

Great Eastern Shipping Company Limited
Earnings Conference Call
(July 30, 2010)

Moderator: Good evening ladies and gentlemen. Welcome to the GE Shipping earnings call on declaration of its unaudited financial results (provisional) for the 1st Quarter ended June 30th 2010. I now hand over the conference to Ms. Anjali Kumar, Head of Corporate Communications at the GE Shipping to start the proceedings.

Anjali Kumar: Thank you for joining us on the Q1 call. Our Managing Director, Mr. Bharat Sheth, who normally joins us is been unwell and therefore, will not be joining us today. However, the entire top management team of the Company along with our CFO Mr. Shivakumar is here to answer all your queries.

Shivakumar: Good afternoon and welcome to the conference call to discuss the results for the 1st Quarter of FY 2010-2011. Since the press release on the results is quite comprehensive, I will restrict myself to the main highlights only.

You will see that though the standalone results were slightly worse than they were in Q1 of the previous year, the consolidated results are better reflecting mainly an improved contribution from the growth of the offshore business. Among the shipping business crude-tanker rates deteriorated during the quarter. We had a fairly strong quarter in Q4 of the previous financial year, and also a reasonably good quarter in the 1st Quarter of the previous financial year, the corresponding quarter. In the spot market performance the product segment and the dry-bulk segment was substantially better than they were in the same quarter of the previous year leading to improved day rates on the spot market vessels in those two businesses. However, we had re-pricing of several of our smaller product tankers at the beginning of April with the result at the overall TCY of the product tankers does not show the improvement that I have just mentioned on the spot rates. Among the other factors to note in this quarter results is the additional interest expense of Rs.31 crs on a consolidated basis which is being caused by the depreciation in the Rupee vis-à-vis the Dollar and that explains as a part of an accounting standard AS-16 which relates to interest costs.

Coming to the balance sheet, it continues to be in a healthy position with a net worth of over Rs5400 crs and gross debt of under Rs3600 crs and with the balance of cash and equivalents of Rs3200 crs we have a net debt which is well under control, about Rs300 crs. We, therefore, believe that we are in a good position to take advantage of any opportunities that may present themselves over the next few quarters.

Our order book stands at eight ships, which has total value of over \$570 mn of which we have already paid \$207 mn as on date. Coming to the NAV with some improvement in the value of tankers and some of the new building vessels during the quarter and also the strength of the dollar vis-à-vis the Rupee, the NAV has moved up to approximately Rs. 368 per share. This is after providing for the dividend which is to be paid out after the approval of the shareholders at the AGM. On a consolidated basis we have a total debt of about Rs5300 crs giving us a gross debt equity ratio of 0.91 and net debt equity ratio of just under 0.25.

You would have seen that our offshore oilfield services subsidiaries Greatship India Limited has filed its Draft Red Herring Prospectus the DRHP for its proposed IPO. We are advised that we are not permitted to give out any information that is not in the DRHP. So we will not be answering any questions relating to the offshore business, whether its regard to the company, its financials, the general condition of the market or outlook for the market. We, therefore, request you to restrict your questions to the shipping business and related. For any information on the offshore business we request you to refer to the DRHP which is a very comprehensive document which describes our businesses and the industry factors. Within this framework we are now happy to answer any questions that you may have.

Moderator: We have our first question from Mr. Bhavin Chedda from Enam Holdings.

Bhavin Chedda: Can you give us the spot-term mix for tanker and dry-bulk in this quarter?

Shivakumar: For the entire fleet, 47% of the days were on spot. Spot days for dry bulk were 51% and for tankers it was 47%.

Bhavin Chedda: For the last two quarters in-chartered tonnage has been almost zero days. Why so and from which Company this business is done?

Shivakumar: Inchartering is done by the chartering company in Sharjah. The in-chartering which was done in Great Eastern was on short term contracts where we had taken some contracts here and where we needed to in-chartered ships on a short-term basis to meet those commitments.

