"The Great Eastern Shipping Company Limited's (G E Shipping) Q2FY17 Earnings Conference Call"

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MANAGEMENT: **MR. G. SHIVAKUMAR – CHIEF FINANCIAL OFFICER, THE GREAT EASTERN SHIPPING COMPANY LIMITED**
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Moderator: Good Evening, Ladies and Gentlemen. Welcome to The GE Shipping Earnings Conference Call on Declaration of its Financial Results for the Quarter ended September 30th, 2016. 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'. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. 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 Ms. Kumar.

Anjali Kumar: Thank you, Margaret. Good Afternoon, Ladies and Gentlemen and Welcome to the Conference Call for our Q2 Results. I hope all of you have had a chance to look at the results which we have sent out few minutes ago. I can directly hand over the call now to our CFO -- Mr. Shivakumar who will take you through some of the highlights. Sir, over to you.

G. Shivakumar: Good Afternoon, Everyone and Welcome to the Conference Call. So I will straightaway go into how the markets were in the last quarter and over the 9-month period from the beginning of this calendar year. So we mentioned in the last conference call that Tanker market had weakened since June 2016 and they stayed extremely weak through the second quarter of this financial year and mainly influenced by two factors -- product demand reportedly grew by only 0.8 million bpd, resulting in low crude throughput at refineries and Secondly, there was a supply disruption due to a Force Majeure in West Africa which resulted in a big drop in the number of cargoes which were available for ships to carry. Therefore, both Crude and Product Tankers faced lower demand growth and High Fleet growth. So the Fleet growth in Tankers for both Crude and products is running at about 6% annualized for the first 9-months of the calendar year.

It is also estimated that may be 10 to 15 VLCCs came out of floating storage adding further to the supply pressure.

The good news is that in the last month or so the Force Majeure in West Africa were lifted, cargoes are back and Crude Tanker markets are therefore a little stronger since early October.

On the LPG market, LPG carrier running continue to be extremely weak with huge fleet growth outpacing fairly strong US export growth, but obviously the export growth was not enough to absorb about 20% annualized growth in the fleet.

In terms of US Crude production, we saw it dropping by about 800 kbd in the last quarter, that is over the same quarter in the previous year and this caused the similar increase in imports again, so the trade has grown but not enough to absorb the strong fleet growth. That is a broad message of the Tanker markets.

In Dry Bulk, Dry Bulk freight rates have shown some signs of life especially with commodity prices rising and so Q1 of this calendar year was the weakest, and it moved up a bit on average in Q2, and Q3 has been stronger than Q2 as well. Again, nothing to get too excited about, they are still not profitable numbers on a book breakeven basis, so it does not quite absorb interest and depreciation, but at least it is showing some signs of life.

So there have been quite positive developments on trade -- Iron Ore imports into China have continued to be strong growing by about 23 mt in the quarter and about 65 mt in the 9-month period over the same period the previous year, which has been quite positive for the markets; however, the fleet has grown by almost 2% in the 9-month period, and from the middle of the previous quarter, so that is from May, June or so, scrapping has been very disappointing partly because of the monsoon and partly because of the improving freight rates and the confidence that owners are getting. Indian coal imports also have dropped reportedly by about 10 mt in the first months of this calendar year. So India has not been helping the Dry Bulk market really.

On order books, the order book is at about 17% for Crude Tankers, 11% for Product Tankers and for Dry Bulk it is at about 14%. We are seeing slippages in deliveries especially on Dry Bulk because of the great stress which is there caused by the low freight rate. So it is very unlikely that the entire order book will be delivered. However, even if it is 30% to 40% slippage in Dry Bulk it is still going to mean a fleet growth of close to 10%. So that is still difficult to absorb considering the trade growth that we are expecting.

The good news on this is that because of the divergence between second hand values and new building prices, there is little or no ordering in any ship type across the board. So, currently, the ratio of new building to say a 5-year-old ship is close to the highest level it has been in the last 20-years and therefore we do not see much of ordering taking place.

In sale and purchase activity, we have recently contracted for purchase of one Supramax Bulk Carrier and two Aframax Tankers and we expect to take delivery of them in the next 2 to 3-months.

