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Executive Summary

We continue to be concerned by the state of the shipping industry. Container shipping companies are struggling to push through rate increases and liquid and dry bulk operators are contenting with some of the lowest daily returns in years. The cause is overcapacity, which looks unlikely to ameliorate any time soon. Further, there are fresh challenges on the way, including the mega ships being built by **Vale** and **Maersk Line**.

In Iran it seems certain that the country's maritime industry's impressive growth in the face of international sanctions will weaken this quarter as western sanctions continue to target it. The latest blow is the addition of ports operator Tidewater to the list, which will result in a drop in the number of services calling at Bandar Abbas. The country's shipping companies also continue to be in the firing line. Whether Iran's planned 'economic jihad' of investment in the sector will negate these downward pressures remains to be seen.

Headline Industry Data

- 2011 Port of Bandar Abbas throughput growth forecast 1.4%, and to average 2.7% per annum to 2015.
- 2015 Port of Bandar Abbas throughput expected to reach 2,963,131 20-foot equivalent units (TEUs).
- 2011 total trade real growth forecast at 0.1%, and to average 1.7% to 2015.

Key Industry Trends

Tidewater Added To US Blacklist As Sanctions Noose Tightens On Iran: Iranian trade, already severely hampered by US sanctions intended to curb the state's alleged nuclear weapons programme, was dealt another blow in July as the country's ports operator has been blacklisted by the US. **Maersk Line**, the world's number-one container shipping line, has already stated that it will suspend all services to Iranian ports.*Seized Ships Handed Back* - In April 2011, the last of five cargo ships that had been seized was handed back to Iran in Malta. With European banks calling in loans to **Islamic Republic of Iran Shipping Lines** (IRISL), Iranian vessels had been impounded around the world in 2010.

New York Legislators Fire Warning Shots In IRISL Sanctions Battle: The risk of doing business with any company with possible links to **IRISL**, formerly known as the **Islamic Republic of Iran Shipping Lines**, has been further highlighted in June by a 317-count indictment filed in New York against the company and 10 alleged alias corporations. The contagion is such that French shipping line **CMA CGM**,

accused by a number of US politicians of being lax in their checks up to now, has set up a special 'Iran desk' to ensure no further contraband cargos are carried on their vessels.

Iran Wages 'Economic Jihad' To Boost Marine Security: The Iranian maritime sector has big development plans for the current Iranian year, which runs to March 2012, with 103 projects in the pipeline. These include 89 infrastructure development projects and 14 equipment projects. **BMI** notes that throughput at the country's ports has continued to show remarkable growth in the face of US-led sanctions, and that these works will help this, though with sanctions intensifying all the time we wonder for how long the growth can continue.

Key Risks To Outlook

The sanctions imposed on Iran provide considerable risk to our forecasts. With the nuclear-energy development programme, which the Iranians insist is not for the development of weapons, elevated to the status of a national cause, it seems unlikely that it will be dropped anytime soon. It has long been known that Tehran's intention is to become a political and military powerhouse in the Gulf, a situation that has proved unnerving to its regional neighbours. That several Middle Eastern states have been actively calling for military action against Iran's nuclear facilities, despite the massive risks to regional stability that this would pose, clearly highlights their concern surrounding the possibility of a nuclear-armed Tehran in the region.

The addition of Tidewater, and the company's ports, to the boycotted list, will have massive ramifications for the port of Bandar Abbas, and will halt the double-digit growth the facility has enjoyed in recent months.

Equally, as Iran is so reliant on the export of its oil to feed its economy, any fluctuation in the price of fossil fuels could provide risk to our projections.

SWOT Analysis

Iran Shipping SWOT	
Strengths	▪ The port of Bandar Abbas managed to defy the global downturn in shipping, posting positive growth in 2009 and 2010. ▪ Iran's location on the Gulf allows it access (via the Straits of Hormuz) to major shipping lanes heading both east and west. ▪ Iran's ports feature as ports of call on Maersk Line, IRISL, MOL and Evergreen services. ▪ Iran's navy is involved in protecting Iranian vessels from pirate attacks in the Gulf of Aden.
Weaknesses	▪ The reputation of IRISL, Iran's national maritime carrier, has been tarnished by reports that vessels that it has chartered have been exporting arms illegally. ▪ Foreign companies have distanced themselves from operating in Iran's maritime sector, with HPC pulling out of a contract to renovate the port of Bandar Abbas. ▪ Tidewater, operator of the container terminal at Bandar Abbas, has been added to US sanctions.
Opportunities	▪ Iran has launched its first domestically-produced container vessel. ▪ Kuwait has earmarked a specific port for Iranian imports following an improvement in trade ties between the two nations.
Threats	▪ The threat of conflict in the Straits of Hormuz remains, and Iran has said that it will close the straits if it is attacked by the US or Israel. ▪ Further sanctions imposed by the international community could increase the damage visited on Iran's trade. ▪ The US Treasury Department has sanctions in place against IRISL and many of its affiliates. ▪ The UK Treasury has ordered the ceasing of all business between UK financial services and IRISL. ▪ Israel has displayed its ability to place diplomatic pressure on foreign countries dealing with Iran, a recent example being HPC's decision to abandon a project at Bandar Abbas.

Iran Political SWOT	
Strengths	▪ Since the overthrow of the Pahlavi family in 1979, there has been some reduction in the level of political corruption, while wealth distribution has improved marginally. ▪ The Revolutionary Guard and Basij militia are fiercely loyal to the supreme leader, helping to maintain social stability.
Weaknesses	▪ The Islamic Republic has one of the poorest human rights records in the region, and authorities do not hesitate to quell dissidents. A number of journalists and anti-government protesters are being held in custody. ▪ While decision-making ultimately rests with the supreme leader, the regime is heavily fragmented and consensus is hard to reach. ▪ Widespread perceptions of electoral fraud during the course of June 2009's presidential elections have damaged the regime's legitimacy in the eyes of many Iranians.
Opportunities	▪ The *Majlis* (parliament) is more than just a rubber stamp - the move by 150 parliamentarians (out of 290) to hold the president accountable for his handling of the economy is a positive indication that checks exist.
Threats	▪ Ongoing nuclear tensions raise the prospect of further US and UN Security Council sanctions and the - albeit very limited - possibility of a military strike by the US or Israel. ▪ Ethnic tensions are on the rise. ▪ High youth unemployment. ▪ The rising influence of the Revolutionary Guards within the political and economic arena may present a challenge to the status quo over the long term.

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Iran Economic SWOT	
Strengths	▪ Iran has the world's second-largest proven oil reserves after Saudi Arabia, and the world's second-largest proven gas reserves after Russia. ▪ Oil and gas aside, Iran is rich in other resources and has a strong agricultural sector.
Weaknesses	▪ Local consumption of hydrocarbons is rising rapidly and this, coupled with ageing technology in the oil & gas sector, will have a negative impact on its oil- and gas-exporting capacity. ▪ The commencement of the country's subsidy reform programme has lowered its growth prospects and accelerated inflation. ▪ International sanctions discourage foreign oil companies from bringing much needed technical knowledge and equipment to maintain oil output levels.
Opportunities	▪ The gas sector remains underdeveloped, and there is considerable room to maximise this source of revenue. ▪ A growing population, combined with a shortage of housing, provide opportunities for investment in residential construction.
Threats	▪ A decline in global oil prices would have a marked impact on the economy. Although an Oil Stabilisation Fund exists to protect the economy at times of weaker oil prices, it has increasingly been used to fund government over-spending and could be close to empty. ▪ A further deterioration in Iran's relations with the international community over its nuclear programme could result in the imposition of more extensive economic measures by the UN Security Council or the US. ▪ There is a serious risk of capital flight owing to fears of conflict or sanctions.

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Iran Business Environment SWOT	
Strengths	▪ The Foreign Investment Promotion and Protection Act gives some protection to foreign investors and now allows relatively good terms for the repatriation of profits. ▪ Although stifled in the years since the Islamic Revolution, Iranians have traditionally been renowned for their entrepreneurial skills - a factor that is potentially a strong pull for foreign investors.
Weaknesses	▪ Progress on the privatisation front remains slow, despite some recent encouraging signs. ▪ Foreign firms are currently unable to own Iran's hydrocarbon resources. The resultant 'buy back' deals offer less advantageous terms than those elsewhere, limiting hopes of new investment.
Opportunities	▪ As part of the fourth five-year development plan 2005-2009, the government ended tax and customs concessions afforded to the country's quasi-statal bonyads, or foundations. ▪ The government has inaugurated the first phase of an oil swap project with Russia, Kazakhstan and Turkmenistan. The project will compete with the rival US-backed pipeline that will run to the Mediterranean from Baku in Azerbaijan through Georgia to Ceyhan in Turkey.
Threats	▪ UN, US, and EU sanctions on the Islamic Republic pose a significant threat to the participation of foreign firms in the oil & gas sector. ▪ Central bank supervision of charitable funds will be stepped up sharply, after it emerged that a number of these funds had collapsed due to indiscriminate lending practices.

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Global Overview

Container Shipping: Overcapacity Threat To Haunt In The Mid Term, Asia-Europe Most Exposed

Although the volume of containers handled at global bellwether ports continues to increase, rate levels are still falling. **BMI** fears that this overcapacity will continue over the mid term, with a new slew of mega-vessels - including **Maersk Line**'s 18,000 20-foot equivalent unit (TEU) fleet - due online from 2013.

Our fear is that with 2012 set to be another year of record growth in the global box-shipping fleet, the sector will not find any relief from overcapacity, and this is bad news for container lines' bottom lines.

Drivers

Key Views

- Throughput volumes up year-on-year (y-o-y), but weakening consumer sentiment is a threat to the recovery's strength.

- Another downward revision from **BMI** on the US economy is on the cards.

US Consumer Sentiment In Decline

Following disappointing economic data in the first half of 2011, **BMI**'s country risk desk has factored down its forecasts for the country's real GDP growth for the whole of 2011 to 2.6%. The poor performance from the US economy, in our view, stems from poor weather and high oil prices, which have offset the positive effects of payroll tax cuts and have led once again to consumers tightening their belts.

Although retail sales in June recorded a 12th consecutive month of growth, consumer sentiment is weakening. Both the University of Michigan and Thomson Reuters index of consumer sentiment and the Conference Board's US consumer confidence index, two of the leading US indexes for the measurement of consumer confidence, recorded consumer sentiment decline.

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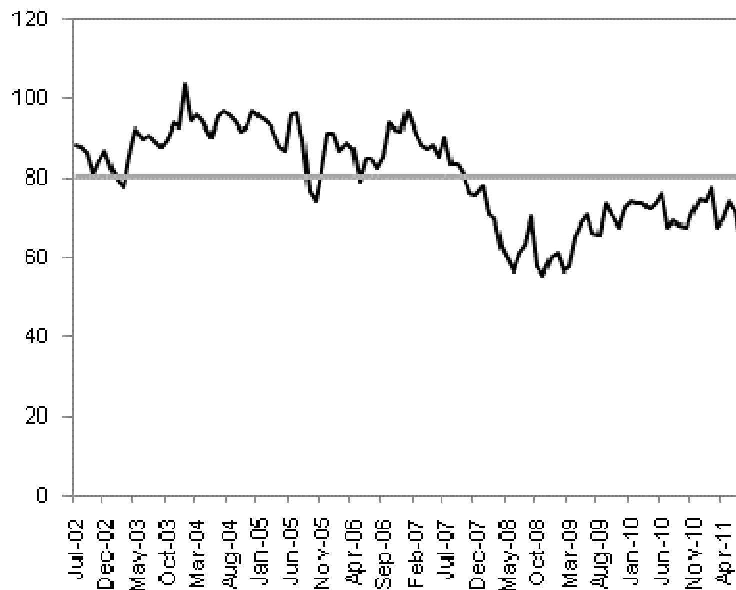
Confidence Waning

Reuters/ University of Michigan Index of Consumer Sentiment



Source: Reuters

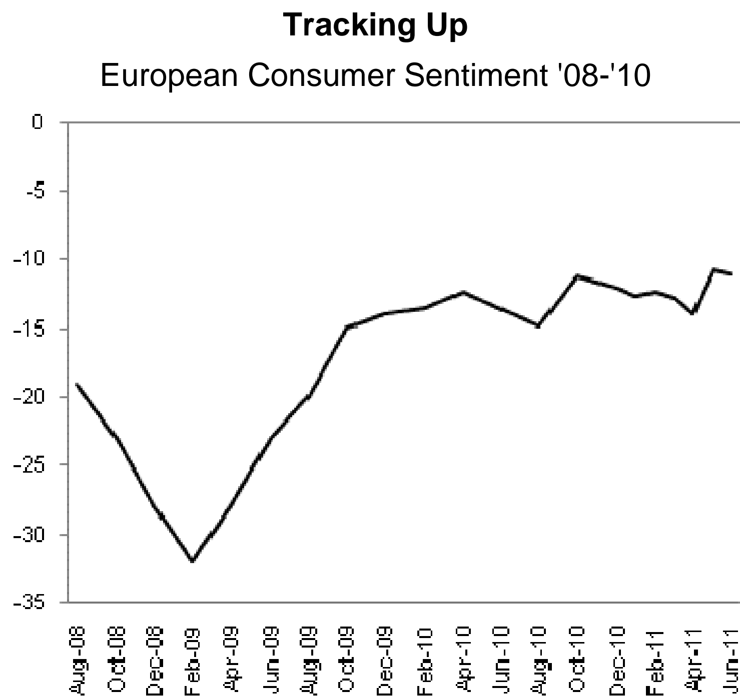
Conference Board's US overall consumer confidence index fell to 58.5 (1985=100) in June from 61.7 in May. University of Michigan and Thomson Reuters index of consumer sentiment reading is now in its fourth consecutive month of decline, falling to 63.8 - its lowest level since March 2009.

