# "The Great Eastern Shipping Company Limited Q3 FY 2017 Earnings Conference Call"

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**Moderator:** Good Evening, Ladies and Gentlemen, and Thank You for standing-by. Welcome to the Great Eastern Shipping Q3 FY 2017 Earnings Conference Call. At this moment, all participants are in listen-only mode. Later, we will conduct a question-and-answer session at that time, if you have a question, please press "*" then "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, Ms. Kumar.

**Anjali Kumar:** Good evening, ladies and gentlemen, welcome again to the Conference Call for our Q3 results. Since the results were out on Friday, I am presuming all of you had a chance to have a good look at it and the release was also out by afternoon on Friday.

So, I would like to just without wasting much time hand over the call to our Group CFO -- Mr. G. Shivakumar. Over to you, sir.

**G. Shivakumar:** Hi, Good Afternoon, Everybody and Thank You for joining us for this conference call. Since we have just come to the end of a calendar year we will make all comments on demand and supply on the basis of the full-year data, not just for the quarter.

So during the year, crude imports into the U.S. and China grew quite strongly, up about 600 kbd and 900 kbd respectively. This resulted in an about 4% growth in crude oil demand.

Unfortunately for the freight market the fleet grew by almost 6% in the same period leading to a significant drop in earnings between 2015 and 2016.

As of January, the order book for crude tankers stood at about 15% with a strong fleet growth expected in 2017, excess of 7% and probably 8% or 9% and while the old ships, the fleet with about 20 years of age stands at about 5% of the fleet.

The OPEC decision to cut production caused a spurt in spot cargos in December leading to a little bit of excitement and a spike in freight rates. However, it is reported that the level of compliance has been very high in January and this will of course have an impact on the crude tanker market. It is having an impact and it will have an impact going forward.

The refined product rate saw strong growth as well but this was also outweighed by fleet growth of almost 7% during 2016 and the order book for product tankers is at 13%. It has come off from the highs of about two years ago, but we expect that this will be the last year of solid fleet growth. So, we should start seeing some bottoming out in the market.

In the last year, the demolition of tankers was very low across size classes, at about 1% or lower.

With regard to LPG carriers, the earnings finished very weak in the year as was expected and as has been expected since 2015, that 2016 with all the deliveries will be quite a weak year. So, we saw fleet growth of 21% in calendar year 2016 and this huge fleet could not be absorbed even though there was very strong U.S. export growth.

The order book still stands at 18% of which 13% is for delivery in 2017. Ordering has been very low across ship types down about 80% year-on-year.

So in dry bulk, dry bulk freight rates have shown some signs of life especially with the rise in commodity prices towards the late part of 2016. China provided a big boost to the commodity trade and they increased their iron ore imports by about 71 million metric tonnes and coal imports by about 33 million metric tonnes. That itself provided with some small drop in other cargos. China is expected to have provided about 80 million metric tonnes of additional cargo demand for dry bulk.

With regard to India, Indian imports of coal declined by about 70 million metric tonnes. So the dry bulk fleet grew by about 10% in the year. We saw very strong scrapping in the first-half of the year because the market was at rock bottom at that time, even below operating expenses.

So, we saw about 22.5 million dwt being scrapped in the first-half but only 6.5 million dwt being scrapped in the second-half as the freight market bounced and have brought back some confidence into the dry bulk ship owners.

With regard to the net asset value, the standalone net asset value has gone up from Rs. 311 to Rs. 321 per share. Tankers are down on average about 10% to 15% in the quarter and about 30% to 35% in the year.

Dry bulk was flat in the quarter and the year. However, values have gone up about 15% to 25% from the lows of March & April 2016. So, offshore value has continued to be in a state of flux so we are not declaring our consolidated net asset value.

In sale and purchase, since our last con-call we have contracted to purchase three secondhand Suezmax tankers, over and above the two Aframax that we did in October.

These purchases are being made not based on a forecast of a quick recovery but it is part of a process of re-building the fleet at prices that we believe are reasonable. As I mentioned earlier, prices have dropped by about 30-35% in the year and we think it is reasonable now to make investments. We think these investments will make us a decent return over the long-term and that is why we are investing in these. We are not calling the timing of a market recovery, we are not expecting it to be quick but we are making investments when we find good ships at a reasonable price.

Similarly for time charters, you may find that our forward cover drops as we go forward, if time charter rates remain low and we believe that we are not hedging any risk by locking in ships at those low rates. You may find that our time charter coverage comes off. We believe again, as we do with regard to ship values that in the low part of the market you should not be selling your capacity and over a longer period of time, we believe that this will pay us dividends and that we will make superior day rates from keeping our ships open in the low part of the market, not fixing at the lower part of the market and only fixing when we get the rates that we want that we think give us a good return.

Coming to offshore, the market continues to be quite dismal. E&P spending estimates are coming in for offshore spending at still a negative number may be 5% to 10%. People are expecting that overall E&P spending might be a positive number but most of the positive is going to happen in onshore specifically in U.S. shale. We are still expecting a negative spending growth in offshore E&P activity.

However, a large part of this, we believe, will come from rate reductions rather than from the number of assets being employed. It is a question of time before the market bottoms out. We are currently at terrible utilization levels, globally utilization is estimated to be at 55% or below for both vessels and for rigs.

And I mentioned this in the last con-call as well, this will be the third consecutive year of cuts, if it really turns out that this is the third consecutive year of cuts in E&P spending in offshore that would be the first time in living memory that we have had three consecutive years of cuts in spending. This is putting pressure on replacement requirements for oil companies. We have seen that reserve replacement ratios have dropped to below 20% and possibly even at 10%, which is that they have replaced only 10% they have found new oil equivalent to only 10% or 20% of the oil that has been produced. These are the kind of things that result in a pullback in prices, when the reserve replacement goes down to such low levels.

