



“The Great Eastern Shipping Company Limited Q3 FY 2019  
Earnings Conference Call”

**February 11, 2019**



**MANAGEMENT: MR. G. SHIVAKUMAR – GROUP CFO, THE GREAT  
EASTERN SHIPPING  
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COMMUNICATIONS**



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**Moderator:** Good evening, ladies and gentlemen. Welcome to Great Eastern Shipping Earnings Call on Declaration of its Financial Results for the Quarter ended December 31, 2018. At this moment, all participant lines are in listen-only mode. Later, we will conduct question-and-answer session. At that time if you have a question, please press '\*' and '1' I now hand the conference over to Ms. Anjali Kumar – Head of Corporate Communications at The Great Eastern Shipping Company Limited to start the proceedings. Thank you and over to you.

**Anjali Kumar:** Good afternoon, everybody and thank you for joining us for the conference call for the Q3 Results. I hope all of you have already received the soft copy of the results. I would now hand over the call to our Group CFO, Mr. G. Shivakumar to take you through the Salient Features and we will later do Question-and-Answer Session. Over to you, sir.

**G. Shivakumar:** Hi, good afternoon, everyone and welcome to the results conference call for Q3 FY19. I trust you would have been through our results and press release. And as happened in the last quarter, the results have swung by the movement in the exchange rate during the quarter. In the previous quarter, we had a swing due to weakening of the rupee by Rs.4 versus the dollar, that is between June and September. In this quarter part of it was reversed, we saw the rupee strengthening by Rs 2.77 to the dollar and that obviously had a beneficial impact on the P&L account. For the nine months, of course, we still have a negative impact because we started in March at about 65 and December end we were at 69.77.

Looking at what happened to the business, first, asset prices. During the quarter, the bulker asset prices were flat Tanker values moved up almost 5% as a result of basically the strong markets that we saw in Q4 of calendar 2018. As a result of it, our standalone net asset value moved up by about Rs.15 per share to about Rs.369 and including offshore where asset values have remained unchanged, the consolidated NAV range has moved up to 420-445.

Coming to how the markets have performed, after performing very badly in the period from April to September, both crude and product markets delivered a positive surprise in the October-December quarter. We touched upon this when we had a conference call in November. The major factor in this crude tanker performance seems to have been the increase of 2 million barrels per day in Chinese imports year-on-year which led to a reported stock build of about 1.5 million barrels per day in Q4 of 2018. Providing this of course, US crude oil exports continue to grow at about 900 kbd for the quarter and Middle Eastern crude exports were up as well. For the year the crude Tanker fleet grew by about 0.5% while trade grew by about 1%. The current spot rate for crude tankers across the board, whether it is Aframax, Suezmax or VLCC, are down to the teens, so (+/-15,000).

While product demand continued to be quite poor with zero to marginal negative trade growth, some switching of ships to the crude trade following the strength in the crude Tanker market gave us a small spike in earnings in the latter part of the quarter. The fleet for the year grew by about 2.25% and trade was marginally negative. The order book for product Tankers continues



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to be low at about 8%. Current spot rates are back to the low teens now, a little above \$10,000 a day for MR Tankers. US LPG exports were positive and this was a contributory factor to market recovering somewhat from the middle of 2018 to the end of 2018; however, current spot rates are down again to the lows that we saw in April 2018 at around \$5,000-6,000 a day for VLGC. Last year, the trade growth was marginal for LPG. While the VLGC fleet grew by about 2% during the year. The order book for VLGCs stands at about 15%.

Coming to Dry Bulk, China disappointed somewhat during the year; the Dry Bulk trading to China grew by only about 13 MMT in the year. Iron ore trade saw small negative and the last quarter was very negative for coal specially the last month as there was a sudden clampdown on coal imports in China and imports dropped from over 20 mt in the month of November to only about 10 mt in December. This led to a significant fall in spot rates.