Coming to Asset Values, the standalone net asset value (NAV) per share has gone down from Rs.317 to Rs.311. This is due to a drop on average of about 10% in Tanker values, in the 9-month period from January to October these values are down about 30% to 35% in Tankers. Dry Bulk values were up marginally in this quarter, but still down about 25% in the 9-month period. So we do not yet have a fix on offshore values, again the ranges that you are getting for valuation of the rigs are extremely wide and therefore we do not have a consolidated NAV to declare. If we just had the range, we expect that we would have to give a range of about Rs.70 to Rs.80 per share which really does not make sense for us to do.

Coming to the Offshore Market, A&P spending estimates are what everybody looks forward to and the reports that we have been seeing lately people are talking of a further 15% cut in A&P spend in 2017, this is on the heels of 25% cut in 2015, 20% cut in 2016. So that is the third consecutive negative year which is for the first time in living memory. I think once I mentioned in a couple of quarters ago that we had seen as bad cuts as 2015 and '16 only once before and that was in the mid-80s, but those were only two years of cuts and there was a strong bounce back. So this is now sort of in unchartered territory.

Utilization levels continue to be dismal for the global offshore market, with utilization estimated at below 60% for Rigs and around 50% for Vessels. Business conditions are extremely difficult and we count one win which we had in the international market of a 2-year contract for one of our Vessels, we count that as a big success for our marketing and operational capability.

The balance sheet continues to be very strong; our net debt standalone is at around $150 million, our consolidated net debt is at around $400 million or slightly lower than that, so we are comfortable there and that is what is giving us the confidence to go out and do CAPEX in these weak markets, we have committed to CAPEX of almost $150 million since the start of this financial year.

So now with that brief summary of the happenings in our business and what we have been doing I invite questions and we would be happy to take any questions on the markets or on what we see for the future. Thank you.

Moderator: Thank you very much. We will now begin with the Question-and-Answer Session. The first question is from the line of Vaibhav Badjatya from Athena Investment. Please go ahead.

Vaibhav Badjatya: I have a slightly broader question just on the recent quarterly numbers. I just want to know what our hedging policy is. How do we hedge our exposures? Do we just take a view on exchange rate or we say that given whatever cash flows are in US dollars, so whatever is in rupees on our balance sheet we will just hedge it to US dollar?

G. Shivakumar: The approach that we take is that our earnings, our assets are denominated in dollars, therefore we do not need to do too much hedging, so we have our earnings in dollars, our loan repayments are all dollar-denominated, and therefore we do not necessarily have to edge at all, so we have incomes in dollars and we have outflows in dollars except for the expenditure that we do in India.

Vaibhav Badjatya: The reason I was asking this question is that somewhere in 2009 or '10 we had some INR debt and we send it to US dollar, I think we had about Rs.1100 crores of negative balance sitting in our networth and the way I see it is that if that Rs.1050 crores will come to our PL and cash flows over FY'18 to FY'21, on the top of it if the exchange further depreciate by say similar amount over FY'21-22, then it will be another Rs.1050 crores and the Rs.2000 crores of P&L hit, out of which Rs.1000 crores will be additional to net worth, it's kind of too big an impact for us in the next year given that our last year profit was Rs.2000 crores. So would it not be that prudent that given the long-term rupee depreciation that is there historically, that will leave our INR liabilities as it is and unhedged than to convert INR liabilities in two years' dollar liabilities?

G. Shivakumar: There are few questions within your overall question, so I will try to address all of them if I remember them and we will come back to any that I miss out. So first one is I will take the last bit which you said which is of continuous depreciation which is an interesting point, but we are not there to take a view on the differential between rupees and dollars because if we actually borrow in rupees for a dollar asset we are actually creating a risk, correct, because our funding currency is rupees and our earning currency is in dollars. So we do not want to now introduce a new element of risk, shipping markets are risky enough without introducing a new element of risk.

Vaibhav Badjatya: Even the basic premise of investing in assets is that they will generate some positive cash flows at least, and if that is the assumption and then if there is some US dollar cash flows net-net, that will be there from the asset, then those cash flows given the historical INR depreciation are unhedged, then definitely it would help us if the cost of hedging is not unfavorable?