Therefore, we think that at some point this cycle will bottom out and there will be interest again. Of course, the price being in the $55 to $65 range will also help people to get confidence to start investing again in the E&P business.

Again, we are not expecting this to happen quickly there is a lead time of typically 9 months to 12 months before budgets are sanctioned before people get the confidence, the budgets are sanctioned, and people start taking in new assets. But we would expect that if the oil prices stay at around these levels then we should have a recovery starting sometime in the next year or two.

In the meantime, we have currently one rig idling, our Greatdrill Chetna has come off contract in January and she is idling waiting to get next employment. We also have four supply vessels idling. A further three vessels are scheduled to come off contract during 2017 and we will have to find work for them.

We sold the oldest supply vessel in our fleet, the Greatship Disha. We expect to deliver her to the new buyers in this quarter itself probably in February. The balance sheet continues to be strong in the Group, we have almost $700 million of cash or maybe slightly in excess of $700 million as of December and we expect to have at least $600 million to $650 million of cash as of March 2017 after our entire CAPEX is done.

We expect our net debt on a standalone basis to be around $300 million as of end March and the consolidated net debt to be at under $500 million and you may have noticed that we have committed a CAPEX of almost $250 million or we have actually taken delivery of ships of value amounting to more than $300 million during the current financial year.

Thank you. Now, I will open the floor to comments, questions and we will be happy to take them.

**Moderator:** Thank you. Ladies and gentlemen, we will now begin with the Question-and-Answer Session. We take the first question from the line of Bhavin Gandhi from B&K Securities. Please go ahead.

**Bhavin Gandhi:** Sir, just one question from my end. In the previous quarter, we did indicate a broad range of consol NAV of Rs. 380 to Rs. 460. Is the confidence around that range gone down a bit or it is more of the same kind of range that we are looking at?

**G. Shivakumar:** Yes, the lower end of the range is probably around the Rs. 375-380 and upper end of the range, I think would probably be around Rs. 430-440, we narrow it slightly I think from there.

**Moderator:** Thank you. Next question is from the line of Suman Bhatt, who is an Individual Investor. Please go ahead

**Participant:** Interested to note that you mentioned earlier in the call that you take a long-term view on asset purchases. I would like to know do you all have any sort of internal metrics on what would turn out to be a successful investment over 5 years, 10 years or 20 years. And if at all you all do then do you actually go back and review investment decisions in the past and determine whether it has met those criteria?

**G. Shivakumar:** Yes. Hi, good afternoon, Mr. Bhatt, and thank you for your question, that is indeed an interesting and thought-provoking question. Yes, we do, the answer is yes. We do look at each of our investments and we review them on a quarterly basis. And we can do that in shipping because you get a price for your assets every quarter and it is fairly liquid. And we look at how they have done historically and we look at from the time of investment how they are doing. So, we do kind of a mark-to-market and we also compare that with what we expected at the time that we made the investment. So, if there are any lessons to be learnt from that investment, we can take heed of those and use them for the future. We do not necessarily have a target for what we would like to earn. But I think that across the fleet, we would like to make something like a 10% return in dollar terms.

**Participant:** That is on assets.

**G. Shivakumar:** Yes, on the assets.

**Participant:** Okay. And on equity that would translate to may be 15%**.**

**G. Shivakumar:** Yes, depends on what leverage you put, what cost, etc. So if I had to put a number that would probably be the number but we do review this all the time and so we are reviewing our entire portfolio all the time. So, on a monthly basis we look at every single ship in our fleet and we look at what the price could be and whether it makes sense to hold or to sell.

**Participant:** Okay. And just inverting the scenario a bit. Obviously, you also get purchase opportunities on a very regular basis definitely in the shipping and probably also in offshore. Do you also review possible acquisitions that you all passed over to see was there something that was in your assumptions that was wrong and in the future you should take those investments?

**G. Shivakumar:** Yes, we do. So, it is like you are sitting here in the room with us. So, yes, we do.

**Participant:** That is very good to hear. It is not often that companies take a view like that, so good to hear.

**G. Shivakumar:** It is a tough business, so we like to keep learning these things and so we make our share of mistakes, but the one thing that we need to come out at the end of this is that we need to have learned something from that so that we do not repeat that mistake.

**Participant:** Okay. I also noticed an impairment charge in your offshore income statement. Is that related to the ROV sales?

**G. Shivakumar:** It is related to the PSV that we sold, yes. The Greatship Disha, we sold her, the oldest vessel in our fleet and obviously given where the market is we have had to take an impairment on that sale.

**Participant:** Okay. And it happens as an impairment rather than a loss on sale transaction, why is that?

**G. Shivakumar:** Yes, so it will become a loss on sale eventually but since we have contracted for the sale up to the time that we executed, it will be an impairment, so then, it will be a loss on sale after the sale is executed.

**Participant:** Okay. And any thoughts on the offshore market, obviously it is in a difficult situation, but any thoughts on how confident are you all to get contract for the Greatdrill Chetna? Is something that you are all confident about or is it just too uncertain to know?

**G. Shivakumar:** Yes, it is just too uncertain because there is nothing in your hands really that you can do. In the sense that it is up to the customer. So, that is one thing which is there in the offshore market, which is that it is up to the customer when the customer has a requirement and wants to come up with a tender, etc. So, you have no choice but to wait and the customer chooses the tenure whether he wants a three years' contract, one year contract, five years' contract. So, you do not have much of a choice in this matter and sometimes it is just a procedural thing where you have to go through a process and that just takes time.

**Participant:** Okay. As far as warm stacked goes, how much money does it cost on a quarterly or a monthly basis to keep a rig warm stacked?

