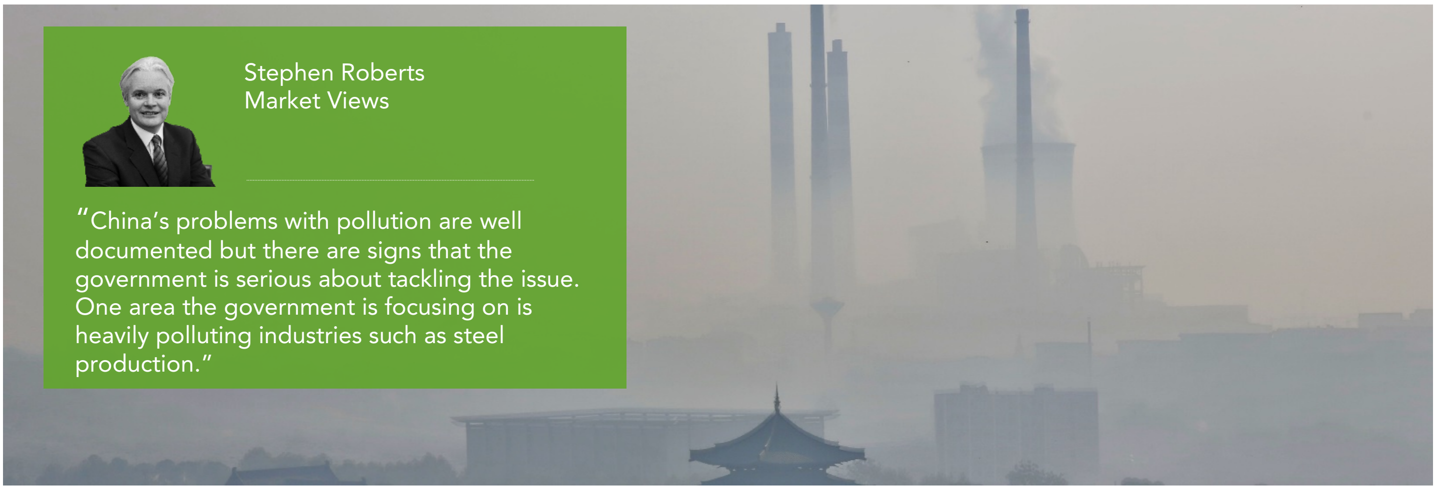
THE BUY CASE FOR DRY-BULK SHIPPERS

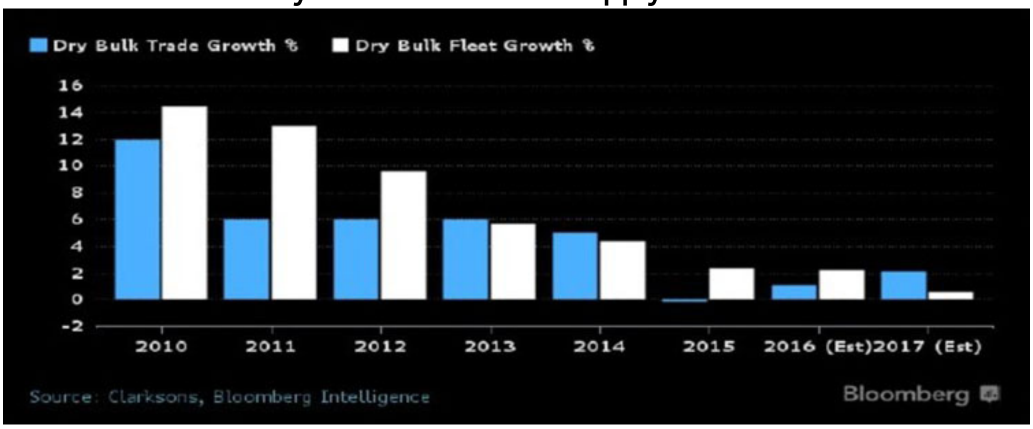


China's problems with pollution are well documented but there are signs that the government is serious about tackling the issue. One area the government is focusing on is heavily polluting industries such as steel production. The iron ore and coal which the Chinese steel mills use to produce steel have historically had a high sulphur and ash content. The changes in legislation will require the mills to burn less pollutive materials which will, in turn, require the Chinese to import "cleaner" fuel from places such as Australia and Brazil. Dry-bulk shipping demand is expected to accelerate to 4% this year, from 2% in 2016 (according to projections by Clarksons). Iron ore trade is expected to grow by 5%, coal by 3%.

China Customs Iron Ores and Concentrates Total Imports

Following a supply boom during the end of the last commodity cycle, daily shipping rates have collapsed resulting in the order book for dry-bulk ships falling to a 25 year low. Dry-bulk trade growth is finally shaping up to exceed fleet growth again. Going forward, the gap is expected to widen, since it takes around two years from a vessel being ordered to its completion.

Dry-bulk Demand and Supply Growth



Changes in international fuel regulations are being introduced, to curb emissions from ships. This will require all ships to cut the sulphur limits in the marine fuel they use from 3.5% to 0.5%. According to Wood Mackenzie, shipping industry fuel costs could rise by up to $60 billion in 2020, resulting in an increase in fuel costs of approximately 50%. In order to run ships more economically, speeds will need to be reduced from 13 knots to 10 knots. Precious Shipping have commented that this cut in average speed will effectively cut the global fleet by 17%. This, along with the scrapping of older inefficient ships, will result in a substantial tightening in the global fleet.

With ship supply going down and demand for dry bulk commodities expected to increase, the logical consequence is for daily shipping charter rates to increase. The best indicator for shipping rates is the Baltic Dry Index, a composite of different dry-bulk vessel rates. Based on our analysis, we believe it could double or even triple from its current levels.

Baltic Dry Index

If shipping rates do see a significant increase, the shippers will see a substantial impact from operational gearing along with an increase in the value of their underlying fleet. Golden Ocean Group Limited is a typical example, based on our analysis, their average daily achieved shipping rate could double from the levels achieved recently, which would still only be half of previous peak levels. The stock would trade on a forward EV to EBIT of only 6x but currently trades at only 0.6x book value.

We believe that as Governments, particularly India and China, get more serious about pollution many opportunities exist.

INFORMATION

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