G. Shivakumar: So let us take that again; one, yes when we make investments we expect to make positive net cash flows from that investment on a dollar basis. So let us go to that issue which you discussed with regard to the swaps that we did in 2009 to 2011. So we raised funds in rupees, swapped them into dollars, so we created a dollar liability effectively, right. What did we use the dollar liability for? Most of it was used for acquisition of dollar assets. Now those dollar assets do not get revalued on an MTM basis. So while you see an MTM on the rupee-dollar swap you do not see an MTM on the ships. So we will not revalue the ship upwards, let us say you buy a ship for $10 million which in 2011 was Rs.45 crores and let us say it is still worth $10 million, that today was Rs.66 crores. The swap will be valued at another Rs.20 crores of liability on that exact same deal, if you funded with that $10 million equivalent and swapped it, but the ship has not got revalued on the opposite side; however, that value is sitting in our balance sheet. So on a commercial basis it makes sense. I agree with you that this P&L thing is an uncertainty and nuisance because of the way that these two different legs of the transaction are being treated; however, we cannot escape that. We have to make the decision not on the basis of accounting what works best in accounting but what works best on a commercial basis. The decision that we made is that on a commercial basis and on a risk management basis it makes sense for us to create liabilities in dollars because our assets and inflows are in dollars. So that is one. Now coming to what is going to happen to them eventually? So we have the MTM which has happened which is there as of last year where you put some numbers, I would not go into exactly what the numbers are, it is there in the balance sheet in any case, but basically some of it has gone out in the transition and it was there in our net worth all along. So even when it comes into the P&L it will go from the net worth from a hedging reserve into a P&L. Some of it has already gone in the transition; it has already gone through the transition reserve and therefore will not come into the P&L. Now let us look at henceforth, so henceforth all MTM changes will come through the P&L and they are coming through the P&Ls from the last quarter itself. This introduces an element of volatility in the P&L and you can see that, in this quarter also we have had a gain on the MTMs and therefore we have this volatility. So we have had a higher profit in this quarter because of that. But, we will not have as you are expecting a big chunky amount of hit which we have to take in our P&L in 2018,'19, '20. So that concern need not be there, that is going to be on an ongoing basis.

Vaibhav Badjatya: Assuming that the rupee will not depreciate further?

G. Shivakumar: No, so again we are coming down to taking a view on currency, our business is not to take a view on currency, and our business is to take a view on shipping markets. So we are not going to take the view on whether the rupee is going to depreciate. So today the interest rate differential is 5% between the rupee borrowing and the dollar borrowing. So we are not going to take a view on whether it is going to depreciate by 6% or 4%, we are going to say I am going to match asset and liability because that is what it makes sense for us to do. We consider ourselves to have some knowledge about shipping, we consider ourselves to have not much knowledge about the currency markets, and we prefer not to take those views aggressively. It would be convenient for us from accounting purposes and to smooth out our P&L to just take this 5% extra hit, but on risk management basis, on commercial basis it does not seem to make sense for us, and that is the decision that we have taken.

Vaibhav Badjatya: I agree on that front, accounting is the way it is and we should not take that into account in our decision-making, whatever commercially makes sense we should do that, but I am just trying to understand given commercially if you see that we are creating asset in US dollar and MTM value of the asset because ultimately we want to derive value from the cash flows than MTM. So, over a period of time, the cash flows from that asset will give us the benefit on the MTM value of the ship. So if the cash flows are going to be in US dollar…sorry, I will join back the queue.

Moderator: Thank you. The next question is from the line of Bhavin Gandhi from B&K Securities. Please go ahead.

Bhavin Gandhi: Just one clarification. You mentioned the range and the offshore value of about Rs.70 to Rs.80. Can you elaborate a little bit more on that?

G. Shivakumar: We get a range of valuations. Our brokers are having difficulty giving an exact number because we have not seen too many transactions. So if you just take the bottom of the range and the top of the range that will work out to about Rs.80 per share if you take the top and bottom.

Bhavin Gandhi: If I am not mistaken, the last declared consol minus standalone NAV was about Rs.200, is that correct?