**G. Shivakumar:** I would not go into the details. It will be significantly less than our standard operating cost. But we are also cognizant of the need to keep the rig in a condition that she can go into operation whenever we get a contract. So, we are not going to cut down to the bare bones. So, in the sense that to cold stack the rig and where there is a chance that you may take a long time to revive the rig for operation. So we will take the chance of spending a little bit more money. We will take the cost of spending a little bit more just to ensure that we can get back into operation quickly.

**Moderator:** Thank you. Next question is from the line of Dhimant Kothari from Invesco Mutual Fund. Please go ahead.

**Dhimant Kothari:** Sir, can you please give me the coverage for the rest of the three rigs?

**G. Shivakumar:** Rest of the three rigs?

**Dhimant Kothari:** Yes.

**G. Shivakumar:** Yes, so there is one each coming off in first quarter of every calendar year. So, there is one which comes off in a year's time, another which comes off in two years' time, another which comes off in three years' time.

**Dhimant Kothari:** So that would be calendar 2018, 2019 and 2020.

**G. Shivakumar:** That is correct.

**Anjali Kumar:** Yes, but the last one will be FY2020.

**G. Shivakumar:** Yes. Calendar 2018, 2019, 2020, that is right.

**Dhimant Kothari:** Okay. And where are these three rigs deployed in terms of location?

**G. Shivakumar:** All here in India.

**Dhimant Kothari:** Okay. With the ONGC if I may ask?

**G. Shivakumar:** On the west coast of India, we do not like to name our customers.

**Moderator:** Thank you. Next question is from the line of Vaibhav Badjatya from Athena Investment. Please go ahead.

**Vaibhav Badjatya:** I saw a large portion of MTM gains I think, foreign exchange hedging contracts in your P&L. So, I just wanted to understand when rupee depreciates this number would be a gain and rupee appreciates, this number would be a loss or how does it work because I understand most of it might be due to the rupee debt that you have hedged into dollar. I was just wondering how the rupee depreciation will lead to the gain in the P&L?

**G. Shivakumar:** Yes, so it is a little complicated and you would have seen last quarter as well we booked a gain and that was when the rupee appreciated and this quarter we have booked a gain when the rupee depreciated. So, the derivatives include currency and interest rate swaps, so we have borrowed in rupees and swapped it into dollars. So, we have created a dollar liability out of a rupee liability. Now during the quarter, dollar interest rates have gone up and therefore the swaps that we have done are in the money to that extent and therefore, that has more than offset the depreciation of the rupee versus the dollar. So there is no one for one relationship. So the one thing which happens is we have a dollar cash balance which gets revalued so when the rupee depreciates against the dollar that is a positive impact that is very straightforward. But on the derivatives transactions where we have swapped our rupee liability into dollar liability there is no straightforward impact. We know that there will be a negative from the rupee depreciating versus the dollar but you have to take into account what happens to interest rates as well. So it is a complicated equation and so there is no straight answer on that, sometimes it will be up, sometimes it will be down.

**Vaibhav Badjatya:** Okay, got it. And this interest rate is, what in LIBOR it is, what is this interest rate that goes into this asset base?

**Anjali Kumar:** It is converted to fixed rate. So, dollar swap. That is what Mr. Shivakumar said, that when the interest rate that is a dollar swap rates go up then some of the losses from depreciation are negated by the gains on interest rates because we have already fixed our liabilities and in the current environment that is a fact

**Vaibhav Badjatya:** Yes, right. Yes, that is what I was trying to understand, so if you have fixed your interest rate liability on a particular rate and then you measure a gain against the current interest rate. So, what the current interest rate is, is it LIBOR plus some spread or it is some benchmark yields on some security?

**Anjali Kumar:** No. So what we have done is like I mentioned, it is converted from a rupee fixed rate bond to a dollar fixed rate, okay. Now, this dollar fixed rate is actually priced on screen by the USD IRS swaps. When you do the swap, it is first converted into a floating rate liability which is LIBOR plus margin and then that LIBOR bit which is the floating leg is converted on to a fixed rate platform which is of the USD IRS curve which is onscreen again. So that USD IRS screen, that rate which moves up and down also has an impact on the pricing of the derivative because across the board the USD IRS which is the interest rate swap is basically matches the US Treasuries. As the treasuries move up and down, the USD IRS also move accordingly because last quarter we would have marked them down to a much lower level but now in the last three months since IRSs has moved up therefore, the swap to that extent to the IRS extent it is positive for us.

**Vaibhav Badjatya:** Interesting, very interesting. So, I got this. On second question on the similar line, I think you have recently raised another INR NCD, if I am not wrong.

**Anjali Kumar:** That is right, Yes, we have.

**Vaibhav Badjatya:** So do you plan to hedge these cash flows as well into USD or will it be open?

**Anjali Kumar:** Yes, entirely we plan to hedge all the rupee bonds that we have taken.

**Vaibhav Badjatya:** Okay, and one more question if I may ask. So, I mean historically when I look at the business performance it has done fabulously well in terms of what business and their return on equity and other parameters. Have we tried to see that how much of the return on investments are coming from actual cash flows in terms of hiring and chartering the ship versus the gains or net of losses on purchase in sale of ships? Is there some kind of a number that you have in mind that how much the business is generating say it is 13%, 14% ROCE, 10% is coming from the hiring chartering of the ship and 4% is coming from increasing your abilities to time the purchase at time the sale of ship very well?

