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

Week ending 12th October 2012

ECONOMIC ENVIRONMENT

Eurozone recession seems to have no end with International Monetary Fund warning that France, Spain and other several eurozone governments will not accomplish the budget deficit targets agreed with European authorities. The IMF said in its semi annual economic outlook that it expects France's deficit to be 4.7% of GDP this year and 3.5% of GDP at the end of 2013, from its 3% of GDP deficit target in 2013. Spain's deficit is expected to hit 5.7% of GDP in 2013, well above from the target of 4.5% of GDP. Italy seems to be complying with the 3% budget target and missing its deficit target of 0.5% of GDP next year with estimations for Italy's deficit next year to be at 1.8% of GDP.

In Greece, government debt is accumulated much faster than expected with IMF estimating to reach 171% of GDP this year and 182% at the end of 2013. However, German Chancellor's visit in Athens gave positive signs for the country's economy and its existence in the eurozone. German Chancellor Merkel recognized the Greek government's reform efforts and proclaimed that she wants Greece to remain in the eurozone by pledging support to the country. According to EU Economics Chief Olli Rehn a decision on the EUR31.5bn bailout tranche for Greece can be expected in November at the latest, while a two-year extension to Greece's fiscal targets will have to be considered. Greek Prime Minister said that Mrs Merkel's visit was a "token of proof" in the progress Greece has made by adding that Greece would stick to its reform pledges and eventually be a "European success".

In Spain, rating agency Standard & Poor's cut Spain's credit rating by two notches to triple B minus from triple B plus, just one notch above junk level, citing the country's deepening economic recession and inability to handle mounting borrowing costs.

International Monetary Fund also cut is forecasts for global growth from the failure of US and eurozone policy makers to tackle fiscal issues. IMF expects economic output to expand by 3.6% in 2013, down from July's estimate of 3.9%. One optimistic indicator for US economy was the fall of US jobless rate to the lowest level in September from January 2009. According to data from US Labor Department, US economy added 114,000 jobs in September with the unemployment rate declining to 7.8% from 8.1%.

Asian economies are also suffering with World Bank saying that Asia's growth is slowing more sharply than expected due to weak global demand by cutting its growth outlook for Asia to 7.2% this year, down from its May forecast of 7.6%. The bank also warned that China is facing a risk of a stronger slowdown than expected due to government efforts to cool an overheated economy and inflation hurting global demand. It cut its outlook for China to 7.7% growth for this year, from May's forecast of 8.2% and to 8.1% growth for 2013, from its earlier prediction of 8.6%.

The World Bank is bullish for Southeast Asian economies due to strong demand and high investment spending in Thailand, Malaysia and Indonesia. It said that the ratio of investment to gross domestic product has now returned to pre-Asian financial crisis levels for Indonesia. World Bank kept its 2012 GDP growth forecast for Indonesia and Thailand at 6.1% and 4.5% respectively, while it raised its 2012 growth outlook for Malaysia to 4.8% from 4.6% and 5.0% for Philippines from 4.2%.

In South Korea, The Bank of Korea cut the base interest by 25 points to 2.75% for the second time this year, following a similar cut in July, in a move to shore up Asia's fourth largest economy from the economic slowdown of US, Europe and China. The decision came after International Monetary Fund trimmed the country's growth forecast for 2012 to 2.7% from its September projection of 3% and its estimate for next year's growth to 3.6% from 3.9%. The movement underlines the growing concerns of Korean policy makers for the negative impact of the global economic slowdown on the export driven South Korean economy.

SHIPPING MARKET

The third quarter of 2012 does not change the current outlook of shipping market with dry bulk carrier and tanker segments facing serious losses, while in the container, the normal peak winter season has a weak outcome on spot freight market environment. The first days of October give a bright eye for large bulkers, capesize and panamax, with subdued newbuilding activity and appetite for scrapping offering a sense of comfort for the difficult rest of the year and forthcoming 2013. Secondhand and newbuilding asset prices continue their downward trend offering investment opportunities for potential buyers with sellers trying to digest the low levels as freight markets do not support higher values.