Bhavin Chedda: So GE Shipping does not do any in-chartering.

Shivakumar: No, GE Shipping could also do in-chartering but that is more for short-term requirements that it has to meet any cargo commitments.

Bhavin Chedda: How many ships were on dry dock during the quarter?

Shivakumar: During the quarter there were two ships which were in dry dock.

Moderator: We have our next question from Mr. Chetan Kapoor, from IDBI Capital.

Chetan Kapoor: My question is regarding your Point 2 in your notes to the results, i.e., the loss/gain what you have shown. Can you elaborate further on it?

Shivakumar: This has been appearing now since the 1st Quarter of last year. The accounting standard is that we have to re-value current assets and liabilities which are valued in foreign currency. We have to revalue them at the end of every quarter at the prevailing exchange rate at the end of the quarter. So for instance, if we had \$1 mn at the end of March that would have got valued at Rs44.89, that was at Rs4.48 crs as of end March and in end of June which is Rs46.5, it would have got valued at Rs4.65 crs. The difference is valued as a gain or loss on revaluation.

Chetan Kapoor: Revaluation of the contracts?

Shivakumar: Not the contracts, this is actually current assets or liabilities. So it debtors, creditors and bank balances.

Chetan Kapoor: In Point No.5, we have given that our holding in GIL has reduced to 97.6%. What percentage of the warrants have been converted?

Shivakumar: The 2.38% is the percentage which has been converted.

Chetan Kapoor: No, of the total warrants being held.

Shivakumar: Half the warrants which were issued have been converted.

Chetan Kapoor: Okay, it's not the full warrants?

Shivakumar: There are no further warrants outstanding, if that is what you are looking for.

Chetan Kapoor: Okay. And the other thing was, regarding our renegotiations what are likely to have on our fleet in the year FY11. What percentage of the fleet would be up for renegotiation can you give in terms of the percentage?

Shivakumar: Four to five vessels are up for renegotiations during this year and during the remaining part of this financial year and that is 12% to 13% of our fleet. That was in terms of number of ships. They are coming off contract. Now it is a question of whether we put them back on term charters or keep them in the spot market but they are coming off their time charter within the next nine months.

Chetan Kapoor: We have been keeping certain amount of our vessels on spot. So is this an initiative taken on our part that you want to keep certain vessels on spot because we are not getting right rates right now and we hence expect that the charter rates will move up?

Shivakumar: Actually we do this spot and time charter mix for a couple of reasons. One has to lock in some amount of cash flows to provide the base of safety. Second is also based on our market view and third is when you want to keep your position in a certain trade that we keep ships on time charter there. We also like to keep some ships on the spot market because the market is extremely volatile and you could go through 6 to 9 months of weak market and suddenly get to three very strong months that more than make up for the rest of the year. So in shipping it generally pays to have exposure to the market and therefore, we generally keep about half our ships on the spot market at any point.

Chetan Kapoor: That's true but this time what we are seeing is that a slightly higher percentage of our vessels are in the spot, so are we expecting an improvement from here?

Shivakumar: One is that it is not really a higher percentage of vessels that we are running on the spot market as compared to say one year ago. It is generally between 40% and 60%, the spot ratio. So its right in the middle of that, we are at about 50%. And to answer your other question, yes, at the current rate it does not seem to make much sense to lock in ships at time charters at the current rates in some of the segments.

Moderator: We have our next question from Mr.Vikram from Antique Securities.

Vikram: There is a sharp increase in interest cost and I don't think we have raised any debt. So what could be the reason for increase in interest cost?

Shivakumar: You see the Note No. 1, which I mentioned in my opening statements with regards to the interest cost. We have our borrowing mainly in dollars and the accounting standards says that when the rupee depreciates against the dollar the first part of the depreciation goes towards the notional interest differential between the rupee and the dollar. Therefore, the interest cost is high because the rupee has depreciated against the dollar by 3%.