More worrying is the weak sentiment looking ahead. According to data from the Conference Board's US consumer confidence index, positive expectations for the next six months have weakened, with the majority of respondents predicting that business conditions, employment and income will remain at the current levels.

Although **BMI** expects a modest acceleration of growth in H211 and has in fact factored up its real GDP growth forecasts for 2012 to 3%, we reiterate our core view that the recovery in the US economy is set to be erratic and on the whole weak as households continue to deleverage.

European Consumer Market Strengthening

Consumer confidence in Europe, while staging a y-o-y recovery, has weakened month-on-month (m-o-m), with the Flash Consumer Confidence Index falling to -11 in June from -10.7 in May 2011. The economic outlook in Europe's largest consumer markets (Germany and France), however, continues to strengthen.



Source: European Commission's Business and Consumer Survey

BMI holds an above-consensus outlook for Germany and has increased its real GDP forecast to 3.5% due in part to strong confidence indicators and a tightening labour market.

We have also upgraded our economic outlook for France, with growth of 2.2% predicted, up from our previous forecast of 1.7%. The increase in our real GDP forecast comes on the back of France's broad-based recovery, with industry and manufacturing supporting the already strong recovery in private consumption.

Bellwethers

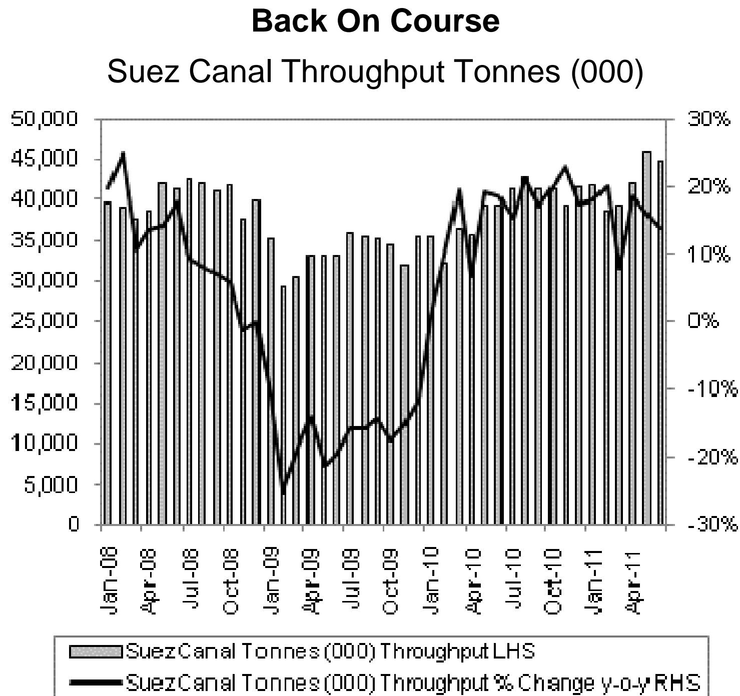
Key Views

- Global volumes increasing y-o-y.
- Shanghai to remain the global number one container port.
- Decline in number of vessels through the Suez Canal, but increasing volumes is a trend set to continue in the mid term as more mega-vessels come online.

Number Of Ships Drops, But Volumes Rise

The global recovery in container-shipping volumes continues to play out, with data from global bellwether the Suez Canal recording that volumes shipped through the waterway, which links Asia to

Europe, are up y-o-y by 10.4% in H111. Year-to-date (YTD) figures show that volume throughput on the Suez Canal has returned to pre-downturn levels.



Source: Suez Canal Authority

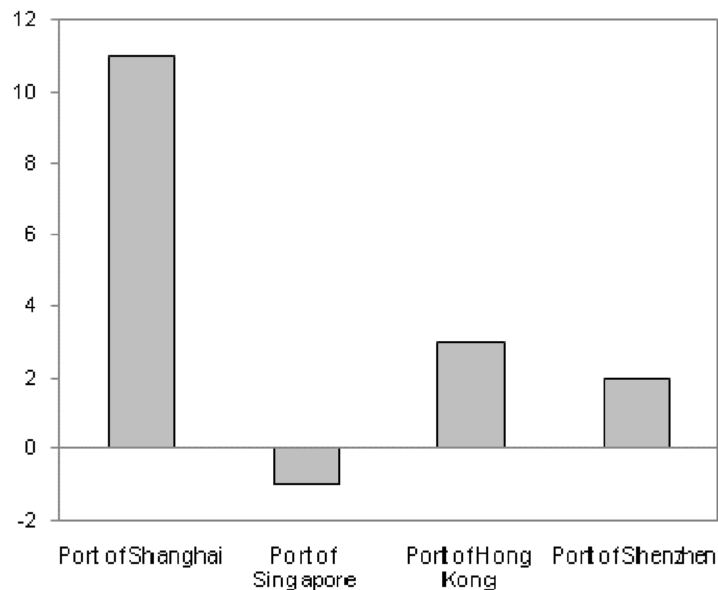
One interesting trend that has emerged is that while vessel numbers are decreasing, volume growth has continued, showing the impact of larger vessels on this major container route. In H107 the number of box vessels transiting the canal reached 3,641, with tonnes via the waterway recorded at 204,382 tonnes; in H111 the number of container vessels sailing through the Canal had dropped to 3,578 vessels, while volumes increased to 252,358 tonnes.

Shanghai Streaking Ahead, Singapore In Decline

The continued uptick in volumes is noted in **BMI**'s monthly bellwether ports tracking data. China's top two container ports, Shanghai and Shenzhen (the world's number one and number four box ports in 2010), are both posting throughput growth for the YTD (January-May 2011). In the first five months of the year Shanghai recorded a y-o-y box throughput rise of 11%, and Shenzhen a y-o-y rise of 2%. Throughput, while increasing, is growing at a slower rate than in 2010, which is understandable considering base effects in 2010, as volumes recovered from the record lows of 2009. This trend will continue, in **BMI**'s view, for the full year, with **BMI** forecasting y-o-y growth in 2011 of 6.44% at the port of Shanghai and 1.45% at the port of Shenzhen.

Out In Front

Asian Bellwethers Jan-May 2011 % Change y-o-y



Source: Port Authorities, BMI Research

This forecast will enable the ports to hold their global positions of first and forth respectively, with **BMI** predicting throughput of 30.9mn TEUs at Shanghai and 22.8mn TEUs at Shenzhen.

Singapore, the one-time number one, is faring less well. In H111 box levels at the facility dropped by 1% y-o-y. It appears that **BMI**'s core view that mainland Chinese ports will increase their role in the global box-shipping sector to the detriment of traditional Asian transhipment hubs is playing out.

This has led **BMI** to factor down its forecast for the port to a y-o-y increase in throughput of just 2.96%. Growth at such a level will not enable the port to recover to its pre-downturn level. In 2011 **BMI** is forecasting box levels at Singapore to reach 29.2mn TEUs, still off the port's 2008 throughput level of 29.9mn TEUs.

US Ports Getting Back To Pre-Downturn Levels

The US bellwether ports of Los Angeles and Long Beach have painted a mixed picture for the year so far. At Los Angeles volumes increased by just 1% in H111, while at Long Beach stronger growth has been recorded, with box levels for the first half of the year increasing by 6%. **BMI** had originally been expecting stronger growth by this time, so we have factored down our full-year forecasts. Although we still expect levels to increase y-o-y, growth will be considerably slower than that posted in 2010, with **BMI** forecasting that container throughput at Los Angeles and Long Beach will increase by 1.9% and 4% respectively. This projected growth will place the port of Los Angeles back to its 2008 level, but still some way off its record throughput year of 2006, when it handled 8.46mn TEUs. We believe that the port will be able to reach this milestone figure once more, but not until 2013.

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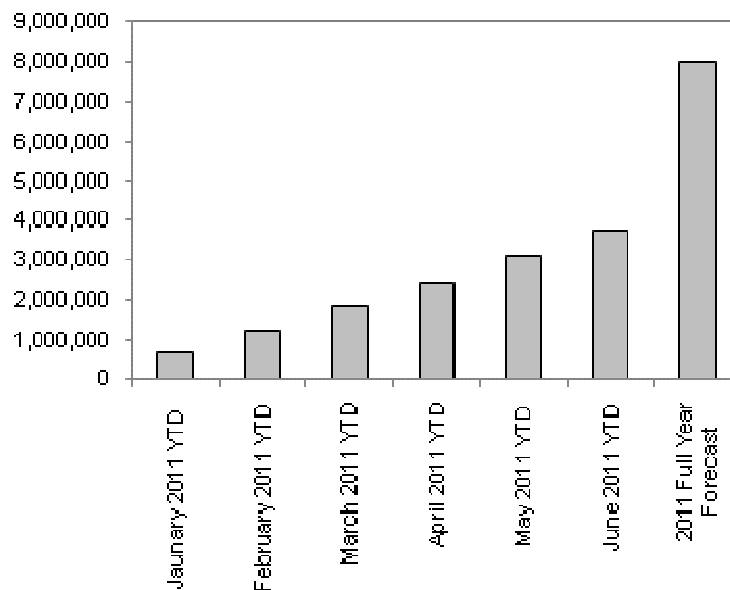
On Target

Port Of Los Angeles Container Throughput (TEU)



Source: Port Authority, BMI Forecast

European Box Continues

Europe's second largest port, the Belgian port of Antwerp, is so far the only European box bellwether to release its H1 data. The port's throughput for the first half of 2011 stands at 4.4mn TEUs, an increase of 4% y-o-y. Further growth is expected at the port during the peak season and in the lead-up to Christmas, leading **BMI** to increase its full-year forecast, with a growth revision of 9mn TEUs, taking the port back to its pre-downturn level.

Europe's largest port, the Netherlands' port of Rotterdam, and the region's third-largest facility, the port of Hamburg, have not yet released their H1 data, but their Q111 data displayed that the recovery at both continues with Q1 volumes at Rotterdam and Hamburg up 10% and 18.2% respectively y-o-y. For the full year at the port of Rotterdam we project an increase of 11.5% on 2010's figure, and y-o-y growth of 8.3% at the port of Hamburg.