In the **dry** market, panamax rates are on increase from improved Pacific and Atlantic activity lifting BDI to higher levels, with capesize still being on the high side, while supramax and handysize rates experience weaker levels of earnings. Capesize average time charter earnings are still above $10,000/day, while panamaxes are earning more than $6,500/day with Chinese and Indian thermal coal fixture volume being on rise and boosting further panamax rates. According to Commodore Research, Chinese demand for imported thermal coal cargoes has stayed particularly firm with coal stockpiles at Qinhuangdao floating well below 7 mil tons at only 5.5mt allowing Chinese thermal coal fixture volume to surge.

Iron ore inventories have eventually fallen to lower levels than 2011, a positive sign for stronger capesize earnings. Chinese iron ore port stockpiles were before the Golden Week Holiday in China at about 94 million tons, which marks the lowest level since late October 2011, implying that Chinese steel market is gaining strength. Before the Golden Week Holiday, Chinese iron ore fixture volume fetched record levels with 33 vessels chartered to haul iron ore to China on the week ending September 28th and 29 vessels on the week ending September 21st, as per data from Commodore Research. After Golden Week, there has been a small retreat in capesize earnings from a moderate week in Chinese iron ore fixture volume, but capesize congestion from previous hefty fixture volume of activity still supports the market.

BDI is on the high side from September 12th by closing, **Friday October 12th**, at 926 points, up by 5.8% from last week's closing and down by 57% from a similar week closing in 2011, when it was 2,173 points. Panamax segment records the highest gains this week with capesize earnings holding a firm momentum, while supramax rates still experiencing a downward revision and handysize are relative stable. BPI ended in green, BSI and BCI in red and with no change for BSHI. The highest increase has been in the panamax segment for a second consecutive week, **BCI** down by 0.9% w-o-w, **BPI** up 46% w-o-w, **BSI** down 2.3% w-o-w, **BHSI** no change.

Capesizes are currently earning more than $11,074/day, down $163/day from a week ago, while **panamaxes** are earning $6,937/day, an increase of $2,168/day. At similar week in 2011, **capesizes** were earning $31,329/day, while **panamaxes** were earning $16,702/day. **Supramaxes** are trading at $8,110/day, down by $205/day from last week's closing, about 27% less than capesize and 17% more than panamax earning. At similar week in 2011, **supramaxes** were getting $16,671/day, hovering at 47% lower levels than capesizes versus 27% today's lower levels. **Handysizes** are trading at $6,536/day; up $1/day, when at similar week in 2011 were earning $11,911/day.

In the **wet** market, the slow pace of demolition activity empowers worries for the troubled crude tanker operators. In the very large crude tanker segment, the AG-USG route remains distressed with WS loosing 0.25 points and standing at WS23.25 at negative time charter equivalent earnings of $(8,700/d) from WS29 at $4,900/day at the end of June. In the AG-SPORE and AG-JPN routes, WS lost one point at WS35 with $5,400-$4,700/day time charter equivalent earnings respectively, from WS41 $18,600/day at the end of June. The WAFR-USG route declined to WS40, 2.5 points less than a week ago, while

WAFR-China rates were stable at WS40 with $11,400/day time charter equivalent earnings, from WS43 at $20,500/day at the end of June.