The fleet grew by about 3% in 2018 while trade is reported to have grown by about 2%. The order book stands at about 11%. And recently spot rates have dropped off significantly, thanks mainly to the Vale dam disaster which you may have read about, and the disappointing grain trade. So rates across the board are below \$10,000 a day for Capesize, Kamsarmax, they are probably somewhere around the \$5,000 to \$7,000 range.

The net result of most of the above is that we have had the strongest quarter for TCY's since probably end of FY17 or early FY18 across all sectors and you would have seen that in our press release as well.

The offshore market continues to be a challenge. The news on the offshore vessels is that we have obtained long-term contracts of five years for four of our vessels in the Indian market. These rates are significantly higher than the last rate that we fixed. Those rates were actually for only 9-10 months period, not strictly comparable but there has been some improvement in the rates for vessels.

We have also obtained a three year contract for our rig Greatdrill Chitra which is coming off contract next month. The rates have been quite disappointing; they have not moved up since the last pricing which was done in end of 2017. Currently, Greatship has three assets without contracts. One PSV, one 80-ton anchor handler and one MPSSV.

With regard to sale and purchase activity, we have sold one VLGC, the 'Jag Vishnu'. This is our oldest VLGC, it was built in 1994. We expect the vessel to be delivered to the buyer sometime in the first half of FY20. In shipping, we continue to have a large spot exposure. We expect there will be significant turmoil in the market as we get towards the IMO 2020 rule taking effect from 1<sup>st</sup> Jan 2020 and everybody prepares for the fuel changeover and we are keeping significant part of our fleet spot.

With that, I conclude my briefing. I am happy to take questions along with the team here.



- Moderator:** Thank you very much, sir. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Vaibhav Badjatia from HNI Investments. Please go ahead.
- Vaibhav Badjatia:** Just wanted to understand management's thought process regarding buyback. I notice that last time we did buyback sometime in 2013. Just wanted to understand that while we are deciding to go for buyback or not to go for buyback, what kind of valuation benchmark do we look at – do we decide based on NAV, do we decide based on some other factors?
- G. Shivakumar:** Buyback is something that the board considers from time-to-time when they see the opportunity to create value by doing a buyback. It is one of the capital allocation tools which is available to us. So again we have a finite amount of money based on our risk appetite, that we can invest. Now, whether we invest in ships or we invest in our shares, depends on where we see relative value. Last time we did it, it was based on the discount we were getting to net asset value, and at that time our stock was trading at 45% discount to net asset value when we did that. We do not have a number in mind. But that is the decision which is taken, that is something that will be seen if and when an opportunity comes up and what other opportunities are there, whether ships are available to buy cheap, etc., what kind of ships are available and what our balance sheet is like. But typically the important factor is what is the net asset value.
- Vaibhav Badjatia:** Just to continue on this, last time when we did buyback it was around 280 per share and though we have done well relative to the competition and I think we will continue to do well and kudos to management for all these great efforts. But in terms of book value per share or in terms of NAV from that point to this point, I do not see substantial returns and rated on that buyback money deployed. Just wanted to understand where did we go wrong last time or do you think that we went wrong at that point when we decided to go for buyback?
- G. Shivakumar:** It is a good question you are asking it is something that we asked ourselves as well because we bought the stock really cheap at that time at 40% discount to net asset value. What happened is that the NAV itself collapsed because of what happened to offshore markets. The shipping markets were at a low point in the cycle in 2013 but the offshore markets were not. So rigs at that time used to be valued at \$200 million which came down later and currently trades at \$100 million or lower and that is where the NAV itself collapsed, and that is where the question comes up when you are thinking of doing a buyback do you want to buy a portfolio of assets which includes Bulk carriers, Gas carrier, Product tankers, Crude tankers, Rigs and supply vessels or do you want one focused investment which maybe at a very cheap point. That is the difference between a buyback and buying a ship. One is buying a portfolio of assets, the other is buying one very specific asset and taking a call on that market. So that is the reason why that investment has not done very well...of course, there has been some dividend, etc., but you are right, it has not done great. For instance, if we had bought a Crude tanker at that time, we would have made 10% plus IRR on that investment.



