GOLDEN DESTINY

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

Week ending 2nd March 2012

ECONOMIC ENVIRONMENT

The turmoil in Greek economy persists with the Eurozone finance ministers delaying the approval of more than half of the EUR 130bn bailout after claiming that the country has not still concluded all 38 "prior actions" required to receive the second rescue in two years from the European Union. According to Eurogroup Chairman Jean-Claude Juncker Greece has met almost all the requirements demanded to qualify for a new EUR130bn loan and now Eurozone is waiting for the completion of the private bond swap deal. In Germany, Angela Merkel, the chancellor, has managed to secure the resounding backing of the German parliament for a second financial aid package for Greece even after she warned that the success of the new program is uncertain. "There is no 100% guarantee that the second bailout programme will succeed," she told the Bundestag (lower house). Germany will have to pay more than any other country for the 130bn euro ($173bn; £110bn) package, agreed by eurozone states last week. Under the terms of the bailout, Greece has to approve 3.2bn euros in budget cuts and has already backed a debt swap with banks and private investors to wipe out 107bn euros of debt.

In the meantime, Standard & Poor's has cut Greece's long term ratings to "selective default" by following similar movement from Fitch due to country's announcement for a bond swap deal to lighten its debt burden. S&P said that once the debt exchange is concluded, it would likely raise Greece's sovereign credit rating to the speculative "CCC" category. Athens said that the downgrade was expected and would not hurt its banks since the central bank had already made provisions for it. The U.S. rating agency also said that any upgrade to the "CCC" category rating would reflect its view of Greece's uncertain economic growth prospects and still large public debt, even after the restructuring is concluded.

In the eurozone, the European Central Bank injected EUR530billion into the eurozone financial system from the ECB's longer term refinancing operation, which offers to 800 banks across the euro area low interest loans of just 1% as a means of strengthening the position of the backs from the ongoing sovereign debt issues. However, Steen Jakobsen, chief economist at Saxo Bank, said: "Despite the euphoria in the banking sector following the ECB's loan programme, the real economy remains very depressed and the key factor is the unemployment rate, both socially and because of the damage to growth. The unemployment of the zone is on rise with the Eurostat announcing that it hit another record high in January. The jobless rate in the 17 countries that use the euro jumped to 10.7% in January, while December's figure was revised up from 10.4% to 10.6%. Spain continues to have the highest unemployment rate in the euro area at 23.3%, while Austria has the lowest at 4%. Italian unemployment had stood at 8.9% in December, but it is now at the highest rate since the first quarter of 2001, as the country is in a second recession in four years. Separate data from Eurostat showed that inflation in the euro area rose to 2.7% in February, rising slightly from 2.6% in January. It marks the 15th month in a row that inflation has been above the ECB's target of just below 2%.

In U.S., the economic growth was revised upwards during the final quarter of last year. According to data from the Commerce Department, the economy grew at an annualized rate of 3% in the October to December quarter, up from its previous estimate of 2.8%, and it is the fastest rate of growth in a year and a half. The upward revision of the growth is due to customers spending more and less spending cuts from businesses. The chief of the US central bank said that the US economy is continuing to recover, but that growth is modest. Chairman of the US Federal Reserve Ben Bernanke was updating Congress on the health of the US economy. He said the decline in unemployment has been more rapid than expected. The jobless rate, which had been stuck at 9%, started to drop at the end of last year and hit 8.3% in January. The Fed Chairman said that the labour market "remains far from normal". "The unemployment rate remains elevated, long-term unemployment is still near record levels and the number of persons working part-time for economic reasons is very high." he said.

In China, there are growing fears for a stunned slowing growth with World Bank warning that the country must urgently implement sweeping economic and political reforms to maintain the pace of growth level that it managed over the past three decades of an average 10% annual growth. “China has now reached a turning point in its development path,” said Robert Zoellick, World Bank president. “As China’s leaders know, the country’s current growth model is unsustainable.” After three decades of averaging 10 per cent annual growth, China is the world’s second-largest economy and the largest exporter of goods but there is growing evidence that it’s export-dependent, investment-led growth model is running out of steam. The World Bank report estimates that even if Beijing implements steady reforms and avoids any major shocks to the economy, annual growth will decline to 5.9 per cent by 2021 and to just 5 per cent by 2026. Even at that lower rate, China would still replace the US as the world’s biggest economy by 2030 and its influence in the global economy would be comparable to that of the UK in 1870 or the US in 1945.