Vikram: We have seen strong run-up in crude tankers rates in May particularly and we have decent capacity in spot market in tankers. But I have not seen any improvement in TCY in tankers. So what could be the reason for that?

Shiakumar: There was a run up in crude tanker rates but it did not last very long and it was not very strong rates. They were much stronger in the 1st Quarter of last year, the 1st Quarter of this calendar year, that was January-March and this quarter has been quite weak in fact on crude tanker rates. We saw a little bit of spike in between but then its weakened substantially.

Vikram: And what is the predominant route on which our tankers around typically?

Shivakumar: There is no fixed route, we try to see wherever the rates are the strongest, where we expect the rates to be the strongest. We are not restricted in the routes that we can run because we are running our modern fleet of double hull ships and therefore, our ships are running all over the world.

Vikram: We are sitting on cash looking for buying opportunities and, in fact, we are now seeing the improvement in NAV because of asset prices improvement. So does it become more and more difficult to now buy ships in secondhand market?

Shivakumar: Yes the values of ships have gone up. It is probably driven by additional liquidity coming into the markets. So we are not yet seeing a buying opportunity. You are right that values have gone up over the last few months but we are not yet seeing the prices at which we would like to buy. The price to value equation is not yet turned attractive for us.

Moderator: We have our next question from Mr. Mihir from Angel Broking.

Mihir: Would you be able to tell us the vessels which are coming off charter in FY11?

Shivakumar: The smaller product tankers come off charter at the end of every year. They are all on one year charter. So there will be at least six vessels coming off charter just the product tanker.

Mihir: We have seen a huge jump in the interest cost. The debt has not been rising accordingly. Can we have the number as in the cost in the debt which you have added in this quarter or probably last quarter?

Shivakumar: Actually we have not added debt. We reduced the debt a little bit from the previous quarter because we paid down some debt. This is completely due to the exchange fluctuation which we had of which the first part comes into interest and actually the amount of debt has come down over the quarter.

Mihir: So the cost of debt stands at?

Shivakumar: The average cost of debt stands at 4.2%, this is in dollar terms.

Moderator: We have our next question from Mr. Bhavin Gandhi from B&K Securities.

Bhavin Gandhi: Can you give us some color on where the spot and time charter markets are in each individual segment. What is the kind of differentials you are seeing in every market?

Shivakumar: In tankers we are seeing time charters substantially above the spot markets. For instance, VLCC segment you would see time charters at maybe between \$35,000 to \$40,000 a day for any period between one and five years. While the spot rates are somewhere between \$10,000 to \$20,000. Suezmax will see similar spot rates and charters probably in the high 20s. But generally they are at a premium. In the dry bulk side again on the larger sizes, the capesize for instance, because the spot rates are so low the time charter rates are higher than the spot rates. Spot rates are at \$15,000 which you probably have seen in the Baltic index and on the other sizes the time charter rates are more or less around the spot rates between \$15,000 to \$20,000 for Panamax and Handymax.

Bhavin Gandhi: What kind of slippages are seen in deliveries now?

Shivakumar: In the first half of 2010, we have seen lots of slippages, somewhere between 40% and 50% for dry bulk and about 30% for the tanker and still going at the very strong rate.

Bhavin Gandhi: What is your take on the balance half of the year. You have seen some of these deliveries now coming through or they are likely to be further delays?

Shivakumar: It's anybody's guess. We just cannot figure out what is the reason for this slippage and whether there have been actual cancellations or it is just delays in the deliveries.

Moderator: We have our next question from Mr. Avishek from PUG Securities. .

Avishek: Can you quantify the effect of exchange rate fluctuation on the interest cost?

Shivakumar: It is Rs31 crs on a consolidated basis. On a standalone basis it is Rs28.5 crs.

Moderator: We have our next question from Mr. Prasoon from Jaypee Capital.