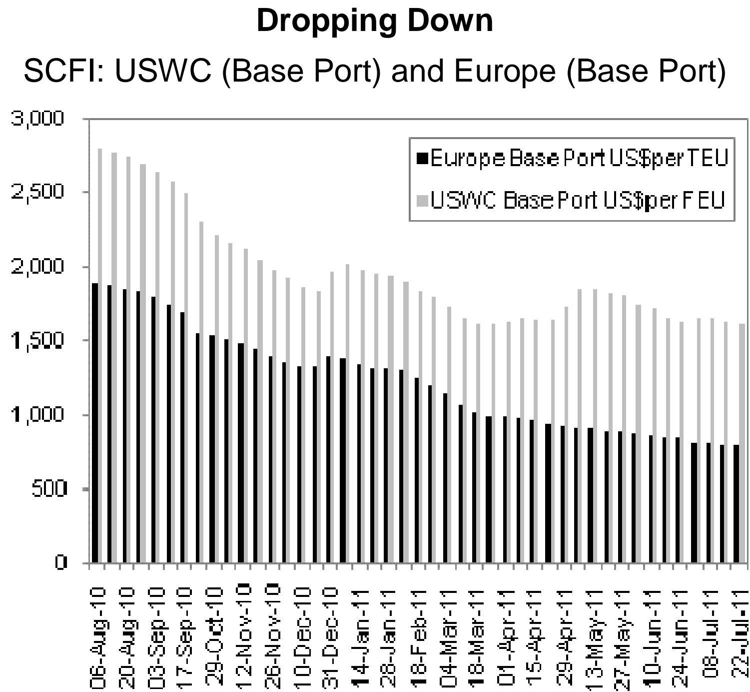
Rates

Key Views

- Rates to continue ticking lower.
- **BMI** is more bullish on the transpacific, as lines have been decreasing capacity.
- Strategy of expansion to expand on Asia-Europe stems from the curse of the mega-vessels.

Big-Money Routes No Longer Raking In The Cash

The Shanghai Containerised Freight Index (SCFI) dropped 34.66% from August 6 2010 to July 22 2011. After stabilising for one week at the beginning of July, the index looks set for another round of declines as the industry struggles to get a handle on the overcapacity that is plaguing the sector.



Source: SCFI

The reason behind the decline in rates continues to be the 'big money' routes of the transpacific and Asia-Europe. Between August 6 2010 and July 22 2011 rates on the transpacific and Asia-Europe declined by 41.8% and 57.4% respectively. Despite the beginning of the peak season on the transpacific and the fact that a liner agreement still exists on the route lines have failed to push up rates.

On the Asia-Europe trade route rates have plummeted to a new low of US$800 per TEU and **BMI** fears that they still have not reached their nadir, with the trade route having had no respite from the declining rates since the beginning of the year.

Bailing Out Of The Transpacific

Understandably, as rates have ticked lower operators on the transpacific have been bailing out. The latest player to decrease its exposure to the route is **Grand China Shipping** (GCS), which is going to revert to its original one-loop transpacific service by joining its two loop services together. The carrier launched its second transpacific crossing in May 2011. By implementing this strategy the company will reduce the number of vessels it will operate on this trade route from 10 to nine.

Abandon Ship

Shipping Lines Which Have Decreased Their Transpacific Exposure

Company	Action Taken
CSAV	Transpacific service suspended
TS Lines and Hainan Pan Ocean	Transpacific service suspended
Maersk Line, MSC and CMA CGM	Postponed their planned new transpacific service until Q212
Grand China Shipping	Merging two transpacific routes and decreasing the number of vessels on the loop

Source: BMI Research

GCS joins Hong Kong-based **TS Lines** and China-based **Hainan Pan Ocean Shipping**, which in July announced that they would suspend their TP1 loop. The majors are not immune, with the world's three largest container lines, Maersk Line, **MSC** and **CMA CGM**, which operate a vessel-sharing agreement on the route, announcing that they will now postpone their planned TP1 service (as the service is known by Maersk, Jaguar is MSC's name and Hangzhou Shuttle is what CMA CGM will call it) until Q212.

The Curse Of Mega-Vessels

Interestingly, despite the fact that rates on Asia-Europe have been hit harder than those on the transpacific, a strategy of suspending routes has not been implemented; in fact lines have been increasing their exposure. Hong Kong's **OOCL** has become the latest line to announce a new service plan, with the company's North Europe Express Service (NE4) due for launch on August 4 2011.

BMI puts this tactic down to the curse of the mega-vessel. These vessels can only be operated on the Asia-Europe service, so lines have been increasing their operations on the trade route as they are prepared to take a hit on their bottom lines rather than mothball these brand-new vessels.

If Two Peak-Season Surcharges Fail, Try Again

A strategy that operators on both trade routes are trying to implement is rate increases. It is now the peak season on both trade routes, and lines have been trying to push through peak season surcharges (PSS) since June.

A PSS announced by the Transpacific Stabilization Agreement (TSA) was due to be launched on June 15 2011,; this was later pushed back to July 15 2011 and now has been moved to August 1 2011. PSS on the Asia-Europe route have also been postponed three times, with operators set to try their luck again on August 1 2011. **BMI** believes that overcapacity on both of these routes will ensure that a PPS fails to materialise this year. We note that a similar situation arose last year, and 2011 looks set to be the second consecutive year when lines were unable to implement PSS.

BMI is slightly more bullish about operators on the transpacific being able to implement a rate increase than we are about those on the Asia-Europe route, as lines on the transpacific have being trying to decrease supply by suspending routes in a bid to bring supply and demand back into equilibrium.

Capacity

Key Views

- Overcapacity to continue plaguing Asia-Europe in particular, due to more mega-vessel orders.
- Emerging trade routes are the best protected from the rate decline.
- Companies set for a loss for 2011 as rates continue their downward trajectory.

When Will Supply and Demand Reach An Equilibrium?

More mega-vessels are due online in 2011, and there are fears that the cheap new-build options that saw mass-ordering in H210 and H111 will haunt the industry again in 2013, when the majority are due online. Although we note that demand is picking up, with bellwether ports worldwide posting y-o-y growth, we are sceptical about whether this growth will be great enough to soak up the supply of vessels coming online.

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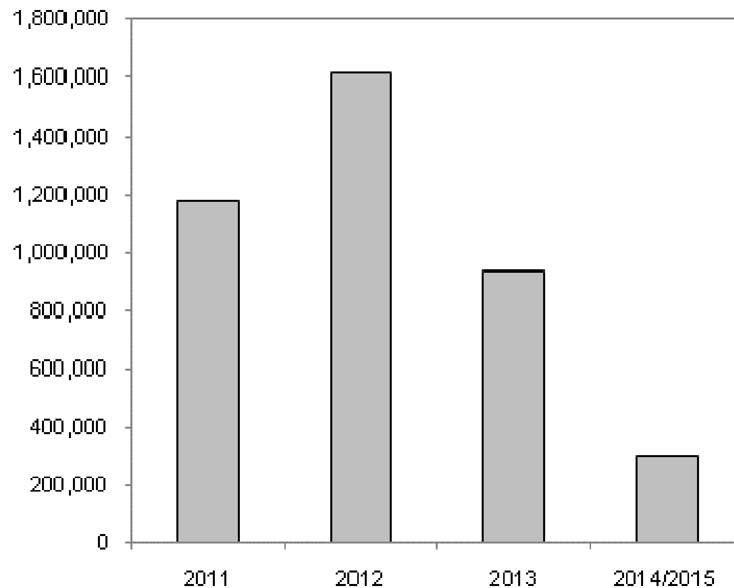
Supply Drowning Out Demand

Newbuild Deliveries Vessel Capacity (TEU)



Source: Lloyd's List Intelligence

Another 1.178mn TEU of capacity is due online in H211 according to Lloyd's List Intelligence. **BMI** fears that overcapacity will continue to plague the box-shipping sector in the mid term. In 2013 another slew of mega-vessels are due online, with Lloyd's List Intelligence estimating that as current orderbooks stand 937,655TEUs are due online in this year. Just as worrying is the delivery schedule for vessels in 2012, indicating that there will be no respite for operators as a further 1.6mn TEUs is due to be launched in 2012.

The route that will be most plagued by overcapacity, in **BMI**'s view, is Asia-Europe, with a large percentage of the box orderbook being for mega-vessels, which can only operate on the Asia-Europe trade route. Further compounding this threat is the new generation of mega-vessels, which is due to start coming online from 2013: the 20 triple E-type vessels that Maersk Line has ordered will boost a capacity of 18,000TEU and will only be able to operate on the Asia-Europe route.

Table: Newbuilds Due Online In The Mid Term

Company	Vessel Size	Date Due
OOCL	10- 13,000TEU (4 on charter to NYK)	6 delivered by 2013 4 more 1st delievered from 2013
OOCL	2- 8888TEU	n/a
NOL	10-8,400TEU, The line has also signed a letter of intent for two 10,700TEU vessels, which would bring the total NOL order package to US$1.2bn. Two of 8,400TEI	n/a

Table: Newbuilds Due Online In The Mid Term

Company	Vessel Size	Date Due
	fleet upgraded to 9,200TEU	
Evergreen	10- 8,000TEU	in 2012
Hamburg Sud	8- 3,800TEU	n/a
Hamburg Sud	6- 9,600TEU	May-13
Hapag-Lloyd	4- 13,200TEU Upgraded earlier order of six 8,750-TEU to 13,200TEU total of 10 13,200TEU	mid-2012 and the end of 2013
CSAV	2- 8,000TEU	June and July 2012
CSAV	5- 8,000TEU	2011 and 2012
NOL	10-14,000TEU	2013 and 2014
Maersk Line	Order of 20- 18,000TEU Option of 10 more	2013-2015
Hanjin Shipping	3- 4,700TEU	1st-2012, 2&3-2013
Costamare- Long term charter for Evergreen	5- 8,000TEU	2013
Evergreen	10- 8,000TEU	1st in 2013

Source: BMI Research

As the overcapacity issue continues **BMI** expects strategies last viewed in the downturn to come to the fore again. Laying up vessels is the easiest way to decrease capacity. But deferrals and perhaps cancellations of newbuilds are also possible tactics. **BMI** would also expect to see an uptick in scrapping in the mid term and we note there are plenty of candidates, with Lloyd's Intelligence Unit estimating that over 1.2mn TEU of fleet capacity is now 25 years or over.

Shelter From The Storm

BMI highlights that although the traditional big-money routes of the transpacific and Asia-Europe have been worst hit, emerging trade routes (ETRs) have either witnessed minimal declines or increases in rates over the past year. **BMI** highlights the intra-Asia trade route, with its growing demand and resilience to the rate decline, as the best trade route option for box operators looking to expand their operations. Rates on routes to Japan, Hong Kong and South Korea have in fact increased between August 6 2010 and July 23 2011.

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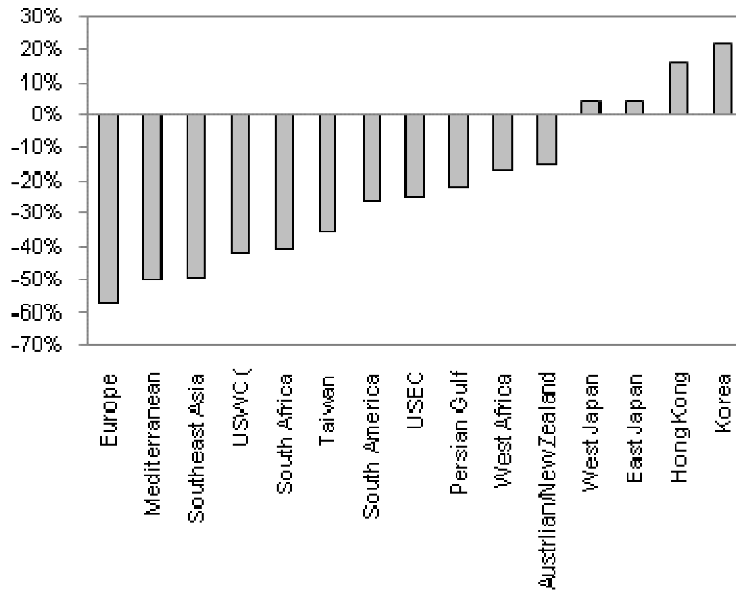
Intra-Asia A Safe Haven

SCFI Index % Change (US$ per TEU/FEU) (August 6 2010- July 22 2011)



Source: SCFI

We are waiting for H111 results from the majors, but Q1 already highlights the impact of overcapacity on the rates. A few of the majors (Maersk Line and Evergreen) managed to keep their heads above water, but the majority of lines sailed once more into the red in Q111. We fear this will be a year-long trend as the big-money routes actually start to lose carriers money. The lines best positioned to ride out this decline in revenue are obviously the larger more diversified companies, but **BMI** would also highlight shipping lines that are heavily exposed to ETRs.