G. Shivakumar: Yes, it would have been about Rs.200. Just to give you a small picture of it, the base one would be somewhere around Rs.380 at the low end, going up to say Rs.460 at the high end.

Bhavin Gandhi: Also wanted to get some sense on the utilization for our OSV fleet. What is it currently and what is the repricing due during the course of the year?

G. Shivakumar: We currently have four vessels idle and we have two more repricings coming up by the end of this year and we have one rig repricing coming up in the next 2-months.

Moderator: Thank you. The next question is from the line of Himanshu Upadhyay from DHFL Pramerica Mutual Fund. Please go ahead.

Himanshu Upadhyay: Out of that $150 million CAPEX what we have committed this financial year, how much is pending? What we have paid in six months and what is remaining due in the next six months?

G. Shivakumar: About 45% is due in the next 3-months.

Himanshu Upadhyay: So in this year only it will get completed?

G. Shivakumar: This $150 million is what we have committed in the last 6-months in the beginning of April. So we have some commitments made two years ago which are still to come, that is not counted.

Himanshu Upadhyay: What is the total commitment in next six months?

G. Shivakumar: That is about $100 million, let us call it.

Himanshu Upadhyay: In the offshore market side, number of revenue deals has reduced drastically, means 1835 YoY to 1521. So, how many ships were idle or boats were idle in last quarter versus last year?

G. Shivakumar: Two were idle through the quarter and two for part of the quarter.

Himanshu Upadhyay: Right now four vessels are idle?

G. Shivakumar: That is correct.

Himanshu Upadhyay: Repricing, are we negotiating or have we completed those negotiations?

G. Shivakumar: No, discussions are on, but we do not have much clarity yet on the next employment, so we are in discussions and we are awaiting a tender actually.

Himanshu Upadhyay: This rig comes out when?

G. Shivakumar: Due somewhere between mid-December and end-January based on the contract.

Himanshu Upadhyay: On the crude tanker market where we have seen a lot of ordering activity happened in last one year or in one-and-a-half year. What is your sense -- will there be similar or what type of deferment, slippages do we expect on the Crude Tanker market?

G. Shivakumar: I am not seeing much order here in the last 1-year. So according to my data ordering in the first 9-months is 5.5 million deadweight Crude Tankers. So that is one of the positive aspects that we see in the market that there has not been much ordering.

Himanshu Upadhyay: But the order is around nearly 14-15%.

G. Shivakumar: The order book, yes. Most of the ships will get delivered. It is not such a weak market that people would not be able to take delivery, it is not like in the Dry Bulk market in the past where you ordered a ship at 100 million and by the time you took delivery it was worth 40 or 50. These there might be 15-20% MTM loss. So I think those ships will be delivered.

Himanshu Upadhyay: The prices have started coming off and are reaching those 2013 level means nearly 10-15% further away, but we are still seeing charter rates or the period charter looking okay. What is the sense on the period charters in Crude Tanker market and again Product Tankers if you can just give some view?

G. Shivakumar: Rates on period charters have dropped quite a bit from the start of this year. Asset values I mentioned have come up by 30-35% from the beginning of this year. So charter rates also have come off by a significant number.

Himanshu Upadhyay: I was just saying that in 2013 we used to see that VLCC say around $10,000-12,000 and even period charters around that level, we are still seeing around $28,000-29,000?

G. Shivakumar: No, there were no period charters done at $10,000-12,000, the spot market hit $10,000-12,000, I do not think it went below $20,000 at all for VLCC, in fact, I do not think decent quality Suezmax also would have done charter, not a 15-20-year-old ship, would have done less than $17,000-$18,000. So it has not been that bad. So rates today are also probably so far Suezmax probably a 1-year charter must be somewhere in the $18,000-20,000 range which is sort of where it was in 2012-’13, so not far off, may be today it is marginally higher than it was then which is probably why asset value is also slightly higher than they were at that time.

Himanshu Upadhyay: What is the outlook for the season, I mean in general the third and four quarter are the stronger ones or the fourth and first quarter?