Prasoon: Do you have any vessel in remaining part of FY11 to go for scrapping from tanker fleet or bulk fleet?

Shivakumar: Yes we expect probably two more vessels to be phased out during the current financial year. We have already phased out two of the older tankers and we expect at least two more to be going out in the remaining part of this financial year, maybe three.

Moderator: We have our next question from Mr. Raj Gandhi from Principal Mutual Fund.

Raj Gandhi: Based on the current freight rates, if you see on the tanker side your average realization are much lower than what your benchmark rates typically would be so is it there where you are looking for lot of re-pricing to happen?

Shivakumar: Okay the time charter rate it is difficult to take that because we have not put any ships on time charter and the spot rates, generally the way that they calculate it it's a little different from how it happens in real life. It does not take any waiting into account and it has also got a lag. See what happens is that they do it on the basis of the index between 1st April and 30th June, the average of the index and it's for one particular route. Now what happens is that the earnings which reflect in the April-June quarter is actually more likely to be average of rates from March to May because you fix it March, then it loads and then it discharges during, say April, and that result comes into April results. So there will always be a little bit of a lead and lag in that.

Raj Gandhi: But you are saying mostly your Aframax and Suezmax are on spot that is not where you have done a lot of time chartering.

Shivakumar: No, in Aframax there are only two ships which are on spot the remaining are on time charter and the Suezmax are all on the spot market.

Raj Gandhi: On the product side if you can tell when are they coming up for renewal?

Shivakumar: The products will come up for renewal at the end of the financial year. These are generally done on a financial year basis, the smaller product tankers which are on the coast.

Moderator: We have our next question from Ms. Ashwini Desai from Bajaj Allianz.

Ashwini Desai: You have debt of Rs5300 crs; can you give me a sense of what is the amount due for repayment in the next 2 to 3 years?

Shivakumar: On a consolidated basis; typically the repayments in one financial year are about a \$113 mn.

Ashwini Desai: You have always maintained such high amount of debt and similarly high amount of cash. Is it that you follow this strategy or globally shipping companies do this?

Shivakumar: Some people do this; some shipping companies including some listed ones take no debt at all. And then there is the other end of the spectrum where companies take 4:1 debt. So we are actually somewhere in the middle I suppose but more towards low debt. There are shipping companies which take huge amount of debts and which take no debt at all.

Ashwini Desai: Okay and this is how you will continue to be, such high debt and cash?

Shivakumar: Actually it depends on how the cycle goes. The idea of keeping this cash is not that this cash is going to stay on our balance sheet permanently which would be a bit of a waste of resources but the intention is that this cash is being kept for us to be able to take advantage of any asset opportunities that may come up. And if we are able to see assets at a reasonable valuation then it will help us to move quickly to buy this. That's the idea of keeping the cash not that it is going to be permanent cash on our balance sheet. And of course, we also have a large order book which needs to be funded.

Ashwini Desai: Sure but your order book is some RS2600 crs.

Shivakumar: That's right, of which already RS800 to RS900 crs has been funded.

Ashwini Desai: My second question is regarding your cost of debt. You said that your cost of debt is 4.2% in dollar terms. How much is the hedging costs?

Shivakumar: No we do not hedge in Rupees because the idea of taking dollar debt is because we are a dollar company. Our revenue flows are mostly in dollars, our assets are in dollars and that is why we borrow in dollars. So we do not hedge the dollar-rupee part of the debt.

Moderator: We have our next question from Mr. Rajesh Ravi from Ambit Capital.

Rajesh Ravi: Sequential decline we are seeing in the crude tankers is around 30%. So have you seen any further deterioration. Like in June we have seen about \$20,000 per day in crude tanker, would we be seeing lower than these numbers in September quarter?

Shivakumar: No, currently the spot market we are seeing slightly better spot rates on the crude carrier and on the product tankers as well.