Dry-Bulk: No Recovery On The Horizon For Dry Bulk As Overcapacity Cloud Hangs Low

BMI expects dry bulk shipping's troubles to continue for some time to come, with overcapacity putting continued downside pressure on rates. While demand remains strong, there are fears that Chinese imports of iron ore may ease due to monetary tightening, a worrying scenario at a time when the market is already saturated with vessels. A possible drop off in Chinese demand, as well as a hefty orderbook, means it is unlikely we will see the return of supply/demand equilibrium over the medium term.

Drivers

Key Views

- Chinese demand to remain the main driver of dry bulk shipping.
- Major producers to increase output of coal and iron ore year-on-year (y-o-y).
- India and China to remain heavily reliant on coal imports for electricity generation.
- Chinese demand for iron ore to moderate y-o-y due to strong inflationary pressures and tight monetary policies, but to remain strong.

Australia continues to dominate iron ore exports. We forecast that Australian iron ore production will reach 630mnt (million tonnes) in 2015, up from 438mnt in 2010, marking an average annual growth of 7.6%. Meanwhile, Brazil's iron ore sector is poised to continue its recent expansion, which has seen the country consolidate its status as the second largest exporter in the world, after Australia. Total production is forecast to reach 412mt in 2011, up 11.4% y-o-y.

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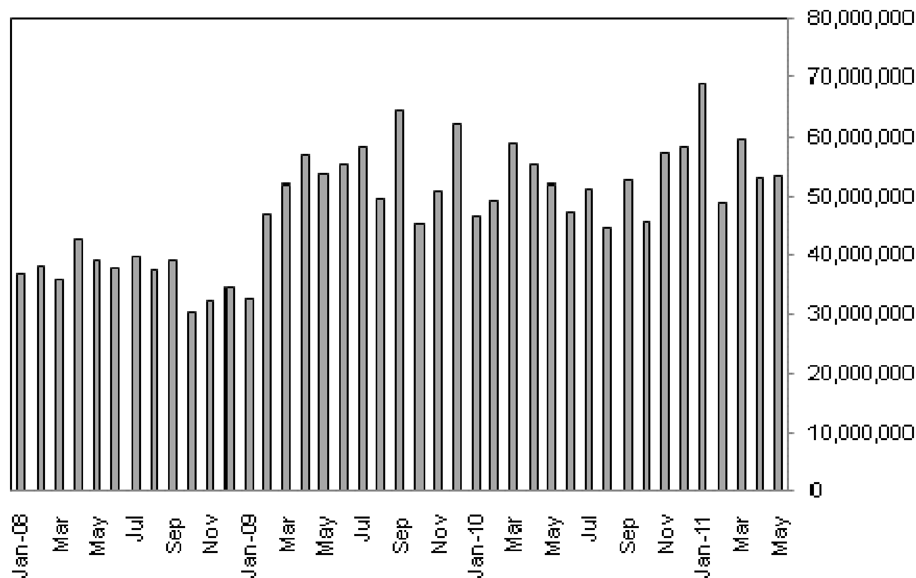
Dragon's Appetite Slows, But Still Strong

Chinese Iron Ore Imports (tonnes)



Source: Bloomberg

Australia is also the world's biggest coal exporter, and we forecast production to fall by 1.7% y-o-y to 405mnt in 2011, due to the flooding at the start of the year that halted operations in Queensland, the major coal-producing region. However, over our medium-term forecast period to 2015 we expect the coal sector will rebound, with annual growth averaging 6.5%, reaching 561mntpa (million tonnes per annum) in 2015, from 412mntpa in 2010. In Indonesia, which is the world's second largest coal exporter, we expect coal production to increase by 7.2% in 2011. According to the Indonesian Coal Mining Association (ICMA), almost all coal miners in Indonesia, including the country's top two producers, **Bumi Resources** and **Adaro Energy** , have indicated that they will expand production in 2011 to meet rising demand from China and India.

We expect demand for these two commodities to remain strong, with Asian appetites leading the way. The major Asian economies remain heavily reliant on coal for electricity generation. Despite India's vast reserves of coal, estimated at 60.6bnt, it has a domestic shortage and remains one of the largest importers in the world, as regulation and slow environmental clearances delay new investment into the sector. There is a similar situation in China, where at present approximately 80% of electricity production is from coal. The country's coal consumption increased by 40% to 3.25bnt in 2010 from 2.32bnt in 2005. We forecast that Chinese demand will outstrip domestic supply. This shortfall would have to be met by importing coal from Indonesia, Mongolia, Australia and other coal exporting countries.

Our outlook for Chinese iron ore imports is slightly more moderate, due the government's drive to ease inflationary pressures by decreasing construction, resulting in a reduced need for steel production. We have already begun to see the effects of this, with Chinese iron ore imports falling considerably from

68,970,084 tonnes in January 2011 to 53,303,173 tonnes in May. Imports remain well above the historical average, however. While we expect Chinese ores and metals imports to moderate from 2010's estimated 24.22% y-o-y growth, we still expect strong demand, with 10.38% growth in imports predicted in 2011.

Capacity

Key Views

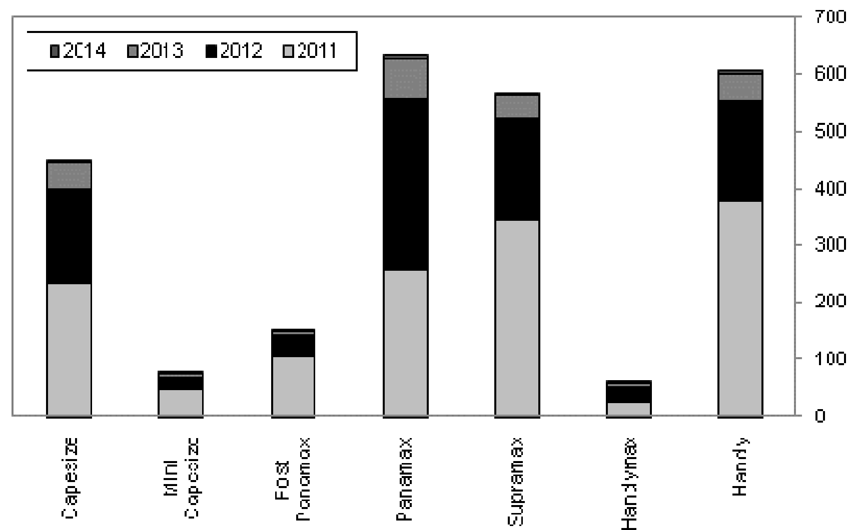
- Overcapacity to remain the sector's single biggest worry.
- Large orderbook is a major cause for concern.
- Rates to remain depressed due to supply/demand imbalance.
- Scrapping likely to increase due to strong steel prices, but unlikely to make a significant dent in global fleet size.

Orderbook Remains A Threat

Last quarter we highlighted the threat of overcapacity in the sector, and it appears that little has changed, with a stream of new vessels coming online and the hefty orderbook remaining a cause for concern. According to Lloyd's List Intelligence, the current global dry bulk fleet stands at 8,156 vessels or 560.21 deadweight tonnes (DWT). There are 2,515 vessels on order, equating to 31% of the current fleet, or 108.78DWT. Of these, 1,324 vessels, or 16% of the current fleet, are due online in 2011.

Heavy Orderbook Weighs On Rates

Fleet Orderbook By Vessel Class 2011-2014



Source: Lloyd's List Intelligence

Capesize Capacity Crisis On Cards

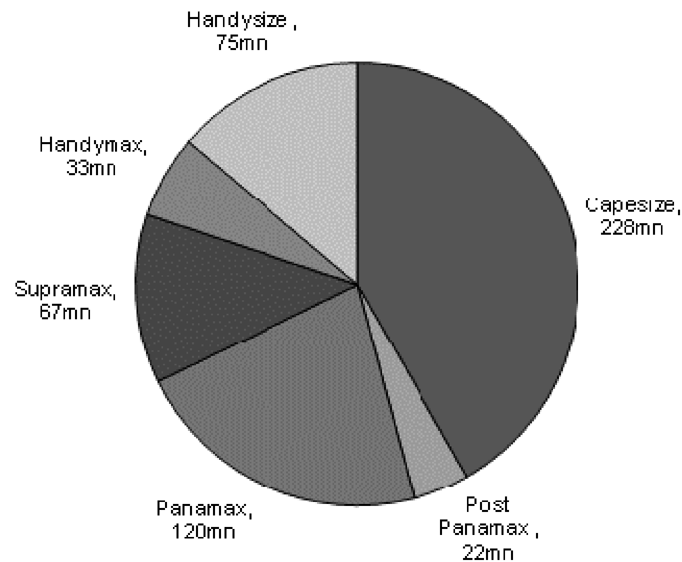
This vessel size could find itself in particular trouble, due to a large orderbook, as well as the twin pressures of a potential slowdown in Chinese iron ore demand and the introduction of Vale's Chinamax ore carriers, which aim to keep freight rates as low as possible.

COSCO UK 's chairman, Simon Young, recently warned Capesize operators to expect a slowdown in Chinese demand for iron ore as the government tries to slow construction activity, thereby reducing the need for steel production. However, as mentioned above, while we do expect a y-o-y moderation of demand for iron ore on the back of monetary tightening, meaning that demand for Capesizes may ease, we still expect strong y-o-y growth of 10.38% in China's ores and metals imports in 2011. As such, we maintain our view that the main worry for Capesize operators is ever-increasing capacity.

BMI believes the orderbook should be of particular concern to Capesize owners, with 448 of these vessels on order, equating to 37% of the current fleet. Of these, 230 are due online in 2011. On top of the large orderbook, further downside pressure on Capesizes will come from the impact of Brazilian mining giant Vale's plan to develop its own fleet of 400,000-tonne iron ore carriers. The company is spending a reported US$50bn on a fleet of massive Chinamax vessels, the first of which was delivered in May 2011, which it will use to ship iron ore to the world's biggest iron ore importer. The reasoning behind Vale's strategy is clear: it wants to drive freight rates from Brazil to Asia (the destination for 75% of its iron ore) as low as possible. That would reduce the price disadvantage of Brazilian iron ore compared with Australian ore, which is located much nearer to Chinese steel mills. As these vessels come online we expect them to displace Capesizes, which will be left competing for an increasingly small pool of cargo.

Capesizes Dominate

Vessel Class by Dead Weight Tonnes (DWT)



Source: Lloyd's List Intelligence

Scrappage On The Up, But Too Little, Too Late For Dry Bulk

BMI notes that owners have been upping their use of scrappage as a means to control fleet size in response to the overcapacity crisis. Scrapping of Capesize vessels in the first five months of this year hit its highest level since 1996, Bloomberg reported. As of June 24 2011 some 48 Capesizes had been demolished this year, surpassing the previous annual record of 24 Capesize ships being scrapped, in 1996, and far outpacing the 18 vessels scrapped in 2010. **BMI** notes that if scrapping continues at this pace throughout 2011, it could reach 32.6mn DWT.

High prices for scrap steel have undoubtedly encouraged scrapping. In some cases in 2011 Capesize bulkers have been sold for scrap for more than US$10mn, a figure that it could take a Capesize vessel three years to earn on the spot market based on average daily earnings in 2011. Nevertheless, despite the fact that scrappage is gathering pace, **BMI** maintains its view that sustained growth in the global fleet will ensure the supply/demand imbalance remains in place. With 1,324 vessels due online in 2011, the surge in scrapping will not balance out the dry bulk supply/demand imbalance.

New-Build Prices Falling As Carriers Eye Bottom Lines

Another reflection of concerns in the sector are lower new-build prices, which indicate that shipbuilders are trying to encourage orders, while lines are watching their bottom lines and do not want to spend. In August 2010 prices for new-build Handysize, Panamax and Capesize vessels stood at US$27mn, US$35mn and US$59mn respectively. In June 2011 prices had eased to US$25mn, US$33mn and US$54mn.

BMI notes that if new-build prices continue to drop, lines that have not been hit badly by plummeting rates, such as Greece's Diana Shipping, may choose to order, taking advantage of lower prices. Although any orders made now will not be due online until the end of 2012 at the earliest, it remains unclear whether the sector will have regained the supply/demand equilibrium by then. While the majority of the current orderbook is due online in 2011, vessels due online in 2012 already number 921 and we could see this number increase considerably if lines continue to order.