**G. Shivakumar:** Yes, I have got your question. Thanks, that is an interesting question and thanks for asking it so that we can explain this. So if you look at our P&L itself, probably 10% to 15% over the last 15 years would be profit on sale, okay, may be lower now. So in the decade of the 2000, maybe it was 20%, which was profit on sale as a proportion of our PAT, it is easy to find this number out, okay. However, that is not all that comes from doing the timing of the market it is for instance supposing you just to take a stock market example, you can buy a stock when the market is really poor let us say, at Sensex 8,000 you buy a stock and then you are at Sensex 25,000 and you are continuing to grow and because you have got it cheap and you have got flows and you have got dividends, etc., you can neither hold it or you can book it. So if you book it in one year it comes as a profit on sale or whatever it is okay or you can have a running income which comes every single year because you have a strong dividend yield on that one. So, we believe that a large proportion of our outperformance will come from timing the purchase and sale. However, we will not sell all the assets so let us say we bought five crude tankers right, in the last three months we do not intend to sell all five of them to capture that gain, some of them will be so good that we will say that this is a low breakeven for us. It is a low-cost ship, it gives us a low breakeven, we will hold it till the end of life, okay. So, you will never see a profit on sale from those vessels, okay. But you will see a better return on capital on those vessels because the breakeven on those ships is lower by $5,000 per day I am just giving you a number as an example because the breakeven is lower by $5,000 per day the profitability on that ship will be superior. So, we think that a large part of the outperformance that will come for a shipping company in our businesses, I am only talking about shipping will come from timing the purchase of ships. It is an important part of doing the shipping business. So you do an SIP on a ship you may not make the kind of return that we hope to make because you will buy in all markets and you will sell in all markets, let us say or you will not sell. You can only do it by timing the market and timing the market does not mean that you will sell also you may just buy and because it is cheap you may hold for the rest of the life of the ship. So, it will never show up as a profit on sale but it will show up as superior operating profits through your life.

**Vaibhav Badjatya:** Yes, that is what actually I wanted to understand that when you book a profit it would be obviously, on sale so that is what I just wanted to understand how much is from the sale of ships, purchase obviously, I mean once you bought it and it is giving you good yield there is no point selling it if you are confident that yield will continue. So, I think I got my answers. That is it from my side.

**Moderator:** Thank you. Next question is from the line of Rohan Shah from Alpha Enterprises. Please go ahead

**Rohan Shah:** Just to rephrase the last caller’s question, is there a long-term IRR that you track in terms of buying and selling ships so you aspire doing the longer?

**G. Shivakumar:** No, so I think I mentioned to the previous caller that we would be disappointed if we did not make 10%. But it is not a number that we put that is in stone, it is written in stone or it is a hurdle rate, we would like to outperform the markets and we measure that quite frequently.

**Rohan Shah:** Okay. And this would be the unleveraged IRR or it would be post…

**G. Shivakumar:** On capital. On total capital so that should be unlevered on the ships that we buy.

**Moderator:** Thank you. Next question is from the line of Raunak Shah from SJC Advisors. Please go ahead.

**Raunak Shah:** Since you guys were just talking about how important it is to time the purchase and sale of ships and it is an important part of what drives our performance in the sector. My question was your thoughts around trading your own stock in terms of thinking about a buyback. Just because if I look at the cash earnings per share versus the stock price you have today you are trading on probably between kind of three to five times multiple and who knows whether kind of what part of the cycle we are in as far as the business is concerned but it is certainly nowhere near the top. So, it is a pretty low multiple on what is a pretty low cyclically depressed earnings per share number, so just wanted to get your thoughts around that.

**G. Shivakumar:** Yes. So one thing that I just want to correct you on before we go into trading the stock which is a phrase I do not like but we have not had cyclically depressed numbers with regard to earnings. So, the offshore business still has several old contracts which were done in the good days especially on the rigs which constitute a large part of the offshore business. Shipping itself is coming off a period of strong earnings and therefore we have some contracts, time charter contracts, which were done with strong earnings. So, in terms of earnings, these are not cyclically depressed if you just go back a little in history, 2011 - 2012, 2012 -2013 is when you had really depressed earnings, the last time we had, so the last low that we had on earnings. That is just one thing so it is not that I am saying that we are going back there or anything, though the outlook that I give looks a little depressing it is not that we are in such bad market earnings wise currently. But coming to the buyback question it is something that the Board will consider whenever it is appropriate, it is not something that we like to do on a frequent basis. Our preference is to buy ships because that gives you a value for the long-term. So, that is all I can say about that. Since you said trade, you cannot close out that trade while in a ship, you can actually close out the trade.

**Raunak Shah:** Yes, fair enough. My point more was do you think about a buyback in the same kind of IRR terms as you would be in terms of purchasing ships?

**G. Shivakumar:** No. So a buyback gives a whole portfolio of assets while a ship is a very-very focused bid on one particular type of asset at one particular price. So, your stock is a combination of shipping offshore crude product, gas, dry bulk, rigs, supply vessels everything so they are very different things really. So, they are different animals, so when we think about it, we think about it a little differently.

**Moderator:** Thank you. Next question is from the line of Yash Matai from Vibrant Securities. Please go ahead.

**Yash Matai:** My question got partially answered but I still would put that forward. So, as you can correctly said that our earnings if you look at them they are not at cyclically low levels. So, to compare them to 2007 or 2006 the peak of the cycle was last time around. But I think it is very close to that even more than at those levels I believe. So I was very curious to know that how are we managing to do that considered to the market in terms of the freight rates and all and even the ship prices is at the bottom of the cycle. So, what is the secret sauce here?

**G. Shivakumar:** Secret sauce is not so much a secret but we have a few fixed rate charters, so we actively try to manage the cycle. We try to fix out our assets on charters when we think there are good rates for fixing out our assets or as possible. That is one. The second actually that is sort of it we try to keep our leverage low but that is not really going to help us to outperform in these times. We try to keep our cost base sensible including our cost of borrowing and running cost. So, while running a high-quality fleet, we are still very focused on costs. Most of all it is on timing the market whether it is sale and purchase or charters and so one thing which needs to be appreciated is that more than 50% of our cost base, so our cost base basically is operating expenses, interest, depreciation, overheads. Interest and depreciation constitute more than 50% of that cost, interest, and depreciation are a function of how much you pay for your CAPEX and therefore it matters a hell of a lot how much you buy your ship for and that is what helps you to get a lower breakeven. I mentioned earlier, the breakeven of the ship and that is what helps you to get a lower breakeven, you cannot make much difference in your operating costs really or in your overheads but you can have a very competitive ship if you buy it at the right time, right price and you select the right ship to buy also.