Rajesh Ravi: Sir on the interest cost front again, I would be repeating the same question, AS-16 that you have accounted for. This is the first time that you are using this

AS-16. So would you be treating this additional Rs31 crs that you have incremental cost that you have shown on your P&L, as a notional entry only or how is it?

Shivakumar: It is an entry that can be reversed, for instance, if it goes back to, let us say to Rs44.89 was the rate as of 31st of March this would be reversed in the next quarter.

Rajesh Ravi: Okay, so its not a cash based entry.

Shivakumar: The moment it is paid then it is cash.

Rajesh Ravi: So you would be booking at that point of time, whatever is the difference.

Shivakumar: That is right.

Rajesh Ravi: And sir a general sense on the market how do you see the tanker and the bulk carrier market going forward at least for this and next year?

Shivakumar: The order book in the bulk carrier market is much higher than in the tanker as it appears on paper. The order book is somewhere around 55% to 60% of total fleet. We are continuously having slippages of about 40% to 50%. But it is still a worry because it is very high growth for the order book and the other issue with the dry bulk market is that it is mainly a China story. And we do not know which way China is going to go whether it is going to continue growing at a very hectic pace which will absorb most of the dry bulk tonnage and also you have got Europe which is a very large consumer of steel where steel production has gone down over the last couple of years. On tankers there seems to be some sign of demand coming back in the last few months we have seen storage going down between January and June and again the tanker phase out of the single hulls is likely to happen by end of 2010 or early 2011. Those are a few positives for the tanker business. Also we have got a smaller order book for the tanker between 20% to 30% and that gives a little bit more comfort on the tanker business. Still everything is dependent on the state of the global economy and how the Western economy has recovered.

Moderator: We have our next question from Mr. Ravi Shenoy from Motilal Oswal.

Ravi Shenoy: Sir I wanted to get some understanding of the ship delivery schedule of your new orderbook?

Shivakumar: We have three bulk carriers coming in Q4 of this financial year. In the 1st Quarter of next financial year we will have two more bulk carriers. Then in the 4th Quarter of FY12 we will have two VLCCs and in the 1st Quarter of FY13 we will have the last VLCC.

Ravi Shenoy: My next question was on the FOREX component in our debt, how much would that be in Rs5300 crs?

Shivakumar: It's almost everything in foreign borrowings. Also about 30% to 35% of our cash is held in foreign currency.

Ravi Shenoy: Could you also give some idea of bunker cost during the quarter?

Shivakumar: It's about Rs75 crs for this quarter.

Ravi Shenoy: My last question is on the product tanker side. I did not get the number of product tankers that we had on the time charter at the start of the year.

Shivakumar: There are five in spot market and rest of them are on time charter.

Moderator: We have our next question from Mr. Ashish Jain from Morgan Stanley. .

Ashish Jain: Going through the commentary on the tanker market outlook in your press release and kind of comparing it what we had said in March quarter, it seems we are turning positive on the tanker market outlook. Is that the right interpretation?

Shivakumar: The indications are becoming a little more positive. We are seeing growth in the US demand after a few quarters of negative growth. Gasoline demand is picking up. We have seen the storage demand for gas oil go down substantially between the beginning of the year and now. So the signs for the tanker market seems to be a little more positive than it was a few months ago.

Ashish Jain: On your dry bulk side can you give asset-wise break down of what is on spot and what is on charter?

Shivakumar: On dry bulk we have three vessels on charter and three vessels on the spot market. The Capesize and Panamax are on charter but they have very little time left on the charter, maybe less than a month. One ship is just being redelivered to us and she will go on the spot market and another ship will be redelivered in the next couple of months and there is one Supramax which would be redelivered in the next six months.

Anjali Kumar: Thanks everybody for joining in and we will be putting up the transcript of this call on our website in the next few days. If you have any other queries, please feel free to contact us and we will be happy to answer all your queries. Thank you very much.