Rates

Key Views

- Rates to remain depressed due to supply/demand imbalance.
- Vale's fleet of Chinamax ore carriers could put further downside pressure on Capesize rates.
- Given the volatility of rates another scenario similar to the collapse of dry-bulk shipper Korea Lines cannot be ruled out.

BMI has been following the fortunes of the Baltic Dry Index (BDI) since the beginning of 2011. During the period the BDI has fallen 14%. At the time of writing, in mid-July 2011, the BDI stood at US$1,453, demonstrating that while the index seems to have recovered from the one-year low of US$1,043 it hit on February 4, it is nowhere near recovering to the one-year high of US$2,995 that it reached in September 2010. Our outlook for the index gives little to be positive about, as we see overcapacity continuing to weigh on sentiment.

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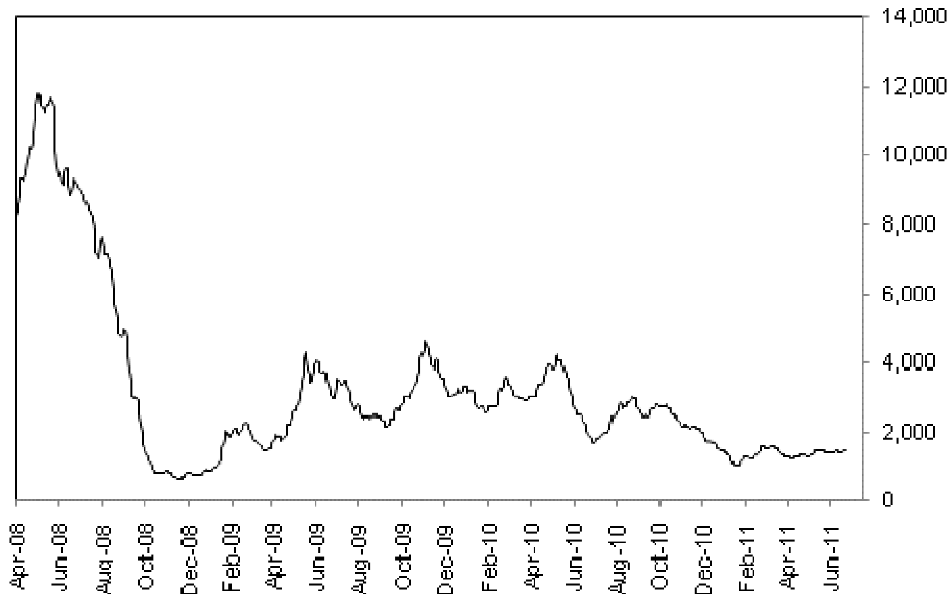
Rates Drown As Overcapacity Crisis Continues

Baltic Dry Index, 3 years



Source: Bloomberg

BMI notes that while vessels of all sizes have been hit by plummeting rates, the largest dry bulk vessel class, Capesizes, have suffered particularly badly. At the time of writing the Capesize index stood at US$2,126, down by a massive 48% from its one-year high of US$4,461 reached on October 27 2010.

Vale's Venture To Displace Capesizes

Further downside pressure on the index comes in the form of Brazilian mining giant Vale's fleet of Chinamax ore carriers, the first of which came online in May (see above). Although Australia has a more advantageous location, Capesize vessels, with a capacity of 150,000 tonnes, are the largest ships that can be used to transport Australian iron ore. So, in what has been called 'the biggest hedge in shipping history', Vale strategists have bet that over the next 25 years it will be cheaper and more efficient to ship iron ore on its own 400,000 tonne capacity ships, rather than at the prevailing spot market price for smaller bulk carriers. As these vessels come online, they could further depress freight rates and displace Capesize vessels, which could result in more tonnage competing for less cargo.

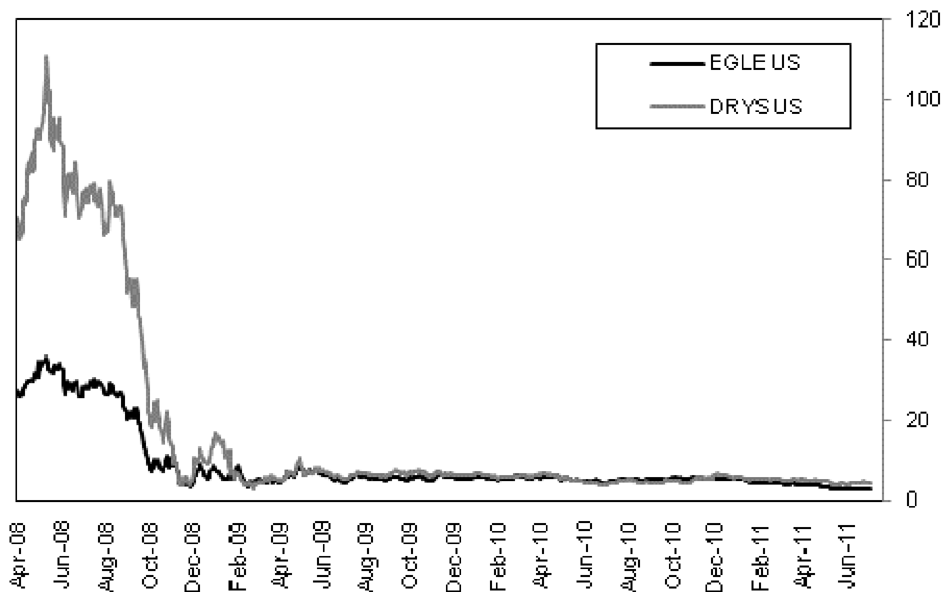
BMI cautions, however that Vale's strategy was called into question when it rerouted the first of its Chinamaxes, Vale Brasil, to Italy on its maiden voyage, coupled with the news that China Rongsheng has missed its delivery target for eight of the 16 Chinamaxes ordered for 2011. **BMI** believes these moves highlight growing concern about a possible easing of Chinese demand for iron ore, a serious cause for worry given the China-focused nature of Vale's strategy.

Declining Rates See Share Prices Plummet

Fears about continued downward pressure on rates due to overcapacity are reflected in dry bulk lines' share prices. At the time of writing many listed dry bulk shippers were trading just above their one-year lows. **Dryships** was trading at US$4.14, up from a one-year low of US$3.56. **Baltic Trading** was trading at US$5.64, up from a one-year low of US$5.44. **Eagle Bulk** was trading at US$2.38, up from a one-year low of US$2.30. With share prices of dry bulk shippers' following a steady downward trend, **BMI** believes that a repeat of the **Korea Lines** collapse and the contagion that went with it earlier in 2011 cannot be ruled out.

Share Prices Suffer As Rates Sink

Eagle Bulk & Dry Ships Share Prices, 3 years



Source: Bloomberg

No Respite On Horizon For Dry Bulk

BMI maintains our long-held view that supply will continue to outweigh demand in the dry bulk sector for some time to come. While the potential easing of Chinese iron ore imports is a cause for concern, we believe the main downside pressure on rates will continue to come from the crippling overcapacity in the sector. In order to regain some equilibrium in the sector we expect to see lines continue to scrap vessels in the coming months. However, the weighty orderbook means that it is unlikely scrapping will make a significant dent in the global fleet. With more tonnage expected to come online in the coming months, that recovery is still out of reach for the dry bulk shipping sector.

Liquid Bulk Shipping: At the Start of a Brutal Down Cycle

Overview

The global crude-oil shipping sector continues to be affected by the overcapacity that is plaguing the container and dry bulk shipping sectors also. Vessels ordered during the boom years continue to come online, and although the ordering appears to have slowed, there is much extra tonnage still scheduled to be floated. Despite reported increased demand from Japan in the wake of the country's nuclear scare in March, and the ever-growing needs of China and other emerging markets, **BMI** does not believe that demand growth will be sufficient to absorb the tonnage, especially given the flat growth we project in the OECD countries this year. As such we agree with leading tanker operators in projecting a continued period of pain for the sector, especially for the larger vessels.

Drivers

Key Views

- Global oil supply and demand to grow, though not sufficiently to absorb tonnage.
- Increased Saudi production potential lifeline for tanker industry.
- US oil imports to fall, China to take up some of the slack.
- Non-OECD countries will drive demand growth.
- Short-term risk to oil import demand from the IEA stockpile release.

BMI's Oil & Gas team forecasts a rise in the global production and consumption of oil in 2011. However, growth in absolute volumes and percentage terms will be slower than in 2010, as the world was recovering from the economic downturn. Global demand is forecast to grow by 1.5% in 2011, which would take consumption up to 86.7mn barrels per day (b/d). This is less than half the 3.2% growth estimated for 2010, showing a slowing in the global recovery. Nevertheless, growth should still be significant, particularly in emerging markets. In terms of global production we see growth of 0.4% in 2011, which would take the global total to 85.93mn b/d.

Exports To Grow

The largest oil exporter in the world is Russia. According to our Oil & Gas team's estimates, Russia exported 7.35mn b/d in 2010. Although the downturn did affect Russian oil exports (they fell by 2.7% in 2008, to 7.07mn b/d), they recouped this fall in 2009, rising once again to 7.34mn b/d. Over the medium

term forecast period we project that Russian oil exports will continue to rise, reaching 7.28mn b/d by 2015.

However, as Russia exports most of its oil via pipeline to Europe, this figure is not as reassuring for tanker operators as it might first appear. Russia's largest oil-exporting facility, at the port of Primorsk, actually saw a decline in throughput in 2010. In 2009 the oil terminal handled 74.7mn tonnes; in 2010 this fell by 6.5% to 69.8mn tonnes. Throughput for January to March 2011 was also down compared to both 2009 and 2010. This may have been due to problems the port had with ice through the first quarter. In April oil throughput at the port was the highest for the period over the past three years, rising to 6.62mn tonnes, though in May throughput was down again to 6.33mn tonnes. For the five months throughput stood at 29.17mn tonnes, down 2% on the corresponding period in 2010.

The second largest crude exporter, Saudi Arabia, is, thankfully for the shipping industry, more reliant on the tanker operators for the export of its oil. Tanker demand from Saudi Arabia will be greater than our initial forecast for 2011 (**BMI** had previously projected a fall in Saudi Arabian production in 2011). In December 2008 OPEC agreed its largest ever cut in production, of 2.2mn b/d, in order to arrest plummeting oil prices in the aftermath of the September 2008 financial crisis and subsequent global economic slowdown. However, with strong demand in emerging markets and economic recoveries in the West, the average price of OPEC basket crude rose from as little as US$34 per barrel (bbl) in January 2009 to more than US$91/bbl in December 2010. In December OPEC met in Oran, Algeria, and agreed to leave production quotas unchanged.

The subsequent 'Arab Spring' upended the global crude oil market. Prices rose sharply as civil war engulfed Libya and traders feared that violence in Bahrain would spread elsewhere in the Gulf. The International Energy Agency (IEA), which represents Organisation for Economic Cooperation and Development (OECD) oil consumers, called on OPEC to increase production in order to ameliorate the price rise. Although the cartel initially blamed financial speculators for forcing prices higher, and claimed repeatedly that the oil market was well supplied, a change of heart was detected in OPEC's Arab Gulf core.