- Vaibhav Badjatia:** Basically, what you are saying is it is primarily because of the decline in offshore asset that we have not been able to ...?
- G. Shivakumar:** Yes, that is absolutely correct.
- Moderator:** Thank you. The next question is from the line of Bhavin Gandhi from B&K Securities. Please go ahead.
- Bhavin Gandhi:** Firstly, on the Vale thing, how do you think this will play out, this is slightly structural in nature or you think it can get sorted out in six months' timeframe?
- G. Shivakumar:** The problem is with the tragedy of this magnitude is that it will go beyond the normal commercial things and the courts are in it and there is a lot of uncertainty about the direction now. When it first happened, they said we are going to shutdown 40 mt of production but that we will compensate a large part of it from our other mines. Now there is another dam which has been ordered to shut down by the court and that is around 20-30 mt. So we do not know how it is going to play out. One thing we know is that it is not good news. If anything, it is bad news because even if that cargo is sort of compensated it is going to be much lower in terms of tonne-miles.. So, it is a significant negative for the market. And that is priced in now, you can see it in time charter rates, you can see it in the spot market of course where capes are \$8,000/day.
- Bhavin Gandhi:** Secondly, just wanted to understand the tax element. It seems to be very-very volatile. So if I look at a consolidated number, that has gone up to again 43, 44 crores or it used to be 10 crores run rate in the first half. So how should one look at this?
- G. Shivakumar:** Lot of this is MAT and this will keep swinging because we have one transaction to be completed which is the purchase of the rigs, we have to close out that purchase of the rigs from our Singapore subsidiary and there will be a significant tax swing on account of that because there will be some gains on our investment in that subsidiary just on account of exchange rate. So it will swing a bit but that is only a factor this year. Also because the drilling business is still producing profits and that is the only thing which is really taxed, and a swing in the last quarter is also because there was a drilling loan revaluation which was a loss hitherto which now got reversed partially when the rupee strengthened.
- Bhavin Gandhi:** Sir, if you can just take us through the spot exposure in the three segments that you have now?
- G. Shivakumar:** In Gas Carriers, we are fixed in a big way, so we have one which is to be sold and which will be delivered immediately on completion of a current time charter, we have two which are on time charter to the very end of this year or early next year, we have one which is on time charter for at least four to five months more and we have one which is on time charter for three months more, that is five of them and there is one which is currently spot. We have locked in a large part of our gas carrier fleet which is comforting because the rates are so terrible now.

- Bhavin Gandhi:** On crude and product?
- G. Shivakumar:** In crude, we have one contract which ties up 2 ships effectively all the way up to April, so that is two out of our 12 crude Tankers, the remaining 10 operate in the spot market, then in the product Tankers we have four of our ships on time charter, again they do three to six months time charter as well, I would say across the board 80% on spot, for the next one year forward I would say 85-90% spot exposure because a lot of the charters are just rolling off as they are short-term charters.
- Moderator:** Thank you. The next question is from the line of Khushboo Dadia from Capgrow Capital Advisors. Please go ahead.
- Khushboo Dadia:** I just wanted your outlook on the trade rates and asset prices on segment of crude oil and dry Bulk in coming 12 to 18-months?
- G. Shivakumar:** So, let us look at what we are expecting for the markets in these sectors. In both of them there is one common factor which is the new IMO 2020 rule which is coming in from 1<sup>st</sup> Jan 2020 on sulphur emissions. We think that there will be a significant disruption to the trade itself towards the end of this year as everybody starts cleaning their tanks to prepare for the new sulphur norms and for the new fuel. So that is something which we expect to happen by the end of this year. And as we go into 2020, one thing which broadly will tend to happen is that if you get more expensive fuel, ships will tend to go little slower, and that was common to both of these things. Now, looking at Crude tankers, we think that the next couple of months are likely to be weak because we have a lot of deliveries coming in this year. This is the highest number of VLCC deliveries ever in terms of number of ships and therefore it is quite heavy in supply; however, towards the end of the year as the new fuel norms kick in, we think that the Tanker trade itself could potentially pick up and trade patterns could get adjusted in a significant way. Also, we expect that a lot of the ships which are going to fit scrubbers will go into the ship yards and not be available for trading which will constrain the supply of those ships artificially. Therefore, the market is expected to tighten by the end of this year and that tightness should continue and strengthen through 2020. So that is for the Crude tanker market. In the Dry bulk market, same factors will apply with regard to ships which are fitting scrubbers and with regard to the high price of fuel; however, the demand side is not as clear, the Dry bulk is mainly a China story, it has now also turned out in the last few weeks to be a story of Vale and Brazil because it is the cargo which is not available, then the ships are certainly going to face a deficit. So it is a little more uncertain. We could easily have this coming back in the next six months and then you are having to catch up with those cargos and therefore you have a long weak period and suddenly have strength in the dry Bulk market. But it is not easy to call, its much more uncertain than the tanker markets because it is not as steady in growth. So in the Crude tanker markets, we would say that there should be a turnaround by the second half of this year. In dry Bulk, hopefully there will be a recovery because we cannot do without these 40 mt of cargo of iron ore. It will come