**Yash Matai:** So is it correct to say that we have been much better at capital allocation or timing the market compared to our peers I mean that is what differentiates us from them?

**G. Shivakumar:** We do not compare ourselves to our peers. We have not been as good as we wish we could be. We have made our share of mistakes, the one thing I can say is that we hope we have learned from them and we will not make the same mistakes again. We may make new mistakes but not the old mistakes.

**Moderator:** Thank you. Next question is from the line of Samir Kapadia from Fortune Interfinance. Please go ahead.

**Samir Kapadia:** Two things in regards with one thing was like we are observing some consolidation which has happened at the industry level. So, if you can throw some light on that? And secondly, in regards with the government initiatives in regards with the Sagar Mala project whereby they intent to develop various ports and how could it impact our revenue or our business?

**G. Shivakumar:** So I do not know about this consolidation. It is probably international, right you are talking about international players consolidating.

**Samir Kapadia:** Right.

**G. Shivakumar:** And that is probably more in the container business than in our tanker and dry bulk business, of course, people are still trying to do something. The business is so fragmented in the commodity shipping space that we do not expect there to be any significant benefit from a consolidation. We do not think that there is any great advantage of scale beyond say 30 ships and we operated at one time 49 ships, we have operated 28 ships also in the last five years. So, there is no great advantage in this consolidation. You get no pricing power really by consolidating. So, we do not see it as a huge development either way but anyway there is not much of it happening. Ship-owners are very independent minded people and they do not like to consolidate and share and sell out to other ship owners. They may sell ships but to sell their entire company and merge into another shipping company is unlikely. Anyway, it would not have much of an impact on the market. And your second question was on Sagar Mala. Sagar Mala, yes, being an Indian shipping company we believe it will have a good impact when it comes through we would like to see more cargo carried around the coast of India. China, for instance has some 600 million tonnes or 700 million tonnes of cargo carried on the coast. India has got a big coastline as well and lot of opportunity for carriage of cargo but I think our coastal cargo is probably 100 million tonnes. So, there is a lot of scope for it if it can be developed, we will be very happy and anyway we participate in a big way in trades on the coast of India whether it is tankers or dry bulk and we welcome any developments with regard to the development of ports and coastal shipping.

**Samir Kapadia:** Just wanted to understand, see like the thing is like government is really pushing it very well and like we see a significant improvement on that side or like what?

**G. Shivakumar:** I think we will have to give it some time because it takes time to develop these ports. So these are slightly long lead time projects.

**Moderator:** Thank you. Next question is from the line of Rajendra Mishra from IDFC Mutual Fund. Please go ahead.

**Rajendra Mishra:** So just wanted to check, can you throw some light on how is the capital deployed over last four quarters, five quarters in terms of fleet or in terms of amount how much has been deployed, just to understand over the last four quarters, five quarters since let us say Q1 of last year?

**G. Shivakumar:** No, no. So do you want to know what CAPEX we have done?

**Rajendra Mishra:** In terms of both fleet and amount?

**G. Shivakumar:** Incremental CAPEX that we have done, good question. Yes, it is all in shipping. So, we bought different types of ships including dry bulk, gas, product tankers, and finally five crude tankers that is with regard to the commitments but we have also taken delivery of ships that we had contracted earlier. So in this year, I think we would have paid out about $300 million towards CAPEX or we will, including the last two ships that we will take delivery next month.

**Rajendra Mishra:** In FY 2017?

**G. Shivakumar:** In FY 2017, that is correct.

**Rajendra Mishra:** Okay. And just to understand the context that you are saying no because you time a lot in terms of purchase of assets, so when you enter into a contract to buy the fleet, the timing is at the time of purchase, right?

**G. Shivakumar:** That is correct. I am talking about the time of the purchase, entering into the purchase transaction.

**Rajendra Mishra:** So your outlook about the cyclical lower asset prices would be at a time of purchase?

**G. Shivakumar:** That is correct and we do vice versa at the time of sale as well.

**Rajendra Mishra:** So just a related question. Is it also to do with your call or let us say the underlying commodity or it is just a call on the asset supply demand?

**G. Shivakumar:** So it is a little bit on the commodity and how we think that the trade will develop over a period of time. For instance, if the ship is one commodity ship and there are very few ships of that type. But let us say a crude tanker and I am just giving you an example just for illustration. Should we think the crude trade is just going to go down and not come up at all then we would certainly take a view on that. So we start off with saying that it is not going to be in secular decline. So, that is one broad view we take and apart from that then we look at how cheap it is in historical terms, what kind of supply there is coming into the market, etc.

**Rajendra Mishra:** Okay. And this $300 million can you break up in terms of different types of fleet in the products that you told me?

**G. Shivakumar:** Yes, we would have about 40% in dry bulk, 40-45% in crude tankers and the remaining in product tankers and gas, so I think, about $320 million.

**Rajendra Mishra:** Okay. Typically, in terms of your price to NAV of the asset, normally what is the range at which you would technically start looking at?

**G. Shivakumar:** Look at what?

**Rajendra Mishra:** So let us say the…

**G. Shivakumar:** You mean buyback?

**Rajendra Mishra:** No, the price of the asset so what triggers as you said…

**G. Shivakumar:** So we look at historically what the price is, we will look at it in comparison with what are the expected earnings. So, we also model for different scenarios with regard to earnings, so we do a fairly detailed research on all the commodities and all the types of ships and the trade development for each type of ship. So, we do a little bit of modeling with regard to that and we also look at where we think earnings will be and we also look at where we think the price could go to over a period of time. So we model all these things and then we decide on the purchase or otherwise. So, in some cases we could also look at say, if we are able to lock in some of the earnings which de-risk it if we are able to get a good contract but those are very few and far between. So we look at all these factors, so we have sort of a view on most commodities, the trade at most points in time.

