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

Week Ending: 16th November 2012 (Week 46/2012)

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ECONOMIC ENVIRONMENT

Worldwide economy is facing serious challenges with major countries in and out of eurozone facing negative growth. The third quarter of the year ended with eurozone sliding back into recession as its output shrunk 0.1% for July-September period following previous quarter decline of 0.2%. Gross domestic product for Italy, Spain, Netherlands and Portugal shrank during the third quarter of the year with France and Germany showing a stronger growth. Out of the eurozone, Japan is facing a severe slowdown with US and UK economies posting a stronger output growth. In emerging countries, China gives a green light to the current severe globalized economic slowdown with Brazil also showing signs of recovery after a slowing demand of exports that led to a year of stagnation, while India still faces the slowest economic growth in the last decade.

How some eurozone economies are faring

	Q4 2011	Q1 2012	Q2 2012	Q3 2012
Eurozone	-0.3	0	-0.2	-0.1
Germany	-0.1	0.5	0.3	0.2
France	0	0	-0.1	0.2
Italy	-0.7	-0.8	-0.7	-0.2
Spain	-0.5	-0.3	-0.4	-0.3
Netherlands	-0.6	0.2	0.1	-1.1
Portugal	-1.4	-0.1	-1.1	-0.8

SOURCE: EUROSTAT; FIGURES SHOW % CHANGE COMPARED WITH PREVIOUS QUARTER

How are countries outside the eurozone doing?

	Q4 2011	Q1 2012	Q2 2012	Q3 2012
US	1	0.5	0.3	0.5
UK	-0.4	-0.3	-0.4	1
Japan	-0.3	1.3	-0.1	-0.9

SOURCE: EUROSTAT BASED ON THE RESPECTIVE NATIONAL STATISTICS AGENCIES; FIGURES SHOW % CHANGE COMPARED WITH PREVIOUS QUARTER

Gross domestic product contracted by 0.2% in Italy, 0.3% in Spain, 1.1% in Netherlands and 0.8% in Portugal during July-September period. In France, GDP rose by 0.2% in the third quarter compared with a previous 0.1% negative growth avoiding a further recession, while Germany's output rose at a slower pace by 0.2% in July-September period, down from a 0.3% growth recorded in the previous quarter and 0.5% in the first quarter of the year. In the meantime, Germany has already cut its growth economic forecast in 2013 from 1.6% to 1%, citing as main reasons the eurozone crisis and weaker growth in emerging nations of Asia and Latin America. Compared with previous years, Germany's gross domestic product grew by 4.2% in 2010 and 3% in 2011.

Greek economy posted a steeper recession in the third quarter as it shrank by 7.2% in the third quarter, from a 6.3% fall in the second quarter, according to statistics agency Elstat. Under the serious challenge to tackle its huge debt and meet the targets set from IMF and eurozone finance ministers, Greece keeps its battle to secure the delayed bailout installments till the end of the year. European Finance Ministers have already welcomed the decisions of Greek parliament to ratify the new austerity measures and the 2013 budget by providing Greece two more years until 2016 to meet the 4.5% primary surplus target. In addition, an extraordinary Eurogroup meeting was announced for November 20th for the approval of the release of EUR31,5bn June delayed tranche. German Finance Minister Mr. Schaeuble, speaking to reporters in Brussels, stated that Greece had made significant decisions in the right direction' and would

get three aid tranches before the end of the year, but Eurozone governments need to come up with an enhanced ‘control mechanism’ for the country’s fiscal program and make its debts sustainable into the next decade.

In Japan, the economy has shrunk at the lowest pace since the first quarter of 2011, when the country was hit by tsunami, with government data showing that Japan’s output declined by 0.9% in July-September, mainly due to a fall in country’s exports to key markets of China and Europe. On an annualized basis, gross domestic product fell 3.5% in the third quarter with Japanese Prime Minister describing the decline as severe and the seventh since Lehman’s collapse in 2008. Japan’s Prime Minister, Yoshihiko Noda, surprised by announcing that will dissolve parliament on Friday and call December election leading Japanese yen to a sharp fall from political turmoil.

