of Logistics and Purchasing, stood at 49.8 on September compared with 49.2 in August, but it is still below 50 indicating contraction.

In U.S., manufacturing activity expanded in September after three consecutive months of contraction, but it is still below 50. The JP Morgan global manufacturing purchasing managers' index, a compilation of manufacturing surveys in countries over the world, was 48.9 in September, slightly higher than the three year low of 48.1 recorded in August.

SHIPPING MARKET

Despite the adverse position of Chinese on aborting the ban for the entrance of Vale's very large ore capesizes in their ports, Qingdao port announced that its iron ore terminal located in Dongjiakou will be ready this year. Currently, a floating iron ore transshipment hub is operation in the Philippines and there is an ongoing construction on a shore based transshipment hub in Malaysia for Vale to service the unloading of its very large ore capes. Vale is already in discussions for building a third transshipment facility in Asia, but no details have been yet emerged about the location of the hub and the time of decision.

Vale's very large ore capes creates additional worries for the current vessel oversupply and the future increase in ton mile demand, given also the weak economic fundamentals of China with a downward revision of economic growth below 8% for this year. However, Norwegian bank's DNB Report brings optimism in the dry bulk demand side as it estimates that global trade in iron and coal will double in the coming five years. The bank estimates that exports of the two main bulk cargoes will reach 1,9bn tones this year and will grow to 3,5bn tones by 2017. However, the report underlines that utilization rates will increase from 83% this year to 89% in 2017 despite ambitious coal and iron ore loading expansion programmes underway or planned, according to data collected by the bank from more than 100 significant dry bulk terminals and ports worldwide.

In the **dry** market, capesize and panamax vessel sizes showed upward revisions amid China Golden Week National Holiday with smaller sizes, supramax and handysize units loosing gains on a daily basis. Capesize average time charter earnings are now more than $10,000/day for the first time since end January, while they are 298% up from the bottom low levels of $2,644/day on August 21st. Panamax average time charter earnings are now more than $4,000/day, recording weekly gains of more than $900/day, but they are still standing at the historical lows of end December 2008. Supramax average time charter earnings remain at less than $10,000/day from the beginning of August, while handysize earnings fell to less than $7,000/day from last week. The positive movements in large vessel sizes lifted the Baltic Dry Index to levels of more than 800 points, when in mid September recorded again historical low levels of 1986 and December 2008.

Spot iron price gave signs of stabilization with benchmark iron ore of 62% iron ore content ended unchanged at $104.2 at the beginning of the week, according to data provider Steel Index. "More than 50 percent of mills, traders and banks think iron ore prices will rise when the Chinese return next week," said a Singapore-based trader. Mills have to restock after the long holiday, but the question is how long the restocking can last," he said, adding that the move could send iron ore prices to between $110 and $115, levels last seen in August. Standard & Poor's Ratings Services said in a report that it doesn't believe iron ore prices will climb much further in the near term and despite an incremental recovery in the next two years, they are likely to be less than $100 a metric ton beyond 2015 as Australia and Brazil cut output of the raw steelmaking ingredient. The report added that prices need to average above $120/ton near-term to alleviate potential negative rating pressure for some producers, assuming costs and foreign exchange rates remain steady.

Chinese steel demand remains weak for the whole year with Australia's Port Hedland iron ore exports to China falling in September of 2012, as per figures from port authority. Port authority said that shipped 15.1 million tons-or 76% of total volume shipped to China in September, down from 16.7 million tons a month earlier. In August, exports from Port Hedland fell by 13% to 19,9 million metric tons.

At the current week, BDI recorded gains for six straight days by closing, **Friday October 6th**, at 875 points, up by 14% from last week's closing and down by 56% from a similar week closing in 2011, when it was 2,000 points. Capesize and panamax earnings are on increase with the BCI approaching the levels of 2,000 points. BCI and BPI ended in green, while supramax and handysize segments are on a downward incline. The highest increase has been in the panamax segment, **BCI** up by 19% w-o-w, **BPI** up 41% w-o-w, **BSI** down 4.2% w-o-w, **BHSI** down by 5.9% w-o-w.