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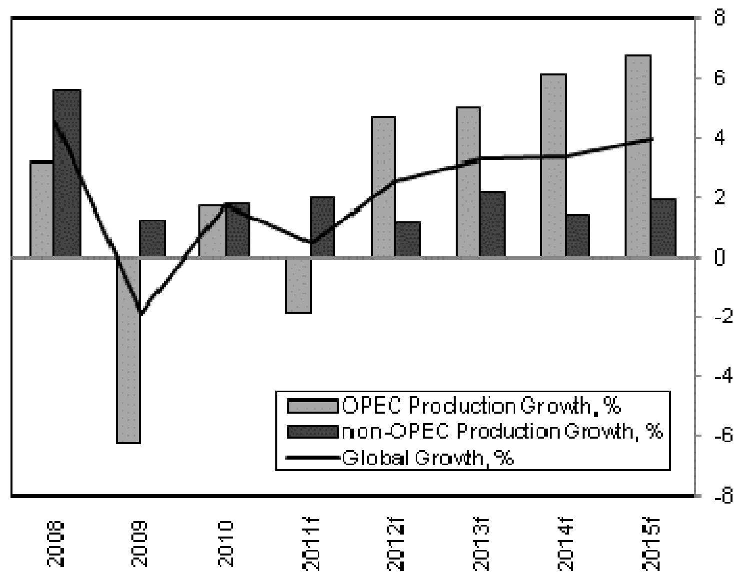
OPEC Leading The Way

BMI Oil Supply Forecast To 2015



Source: BMI

An unnamed delegate from an Arab Gulf OPEC producer told Reuters on June 5 2011 that the cartel needed to increase production by 'at least' 1mn b/d after expressing dissatisfaction with prevailing crude prices. Another Gulf OPEC delegate told Reuters that the cartel intended to meet higher H211 crude demand 'without flooding the market'. OPEC's own data, published in its May 2011 oil market report, forecast a rise in global oil demand by 2.16mn b/d quarter-on-quarter (q-o-q) in Q311, broadly in line with IEA estimates. With only a tiny increase in non-OPEC supply forecast for Q311, the cartel essentially conceded the argument on fundamentals: more oil was needed.

The Financial Times quoted an unnamed industry source as saying on June 6 2011 that Saudi Arabia added about 200,000b/d of supply in May 2011 and was expected to add a further 200,000-300,000b/d in June. Saudi Arabia is now set to boost output to around 9.1mn b/d, the first time it has exceeded 9mn b/d since 2008. With smaller increases from Kuwait and the UAE likely, global oil demand is likely to be easily met in Q311, given Saudi Arabia's mammoth 3.5-4.0mn b/d spare production capacity. The considerable tonne-miles generated by shipping to anywhere from Saudi Arabia should be good news for tanker operators.

Although we do still forecast a 1.8% fall in production by the OPEC countries in 2011, **BMI** believes this will be offset by a 2% growth in non-OPEC production growth, which will account for 60.7% oil produced in 2011.

Demand Driven By Non-OECD Countries

With production growing and the holder of the world's largest spare capacity set to increase its exports,

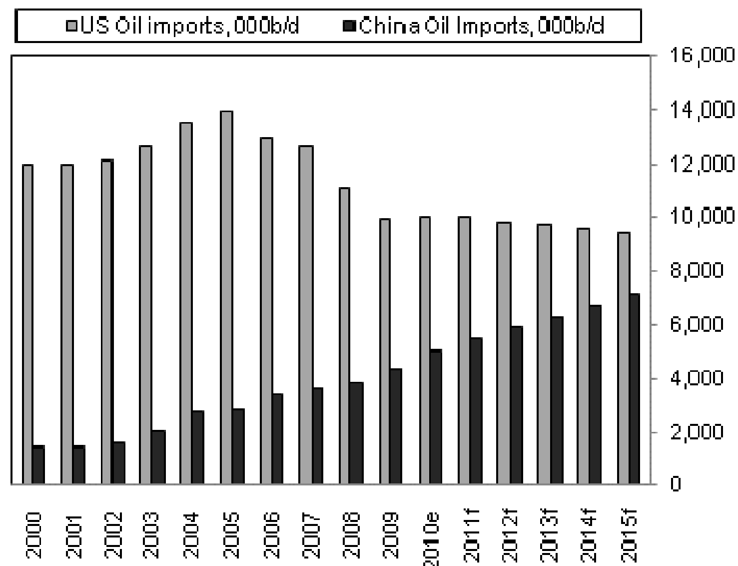
the key variable for the global crude oil shipping sector is demand. **BMI** sees the outlook for crude demand in 2011 as a two-part story, essentially flat growth in developed states and a steady pick-up in emerging markets. We forecast global growth in oil consumption at 1.5%. However, this is being driven almost entirely by non-OECD countries, with growth in their oil consumption forecast at 3.4% in 2011, while in the OECD states we forecast flat growth.

This is best demonstrated by looking at the converging figures for US and Chinese oil imports, which have been getting closer since the turn of the millennium. The world's largest oil importer based on 2009 figures, the US, is set to see a fall in its oil consumption in 2011. **BMI** forecasts that the country's oil imports will dip by 0.3% year-on-year (y-o-y) to 10.02mn b/d. As the US looked to other sources of energy (and its industry has suffered the effects of the downturn), oil imports declined between 2005 and 2009. Although we estimate there was a slight pickup in 2010 (0.6%), our overall trend is one of decline, and we see US oil imports continuing to fall to the end of our forecast period, a worrying trend for tanker operators.

While US oil demand falls, China, the world's second largest oil importer, will take up some of the slack. The country's oil consumption is steadily increasing, growing by an estimated 4.8% y-o-y in 2010 to reach 9.77mn b/d. In 2010 it is estimated that China imported 5.04mn barrels, and we forecast this to increase by 8.7% in 2011, to 5.48mn b/d. Although this is still less than the US imports, China's growing demand will suck up some of the surplus capacity in the tanker sector. However, much will depend on where China sources its oil from. The tonne-mile multiplier was hit in 2010 when China increased its imports from the Middle East at the expense of those from West Africa, therefore shortening the journey tankers had to make, reducing time at sea and increasing the supply of tankers. The Middle East is expected to remain China's favoured supplier, but will face growing competition from Russia, with the East Siberian Pacific Ocean (ESPO) pipeline in operation and having reached its capacity of 300,000b/d at the beginning of 2011.

Chinese Imports Solace For Tanker Operators

US & China Oil Imports



e = estimate, f = forecast; Source: Historical data - BP Statistical Review of World Energy June 2010; Estimates/Forecasts - BMI

IEA Stockpile Release To Hit Industry

The IEA announced on June 23 2011 that it would release emergency stockpiles of oil. The IEA is a 28-country organisation founded in the wake of the 1973-1974 oil shock that works to ensure that a steady supply of oil can be guaranteed in times of crisis and serious oil-supply disruption. Member countries must hold a reserve of oil equivalent to 90 days of net imports, although currently countries are exceeding this, with 146 days of net imports equivalent. The IEA's June announcement stated that the organisation would make available 60mn barrels of oil in response to the ongoing Libyan crisis, which has taken an estimated 132mn barrels of light sweet crude off the market. The release is intended to plug the gap until oil-producing countries ramp up production sufficiently. It is only the third time stocks have been released since the creation of the IEA. The previous occasions were during the 1991 Gulf War and following Hurricane Katrina in 2005.

The near-term outlook for the crude oil shipping sector in light of this announcement is poor. The release of oil stocks already in a country could lead to a fall in imports, and leading shipping companies have seen their share price fall as a result. **Frontline**, **Teekay Tankers** and **Overseas Shipholding Group**, three of the world's biggest tanker companies, all closed on June 24 with their share price down by 3.7%, 0.6% and 2.5% respectively. Longer term the outlook is slightly better, however, as the IEA countries will need to replenish their stockpiles once global oil production returns to its usual level.

Capacity

Key Views

- Liquid-bulk sector to continue to suffer from overcapacity in the market.
- Very few vessels remain to be scrapped.
- Slow-steaming on ballast legs is becoming industry practice.
- New orders slowing, but tonnage still coming online.

With more tonnage on the seas and more set to come online **BMI** holds to its key view that the liquid bulk shipping sector is suffering from overcapacity in the market. According to Lloyd's List Intelligence, as of June 1 2011 the total active crude tanker capacity was 320.98mn deadweight tonnes (DWT), spread over 1,821 vessels. This represents growth of 1.3% in the fleet's capacity since our last liquid bulk overview in April 2011, and is up 3.3% on that of June 1 2010 (310.5mn DWT), though this was over 1,757 vessels. Although vessels are being idled, these currently stand at 44, with a combined weight of 9.81mn DWT. In June 2010 there were 40 vessels idled with a combined weight of 7.89mn DWT, suggesting to **BMI** that larger vessels are being scrapped. There are some means by which the tanker operators can ameliorate overcapacity, although as the threat of this problem has been looming since the global downturn (vessels ordered during the pre-downturn shipping boom years of 2007 and 2008 have been coming online since then), the sector is running out of options.

All Scrapped Out?

Once again, **BMI** does not expect many vessels to be scrapped in the liquid bulk shipping sector over the coming quarter. This does not stem from a belief that overcapacity is ameliorating, but rather that there are few older vessels left to scrap.

The liquid bulk sector was scrapping in 2010 in a bid to stem tanker overcapacity. The cull saw a 51% and 80.7% decline in vessels aged 20-24 and over 25 respectively in 2010. The number of vessels aged 25 and over afloat at the beginning of 2010 stood at 114 vessels; at the end of the year just 22 of these vessels were still sailing.

In our first liquid bulk overview of 2011 we said it was unclear which vessels could be sent to the breakers' yards if tanker operators needed to reduce their capacity further through scrapping in 2011. Younger vessels dominated the make-up of the global tanker fleet, with vessels aged zero to four years increasing their share of the total from 27.7% in January 2010 to 36.2% in December 2010. The share of vessels aged 20 years and over declined from 11.6% in January 2010 to 4.2% in December. If further

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scrapping is carried out in 2011, we wrote, the vessels headed for the scrap heap were likely to be significantly younger than usual.

From the data on the global tanker fleet provided by Lloyd's List, it would appear that scrapping of vessels has slowed considerably. At the beginning of June 2011 the number of vessels aged 25 and over afloat was 23, down slightly from 25 at the beginning of March 2011, but still greater than the 22 recorded in December 2010, and represents just 1.2% of the global crude tanker fleet. This suggests to **BMI** that the industry has scrapped all it can without writing off vessels that are still in good operational order. The share of vessels aged 20 years and over has also risen slightly since March, from 5.3% to 5.5% in June.

Overcapacity Still An Issue As Deliveries Keep Coming

BMI expects overcapacity to continue to be a problem through 2011, as vessels ordered during the boom years continue to come online.

New vessels continued to come online amid the scrapping and idling of 2010, and more are set to follow in 2011. The orderbook due for delivery in 2010 began at 188 vessels. By December 1 2010 this had shrunk to 37 vessels, due online in the last month of the year. Although new vessels did come into service in 2010, **BMI** believes some orders may have been deferred.

The threat of overcapacity will continue to linger in 2011. At the start of the year 188 vessels were due to come into service, and at the start of June this stood at 155 vessels, or 60.67mn DWT. A further 200 vessels are on order for delivery between 2012 and 2015. **BMI** fears that the number of new builds due online in 2011, coupled with the lack of old capacity available for scrapping, will see overcapacity continue to plague the market. We expect rates to continue to suffer.

BMI notes that the poor earnings now seem to be making tanker operators wary, and in recent months orders for newbuilds have dropped off, especially for the larger vessels, which are especially struggling. According to shipbrokers **Gibson**, 'The first three months of 2011 have seen no new VLCC orders, which has not happened in any quarter during the past five years. Even in the first two quarters of 2009, which followed the free fall of the world economy, owners still managed four VLCC newbuildings. That was despite the fact that within the period of Q2 2008 to Q2 2009, average TCE earnings on the benchmark VLCC route TD3 (ME Gulf - Japan) dropped by 86%, from $140,000/day to as little as $20,000/day.'

Although operators may have stopped ordering for now, **BMI** believes that rates will continue to trend down for some time, as the already sizeable orderbook comes online.

Methods To Combat Overcapacity

Tanker operators have a number of methods other than scrapping to combat overcapacity. **BMI** reported

in our last liquid bulk overview that more and more vessels were slow-steaming, and in the past three months it has begun to look like the industry norm, especially for very large crude carriers (VLCCs), as companies follow market-leader Frontline's example.

Slow-steaming was a trick used by container liners at the height of the downturn in 2009, as demand for their services plummeted and containerised shipping demand fell for the first time ever. The reduction in speed makes for an even greater reduction in fuel expenditure. Since the start of 2011 bunker prices have risen on the back of a general increase of oil prices due to the political unrest in the Middle East and North Africa (MENA), impinging on tanker operators' narrowing (or non-existent) profit margins.