G. Shivakumar: Yes, October has been quite strong specially VLCC has moved up, Suezmaz also have recovered quite a bit, so Suezmax were struggling through August-September specially because of the West Africa Force Majeure and that is a big loading area for Suezmax. So they were struggling at that time and now the market seems to have recovered in October. So it is doing much better, again, so seasonally it is supposed to do much better now.

Himanshu Upadhyay: On the Product Tanker side, ton mile improvement has been there or what is the outlook because there were a number of refineries which were coming in Middle East, Southeast Asia, China, India and the Crude you would move to US, what type of ton mile demand would have happened in Product Tankers in last one year or this calendar year?

G. Shivakumar: Ton mile demand has not been bad, to put a number on it, it is quite tough but 3% to 5%-ton mile demand I think is possible, but lot of the demand has actually come from dislocations or just from trade moving in strange directions and from storage and forced storage. I am not talking about Contango-based storage but basically cargo not finding a buyer. So you have therefore our ships going around Cape of Good Hope rather than through the Suez Canal, etc., because cargoes cannot find buyers.

Himanshu Upadhyay: The new deliveries which will happen in both Crude and Product Tankers, what is the type of view you are forming for calendar year 2017?

G. Shivakumar: '17 is going to still be a pretty heavy year for Crude Tankers, and for Product Tankers I think it will come off, I think we have seen the worst of that delivery for product tankers at least for MRs, may be LRs there might be some delivery. So then it comes off quite sharply. So 2018 should be a decent year. Hopefully also if the rates continue like this, we will see some scrapping, we have the new ballast water rules. So hopefully we will also see some pressure coming from that because people have to spend the money for that as well. So maybe we will see some scrapping in the Container segment. We have seen scrapping now happening of 10-15-year-old ships, several 10 to 15-year-old ships getting scrapped because of where those markets are. We have seen 15-year-old Capes also get scrapped, may be in Crude sometime we will see some ships getting scrapped, last month for the first time since 2014 I think we saw VLCC get scrapped. So maybe that is just a sign of things to come and we will see some scrapping happen in the Crude Tanker segment as well.

Himanshu Upadhyay: The period charter market, how has MR behaved and what is your view?

G. Shivakumar: MRs are down, so from a year ago they are probably down by $5,000 per day exactly a year ago to now, which is a big number for an MR. So yes, that is about where the markets are now.

Moderator: Thank you. The next question is from the line of Saroj Poddar from Equity Master. Please go ahead.

Saroj Poddar: Sir, my question is on the Dry Bulk market. Currently, our vessels are earning EBITDA-positive or they are making losses at EBITDA level?

G. Shivakumar: Our vessels are EBITDA-positive, so in some cases we are covering interest, so we may be just marginally below breakeven. We are covering OPEX and covering possibly depreciation, but again it varies from different vessel, but certainly covering operating cost.

Saroj Poddar: You mentioned scrapping disappointed in Q2 because of monsoon and employing freight rate. So how do you see scrapping in this segment going forward?

G. Shivakumar: Again, this will depend on how the freight markets perform, unfortunately, the moment we see some hope in the freight market people hold back on scrapping, so it will depend completely on how the freight rates perform. The second factor as I was mentioning earlier was on the ballast water treatment where people have to spend money on their next dry dock. They have to spend a significant amount of money to put in some new systems to meet the regulations. So that hopefully will add some pressure. Again it will go according to the dry docking cycle. If the ship is due for dry dock then I think that people will be more amenable to scrapping. So we should see some scrapping picking up again unless we have quick recovery in Dry Bulk which I think is unlikely. So we should see scrapping come back some time in the next 2 to 3-months. So traditionally seasonal weakness is seen in the first quarter of the calendar year. So let us see how it pans out in first quarter next year. So first quarter of this year was very high scrapping and then it stayed like that at least till end April and then after that it came off significantly. This year the first quarter of course was abysmal; cape size was making below operating cost, I think even the smaller sizes were making below operating cost. So we were actually EBITDA-negative in that period, and that really pushes scrapping. So let us see how freight rates develop.

Saroj Poddar: Product Tanker rates have corrected by about 34%, I am talking about year-on-year basis. So is it sustainable or do you see further rate reduction going forward in this product tankers segment?