Capesizes are currently earning more than $10,000/day, an increase of more than $2,500/day from a week ago, while **panamaxes** are earning more than $4,300/day, an increase of more than $900/day. At similar week in 2011, **capesizes** were earning $27,876/day, while **panamaxes** were earning $15,326/day. **Supramaxes** are trading at less than $8,400/day, down by more than $280/day from last week's closing, about 20% less than capesize and 94% more than panamax earnings respectively. At similar week in 2011, **supramaxes** were getting $16,028/day, hovering at 43% lower levels than capesizes versus 20% today's lower levels. **Handysizes** are trading at more than $ 6,500/day; when at similar week in 2011 were earning $11,270/day.

In the **wet** market, tonnage outweighs demand and VLCC rates in the Arabian Gulf-USG route are still below WS30. At the end of September, VLCC spot rates worsened in the Arabian Gulf from oversupply with WS in the AG-USG route falling to WS23.5 from WS 27 at time charter equivalent earnings far below zero levels $(9,300/d), while in the AG-SPORE and AG-Japan routes, WS fell to 36 from WS40 at time charter equivalent earnings $5,300-$5,900/day. WS in the WAFR-USG remained unchanged at WS42.5 at $14,300/day, while in WAFR-China lost one point on a weekly basis at WS 41 with $10,500/day time charter equivalent earnings.

In the suezmax segment, West Africa market remains sensitive to activity and WAFR-USAC came under negative pressure with WS losing 3.5 points week-on-week and dropping to WS56.5 at $7,500/day time charter equivalent earnings. In the aframax segment, Caribbean market was largely stable with WS in CBS-USG route staying at WS90 for two consecutive weeks at $6,200/day, as strong chartering activity was countered by a generally abundant supply of tonnage. In the MR market, the CBS-USAC route for 38,000dwt units gained 10 points to WS115, while AG-JPN route for 75,000dwt units gained one point to WS98 at $15,900/day and AG-JPN route for 55,000dwt units lost two points and falling to WS110 at $11,000/day.

The negative sentiment in the very large crude carrier segment is expected to be to be long term as the rising US shale oil production has hit vessel earnings. According to DNB Report, US crude imports are projected to drop annually by 500,000 barrels/day from 2013 from a rise in US shale oil production, while tanker utilization rate will fall from 87% in 2012 to 84% in 2013 and it could pick up to 85% in 2014 and 86% in 2015. The report said that US reduced crude imports will be equally distributed between West Africa and Arabian Gulf, while China's imports are expected to increase by 300,000 barrels/day. The report added that crude tanker supply growth will fall to 4% in 2013 from this year's 9% and the current orderbook accounts for 14% of fleet capacity with 42% of the orders still being at Chinese yards, which partially explains a high percentage of slippage of 30%.

According to US government data released, crude oil imports fell 7.2% or 670,000/day in July from a year earlier, which were the lowest since April's decline of 9.1%. Crude imports dropped as US oil output rose 15.3% or 832,000 barrels/day from a year earlier, to 6,267 million barrels/day, which was just 35,000 barrels/day below the level recorded in March, the highest since May 1998.

The sentiment in the suezmax segment is also being squeezed by the same reason as imports of light sweet crude into the US Gulf decreased to fewer than $700,000 barrels/day for the first six months of the year, compared with 1.2m barrels/day in 2010, cutting cargoes from suezmaxes on the West Africa to US trade route. The drop was caused by increased production of light sweet crude from the Eagle Ford field in Texas and the Bakken field in North Dakota, according to the US government in a new report. Oil from these fields "has primarily displaced foreign light crudes from Africa", said the report by the Energy Information Administration. The situation is not expected to improve for owners. The EIA expects imports will continue falling because domestic light crude will keep flowing to US Gulf refineries, aided by pipeline expansions. A key pipeline is the Seaway, which can take additional volumes of light crude from Oklahoma down to the US Gulf. Light sweet crude contains less sulphur than heavier grades and is prized because it is easier to process and yields large quantities of gasoline.