**Rajendra Mishra:** Understood. So the fleet size you shared was around 30?

**G. Shivakumar:** No, we will have by March based on the current committed CAPEX 44 ships.

**Rajendra Mishra:** 44 ships?

**G. Shivakumar:** That is correct. So, we would have taken delivery of some 10 ships this year, I think.

**Rajendra Mishra:** Okay and would you be okay to share your view on crude?

**G. Shivakumar:** Crude prices?

**Rajendra Mishra:** Yes.

**G. Shivakumar:** The prices of crude oil?

**Rajendra Mishra:** Yes.

**G. Shivakumar:** We think that it will be in a range, so we think the sealing is probably $65 unless there is some geopolitical event then all bets are off we do not think we will be seeing the lows of last year. So we do not think it will go below for instance $45. In fact, we think that there is a fairly strong base in the high 40s. So if we have to put a number for an average of this year we would think $55 to $60.

**Moderator:** Thank you. Next question is from the line of Raunak Shah from SJC Advisors. Please go ahead.

**Raunak Shah:** Just wanted to understand what will be the maintenance CAPEX you typically incur assuming that all the vessels have work?

**G. Shivakumar:** When you say maintenance CAPEX is that operating cost?

**Raunak Shah:** No, operating cost would be one component but then is there ongoing CAPEX involved every year with the fleet?

**G. Shivakumar:** No, so there is maintenance which happens all the time which is part of what we call operating expenses.

**Raunak Shah:** So that is all expense in the P&L there is no capital….

**G. Shivakumar:** That is correct. So, for a modern asset you have to do a dry dock once in five years and that gets amortized over the period to the next dry dock. So, typically over a five-year period, it gets amortized but this varies, so we do not have a number for it. It varies depending on the vessel size, the condition of the vessel and the age.

**Raunak Shah:** Okay, got it. And from what I understand from reading all the reports around the new vessels you are buying all of these are secondary purchases, right?

**G. Shivakumar:** That is right, second hand purchases.

**Raunak Shah:** Is that something you have always done in terms of usually ordering second hand rather than going primary through the yards? Is that a conscious decision going forward as well?

**G. Shivakumar:** Okay. Good question and thanks for asking it because it is a point that I want to make. So, when we look at making investments, so we have the option of going to a yard as you mentioned to buy a new ship. We always make a comparison of the relative value between a new building ship and say an existing ship. Currently, the pricing of modern existing ships say a five-six year old ship in relation to the price of a new building, so a new contract with the yard is at a low point which means that you are getting a relative discount for buying an existing second hand ship vis-à-vis ordering a new ship. Therefore, it is more attractive to buy a second-hand ship. This is also one of the factors which has led to ordering of new ships coming down by 80% to 85% from the previous year because most people can see this they can see that relatively it makes more sense to buy an existing ship at the current levels than to go to a yard and order at a much more expensive level.

**Raunak Shah:** And this you are saying is true across the various product vessels you look at?

**G. Shivakumar:** That is correct. So the extent of the so-called discount varies but it is true across the board for all the asset classes currently so we add that very actively because these are the options that we consider.

**Raunak Shah:** Right. And I am sure I mean you guys have seen multiple cycles, obviously, so now that we have seen a 80% reduction in new ships being ordered at what stage of the yards order book, so I do not know whether it is two years, three years, four years, after a drop below a certain number of years do you start seeing discounts coming through on the new ship side, has that started happening yet?

**G. Shivakumar:** Yes, historically we have seen when the order book drops below 12 months to 18 months, let us say when they have visibility only for the next 12 months to 18 months they start discounting, so there is a worry, of course so they will start discounting because they start getting worried about the visibility and the employment. However, this time it is a little different because most of the yards are in deep financial trouble and so they are not able to discount to the extent that they would, because they are not being permitted to take orders at discounted levels. Therefore, the yard prices are not coming to the market clearing levels and therefore, because they are sort of being controlled by the banks and their lenders do not want them to take orders below a certain level.

**Raunak Shah:** This is primarily the Korean and Japanese yards?

**G. Shivakumar:** It is a Korean yard, that I am talking about. So, therefore we have not reached the market clearing price for those contracts, and therefore people are not ordering. So we do not know how this will turn out, of course, prices have come down, they have probably come down 20% in the last one year but on the flip side, you have got modern secondhand vessels which have come down by 35% in the last one year. So, obviously, those are looking relatively more attractive.

**Raunak Shah:** So assuming that the discount starts widening at the yards, if the government so allows the yards to do that in terms of them getting more business and the second hand prices also start stabilizing, the reduction in the yard pricing would that affect your second hand NAVs as well?

**G. Shivakumar:** It will, yes. So, normally that puts pressure, so it could put pressure on people who are selling in the sense that it could put pressure on them to drop prices further if they want to clear their ships out because they are not competing with yards who are dropping their prices. So, we do not know how it will turn out. So, first you need the yard to drop the price and then you need to see how it affects the guy who has got a five-year-old ship that he wants to sell.

**Raunak Shah:** Okay. But yard capacity itself has not come down yet?

**G. Shivakumar:** Yard capacity has come down. So, a few yards have shut down, in China a lot of yards have shutdown, in Korea a couple of big yards have shut down, stopped operations, gone bankrupt and so capacity is getting crunched. So, this is one of the things that gives us some hope in the longer-term, that all the excess supply capacity, which got built-up over the good years in the 2000s is now getting removed which sort of lays the foundation for the next recovery.