G. Shivakumar: Actually, Product Tankers last year were exceptionally high, so I am not surprised that we had a drop in those rates, because last year was just an exceptionally strong quarter, this year still has not been bad, but we do not expect it to go much lower from here, we think it will go a little lower, we are expecting that we have not seen the bottom of the Tanker markets yet, probably the next year may be weaker than this year by a little bit, but not too much. So we still have significant growth to come next year, so about 6% gross lead growth in Product Tanker and 8% in Crude Tanker. So that is going to add to pressure. So probably next year is the year when you hit bottom on freight rates in the Tanker space.

Saroj Poddar: On the Offshore market, as you mentioned consecutive third year the rate spending is reduced. So where we go from here? What is the like market outlook going forward?

G. Shivakumar: In offshore, we think that we are probably at the bottom, some reports say that the pace of decline has come off significantly and that has been slowing down though it does not feel like that when ships come off contract and you cannot find a new contract. But we do not think it could get much worse, because the more they shrink now it will be of sharper bounce back. So we think we are sort of close to the worst of the market and that we should see some recovery. The only question is when that recovery comes because even if you see next year an average crude oil price of say $60 per barrel which will incentivize further exploration, further activity and therefore more utilization of assets. That will really kick in with a lag of a year or so. That means that next year's average of $60 will result in improvement in demand in 2018. So it will have a lag and so we will have to be patient and wait out this period. We saw this in 2010-11 as well where it took time for the bad market to hit us and then it lasted past the oil price which went back up to $60.

Saroj Poddar: But sir, do you think this is a structural problem in this oil offshore market like dispute between OPEC and non-OPEC members regarding the oil output?

G. Shivakumar: The structural change can happen only if offshore oil actually does not come back. You cannot have 50% drop in exploration activity and expect that there will be no impact on future production. So you need to physically drill and extract the oil. So this will hit at some time in the future. This is what happened. So why did you have the boom from 2003? Why did oil go from $30 to $140? Because you had a long period of underinvestment in E&P activity. If you have this underinvestment over the last two years, maybe next year or so, you will have a bounce back at some time. The natural trajectory of an oil field is that it depletes. Unless you keep doing work, your production will keep declining. If that keeps declining, you have to make it up sometime, otherwise your overall production is going to drop. So you need that exploration to go on. If you do not do it, you can manage without it for 3-4-5-years but then you will get a sharper turnaround when it happens. This is the same in shipping as well for five years if you do not build any ships you are just laying the foundation for the next boom.

Saroj Poddar: Sir, how do you see CAPEX from Indian players like ONGC in offshore market? Are they coming up with new projects offshore?

G. Shivakumar: We would not comment about specific customers, but India is one of the markets which has been steady in terms of the number of assets being utilized and in some of the markets we have seen some players saying we have taken more assets for longer-term because of the ability to lock in those assets at a cheap point in the cycle. We wish that would happen more here. But in any case it is one of the steady markets around the world, lot of the markets have been reducing assets in a big way, we have seen that in Brazil, we have seen that in maybe the North Sea as well. So it has been fairly steady, it has not increased in anyway.

Saroj Poddar: About our current fleet status in offshore, how many vessels are working, how many vessels are idle or about to go idle?

G. Shivakumar: Four vessels are currently idle and three will complete contracts by the end of this year.

Saroj Poddar: Rest are all working currently?

G. Shivakumar: Yes, the other vessels are working on contract.

Saroj Poddar: You said one rig is coming for replacement?

G. Shivakumar: One rig is completing the contract between December and Jan-Feb.

Moderator: Thank you. The next question is from the line of Manish Kumar from HSBC. Please go ahead.

Manish Kumar: I have two questions. First is you talked about divergence and the price of new build and five-year-old, you also talked about ratio having shot up. If you could share that ratio that will be helpful. My second question is related to what you talked about US crude production declining a little bit, as a result of which food import has gone up, and from what we understand the product export has actually picked up. So do you see this trend strengthening which in turn will help the carriers, or do you see this as kind of plateauing and stay at current levels?