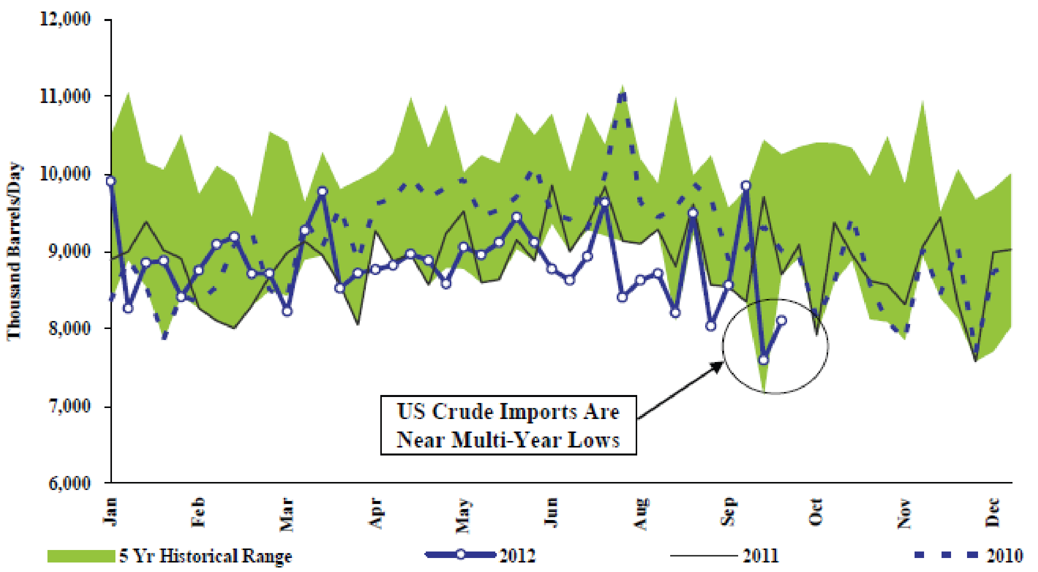
In the suezmax segment, the WAFR-USAC route gained one point on a weekly basis with WS closing at 57.5 with $8,900/day time charter equivalent earnings, from WS65 at $17,200/day at the end of June. The B. SEA-MED route gained 2.5 points to conclude at WS60 at $4,600/day, from WS72.5 at $16,300/day at the end of July.

The Caribbean aframax market has stayed stable for three consecutive weeks at WS90 with $6,700/day time charter equivalent earnings, from WS97.5 at the end of June. The N.SEA-UKC route is also stable with WS85 from August 10th at $11,900/day time charter equivalent earnings, from WS95 with $21,800/day time charter equivalent earnings at the end of June.

The Caribbean market is also quiet for panamax units with WS at CBS-USAC route being stable at WS115 with $11,500/day time charter equivalent earnings, from WS 120 with earnings of $15,500/day at the of June. In AG-JAPAN route, WS for tanker units of 75,000dwt won 3 points by rising to WS101 at $17,700/day time charter equivalent earnings, up by 6 points from WS at the end of June, while WS for tanker units of 55,000dwt lost 3 points and fell to WS107 at $10,400/day earnings, from WS120 - $17,200/day time charter equivalent earnings at the end of June.

The negative outlook of US crude imports by falling to lower levels than 1999 could not alleviate the pain of crude tanker operators from oversupply. According to EIA, cumulative year-to-date US crude imports are standing at 2.34 billion barrels, the lowest level since 1999 (2.31 billion barrels) and down 14% from the peak of 2.71 billion barrels in 2006. According to the EIA, US economy was dependent on imports for 45% of its petroleum consumption in 2011, down from 60% in 2005 and is forecast to reach 42% in 2012. Despite the declining trend in US crude imports, energy consumption of US grows by covering more and more its needs from its unconventional reserves from shale formations in North Dakota (Bakken) and Texas (Eagle Ford) that have been unlocked with new drilling technologies, like horizontal drilling and hydraulic fracturing.

US Crude Imports



Source: EIA, Wells Fargo Securities, LLC

Bunker prices offer a sense of relief for the struggling crude tanker vessel operators with IFO 380 fuel cost in Fujairah and Singapore falling below $640/barrel at the beginning of the week from $661/barrel at the end of September, while in Rotterdam fell to less than $620/barrel from $647/barrel at the end of

September. Brent crude oil price floats above $110/barrel from September 20th, when at June the average price was $95.07/barrel and $124.59/barrel in March. International Energy Agency supports that global oil markets are sufficiently supplied and excessively high prices are threatening to derail the global economy.