In India, economy has posted the slowest pace in three years by recording a 6.1% growth in the quarter to the end of December, deepening fears about the country’s growth prospects. A slowdown in manufacturing, mining and agricultural has pushed Asia’s third largest economy to growth levels below double digit figures. Finance minister Pranab Mukherjee said although the GDP figure was “disappointing, it was not unexpected”. “*There is of course a deceleration of growth rate as far as this quarter’s GDP is concerned. We need to undertake reforms and speed up implementation of various programmes to revive growth (momentum)*,” said Govinda Rao, member of the Prime Minister’s Economic Advisory Council (PMEAC). Manufacturing growth was hurt the most in the December quarter, with a 0.4 per cent rise against 7.8 per cent in year-ago period. Agriculture also saw a sharp decline at 2.7 per cent, down from 11 per cent in the year-ago period. Mining contracted 3.1% compared with a growth of 6.1% a year ago, signalling lower supply of raw materials to industry, as well as lower demand as higher interest rates have put off companies from investing. The falling growth rate may prompt the Reserve Bank to cut rates at its mid-quarterly policy review on March 15.

SHIPPING MARKET

Amid the depressing freight market status that main shipping segments (bulk carriers, tankers and containers) show, investors do not lose their shipping confidence and keep going with their investment plans in the secondhand market on expectations of lower asset prices combined with a plunge in newbuilding business and more intense scrapping removals from the already oversupplied segments. China’s government decision to lower bank reserve requirements may offer a strong support for dry bulk operators, with China investing in infrastructure for its growing urban population, along with a high percentage of newbuilding cancellations. Dry bulk shippers appear bullish about the massive expansion of iron ore production for the coming years with some predicting that could add 500m tones in cargo demand by 2014.

In the **dry market**, positive signs for emerging cargo demand have pushed the BDI this week upward with consecutive gains during the week, but the index remains below the psychological barrier of 1,000 points mark and capesize earnings haven’t shown yet strong signs of revival at levels below $6,000/day. Chinese iron ore inventories have fallen for three consecutive weeks but remain high, around 98mt with spot iron ore prices being on increase. The price of ore with 62% iron ore content delivered to the Chinese port of Tianjin rose this week to a $140.5/ton, according to the London based information provider The Steel Index Ltd., when on October 28th the price plunged to $116.9/ton, the lowest level since December 2009. A firm amount of global grain and thermal coal fixtures came to the market that helped to the boost of earnings for large and small sized vessels with panamaxes still facing pressure from ample vessels’ availability.

Chinese steel production has continued to find a small amount of support but remains relatively low. The China Iron and Steel Association (CISA) reported that daily crude steel production averaged approximately 1.71 million tons from February 1 to February 10. This is an increase of 2% from the 1.67mt daily steel production average that occurred during January 21 to January 31, but down significantly from last year's record 2.02mt daily production average that occurred during June 21 to June 30. The increase in steel output will lead to an increase of iron ore consumption and lower port stockpiles that could benefit capesize earnings via more intense Chinese iron ore buying appetite. However, there are estimations that China, the world's biggest buyer of iron ore, will import less this year putting an instant pressure on the already distressed earnings for capesize operators. According to China Mining Association, China may import as much as 14% less of the steelmaking raw material this year as domestic production increases. Imports may be between 590 million metric tons and 650 million tons this year, while last year's imports were 686 million tons, according to Bloomberg calculations based on General Customs data. China's iron ore imports gained 11% last year to a record, after dropping 1.4% in 2010, customs data showed. On the other hand, China's coal demand is at more comforting levels than iron ore that could contribute to strong earnings levels for supramaxes and panamaxes. According to China Electricity Council, China's coal demand will reach 4.3 billion tons by 2015, an increase of 970 million tons compared with 2010 and an annual increase of 5.2%.

One more negative catalyst factor for the future growth for capesize earnings is China's target to achieve iron ore self efficiency. According to the China Iron ore & Steel Association, China is aiming to improve its self efficiency in iron ore and continue to consolidate the steel industry in a bid to raise the output of its major steel makers by 10% within the next four years. The government expects the country's top 10 steel manufacturers to account for 60% of the country's steel output by 2015, Wang Xiaoqi, CISA vice chairman, said at a trade conference held in Beijing.

The index closed today at 771 points, up by 7.3% from last week's closing and down by 43% from a similar week closing in 2011 when it was 1,346points. The highest rate decrease has been in the supramax segment, BCI up 1.3% w-o-w, BPI up 0.9% w-o-w, BSI up 12.5% w-o-w, BHSI up 10.6% w-o-w.

Overall average time charter earnings are still floating at lower levels than 2011 with stronger weekly performance in all vessel sizes. Capesize average time charter earnings are up by 4.9% w-o-w, panamax up 1.2% w-o-w, supramax up by 12.5% w-o-w and handysize up by 10.8%. Capesizes are currently earning $5,979/day, $651/day less than handysizes, showing an increase of $280/day from a week ago, while panamaxes are earning $6,786/day, an increase of $81/day. At similar week in 2011, capesizes were earning $5,704/day, while panamaxes were earning $15,912/day. Supramaxes are trading at $7,786/day, up by $866/day from last week's closing, 30% higher than capesize and 15% than panamax earnings. At similar week in 2011, supramaxes were getting $15,340/day up by 97% from the current levels and 169% higher levels than capesizes. Handysize vessels are trading at $ 6,630/day; an increase by $650/day from last week, when at similar week in 2011 handysize units were earning $10,481/day.