from somewhere, maybe it will come from Australia for now but at some point we hope that Vale will come back and provide those cargos into the market.

- Khushboo Dadia:** My last question is can I get to know the current debt position for short-term maturity?
- G. Shivakumar:** Short-term maturities I would say between now and March 2020. For Great Eastern Shipping itself we would be about Rs.1,000 crores. And on a consolidated basis, add on another Rs.350 crores.
- Moderator:** Thank you. The next question is from the line of Ranjit Kothari from Vibrant Securities. Please go ahead.
- Ranjit Kothari:** My first question is that the Crude tanker price which had picked up from the last quarter you said has again come down because of supply side pressure. In the Bulk the fiasco has happened in Brazil. Is it correct?
- G. Shivakumar:** Yes, in Crude, it is not so much in the supply pressure, it is just that there was a temporary spike due to some stock building and importing into China and now it is normalized. So it has gone back to where it was in August, September.
- Ranjit Kothari:** But that level itself by historical standard is on the lower end?
- G. Shivakumar:** That is correct, yes.
- Ranjit Kothari:** So do you think what does it trigger which can cause it to come at more attractive levels?
- G. Shivakumar:** Yes, the big trigger actually is IMO 2020 which will trigger changes in trade pattern, refining pattern and therefore we think will increase ton mile demand significantly for crude tankers and product tankers and that is something which will happen by Q4 of this year.
- Ranjit Kothari:** As far as our company is concerned, how are we trying to comply with this – is it by installing scrubbers or is it by using the low sulphur oil or how are we trying to position ourselves?
- G. Shivakumar:** We are doing different things for different ships. We have contracted to install scrubbers on seven of our ships where the numbers justified installing scrubbers. On the other ships, we will use the compliant fuel which is a low sulphur fuel.
- Ranjit Kothari:** I was reading a few reports saying that there could be a shortage of the requisite fuel by the industry. Can you throw some light on that?
- G. Shivakumar:** It is tough to know that. We are already seeing some compliant fuels being offered into the market for testing by some of the big oil companies, but your guess is as good as mine. It is

tough to know what the refining industry is doing in this and we are doing a lot of research in it but we have not yet got a clear picture. We need to find a way to substitute or replace about 2-2.5 million barrels per day of high sulphur fuel oil. We do not know what the refiners are doing and how they are going to deal with it, or whether they have already prepared to replace that. On the other hand, there is a lot of refining capacity which is coming in this year, little over 2 mbpd of new refining capacity is coming in this year, and that will help somewhat to produce more middle distillate. Basically you need middle distillates to substitute for this which is like diesel, it is called marine gas oil. You can also have low sulphur fuel oil which is a blend. So, overall, we don't really know how the refining industry is dealing with it..

**Ranjit Kothari:** So, in this light is it possible that the deadline for compliance gets pushed back or is such a scenario plausible?