**Raunak Shah:** Correct. So, that was the next question, I was ultimately coming to. I know, obviously, impossible to kind of give timelines around any of this, right some of it is political as well in terms of how long the yards are allowed to continue but given where we are in this recovery if we can call it that and looking at where yard supply is going and the crunch you are talking about how much longer do you think it is before the yards start coming back or the new ship supplies start coming back into equilibrium?

**G. Shivakumar:** Again, that is really tough to tell. So, we cannot call the timing of that because again this is not normal market behavior, right, you would normally move your price to be closer to market clearing, if you want to sell your product, but that has not happened. So, it is really tough to call this because it is not normal commercial objectives driving this. So, we cannot call a time on that, but one thing we do believe is that these capacities are going to get constrained for the future.

**Moderator:** Thank you. Next question is from the line of Suman Bhatt, who is an Individual Investor. Please go ahead.

**Suman Bhatt:** You mentioned a few minutes ago that you do not compare yourself to peers but you do compare yourself to what your internal benchmarks are and you have, obviously, made mistakes and learned from them. I am wondering, would you be able to share some examples of mistakes that you have made in the recent past and what you all have got out of it in terms of your outlook for the future?

**G. Shivakumar:** Okay, 10 years ago, we made a lot of mistakes in the boom time and we still live with those in terms of the ships that we bought, which were really expensive.

**Suman Bhatt:** Which segments were those?

**G. Shivakumar:** All the segments were booming, anything you bought in those days was a bad decision because you are trading probably at 50% of those and you are at 50% of those prices within two years after that, because the market has collapsed. But in the recent past, we did a few dry bulk new buildings in 2013, which we probably should not have, we got out of a couple of them, we sold, we converted some orders, but those were orders that we should not have, we were probably a little hasty and early in making those investments and those are probably investments that we should not have done. So we have taken delivery of those ships, we will go through with them, we have reduced our exposure, we have reduced our costs on some of those but the fact remains that those were mistakes that we made which we sort of salvaged a little bit by taking actions later. So, those things happen, so I think one product tanker that we bought a year and a half ago was probably also at an expensive point in the cycle but those are little things that you do.

**Suman Bhatt:** Okay. Yes, thanks for being upfront and honest about mistakes I think, that is not so easy to do. What about roughly the same time that you all had those new build dry bulk orders, the second-hand market was close to its bottom…

**G. Shivakumar:** No, actually not. So we would probably have done worse, if we had bought a second-hand ship at that time.

**Suman Bhatt:** So probably a year or so later?

**G. Shivakumar:** So the problem was not the type of ship that we bought, it was just the timing of the purchase. Any dry bulk asset we bought in end of 2013, so the last order we did was in end of 2013 November, December and at that time, anything that we bought would have done badly.

**Suman Bhatt:** Right. So you would have been a lot better waiting for a year or two to do that?

**G. Shivakumar:** That is correct. Two years, so ideally, we would have been buying in a big way last year at this time.

**Suman Bhatt:** How does that change your decisions making process for the future?

**G. Shivakumar:** It does in the sense that we look very carefully at what the market outlook is looking like, the order book had built-up very substantially in 2013 and I think we were probably or the market was too optimistic about the trade growth going forward and therefore, ordering and that year we saw 100 million deadweight ordered and just to give you a frame of reference last year we probably saw some 10 million to 15 million deadweight order. That was a crazy year for ordering and I think everybody just piled in at the same time there was a lot of capital available and we probably should have that one out.

**Suman Bhatt:** Right. I mean that is interesting that you say that I think, the social proof of everyone doing something sort of pressurizes people to follow the crowd. I mean, do you have any mechanism to prevent that in the future?

**G. Shivakumar:** Yes, sort of. So we have very active discussions on every single investment proposal that we go through. So, Yes, so that is the only way you can do it, which is to look at it from all angles. So that is the only way to do it really.

**Suman Bhatt:** And who would be, I mean, in terms of roles in the organization who would be involved in those discussions?

**G. Shivakumar:** So this is everybody starting from the MD to the Business Head to myself as CFO to the research person to the sale and purchase head to the chartering person. So we have a large group of people who get into the discussions of course, it goes to the board where we have a further round of discussions because we have got directors with a lot of varying perspectives, so the recommendation goes to the board and then the board debates and decides on these.

**Suman Bhatt:** Is that on every asset purchase?

**G. Shivakumar:** That is correct. So Yes, so everything gets discussed at the Board and then it gets approved, of course, we have a Committee of the Board, which finally decides but all the directors weigh in on every single investment proposals that we have.

**Suman Bhatt:** I would imagine that at least in the shipping side of things decisions sometimes have to be taken quickly right?

**G. Shivakumar:** Yes, quickly, but we manage to do these discussions you get at least two days to do these discussions.

**Suman Bhatt:** Okay. And you are able to get the board's opinion in that time?

**G. Shivakumar:** That is enough time to get their opinions and their views and get a discussion going.

**Moderator:** Thank you. Next question is from the line of Manish Bhandari from Vallum Capital. Please go ahead.

**Manish Bhandari:** Sir, my question is regarding the news item which was about the India to levy a Service Tax from the freight for the import of delivered basis. So, what difference would it make to your earnings and your competitive advantages?

**G. Shivakumar:** Okay. I am not very familiar with this and what is the latest development on this, so I would not hazard a guess on it. So, you will have to excuse me on this one.

**Manish Bhandari:** So this was regarding to January 19, there was the Service Tax which was laid on.

**G. Shivakumar:** Yes, that is right. I am not very up-to-date on this one, so I am not going to hazard a guess, I do not know what the situation is, what types of commodities but we will come back on this.

**Manish Bhandari:** Sure. Sir, my second question is, since you mentioned that you have moved back on the buying spree and you see a long-term movement on the charter rates and the value for your ships. So what are the two or three key areas, which you would look at in terms of which would give you an indication the recovery is happening in the shipping business?