Additionally, the rapid growth of suezmax fleet is one more negative aspect as suezmax units fight for their market among other dirty tanker categories. According to Poten & Partners, continued deliveries of suezmaxes have driven 9% growth in its traditional loading regions of West Africa, the Black Sea and the Med. Suezmax utilizations are under pressure at near of just under 80%, consistent with other dirty tanker sectors, with earnings well below cash operating costs. Suezmax units have to fight with VLCCs and aframaxes to stay in the same 80% utilization zone from its 9.3% year-on-year fleet growth compared with 1.2% year-on-year for aframax fleet, while VLCC fleet growth is moving away from its 8% growth pace.

The brent crude oil price hovers above $110/barrel putting additional strain on vessel operating expenses with Bank of America Merril Lynch indicating that prices could climb to $120/barrel by December 2012 on stimulus measures and supply outages in key regions. Saudi Arabia’s oil mininister Ali al-Naimi reassures that there is no shortage of oil, inventories remain adequate and any additional demand can and will be met. The Arab world's largest economy and the Organization of Petroleum Exporting Countries have helped support the global economy by ensuring the international oil market remains well supplied and the oil price does not get out of control, he said. "I hope that the sum total of these efforts will result in further stability," he added. Saudi Arabia is on track to surpass its record oil output this year, offsetting a decline from Iran because of international sanctions against Tehran's nuclear program.

In the **gas** market, Japan’s nuclear phasing out brings optimism for the spot LNG rates in the forthcoming years, but delays in LNG liquefaction projects could depress the freight environment. According to Philip Fjeld, ceo of Flex LNG, in Marine Money Asia Conference, long term charter rates may dip to $70,000/day, from the current levels of $140,000/day for one year, and spot rates substantially below as liquefaction plants are delayed coming on line. The issue for shipowners is while the ships will be delivered on time, the liquefaction projects they are destined to ship for will not be. “My estimate is that the liquefaction projects we are seeing in Australia are going to be 12 to 24 months late,” Fjeld told the Marine Money Asia conference in Singapore. Fjeld said that of the last 10 LNG liquefaction projects worldwide only two were on time while the rest were delayed 12 – 24 months. The problem for the shipping industry was that LNG newbuildings are almost always delivered on time and sometimes even ahead of schedule. “The ships are going to be there. To make it worse some of these projects in Australia have ordered their own ships, these ships will be traded on the spot market,” he said. As a result he said long term charter rates would come down to around $70,000 a day in 2014 and spot rates would be “significantly lower” than that level.

In the meantime, under the recent announcement for Japan phasing out its nuclear power by 2040, Kansai Electric Power, a Japanese utility company, signed a long term contract with Qatargas to supply 0.5 mtpa of LNG for 15 years starting from 2013, which strengthens the strategic relationship between the world’s largest importer and exporter of LNG.

In the **container** market, the Shanghai Container Freight Index fell for six straight weeks by ending on September 28th at 1247.34, down by 1% week-on-week, with 1.1% and 1.3% weekly declines in Asia-Europe and Asia-Mediterranean routes respectively. In transpacific routes, there has been a 0.1% weekly increase in Asia-USWC routes and a 1.4% fall in Asia-USEC.

Asia-Europe rates are down 40% from this year’s peak of $1934/TEU on May 4th, as last Friday September 28th, ended at $1158/TEU, while at the end of September 2011, Asia-Europe rates were at $735/TEU. Asia-Mediterranean rates are now at $1204/TEU, when on May 4th, they stood at the highs of $2033/TEU and in September last year, rates were floating at 16% lower levels than today.

The soft eurozone economic environment and weak peak season are the two headwinds in a prompt restoration of rates. According to Container Trade Statistics, European imports of containerized goods from Asia fell 10.8% year-on-year in August, following July’s unprecedented 13.2% year-on-year fall. A general rate increase of $500 per TEU has been announced by liner operators to be applied from November 1st in Asia-Europe route, while the issue of overcapacity has again to be resolved with liners laying up their tonnage.