**G. Shivakumar:** It is unlikely. Everybody is making preparations, and this has been discussed a couple of times at IMO and there have been some push back saying that it is not going to be changed. So, we do not think it is likely to happen.

**Moderator:** Thank you. The next question is from the line of Chaitanya Shah from Aditya Corp. Please go ahead.

**Chaitanya Shah:** Sir, my primary question is regarding the crude ship market. If we see since the last five to six years return on equity and return on capital employed in this business have generally been poor. So why is it that there is a huge orderbook like you just mentioned we have the largest fleet of the VLCC coming in, I just want to understand what is the motivation behind having such a huge order book when the returns are so poor?

**G. Shivakumar:** That is because there is always a new story which is used for marketing. The story which is being used for marketing to get these orders is that IMO 2020 is coming and that there will be huge demand for ships especially eco ships with scrubbers. So in 2012 when there were no orders, the story then was that they are making super ecoships and therefore you should go and order new ships which will be more competitive than every other old ship. So, there is always a new story and there is always people looking to put money unfortunately. So people are not looking at the past returns necessarily, they are saying that okay, I will build a ship which will be better than every other ship which is existing today and therefore it will make superior returns. Unfortunately, that is the truth of our industry. So we have not had the cycle play itself out. Normally the cycle would play itself out where you have a boom, you have over ordering, you have a bust, you have under ordering and then you get a boom again. This time we have had the over ordering but not the under ordering because lot of cheap money has been available. So, that is the reason for having a high order book.

**Chaitanya Shah:** Do you see the situation changing in the near future because the money is still there right as far as I understand?





**G. Shivakumar:** Money has become more expensive. The critical thing is the availability of equity money really and we saw it in 2011-12 when private equity money came into shipping. Now, there is no new private equity money coming. There are public markets providing money. But they are not providing money at good valuations because they are not believing in the story. So the amount of money coming in has reduced significantly. There will always be a new provider, for instance, you had Chinese leasing companies coming in to fund ships, or Chinese EXIM bank funding orders in the Chinese shipyards. Yes, money will continue to be available. The hope that we have is that shipyard capacity will not be very high and will get reduced over a period of time because ship yard even with these order books are not really making money and slowly but surely ship yard capacity is reducing which reduces the threat of more and more ships coming into the fleet. Again, with regard to money, if next year pans out as we would expect as a strong year, then again you could well see orders going in again into ship yards.

**Chaitanya Shah:** Has scrapping picked up in any meaningful way, something that would be meaningful to reduce the fleet in the industry or just like your view?

**G. Shivakumar:** Yes, scrapping picked up significantly in the first half of last year for crude tankers. So you had negative growth for I think the first six or seven months and then it slowed down when the market became strong again people did not scrap ships. So you still got only 0.5% growth in the crude tanker fleet which is quite good and maybe that is why you had a little bit of strength in the market towards end of the year. So, scrapping is there, scrapping will be a function of rates and it will be a function of how much its going to cost you to keep the ship running. With the new regulations which are coming in, not just the IMO sulphur emission norm, but the ballast water treatment system. That is a dead investment because at least in a scrubber you get money back, but the ballast water treatment system is just the cost of continuing to operate and for VLCC that could be \$1.5-2 million. That is something that people are unlikely to want to spend and that could result in scrapping. And maybe with all these VLCCs coming in this year, maybe we will see a significant amount of scrapping happening at least in the crude tanker space, and that is really the most sensitive to market movements. The other area you can have scrapping in a big way is in Dry Bulk if you have the current markets continuing, you could have scrapping in a big way.

**Moderator:** Thank you. The next question is from the line of Dhruv Jain from Ambit Capital. Please go ahead.

**Dhruv Jain:** Sir, I had a question with respect to fuel cost. So we saw that the fuel cost increased significantly in the quarter. Are we not able to pass this or how it is working?

**G. Shivakumar:** Fuel cost is yes, it has increased because the price of crude oil you would have seen increased. Whether you pass it on or not, the cost will show in your books. If you pass it on, it will show in your revenue, so you will have Rs.30 crores additional cost and you will have Rs.30 crores additional revenue.