In China, there has been a change in leadership with doubts for a new direction in policy as the Chinese Communist party has chosen a conservative team to lead the world’s second largest economy despite calls for a political change and fresh economic reforms. Chinese latest economic data shows an end in the slowdown with the head of the National Development and Reform Commission confirming the country will meet its target of a 7.5% growth this year and it could even surpass it. The October’s Consumer Price Index assures that inflation is currently not a main concern for the government and policy easing will continue in the fourth quarter of the year to support a growth recovery.

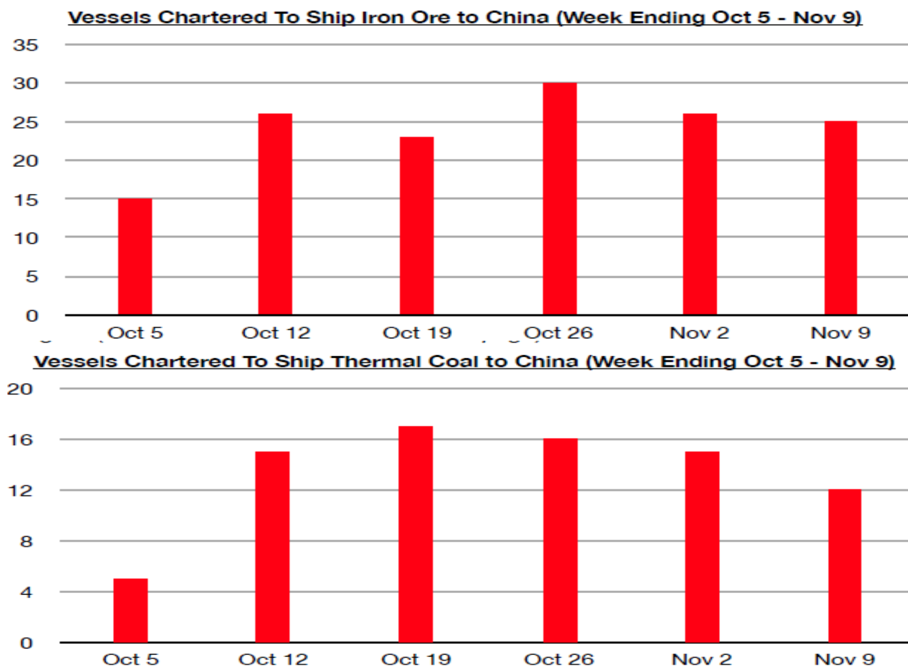
In India, the inflationary pressure seems to have eased but it remains high and above government’s expectations. October ended with inflation falling to 7.4% from 7.8% in September and 8% in August. "The underlying inflationary pressures are firm and this number is not necessarily sufficient to change the Reserve Bank of India's reluctance to cut interest rates," said Leif Eskesen, chief economist for India and the Association of Southeast Asian Nations at banking group HSBC.

SHIPPING MARKET

The latest positive signs of Chinese economy for the fourth and final quarter of the year with a sense of end in the slowdown of the world’s second largest economy give room for a further monetary policy to spur growth and provide support for dry bulk commodities’ demand. The role of China on the dry bulk sentiment is very critical as it alleviates the pain of oversupply from the growth of iron ore demand and higher volume of vessels’ chartering activity.

In the **dry** market, the week opened with an upturn in capesize average time charter earnings and a boost in the Baltic Dry Index as it broke again the psychological barrier of 1,000 points. Chinese iron ore inventories are falling from week ending October 5th by standing currently at levels of about 87million tons lower than June 2011, while capesize congestion in Australian and Brazilian ports is on rise creating a tight vessel availability of capesize vessels and a push in their earnings. In the meantime, spot iron ore price is trading at above $120/ton from $86.7 on September 5th, according to the Steel Index ltd, as Chinese steel demand accelerates. According to World Steel Association, China’s steel consumption will keep a positive trend at it estimates that will accelerate to 3.1% next year, from 2.5% in 2012, while it will be slower that the 6.2% recorded in 2011.