According to a report published by shipbrokers **CR Weber** in May 2011, average costs for bunker at benchmark ports had risen by 33% since the start of the year: 'Observed as a percentage of gross freight on the TD3 VLCC benchmark [tanker dirty route three, from Ras Tanura in Saudi Arabia to Chiba, Japan], bunker costs averaged 57% during Q1. This level jumped to 75% during April and briefly touched as high as 84% earlier this week.' A subsequent 6% drop in bunker costs saw the cost as a percentage of gross weight drop back down to 74%. This led to time-charter earnings on the route gaining 40%, showing how crucial bunker costs are when determining a VLCC operator's profit margin.

As a result operators have begun to slow-steam, and even ultra slow-steam, on ballast legs at least, in an effort to conserve fuel. On the TD3 the savings through doing so are said to be in the region of US$3,000 a day. A further benefit of the strategy is that it helps combat the overcapacity in the tanker fleet as vessels are taking longer to complete their voyages. This helps push rates down, although the rates do not gain enough from this effect to compensate the extra expenditure on bunker.

Idling was a capacity-cutting strategy used throughout 2010, one picked up from the container-shipping sector, and, as we projected last quarter, it has continued to be used in 2011. In January 2010 the idled tanker fleet stood at 6.92mn DWT, and by December 2010 had reached 9.5mn DWT. The global idled fleet has stayed at a similar level through H111, and stood at 9.81mn DWT at the start of March. The number of crude carriers idled stands at 44 vessels.

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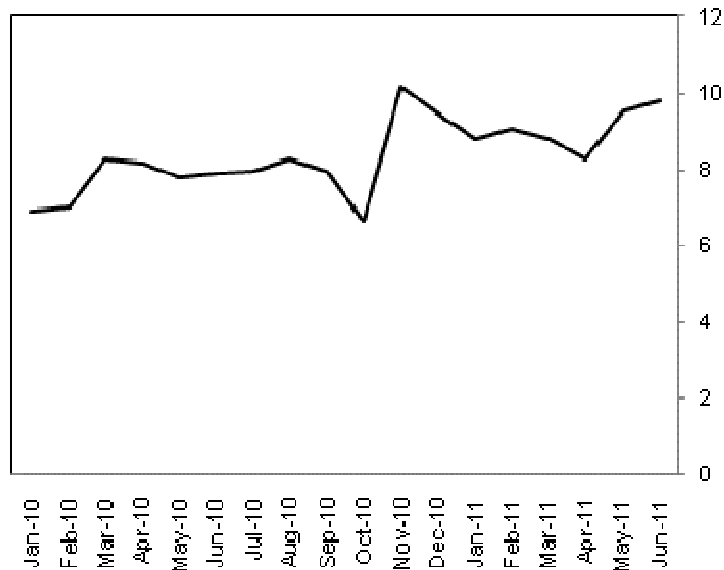
Idling Up

Idled Vessels (mn dwt)



Source: Lloyd's MIU

One way by which the overcapacity may be lessened is if oil prices fall once again and it becomes worthwhile for traders to use VLCCs to store oil at sea in anticipation of another price rise. This is one reason why rates were so much higher in 2008, as a number of vessels were being used as storage. On the downside it masked the true capacity of the global fleet, which may explain the surplus of new orders the sector is currently struggling with. **BMI** has noted one such deal recently. In July 2011 it was reported that **Koch Supply & Trading Company** booked VLCC the *British Purpose* from **Optima Shipbrokers** for 30-60 days.

Rates

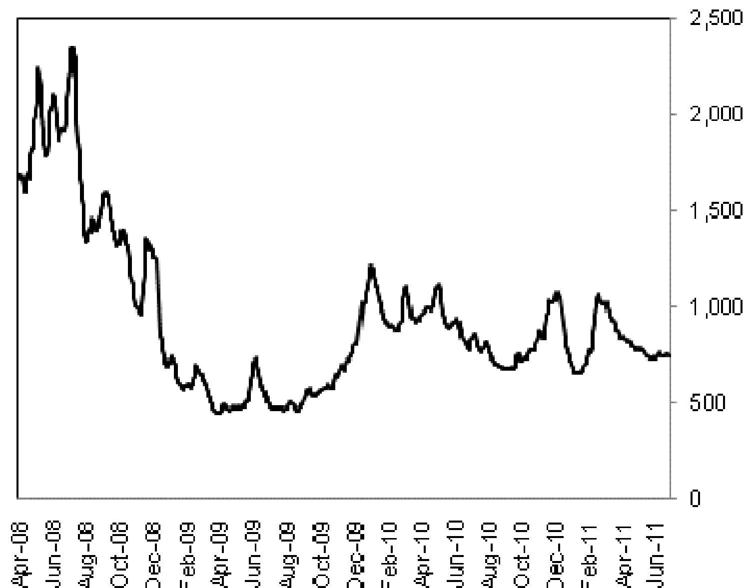
Key Views

- Rates on key index and benchmark tanker routes will continue to fall.
- Tanker operators will struggle to maintain their bottom lines.

The Baltic Dirty Tanker Index (BIDY) is made up of a composite of routes and prices to give an indicator of global crude oil shipping rates. The index has been on a fairly constant downwards trajectory over the past three months, from April 2011. At the time of writing, on July 11, the BIDY stood at US$751, its close from July 8. This is a fall of 14.2% from three months previous, April 8, when it closed on US$876.

Far From 2008 Highs

Baltic Dirty Tanker Index, US$



Source: Bloomberg

The two benchmark routes that **BMI** has been tracking, the TD3 and the TD5 (Suezmax vessels plying the Bonny Offshore, Nigeria to Philadelphia, US) have not fared well in the past three months, and at the time of writing were taking a further battering from the IEA's stockpile release announcement. Daily returns for VLCCs on the benchmark TD3 averaged just US$9,400 in Q211, down from US$22,871 in Q1, and we believe the coming quarter will see them average even lower. The difference between current rates and those of the pre-downturn boom year of 2008, when they averaged US$96,400, could not be more marked.

Frontline released its first-quarter results at the end of May, which highlighted just how much companies focused on the VLCC spot market have been suffering. Its net profits fell 80.6% year-on-year (y-o-y) from US$79,688 to US$15.5mn. The company's Q111 spot VLCC time charter earnings (TCE) were down 36.9% y-o-y from US$45,300/day to US$28,600. Speaking the day before the results were released, Tor Olav Troeim, a director of the tanker operator, said that 'We have to go through a lot of pain before we're back into profitable territory. We have just started on a down-cycle that will be brutal.' With new tonnage continuing to come online, **BMI** shares Troeim's pessimism for the industry.

Opportunities For Some

There are some optimists in the tanker-operating trade, however, looking to the future when the current trough is over. The industry is a notoriously choppy one, but its highs can make the lows worthwhile. This is particularly true for the larger companies, the companies able to weather the bad times more easily.

In April Indian shipping company **Great Eastern Shipping** announced that is to sell three VLCCs that it has not even taken delivery of yet, demonstrating the parlous state of liquid-bulk shipping. However, **Maersk Tankers** was disclosed as the buyer of these vessels. Head of crude at the company, Claus Groborg, stated: 'We have ambitions to grow in the VLCC segment, but without adding to an already large orderbook. At this point we believe that second hand and resale deals offer superior value compared to building and we will continue to search for further growth opportunities.'

This demonstrates to **BMI** the opportunities there are even now for bigger operators, which are able to grow their capacity at low prices in anticipation of the next boom. Frontline owner John Fredriksen has said that he expects the industry to fall further over the next two years, but is already reported to be planning new acquisitions and fleet expansions. As the company said in their Q111 statement, Frontline plans to 'be better positioned by peers to tolerate a prolonged weak trend in the tanker market and be able to react to attractive market opportunities that may occur.'

Industry Trends and Development

Tidewater Added To US Blacklist As Sanctions Noose Tightens On Iran

Iranian trade, already severely hampered by US sanctions intended to curb the state's alleged nuclear weapons programme, was dealt another blow in July as the country's ports operator has been blacklisted by the US. **Maersk Line**, the world's number-one container shipping line, has already stated that it will suspend all services to Iranian ports.

On June 23 the US Treasury Department added **Tidewater**, the ports operator responsible for seven ports in Iran, to its list of Iranian companies with which US entities are prohibited from doing business. The company is designated by the US as being involved with the proliferation of weapons. Furthermore, it is owned by the Iranian Revolutionary Guards, the military organisation suspected by the US government of taking greater control of the Iranian economy as the sanctions begin to restrict private enterprise. The move against Tidewater took place on the same day that new sanctions were imposed against IranAir (*see IranAir Cargo Hits Out Against US Sanctions, BMI, June 28*).

BMI believes that container lines will be increasingly wary of calling at Iranian ports now, even though the sanctions apply only to those vessels sailing under a US flag. On June 29 Maersk Line, the largest container shipping company in the world, with a market share of 15.3%, announced that it would be cutting all services to Iranian ports covered by the new sanctions. Chief operating officer Morten Engelstoft said: '**AP Moller Maersk** and Maersk Line is committed to complying with all relevant foreign trade controls and sanctions programmes, including all relevant provisions of US and EU sanctions related to Iran… Maersk Line has decided to cease acceptance of business to and from the Iranian ports of Bandar Abbas, Bandar Khomeini and Asaluyeh.'

Although Maersk does not sail under the US flag, and is not a US company, it seems likely that the liner did not want to incur the wrath of the US government, as it has a number of big contracts with the administration. Maersk has already got into hot water with the US over its involvement with Iran, and in 2010 voluntarily paid US$3mn to settle allegations by the US Office of Foreign Asset Control that it provided illegal shipping services to Islamic Republic and Sudan between 2003 and 2007.

BMI notes that there are alternatives to shipping to the Tidewater ports, and Maersk Line is likely to try to exploit them. There are other ports in the country, though less developed than those of Tidewater. Feeder vessels from Dubai's transhipment hub of Jebel Ali could be used, though companies with US exposure will need to take care to make sure that they are not infringing any sanctions by doing this.

It seems certain, however, that throughput at the port of Bandar Abbas, which managed to defy the downturn and record four years of double-digit growth from 2007 to 2011, will not see another year of outperformance. We will keep monitoring the monthly throughput at Bandar Abbas and may have to

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revise our forecast down. If more shipping companies cut the port from their rotations, which seems probable following this action by the market leader, then Bandar Abbas may even experience negative growth.

One key consequence of the move by Maersk is the effect it could have on Iranian food imports. Eivind Kolding, Maersk's chief executive, stressed that the company would try not to disrupt food imports, but seemed to acknowledge that it was all but inevitable: 'One thing we are concerned about is that we carry a lot of the reefer cargo, a lot of the foodstuffs to Iran - and of course it's important that a society that depends on that supply chain somehow goes on, even if we have to interrupt our services.' Nor are reefer goods the only cargos to be hit by the fresh US sanctions: one of the Tidewater facilities blacklisted is the Bandar Imam Khomeini grain terminal.

Food prices in Iran have already been rising, and have been subject to the removal of government subsidies. Inflation in the country is the highest in the region; official inflation figures have shown a rapid acceleration in prices, as evidenced by April 2011 CPI and PPI figures coming in at 19.7% and 37.7% year-on-year respectively. We suspect that real inflation could be even higher, as firms flout government-imposed price ceilings (*see our online service, June 17, Inflation To Remain Highest In Region*). Given the massive rise in consumer prices, as well as firms' inability to pass on the majority of their cost increases to customers, we note that economic woes have strong potential to breed widespread discontent among the Iranian public. The sanctions against Tidewater will only exacerbate this.

New York Legislators Fire Warning Shots In IRISL Sanctions Battle

The risk of doing business with any company with possible links to **IRISL**, formerly known as the **Islamic Republic of Iran Shipping Lines**, has been further highlighted in June by a 317-count indictment filed in New York against the company and 10 alleged alias corporations. The contagion is such that French shipping line **CMA CGM**, accused by a number of US politicians of being lax in their checks up to now, has set up a special 'Iran desk' to ensure no further contraband cargos are carried on their vessels.

The US is seeking to curtail all activities by IRISL, which it accuses of being complicit in an alleged nuclear weapons programme in Iran as the main transporter of its procured goods. In addition to charges against IRISL and the 10 other companies, five people have been charged with misleading international banks. These include some of the world's biggest names in the banking sector, such as **Citibank**, **HSBC** and **Deutsche Bank**.