- Dhruv Jain:** So in the offshore business, with respect to borrowing cost, we see that there has been a significant uptick in borrowing cost from last year. What is the reason for that?
- G. Shivakumar:** According to the accounting standards, we borrow in dollars and our average spread is maybe 2% over LIBOR, the dollar borrowing cost is a little under 5% in dollars. So let us say that your rupee cost of borrowing and in that case it is notional because they do not do rupee borrowing, let us say it is 10% and your dollar cost of borrowing is 5%. The first 5% depreciation which is the difference between rupee cost of borrowing and dollar cost of borrowing is to be debited to interest cost and that is why the interest cost has gone up because you had a depreciation of the rupee versus the dollar in the six months of this year, you had in excess of 5% depreciation, right. So, that is why you have a much higher interest cost.
- Dhruv Jain:** We saw the revenue days declined by around 5% in this quarter YoY. Any reason for that sir?
- G. Shivakumar:** We sold a couple of ships, but it could be just on account of incomplete voyages, voyages coming in and going out. So it is not really a significant thing. There is no major reason for this change. It is just a timing difference.
- Moderator:** Thank you. The next question is from the line of Chaitanya Shah from Aditya Corp. Please go ahead.
- Chaitanya Shah:** Sir, this might be a little out of context, but I just want to understand does the stronger Yen affect the shipping and our industry in a significant way?
- G. Shivakumar:** Little bit because if we have a stronger Yen, the ships from the Japanese companies do not tend to come, it affects the second hand ships. So when the yen is strong, then they are not as keen to sell because the ships will be priced in dollars and they will not get as many Yen. The ship building cost maybe a little bit but not a huge impact really.
- Chaitanya Shah:** Sir, are we finished with all the impairment charges that we have to take on the offshore side or do you expect any more impairments to come in?
- G. Shivakumar:** No, I cannot say we are finished on impairment charges. You may notice that I mentioned our NAV at 420-445 while our book value is about Rs.460 a share which means that there is a loss hiding somewhere...when I say hiding, I am not saying we are hiding it but it is there in the books and therefore the market value is lower than the book value of the assets. Now, the impairment calculation or testing is done based not just on market value but on projected future cash flows and sometimes those assumptions change based on what has happened to markets and rates. Again, you could have a change in the asset value, the rig which is valued at say \$80 million today may suddenly be valued at \$50 million, then you could potentially have an impairment. So I cannot answer that question because I do not know the answer to that question.

But certainly, some of the offshore assets are on the books at a value which is higher than the current market value.

**Chaitanya Shah:** Sir, by when do you expect us to have better clarity in terms of the application of IMO norms and what the refineries are doing, the event is a year away, just want to get timeline from you?

**G. Shivakumar:** As far as we are concerned, this is going to happen. So that bit on the application of IMO norms we are fairly clear on. It looks like it is going to happen on schedule. Now, with regard to the refineries, we are looking for information every day. Hopefully at some point we will get some more clarity. But it is really tough to get that information because it is so widely dispersed. There is no one super organization which is going to give you this information like a regulator who is going to say all this is available. So we are just looking at different sources of information and trying to piece together the puzzle. So, we hope to have an idea within the next six months but all we are going to do is prepare for the changeover. We have to prepare for the changeover on the ships that we are not installing scrubbers on. We have to prepare for the changeover to the new fuel. On the ships that we are fitting scrubbers on, we will fit those scrubbers on them and see and then there is nothing much else to be done. We will continue to use the same fuel. So there is nothing really which is pending a decision where we need information for making a particular decision.

**Chaitanya Shah:** Do you have a sense in terms of where is the industry in terms of preparation for this norms to come in, what are your peers doing globally?