Chinese iron ore fixture volume still show a firm amount of vessels chartered to haul iron ore from the second week of October till the second week of November with capesize earnings rising again to more than $16,000/day, while thermal coal fixture activity keeps going with panamax earnings surpassing the levels of $7,000/day.



(Source: Commodore Research)

The dry bulk environment remains fragile with Anglo-Australian mining company Rio Tinto anticipating a continued volatility in commodities demand and prices even as demand for its commodities continues to grow thanks to appetite of China and other Asian countries. Vivek Tulpule, Rio Tinto's chief economist said: "As China's economy matures, demand growth in India and Southeast Asia should more than offset the flat and then falling consumption in China as the trend of urbanization gathers pace and brings rising need for steel, aluminum and other raw materials. Beyond 2025, India will become the most important driver of a number of our markets mainly due to country's growing need of coal for producing electricity as well as other commodities".

Overall, the surge of capesize average time charter earnings of about 400% from the levels of end-August, is a remarkable increase but it remains to be seen how sustainable will be till the end of the year as it could not be yet considered as a full upturn of the market. In November last year, the average value of capesize average time charter earnings was at $26,160/day, 63% above current levels. Smaller vessel segment, supramax is also fighting with levels still far below $10,000/day, when at the end of November last year; supramax vessels were earning more than $14,000/day, about 100% above the current levels.

BDI closed on **Friday November 16th**, at 1036 points, up by 10% from last week's closing and down by 45% from a similar week closing in 2011, when it was 1,895 points. All dry indices closed in green this week except for handysizes, while panamax segment recorded a remarkable increase. **BCI** is up by 6.5% w-o-w, **BPI** up 23% w-o-w, **BSI** up 3.8% w-o-w, **BHSI** down by 0.4% w-o-w.

Capesizes are currently earning $16,411/day, an increase of $1,857/day from a week ago, while **panamaxes** are earning $7,077/day, an increase of $1,289/day. At similar week in 2011, **capesizes** were earning $28,340/day, while **panamaxes** were earning $14,365/day. **Supramaxes** are trading at $7,046/day, up by $259/day from last week's closing, 57% lower than capesize and only 0.4% higher than panamax earnings. At similar week in 2011, **supramaxes** were getting $14,438/day, hovering at 49% lower levels than capesizes versus 57% today's higher levels. **Handysizes** are trading at $ 5,992/day; down by $231/day from last week, when at similar week in 2011 were earning $9,388/day.

In the **wet** market, the second week of November ended stronger for very large crude carriers with WS showing better performance in the struggling AG-USG route. In the AG-USG route, time charter equivalent earnings are still floating below zero levels, but WS gained 3.75 points by rising to WS26.5. In AG-SPORE and AG-JPN routes, WS gained 4.5 points by reaching WS40 at time charter equivalent

earnings at $15,000/day, while WS stayed stable at WS42.5 ($17,700/day) in WAFR-USG route and WS40 ($13,900/day) in WAFR-CHINA route.

There is a stable environment also in the suezmax segment with no weekly change of WS in WAFR-USAC route for three consecutive weeks at WS62.5 ($13,900/day). In the aframax segment, CBS-USG route showed strong gains by rising 35 points above previous weekly level to WS142.5 ($30,525/day), which is one of the highest levels seen during the year.

In the panamax segment, CBS-USAC route posted also strong gains with WS edging at 120, up 17.5 points from previous week, at time charter equivalent earnings of $14,300/day, when similar levels were seen in mid-September. In the meantime, the Caribbean MR market following last week's excessive rise as the aftermath of hurricane Sandy with WS at 210 in CBS-USAC route for 38,000dwt units, it lost last week 30 points to conclude at WS180. In AG-JPN route for 75,000dwt vessels rose 4 points to WS113 ($24,700/day), while for 55,000dwt units lost 1 point by falling to WS137 ($21,800/day).