G. Shivakumar: One is on the ratio, just to take an example of five-year-old capesize value today is at about $24 million give or take a couple of million and it depends on who you ask, it is somewhere in the high 30s million let us say, at least at 1.5x rise for a new build versus a five-year-old ship. Similarly, I expect for an MR product tanker, probably at $21-22 million, something like that for a five-year-old and you are probably somewhere in the low 30s for a new building. So typically, this ratio is at about 1.15x to 1.3x which means that five-year-old second hand ship is much more attractive than the new building. Again, the new building is little different from the five-year-old because the new building will be one of the ecoships but remember at today's price of fuel the ecoship at premium is worth much less than what used to be two years ago and it still does not justify the higher ratio. What is keeping the new building prices up? The yards are unwilling to cut cost because they are not permitted to buy there, say the lenders, or they just think that they will only take orders at these numbers, they do not want to bring down the prices and maybe the earlier orders of their owners will be marked down in value which is good because then it means that less people are ordering new ships because it makes more sense than to buy a second hand ship that gives more value.

Manish Kumar: What is the normative ratio usually which kind of makes a neutral?

G. Shivakumar: So 1.3 is probably the outside, so 1.2-1.25. So that is on the ratio between the new build and the five-year-old ship.

Manish Kumar: My second question was on the increased movement of or maybe scope for further increase in oil product in US?

G. Shivakumar: Big story about US growth in product exports it is there, so it grows but 100,000-200,000 barrels per day growth, it is not a huge number, on the margin it makes some difference. Crude oil coming down is a big thing, but again this is the shale which is coming off we suspect because that is the highest cost crude which is sitting there. But again that is something which can come back if oil prices go up. So this year I think we have seen on average for the year 9-months-on-9-months about 550,000 to 600,000 barrels per day drop in production. Again, this is something that can come back. It is because of the price pressure which we are seeing, but let us see how that plays out. There are more imports going into the US. Unfortunately, it has not helped in a big way the crude tanker business because though the trade has increased to that extent, the fleet has also increased and the fleet has increased more than that and that is why this year the markets are weaker than last year.

Moderator: Thank you. The next question is from the line of John Mathai from Bloomberg Intelligence. Please go ahead.

John Mathai: You touched about this a little time ago about the ballast water regulations. Just wondering how is that going to impact? What are the costs that you are going to see for your vessels? In addition, if I could have your thoughts on the new IMO regulations, how that is going to pan out for the fleet especially if there is sufficient 0.5% sulphur fuel available in the Indian coast?

G. Shivakumar: So the first one, so ballast water treatment system is a done deal and it could cost anywhere between depending on who you ask, for the smaller ships $400,000 to $500,000 and for the bigger ships maybe a $1 million.

John Mathai: That is not much and there are different systems?

G. Shivakumar: No-no, I will correct you there; it is a lot of money for a Dry Bulk operator, let us say you have got a 15-year-old capesize bulk carrier and you have to spend $2-2.5 million on the dry dock if you also have to spend a million dollars doing the ballast water treatment system and on the other side you can get $6 million from scrapping the ship, you have a swing in your cash generation of $9 million. So it is a lot of money. A million dollars is a lot of money in the Dry Bulk market these days. So it is going to be a significant factor in people's decision-making process especially because the markets are weak.

John Mathai: Will any of the yards do it or is it specific yards do you need to take it?

G. Shivakumar: No-no, so your normal drydocking yard will do it, you need to procure the ballast water treatment system and install it at the yard. So when you do your dry dock you will install this as well. So there will be some requirement. So you need to have some extra power capacity on the ship to run it. So you need to have that little bit of surplus on your existing power generation infrastructure on the ship, because you need power to run the ballast water treatment system. So, all those constraints are there, but you need to basically procure the ballast water treatment system and install it at the next dry dock. The requirement is to install it at the time of the next dry dock. So that will be done. It is not too complicated really to do so long as we can find the space and the power for it. Technologically it is not a challenge. Now, coming to your next question on the sulphur rules 0.5%, I cannot comment on what is the availability on the Indian coast. What we have seen is comments from some of the oil companies which said that they may not be ready with this by 2020. So this is comments from a recent conference I think which happened last month where some of the oil companies said that they probably will not be ready with such a large amount of 0.5% sulphur capacity fuel.