**G. Shivakumar:** Lot of listed companies are fitting scrubbers including much smaller ships which we could not justify, A couple of listed companies have said they do not believe in scrubbers. So there are different views between different market participants. But the most important thing is that 90% of the fleet will have to change over to low sulphur fuel oil. That is going to be a massive change because you have to clean out your tanks and prepare for the new fuel to come. You cannot have the residue of the high sulphur fuel oil sitting in your tanks because then you will not be compliant, if you mix your new fuel with that. So that is going to be a massive change in the last few months of 2019. We are preparing for it, we do not know about others but everybody will be preparing for it and there will be a significant amount of turmoil in the market at that time.

**Chaitanya Shah:** Are you optimistic about this projection coming in, how do you feel about it?

**G. Shivakumar:** We think net-net it should have a positive impact on the tanker markets. We think the trade patterns will be changed. We think that there may be more transportation of not just crude oil but also refined products and therefore it should be overall positive. I mentioned a market turmoil. Most disruptions which take away ships from the market are beneficial for freight rates, because you are just reducing the supply of ships, right. So we think overall it should be positive for the market. Operationally it is a big challenge because you have to figure out how to do the fuel changeover and how to do the tank cleaning. As there are 30,000 ships, of which 90% will

have to do this by end of this year. So operationally, it is a big challenge, but we think in terms of how it can affect the market it can have a very positive impact on the market which could go all the way through 2020.

**Chaitanya Shah:** What is the kind of noise that you are getting from China right now? What is your outlook in terms of the market that China is presenting right now for the next three or four years, if you could just give me your view?

**G. Shivakumar:** We do not have any special insight into China but one thing I will say is that we keep talking about China as the big factor and it is a very big factor. So last year the estimates are that the Dry Bulk trade grew by about 110-120 mt, that is 2018 over 2017. Of that, only about 20 mt was actually incremental trade into China. There are other trades which are also providing some boost to the Dry Bulk market. But finally it will come down to China because that is where you see the huge volumes of Dry Bulk goods transportation.

**Moderator:** Thank you. The next question is from the line of Himanshu Upadhayay from DHFL Pramerica. Please go ahead.

**Himanshu Upadhayay:** Can you throw some light on the offshore side of the business and how are you looking at it? Also, what are the expectations for 2019 – do you expect CAPEX to grow from here or the net value of capacity utilization on both offshore vessels and the boats? You are saying that you have taken three years contracts on the offshore boat incrementally. Any views how you are playing in the market based on the conditions which are prevalent in the market, some insight on that?

**G. Shivakumar:** Just one thing I like to correct you, we got five-year contracts for four of our PSVs. We got a three-year contract for one of our rigs. Those are the contracts that we have got. Coming to where the market is likely to go, we are at least likely to see a positive CAPEX number for this year, that is according to some of the reports that we see, offshore CAPEX being positive. Last year I think CAPEX was positive, but it was mainly onshore. So, you will have utilization improvements happening which should take utilization, still utilization is below 60%, hopefully take utilization up to at least 65%. . Now whether this results in pricing power we have to see it. We have seen some pricing power coming in the vessels business in India. We saw a significant increase in rates in the last tender. So 70-80% increase in rates from the last time but not in the rigs. Unfortunately, all of these are micro markets and these are tender-based businesses. So whatever is L1 will get the contract. So while we expect that market should tighten, meaning that the slackness should reduce a little bit at least from 60% utilization to maybe 65%, we do not think there is a huge amount of pricing power which is really coming in. So our approach is really to take the contracts which are available and keep the vessels and the rigs operating so that whenever the recovery comes, because we have pricing happening every year. Next year we have one rig coming off contract, we will have an opportunity to price in the middle of this year. There will be a tender at some point. But the year after that we have two rigs

coming up. We will have an opportunity to price next year. So if the market improves, we will take that improved pricing. So the focus is keep the asset employed and then whenever the market recovers and pricing improves, we will get that pricing in our tenders.