**G. Shivakumar:** Demand and supply are the two key things that we look at. The one thing that you can see is supply of ships because the order book is there and it exists. The other demand for ships, you cannot really forecast very well because it depends on local regulations, national consideration, etc., but more than anything else, it is on the price of the ship and the quality of the ship and whether that is a ship that we would like to own in the long term and at a certain price. So, that is really what we look at we are making a call on a very specific asset when we make a purchase.

**Manish Bhandari:** So you mean to say a price of ship would give in some kind of indication regarding the demand in the business?

**G. Shivakumar:** No, it does not give an indication of the demand. The price of the ship is a factor in our decision to buy, so the same ship at $40 million we may not be tempted but at $28 million we would look at it very seriously.

**Manish Bhandari:** So you may land up in a situation like a BlackBerry or Nokia where a falling asset price would be too tempting but there may be some structural demand destruction which would have happened in that specific set of commodities, is that a possibility which would happen?

**G. Shivakumar:** In theory, yes but we do not think anybody is going to replace the gasoline or diesel running the car with better operating systems currently. Therefore, we do not see it as a risk for now. So, we look at whether there is going to be demand, yes, we look at whether people are still going to be using hydrocarbons for transportation for petrochemicals, etc. So we look at that and once we are fairly confident that it will continue at least for the foreseeable future, then we look at buying the ships. So yes, we cannot if there is a black swan kind of thing, which is that suddenly somebody finds a substitute for hydrocarbons, we cannot do anything about it but if it means that just that demand will drop by 5% and the market will get crushed, yes, we will ensure that we have got the cheapest assets out there or the cheaper set of assets out there so that when capacity has to go down by 5% or 10% to match the drop in demand we will still be around when the market turns we will go through the market downturn and we will be standing when the market recovers unless it goes into terminal decline.

**Manish Bhandari:** I appreciate that. And my last question is in your buying decision making is there any kind of yield you have in your mind that at the current charter rate you would have this kind of yield on this asset and that becomes a reference point for you to buy in that is what usually has proved right over a period of time.

**G. Shivakumar:** Actually, it works better with lower yields and we looked at this for different assets that we have bought at different points of the cycle. The assets that we bought at a low point in the cycle, where the yields were close to zero so, we were on a time charter, so there were two assets that we bought one we bought in 2003 and one we bought in 2006. So, 2003 was before the market took off we bought that asset at a low point in the cycle and we fixed out on charter on a three year charter had an okayish rate for that time. In 2006, we bought another asset at 60% higher price and we fixed out on charter at a much higher price, at a much higher rate for three years at the end even though the first ship was saddled with a poor or a suboptimal charter it turned out as a better project than the other ship than the ship which was bought expensive and had a high current yield. Typically, we found that projects which start off with a poor current yield have been bought at the right time in the cycle. So, what happens in the market, first, port rates drop, then your time charter rates drop, and then your asset values drop. So, when you are buying a ship at a really bad point of the cycle, you are actually going to be losing money on your P&L. So, the best time to buy dry bulk was in March, April last year when ships were making a big negative current yield. The worst time was in 2008 when they were making a 40% current yield so, it is probably inversely related which is that the good assets are bought at a poor current yield we have fallen into this trap before, that is why I am able to tell you this with….

**Manish Bhandari:** No, I appreciate that. And where you would be at this point of time with your current purchases?

**G. Shivakumar:** It will be a low current yield if you would charter it out today and that is why we are not looking to do any major charters unless we get a decent price we are not looking to lock in at poor rates.

**Manish Bhandari:** And you would be locking-in for, what three years?

**G. Shivakumar:** You can lock-in one year, two years, three years, even five years but we would not like to lock in to lower rates for a long period of time.

**Manish Bhandari:** Sure. So you would look at six months or a year max?

**G. Shivakumar:** Yes or run them on the spot market. If we are not getting the prices that we feel we should get for these assets we would rather run them on the spot market. Take the volatility of the spot market but over a period of time, it will give us a better yield on the ships in terms of a day rate.

**Moderator:** Thank you. Next question is from the line of Jayesh Gandhi, Harshad Gandhi Securities. Please go ahead.

**Jayesh Gandhi:** Sir, now since we have Mr. Trump coming in power in U.S. and wanting to revert the trade partnership with big economies of the world. Do you see prolonged weakness in dry bulk rates or any way it affecting us?

**G. Shivakumar:** Actually, as far as we can see it is basically about finished goods where the trade partnerships were there. We do not see it as having any major negative impact on our business. In fact, having more crude oil production from the U.S. could result in more crude oil trade, maybe more product trade as well. So, the main thing is on finished goods really which affects the container business rather than our commodity business.

**Moderator:** Thank you. Next question is from the line of Samir Kapadia from Fortune Interfinance. Please go ahead.

**Samir Kapadia:** Just wanted to reconfirm that by the end of the financial year you would be holding 44 number of vessels. Is it right?

**G. Shivakumar:** That is correct, at the end of this financial year with the committed CAPEX we should be at 44.

**Samir Kapadia:** But then you said you are going to buy three more in the coming quarter, right? And your current vessels stands at 38, if I am right in the presentation.

**G. Shivakumar:** No.

**Anjali Kumar:** We are currently at 42 ships and we have two more ships which we have committed to take delivery for.

**Moderator:** Thank you. Well, that was the last question. I now hand the floor over to Ms. Anjali Kumar for her closing comments.

**Anjali Kumar:** Thank you everybody for your participation in this call and like always, we will have the transcript uploaded on our website in some time. So, thank you all for joining us.

**Moderator:** Thank you. Ladies and gentlemen with that we conclude today’s conference call. Thank you for joining us and you may now disconnect your lines.