John Mathai: This is the one in Singapore?

G. Shivakumar: It is, correct. So, that is obviously going to be a little bit of constraint which means that they may well have to burn diesel oil or gas oil instead of traditional fuel oil if there is not enough low sulphur fuel oil available, which has its own complications with regard to the engine because you need to then take other safeguards with the engine, the engines are built for high sulphur fuel oil. So it is a challenge technically and it is also going to be a challenge to have enough of the compliant fuel available. So we will have to see how this pans out. It is very early days yet. So this is just the feedback which we got from this conference, where the oil companies said we may not be ready with this amount of low sulphur oil. If it is going to be now burning gas oil or diesel instead of fuel oil, that is a big difference to the cost of operations, the smallest of ships will burn 20 tons per day and the difference is maybe $200 per ton, that is $4,000 per day of additional cost which we will have to take. So that is going to be a tough one.

John Mathai: Just from your perspective, the compliance of both ballast water treatment and when the low sulphur fuel happened it is global, the compliance of this especially in the Indian coastal waters, would that be rigorous or the coast guards know about this or they are going to implement it?

G. Shivakumar: I do not know whether they know about it, but there will always be jurisdiction and I am not commenting specifically here and we have seen this with regard to the single hulls and double hulls. Long after the deadlines for phasing out of the single hulls expired, we saw a lot of single hulls trading in specific domestic markets …I am not talking about India here, I think India fully enforced it, but we saw in a lot of markets, lot of the single hulls were trading even after the deadlines expired. So there are a lot of jurisdictions which gives some leeway. We do not know how it will go with this ballast water treatment system or with this sulphur rule. But let us see how it goes really.

John Mathai: You spoke about the utilization rates of OSVs. Do they change during the monsoon seasons especially if it is in the Indian subcontinent?

G. Shivakumar: It is not really a spot market. That would matter only if it is the spot market. That happens in so for instance in the North Sea, you get very low utilization in the winter months because is much more choppy, you have blizzards, etc., and you have much higher utilization in the summer months because there are actually more activity in the summer months. In India, there is not much of a spot market really. So all the ships are on time charter and whatever work you get on the time charter.

John Mathai: How long are these contracts for? Is it one year, more than one year?

G. Shivakumar: Typically, contracts are for 1-year to 5-years. You could have short-term contracts as well; we have done two months' contracts earlier this year. So we came off one contract then one of our customers wanted a vessel for a two-month period, we gave a vessel for two-months. I think currently, we are doing a one-month contract on one vessel as well. Most of the contracts on the Indian coast tend to be time charters of greater than 1-year, typically 3-years or 5-years.

John Mathai: Have you thought about the FPSO market. Is there a market there beginning to come back, I am hearing some projects coming back on line especially West Africa and Brazil?

G. Shivakumar: We know nothing about the FPSO market.

Moderator: Thank you. The next question is from the line of Vaibhav Badjatya from Athena Investments. Please go ahead.

G. Shivakumar: One thing which I wanted to tell you before you signed off the last time is just on this currency depreciation bit, I think you are aware that in 2000 the dollar-rupee exchange rate was 46 and in 2008 it was 40. So that is an 8-year period where the rupee actually appreciated on a point-to-point basis and we were still at 44 in 2011 which was 11-years later. We take it for granted based on recent experience that the rupee will keep depreciating but it is not such a straightforward thing. Again, I am not giving a view, but I am just reminding you of history here.

Vaibhav Badjatya: I completely agree with you sir, I am not trying to derive interpretation from the recent rupee history. So let me just ask one simple question; are you taking a view that rupee will appreciate or depreciation or you are not even taking that view?

G. Shivakumar: No, we are not taking any view.

Moderator: Thank you. As there are no further questions, I would now like to hand the conference over to Ms. Anjali Kumar for closing comments.

Anjali Kumar: Thank you, everybody for logging in and asking interesting questions. As usual, the transcript of this call will be on the website in a couple of days and you are obviously free to call us anytime for any other queries you may have. Thank you so much.

Moderator: Thank you. On behalf of The Great Eastern Shipping Company Limited, this concludes this conference. Thank you for joining us and you may now disconnect your lines.