On the demand side, projections for global oil demand are not supportive for the crude tanker market. The International Energy Agency in its monthly Report of November, estimates a negative trend in world oil demand citing Europe's troubled economy, the risk of weakness in faster-growing regions such as China and India and the residual effects of Hurricane Sandy in North America. The agency cut its oil demand forecast for the last quarter of this year by a sizeable 290,000 barrels/day to 90,1mil barrels/day and it estimates oil demand for the whole 2012 to grow by 670,000barrels/day, which is 60,000 barrels/day less than its previous estimate last month. For 2013, it estimates oil demand to increase by 870,000 barrels/day to a total of 90,4mil barrels/day, 100,000 barrels/day less than its last monthly forecast.

In addition, the treat from the increase of US oil production on the growing VLCC demand becomes stronger following International Energy Agency estimates that US will overtake Saudi Arabia and Russia to become the world's largest global oil producer by 2017. This projection appears the first time and underlines the development of share revolution on the world's oil demand. On the other hand, analysts have warned that the US oil boom is still in its infancy, and continued growth to the levels predicted by the IEA cannot be guaranteed.

Overall, US domestic oil production is on rise for the last five years with an increase of total supply by 2.59m barrels/day, an average growth rate of 500,000 barrels/day a year. The US Energy Information Administration expects production will rise from 6.3m b/d this year to 6.8m b/d in 2013 – its highest level since 1993. The International Energy Agency predicts that US oil production will be as high as 7,8million barrels/day in 2035 and combined with biofuels and natural gas liquids such as ethane and butane will reach the producing levels of Saudi Arabia and Russia at just under 10m barrels/day in recent months.

One more worrying sign is that Chinese oil demand fades. The International Energy Agency in its recent forecast cited a steep deceleration in China's oil need for the period until 2017. "China has led global oil demand growth this past decade, with gains in the 10 years prior to 2012 averaging 7 percent per annum," the IEA said in its Medium-Term Oil Market Report. The Paris-based agency estimates that China's oil demand will rise only 2.6 percent this year. The slippage is the latest sign that China's economy may ease its squeeze on world energy markets after years of runaway growth. The IEA estimates that China's oil demand will reach 9.8 million barrels per day in 2013, about 750,000 barrels below its previous forecast last year. However, China's oil demand is going to be stronger for the fourth quarter of the year as China's two oil giants, PetroChina and Sinopec Group, are planning to process some 31 million metric tons of crude oil in November, according to a Shanghai based energy information consultancy. The reason for the reefing increase is growing demand for oil in the fourth quarter and reduced maintenance of refineries.

In the **gas** market, Japanese Mitsui OSK Lines, on the course of LNG needs and the changing picture of LNG shipping industry as the aftermath of last year's Japan's earthquake and tsunami, is planning to order new liquefied natural gas carriers and charter them under short term contracts of up to seven years by imitating similar movements from other players. In an exclusive interview with Lloyd's List, MOL director of LNG in Europe Mike Rowley said new vessel orders would only be made with a charter secured first. MOL, one of the world's biggest LNG vessel owners with a fleet of around 20, is in

discussions with heavy-hitting charterers such as Shell and BP regarding these short-term deals, Mr Rowley revealed. “We’re considering building new vessels, but only for quality customers for five- to seven-year fixtures. We’ve seen other players doing this.” MOL will not order a batch of five or 10 newbuildings, preferring instead to take a measured approach and order one vessel at a time. The expectation is that the vessels will be delivered in 2015 or 2016 and the likelihood is that they will be ordered at Japanese shipyards.

Japan’s post earthquake nuclear meltdown has triggered an ordering spree with fears that LNG growth fleet will exceed demand in 2012. International Energy Agency estimates that LNG demand will stay stable at 90m tonnes till 2017, while LNG players are expecting an increasing Japanese LNG demand as a support to the LNG fleet growth that RS Platou estimates that will reach 8.55% of the existing fleet in 2014. LNG spot rates are now fluctuating at $120,000/day after peaking $150,000/day in the first half of the year from $34,000/day in 2009.