- Himanshu Upadhayay:** The rates on the offshore boats, are they flattish or they are still muted?
- G. Shivakumar:** They went up by 70-80% from the last done. Though that was for 9-10-months contract, and this is for a five year contract, but it is a significant improvement in rates.
- Himanshu Upadhayay:** So, can we say that based on what fleet, what we have deployed, further deterioration on the offshore is unlikely, based on what the rates we are getting now or we can project a straight line from here on?
- G. Shivakumar:** . I think we have passed the bottom of the market. I think the pricing which happened last year was really rock bottom for the vessels and it had to go up from there which it did. Now whether this sustains or not, is a different matter but at least we have passed them, I do not think we will see the pricing of early last year again.
- Himanshu Upadhayay:** Your CAPEX plans or interest in assets on the shipping side, how are you looking at the market or incremental capital deployment what is your thought process there?
- G. Shivakumar:** We are close to fully invested. We still have a little bit of CAPEX capacity, and we look at whatever is cheap . Whatever asset we find at a good price, we will look at it but having said that we are very close to being fully invested now. So we are not likely to do a huge amount of CAPEX from here on.
- Moderator:** Thank you. The next question is from the line of Ranjit Kothari from Vibrant Securities. Please go ahead.
- Ranjit Kothari:** I have two questions: One is on the offshore business, you said that the vessel rates have increased significantly. Could you throw some light on the rigs side what is likely to happen?
- G. Shivakumar:** On the rig side, the pricing has been at very similar levels to what was done in late 2017 which was quite disappointing. We thought there would be an improvement, but unfortunately there was no improvement. That is what has happened on the rig side.
- Ranjit Kothari:** Second question was on the crude tanker. You said that the two aspects in that particular segment which can help in recovery – one is with the IMO, the supply side, we see some disruption, and on the demand side, the trade routes and patterns might change. So if possible can you just throw some light on the trade pattern side exactly what are the key drivers which will lead to the state pattern shift – is it US shale production which will be exported or is it the production of the low

sulphur oil within refinery, so some color on that, what will drive the state in changes and will it be a scalable change?

**G. Shivakumar:**

I will give you a couple of examples because this is a very complex thing and we are still getting to grip with it. So one thing you mentioned is US exports. That is a big positive we see US exports grew by almost a million barrels a day 2018 over 2017 which is a great thing for the market because it is **long haul** demand because it travels a long way, mostly they come to the Far East. The other way that you could change the trade pattern and this is a hypothetical situation, let us say that you have a simple refinery somewhere in Europe and they will look to take in the lowest sulphur crude because the simple refinery does not have any secondary processing. So whatever fuel oil is produced through the first run, goes out as high sulphur fuel oil which is going to be a losing product. It was always a negative crack product but it will become more of a negative crack product. So they will look to minimize on that. There is a larger disincentive to production of high sulphur fuel oil now. What they will look at is to source the lowest sulphur crude oil which will enable them to produce let us say 0.5% fuel oil which maybe different from the crude oil which we are sourcing today which maybe just be based on the convenience of the closest port or the closest source of crude oil. So now your objectives were let us get it from the closest producer to let us get it from the best possible which is the lowest sulphur which maybe 10 sailing days away from you. That is why trade patterns can change. So the other thing that could happen is if the refining industry has actually not prepared for this sufficiently, is that you could have a requirement to just process another million barrels per day of crude oil just to meet this extra demand for gas oil which is just additional trade of crude oil because refinery throughput is going to go up by a million barrels a day in my example. You could also have a surplus of high sulphur fuel oil because there is not enough demand for it and if you have a large surplus you will run out of shore storage very soon and then you will have to store it on ships which will take up crude tanker capacity because these typically are stored on crude tankers. So these are the various scenarios that can happen. It is a very complex thing and finally it comes down to how the refineries doing to deal with IMO 2020. That is where you will get a clearer picture of what can happen to tanker markets.

**Moderator:**

Thank you very much. Ladies and gentlemen, as there are no further questions from the participants, I would now like to hand the conference over to Ms. Anjali Kumar for closing comments.

**Anjali Kumar:**

Thank you very much all of you for being on the call with us. As usual we will be putting up the transcript in a couple of days. And you are always welcome to connect with us for any further questions that you all may have. Thank you very much again for joining us.

**Moderator:**

Thank you. Ladies and gentlemen, on behalf of Great Eastern Shipping Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.