In terms of oil supply, Saudi Arabia's Oil Minister Ali al-Naimi said that the world's top oil exporter would strive to moderate crude prices and meet demand in the future. One positive development is that Iraq's oil output is estimated to increase to more than double by the end of decade and it will become the second largest oil exporter after Saudi Arabia by 2030, according to International Energy Agency. IEA forecasts that Iraqi oil production, which was roughly 3m b/d in September, will rise to 4.2m b/d by 2015 and 6.1m b/d in 2020. By 2035, it anticipates that Iraq could pump 8.3m b/d, marking an extraordinary recovery from less than 500,000 b/d it produced in the aftermath of the 1990-91 Gulf war.

In the **gas** market, one potential threat for the positive outlook of LNG spot freight market environment emerges as Japan is seeking to cater its LNG import demands with its own vessels. Tokyo Gas, a major buyer of LNG, stated in a conference in London, that it wants to increase the fleet that it already has for bringing supply into the country. Tokyo Gas executive Vice president said that expansion of the Tokyo gas fleet would depend on the company's LNG contracts with its suppliers and they prefer to use their own fleet.

In the **container** market, the Shanghai Container Freight Index was not issued last week due to the China's Golden Week National Holidays with oversupply in Asia-Europe trade route haunting the positive outlook of earnings for the post panamax newbuilding deliveries amid the slowing growth trade.

Major shipping lines have started to announce their plans to increase rates in an attempt to tackle the downward trend of Asia-Europe spot freight rates. Hong Kong's Orient Overseas Container Line (OOCL) has announced it will increase a general rate increase on cargo from Europe to Asia US$200 per FEU and TEU from November 1, while Danish shipping giant Maersk Line will apply a general rate of increases throughout its container service network from mid-October.

Despite the financial difficulties of liner operators consolidation is unlikely in the foreseeable future, according to Alphaliner, due to a number of barriers, with heavy debt of players being a major obstacle. Alphaliner Report points that owners wanting to expand will be more tempted by low shipbuilding prices to grow with the placement of new orders than choose to consolidate. It added that many players who were merger candidates they succeed in obtaining significant amount of capital from outside investors. Frence operator CMA CGM said to be on the verge of receiving EUR 150m ($190m) injection of funds from French sovereign investment fund Fonds Strategique d' Investissement, following Albert Ballin group's investment into Hapag-Lloyd in 2008, Yildirim's investement in CMA CGM in 2010 and 2011 investment of Quinenco in CSAV.

In the **shipbuilding industry**, state owned lender Korean Finance Corp is offering loans to struggling domestic shipbuilders to bridge the gap from European bank lending. Executive Vice President Choi Bong Sik said in an interview in Seoul that state Korean Finance Corp has begun offering working capital loans to shipyards last month and it has already agreed to provide as much as 700 billion won ($629 million) to STX Offshore & Shipbuilding Co.

In the **shipping finance**, Chinese bank lending seems to be the savour of the traditional ship bank lending due to European Banks' pullback from eurozone recession. However, it is still very hard for Chinese financial institutions to become the leaders of the ship financing as Chinese bank lending is a lengthy process with a lot of bureaucracy and stringent credit conditions, while it is being offered only to biggest and well known names. According to data from Marine Money, some of the sizable Chinese banks' ship finance deals between 2010 and 2012 include $1.23bn from Bank of China to Vale and $517m to Pacific International Lines (PIL), $550m from Bank of Communications to Grupo R and $543.9m to China Shipping Container Lines (CSCL), and $440m from Industrial and Commercial Bank of China (ICBC) to Mitsui OSK and China Shipping for a joint LNG project.

Under the tight ship financing conditions of European lenders, Norwegian shipping and energy bank DNB Nor Athens confirms that has been involved in funding with Export Import Bank of China and Thenamaris for two suezmax newbuildings, while a third facility has been signed with Korea Eximbank and Dynacom and other international lenders for three LNG newbuildings.

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