In the **container** market, the Shanghai Container Freight Index declined by 4.7% for week ending November 9th, following two consecutive weeks of increase, with Asia-Europe spot rates falling 7.2% week-on-week to $1,383/TEU and Asia-Mediterranean by 9.2% week-on-week to $955/TEU. Asia-Mediterranean spot rates fell for the first time below $1000/TEU since the end of February, while Asia-Europe spot rates levels are similar to the levels of March 9th, when they ended at $1388/TEU.

Transpacific routes continue to experience weekly decreases with spot rates in Asia-USWC falling to $2310/FEU, down by 4% week-on-week, similar to the levels of end May, signalling five weeks of consecutive drops. In Asia-USEC route, rates fell to $3319/FEU, down 1.7% week-on-week, showing seven weeks of consecutive decrease.

Compared with a similar week of November in 2011, the Shanghai Container Freight Index is 32.9% above year-on-year with Asia-Europe and Asia-Mediterranean spot rates standing at 141.4% and 18.5% higher than the current levels, when they were at $573/TEU and $806/TEU respectively. In transpacific routes, Asia-USWC rates are now 56% up year-on-year from levels of $1481/FEU in 2011 and 22.5% up in Asia-USEC route from levels of $2709/FEU.

Under the current weak winter demand season, the laid up fleet shows a rise as Alphaliner estimates that the global idle containership fleet of more than 500 TEU has reached 762,000/TEU, an increase of 4.7% compared to the idle fleet at November 5th. Maersk is said to be in the frontline of layups with 14 idle ships ranging in size from 4,000 to 9,600 TEU with a combined capacity of 94,000 TEU, six of the ships were displaced from Asia-Europe trade owing to service suspensions. Alphaliner notes that winter service suspensions have a negative impact on demand for large containerships and a further 150,000-250,000 TEU would be laid up till the end of the year. At the size of above 5,000 TEU, 24 boxships are laid up compared to only 2 in early September, while 67 ships of between 3,000TEU-5,000TEU are laid up, 14 more ships than two months ago.

In the **shipbuilding** industry, the president of China State Shipbuilding, Wenming Hu, stated at the Communist Party conference in Beijing that China’s shipbuilding stall is likely to continue for at least three more years as the current demand is weak and the situation in Europe is not stable and there are no signs of bottoming out. Substantial growth in the sector is likely to be blocked by the global economic slump, he warned, so shipping cannot expect short-time recovery. New technologies will spark new trends in shipping, predicted Hu, who pointed out that if new ships can save as much as 20% energy while bunker prices remain about $80 per tonne, new orders might be expected.

According to latest data released by the Ministry if Industry and Information Technology, production at Chinese yards declined steeply during the first three quarters of the year to 41,58 million deadweight tons, down by 18.5% from last year, while new orders decreased by 46.9% year-on-year to 15,41 million deadweight tons.

In the **shipping finance**, one more German ship lender is facing losses from the economic slowdown and the slump of freight rates. Germany’s Commerzbank said in its third-quarter report that distressed shipping loan were the driving force for a 19% increase in loan-loss provision, to €862M ($1.097Bn), in its non-core assets division. Because of the prolonged slump in all major market segments, the bank

considers irrecoverable write-downs of about €270M to be inevitable for its ship finance division in the long run. The bank said that its exposure to shipping dropped from €18Bn to €16Bn over the first nine months, because of amortisation of loans and transferral of non-performing loans into its default portfolio.

Overall, ship financing has become too tight under the severe economic and shipping conditions with Athens-based Petrofin Research stating, in the 25th International Ship Finance and Investment Conference organized by Informa Maritime Events, that the top 40 shipping bank lending has fallen to the point were getting a 10-year loan is "like winning the lottery", with worse to come in 2013 and 2014. According to figures from Petrofin, ship lending as of November 2012 reached $475bn, including the offshore support sector, but excluding rigs and shipyard finance, while total ship financing has and is continuing to fall from previous yearly levels.

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