In the **wet market**, VLCC spot rates are still below breakeven levels on weaker Arabian Gulf activity, while suezmax and aframax rates are on decline since Turkish strait delays declined. The brent crude oil price remains elevated, above $120/barrel, pushing downwards the financial performance of wet players with oil demand prospects not offering comforting levels under the current oversupply of tonnage.

Japan's crude oil imports in January fell 1.9 percent from a year earlier to 122.09 million barrels for the third straight monthly decline, as per data from the Agency for Natural Resources and Energy. Oil from the Middle East accounted for 82.6 percent of total imports, down 4.5 percentage points, the agency under the Ministry of Economy, Trade and Industry said in a preliminary report. Saudi Arabia remained Japan's biggest oil supplier, exporting 41.01 million barrels, up 19.6 percent. The United Arab Emirates was second with 26.29 million barrels, down 8.0 percent, followed by Iran with 10.50 million barrels, down 22.5 %.

The Iranian oil embargo is underway with Iran struggling to find buyers of its crude as top Asian customers, China, India and Japan, that buy about 45% of the Islamic Republic's exports, are planning cuts of at least 10%. Chinese are said to have started buying Libyan oil by even paying more in charter costs for suezmaxes shipping oil from Libya to China to secure supplies on increasing fears from Iran.

In the **gas market**, China's natural gas imports rose 66.7% year-on-year to hit 3.6 billion cubic meters in January. The apparent consumption of natural gas surged 20.1% from a year earlier to 13.7 billion cubic meters in January. The growth pace slows from last year's peak period, but still stands at high levels, the National Development and Reform Commission said. The rise in consumption was mainly caused by high power demands for winter heating and chemical fertilizer production, said the NDRC. Korea Gas Corporation plans to import 36,456,000 tonnes of LNG in 2012, which was disclosed in the documents submitted by the company to South Korea Stock Exchange. Also, KOGAS estimates that its LNG sales volume in 2012 will amount to 36,419,000 tonnes. Based on the data compiled by the company, its sales of LNG in 2011 were 33,747,000 tonnes and its sales in 2012 are expected to increase by 2,672,000 tonnes (7.9%).

In the **container market**, following three consecutive weekly declines after the Chinese New Year, the Shanghai Container Freight finally ended last Friday of February 24th in green, attributable to a 16% in the main haul trading routes from Asia to Europe and Asia to Mediterranean. Week on week, Asia to Europe rates improved by $115 to $826/TEU from $711/TEU, with the SCFI standing at 977, up by 3%. It seems that the European general rate increases scheduled for March that have been announced by some major liner operators have pushed upwards the incline of the index. However, the Shanghai Container Freight Index is still below 5.7% from similar week closing in 2011, when it was at 1,037 with the Asia-Europe route paying $1,200/TEU. On the other hand, the transpacific routes, Asia-USWC and Asia-USEC, showed a retreat by loosing $24 and $21 respectively and closing at $1,774/FEU and $1,798/FEU.

The future of boxship operators is still in uncertainty with Maersk Line betting that European efforts to escape a recession this year will fail. “We think there will be negative growth in Europe this year and that is affecting our view of Asia-Europe trade,” Trond O. Westlie, chief financial officer of A.P. Moeller-Maersk A/S (MAERSKB), the owner of Maersk Line, said yesterday in an interview in Copenhagen. “The solution that Europe is trying to take is different from the solution that the U.S. is taking. We believe that general growth will be higher in the U.S.” “The world is going to have slow growth, things are going to be volatile and this will be the case for a somewhat long period of time,” Westlie said. “Our effective growth rate is going to be challenged because we have a relatively higher exposure to Asia-to-Europe trade compared to our exposure elsewhere in the world.”

In the **shipbuilding industry,** Mitsubishi Heavy Industries, one of the largest shipyards, is finalizing a technology transfer agreement with China’s Sinopacific Shipbuilding to develop energy efficient kamsarmax bulk carriers. Sinopacific Shipbuilding said on its website that it intends to cooperate with MHI for jointly optimising the design of the 82,000dwt kamsarmax bulker. Sinopacific chief executive Simon Liang said that Sinopacif Shipbuilding, a specialist in supramax bulk carriers, is seeking to develop larger and more specialized vessels and MHI can provide the know-how.

In the **shipping finance**, under the tight European financing market, the question if Asian region will bridge the finance gap remains the hot issue for shipping players. The answer of bankers and private equity fund managers at a marine conference of Hong Kong is that Japan looks more positive than previously thought, China will do selectively and conservatively and South Korea seeks deals for high value ships only, LNG vessels, offshore units and ultra large containerships.

MARIA BERTZELETOU – GOLDEN DESTINY RESEARCH DEPARTMENT

For more Research Services, please contact us:

GOLDEN DESTINY
Research & Valuations Department
Sofia M.Kokkinis & Maria Bertzeletou
Email: snv@goldendestiny.com