Despite the lows of the Asia-Europe trade and the worldwide economic recession, Southampton, UK's second-largest box port, has started a £150m ($243.2m) investment in container berths and dredging to accommodate the ultra large containerships of 13,000 teu and above that will account for half of the Asia-Europe trade by 2015. "This is about capability and not capacity," said DP World Southampton managing director Chris Lewis, whose 2.3m teu capacity container terminal handled around 1.6m teu in 2011.

In transpacific routes, Asia-USWC rates are now at $2730/FEU, down by 1.8% from the highs of $2782/FEU on August 10th, when at the end of September last year, Asia-USWC rates were paying only $1557/FEU. In Asia-USEC route, rates stood last week at $3677/FEU, down by 10% from $4098/FEU on August 10th and 20% up from the levels of $3054/FEU at the end of September last year.

In the **shipbuilding industry**, Chinese recent hungry appetite in the very large crude tanker segment injects a new business for the troubled shipbuilders. China Association of the National Shipbuilding Industry showed signs of pick up of activity with orders in August representing the highest monthly tally for the year. During August, a total of 2.34m dwt of newbuilds were ordered, down by 50% year-on-year, with hopes for better figures in September from Chinese buoyant VLCC ordering activity.

Overall, Chinese shipbuilding industry remains weak with newbuilding orders at domestic yards dropping 48% year-on-year to 14,59mil dwt for the period January-August, as per data from the China Association of the National Shipbuilding Industry

China's government-owned Guangzhou Shipyard International warned that it expects losses for the third quarter of the year. In 3Q11 the company had profits of 145.46M yuan ($23M), however, the group said a reversal is expected because of declines in shipbuilding markets. The yard said profits for the first three quarters ended 30 September are now seen more than 50% down, from profits of 408.85M yuan ($65M) during the same period last year. The drop in profits derived from shipbuilding is due to the sharp drop in the prices of the ships under construction, which was affected by the decline in the shipbuilding market, GSI explained.

In the **shipping finance**, European bank lenders are still in troubled position with private equity funding not being able to bridge the gab. Bank of America Merrill Lynch managing director and head of shipping for Europe, the Middle East and Africa Philippe Chryssicopoulos told the Capital Link Forum at the London Stock Exchange that private equity simply would not be able to fill the funding gap. Jeffries senior vice-president Harold Malone said that it has become apparent that some private equity deploys criteria as strict as banks when assessing investment opportunities as they are seeking a comparative advantage.

Managing director Michael Dockman of AMA Capital Partners supported also the same views by adding that private equity players in particular like the idea of eco-ship newbuildings as a competitive advantage. Mr Malone said private equity investors were unlikely to want to step in and help owners with existing obligations on existing contracts. Instead, their preference would probably be to buy up distressed assets at yards, where owners have cut their losses, left the deposit on the table and walked away from the order.

Under the current worsened economic and shipping conditions worldwide, dry bulk owner Excel Maritime announced that it had agreed with its lenders to extend the date for the first tranche of its required equity raise, pushing the requirement for the full $30mil equity raise to December 31, 2012. Excel originally had to raise $20mil by September 30, 2012, with the remaining $10mil required by the end of the year. Excel also received waivers for certain covenants through December 31, 2012, while, as expected, exercised its option to defer payment of $24mil originally due on October 1.

In addition, Torm A/S signed a restructuring agreement that secures a substantial deferral of bank debt, new liquidity and savings from the restructured time charter book. This will enable TORM to become cash flow positive even at the current rate levels and further to secure long-term capital structure. It has taken extraordinarily long time to reach this agreement and inflicted very high costs on the Company, but TORM will now be able to continue its business even in a continued difficult market," says Chairman of the Board N. E. Nielsen. "I am extremely satisfied that an out-of-court agreement has been signed. It has been a long process, but I am very pleased that our long-standing time charter partners and the banks have been supportive. TORM's organization now looks forward to devoting all of its focus solely on the customers and operations again," says CEO Jacob Meldgaard. Furthermore, Indonesia's PT Berlian Laju Tanker is hoping to restructure its $1.9 billion debt by the year-end and switch its focus to niche liquid chemical and gas transport, as its founder and chairman said in a rare media interview.

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