According to a statement filed by the New York district attorney the individuals and companies used the banks to move as much as US$60mn in transactions between them. The deception was necessary as IRISL needs access to US dollars in order to operate effectively in international shipping, but US sanctions have closed its access to the currency. The banks have not been accused and are helping the

authorities with their investigations. It is hoped that the investigation will encourage other banks that may be turning a blind eye to similar activities to halt them. Adam Kauffman, executive assistant district attorney, said that ignoring links to IRISL links 'is criminal conduct and could expose banks to criminal liability'.

BMI notes that the need to be vigilant in any possible dealings with Iranian shipping is clear. French liner CMA CGM, whose vessels have been found in a number of instances to be carrying contraband materials linked to Iran, has experience of this. In March the company was found to be shipping weapons destined for the Gaza Strip aboard its vessel the MV Victoria. Republican congressmen Mike Conaway and Peter King have been vociferous in their calls for US sanctions against the company, the third-largest container carrier in the world. In response CMA CGM stated that 'As regards trade to and from Iran, CMA CGM diligently applies the rules prescribed by the United Nations, the European Union and the US.' Nevertheless, the company has set up a special in-house 'compliance desk' in order to double-check all dealings with the pariah state.

First Non-Iranian Shipping Companies Hit By US Sanctions

The US Department of State has begun issuing penalties against companies for refined-petroleum trading under the Iran Sanctions Act of 1996 and its amendment, the Comprehensive Iran Sanctions, Accountability and Divestment Act (CISADA) of 2010. Seven firms were hit by the sanctions in June for their dealings with the country's shipping lines. **BMI** notes that ignorance is no defence in the eyes of the State Department; companies must be extremely vigilant to ensure that they are not dealing even indirectly with the pariah state if they wish to continue enjoying access to US capital and markets.

State-run oil company **Petróleos de Venezuela** (PdVSA) has been sanctioned for the delivery of 'at least' two cargoes of reformate to Iran in December 2010-March 2011, with a total value of US$50mn - far exceeding CISADA's trigger of US$20mn per cargo. PdVSA will now be unable to bid for US government procurement contracts, secure loans from the US Export-Import Bank (Exim) or obtain US export licences. **PCCI**, a company based in Jersey (UK Channel Islands), and UAE-based firms **Royal Oyster Group** and **Sepahan Oil** were sanctioned after being deemed 'among the largest' suppliers of refined petroleum products to Iran, and for using 'deceptive practices' to further this trade. These three firms will now be prohibited from US foreign exchange, banking and property transactions.

Additionally, three shipping firms - Singapore's **Tanker Pacific**, Israel's **Ofer Brothers** and Monaco's **Associated Shipbroking** - have been sanctioned for the September 2010 provision of an US$8.65mn tanker, the *Raffles Park*, to a front company for state-run Islamic Republic of Iran Shipping Lines (IRISL). While Associated Shipbroking faces the same penalties as the Jersey and UAE firms, Tanker Pacific and Ofer Brothers will be unable to secure Exim loans of more than US$10mn and are also barred from receiving US export licences.

BMI notes that the involvement of the Ofer Brothers, an Israeli company, and its Tanker Pacific subsidiary, has caused something of a stir in Israel. Since the sanctions were imposed on May 24 it has come to light that 13 Tanker Pacific ships have docked in Iran over the past 10 years. It was also Tanker Pacific that conducted the sale of the Raffles Park, but it is the parent company that is being held ultimately responsible. State department spokesperson Mark Toner, in response to the Ofer Brothers denial of culpability, stated: 'We did considerable due diligence in checking out these claims. And what we found is that Ofer Holdings Group is the parent of a company called Tanker Pacific, and that's the company that actually sold this tanker to the Iranians. [Ofer Brothers] failed to do proper due diligence and to prevent this transaction. So they're responsible - I guess my point is that they'd be responsible for the conduct of their subsidiary.'

Even Prime Minister Benjamin Netanahu has commented on the case, stating that the prime minister's office never approved any Israeli ship to dock or unload cargo in Iran, and that no approval had been given for the sale of the tanker. Israel's National Security Council requires by law the seller of any oil tanker to verify that the buyer has no ties with the Islamic Republic, defined by law as a hostile state.

BMI notes that the Ofer Brothers Group's subsidiaries, which include Israeli container line **Zim**, employ thousands of people in Israel and are a major contributor to the country's economy. The sanctions against the company, if held, will cause major difficulties for Ofer Brothers in securing finance and in its day-to-day operations. One need only look to the trouble Iranian firms such as IRISL have had with its finances. In December 2010 three ships, the *Tuchal*, the *Sabalan* and the *Shand*, all registered to different companies, were held in Singapore on mortgage-default grounds, though they were released in January following the company repaying in full the US$200mn outstanding.

Interestingly, Ofer Brothers is not the only party to strenuously deny the connection between the company and the Islamic Republic. Mohammad Nahavandian, chairman of Iran's Chamber of Commerce, Industries and Mines, the country's top trade body, also rebuffed the claims, stating: 'Based on the laws of the country, any kind of trade or economic transaction with the Zionist regime and its affiliated firms is against the law.'

Iran Wages 'Economic Jihad' To Boost Marine Security

The Iranian maritime sector has big development plans for the current Iranian year, which runs to March 2012, with 103 projects in the pipeline. These include 89 infrastructure development projects and 14 equipment projects. **BMI** notes that throughput at the country's ports has continued to show remarkable growth in the face of US-led sanctions, and that these works will help this, though with sanctions intensifying all the time we wonder for how long the growth can continue.

The head of Iran's Ports and Maritime Organisation, Ataollah Sadr, announced the plans in May, stating that the cost of the enhancements would be US$630mn. He stated: 'Since this year has been named as the

"Year of Economic Jihad", we intend to initiate a jihad in expanding marine security and safety and confronting pollution.'

BMI notes that Iran's primary container terminal of Shahid Rajaeei at the port of Bandar Abbas handled 2.6mn 20-foot equivalent units (TEUs) in 2010, an increase of 17.5% on the 2.2mn handled in 2009 (which was itself double-digit growth of 10.3%). From 2011 to 2015 we project that annual growth will slow dramatically as US-led sanctions against Iranian shipping are intensifying (*see our oil and gas team's article, US Gets Tough On Sanction Dodgers As Iran Thirsts For Refined Products, BMI Online Service, May 25*). These development plans, however, could provide some upside risk to mitigate against the effect of the sanctions, especially if the port manages, against the odds, to successfully establish itself as a transhipment hub for the Gulf region. Further, the port has reportedly been experiencing congestion in recent months, with **Hapag Lloyd** announcing in May that it would be adding a congestion surcharge to boxes destined for the port, suggesting that the facility is not equipped to handle the rapid growth it has experienced in recent years.

Sadr pointed out that transhipment of containers at the port in the Iranian year 2010-2011 reached 303,000TEUs, growth of 4.8% on the 289,000TEUs handled the previous year. Incentive policies have been attracting new shipping lines to use the port as their hub. Some of the new policies will be geared towards turning Bandar Abbas into a premier regional hub for transhipment throughout the Persian Gulf region. However, **BMI** notes that Bandar Abbas is just one of many projects in the region all hoping to emulate the transhipment success of Dubai's Jebel Ali. In May this has caused a worsening of relations between Kuwait and Iraq over concerns that Kuwait's development of Mubarak al-Kabir will take the business Iraq was developing its new port on the al-Fao peninsula to cater for.

Although Iran has had some success in growing its transhipment business and its immediate neighbours may continue to trade with the nation regardless of sanctions, **BMI** does not believe that in the long run there will be sufficient trade to insure against potential loss of international business as western sanctions escalate.

MSC Lauren Arrives At Shahid Rajaei Port

The world's third largest container vessel, MSC Lauren, arrived at Iran's Port of Bandar Abbas on June 5 2011. The vessel's offloading/loading process at the port was expected to be completed in a maximum period of 40 hours. The ship is owned by Switzerland-based shipping line **Mediterranean Shipping Line** and has a cargo capacity of 12,967 20-foot equivalent units (TEUs). The port is one of the 30 ports across the world that offers docking facilities for bigger container ships.

Hapag-Lloyd To Levy Congestion Surcharge

German shipping company Hapag Lloyd will impose a port congestion surcharge on all containerised freight transported from Oceania and Asia to the Iranian Port of Bandar Abbas it announced in May. The

company intends to impose a surcharge of US$100 per TEU on all containerised freight with effect from June 1 2011. Hapag Lloyd stated that the emergency surcharge is required to compensate for the extra costs incurred due to the deteriorating state of operations at the port.

Market Overview

Iran Container Shipping Overview

Despite the threat posed by sanctions against shipping lines involved in Iran's container sector, **BMI** believes that Iran's consumer outlook and strong demand for containers, with the country's major box port of Bandar Abbas defying the global downturn in 2009 by continuing to post year-on-year (y-o-y) increases, will mean that lines will find it hard to resist this high-growth market.

Nevertheless, increased US sanctions which now not only target the country's shipping lines but also its ports, are starting to affect the country's imports. Iran's primary container facility at Bandar Abbas is now a no-go facility for market leader Maersk Line after port operator Tidewater was added to the US blacklist, and the port's throughput growth in 2011 is unlikely to top 2%, much less near the double-digit expansion enjoyed in recent years.

- Box throughput at Iran's main container port managed to continue growing during the downturn, highlighting the strength of box shipping demand.
- Large, young consumer base spurring container demand.
- Sanctions present obvious downside risk to lines operating in Iran's container shipping sector.
- Port development likely to become reliant on domestic firms as international companies are warned off.

IRISL - Target For Sanctions
Iran's exposure to the container shipping sector is dominated by the country's state-owned shipping line, **Islamic Republic of Iran Shipping Lines** (IRISL), which operates in the dry bulk, general cargo and container shipping sectors. The line's box operations mainly link Asia and Europe to the Arabian Gulf and the Indian subcontinent. The national carrier ensures that rates are kept competitive with other international lines serving Iran's trade needs.

The line's connection to the Iranian state is also, however, its curse and it is normally the first target of sanctions. A set of sanctions agreed in May 2010 called for vigilance against Iran's main international freight transport companies, IRISL and **Iran Air**, with a ban mooted that would make it illegal for countries to harbour vessels suspected of shipping banned goods into Iran. In practice, **BMI** expects that the call for vigilance means more stops and searches of IRISL vessels, a development that Iran has reacted strongly against. Iran's Majlis (parliamentary) speaker Ali Larijani has stated: 'I am warning the

US and certain adventurous countries that in case they plan to inspect the cargo of Iranian ships and planes, they should rest assured that we will do the same.'

BMI notes that IRISL vessels are not strangers to being stopped and searched. In 2009, US warships intercepted a ship chartered by IRISL that was bound for Syria, which was found to be carrying munitions. In another incident, Israeli commandos boarded a vessel off Cyprus and found illegal arms; IRISL was later named as the shipping agent.

The threat of stops and searches in our view damages the growth prospects of the Iranian container shipping sector. We believe that shippers will not want to use a company that has effectively been blacklisted by a number of states - the US placed direct sanctions against the carrier in 2008, banning all transactions between the company and US citizens, and freezing IRISL assets that are under its jurisdiction. The UK in 2009 ordered all UK financial service firms to cease business with Iran under the Counter-Terrorism Act 2008. Reports have also emerged that UK- and Bermuda-based insurance companies have stopped doing business with IRISL, with the company having to search elsewhere for insurance.

We believe that further sanctions would also target IRISL, as the line is suspected of offering transport and logistics services to aid Iran's plans to develop its nuclear capabilities. On October 27 2010 the US slapped sanctions on 37 'front companies' related to IRISL. According to the US statement the action 'targets IRISL's complex network of shipping and holding companies and executives and further exposes Iran's use of its national maritime carrier to advance its illicit weapons of mass destruction program and to carry military cargoes'.

The sanctions have also derailed IRISL's new-build strategy. The line has struggled to secure financing as banks around the world have become wary of violating any sanctions on dealing with the shipping company or its affiliates. This led to a number of its vessels being detained in Singapore at the end of 2010. The three ships, the *Tuchal*, *Sabalan*, and the *Shand* were all registered to different companies and were held over mortgage-default payments.

However, **BMI** notes that all three vessels were released in January 2011 on the order of Singapore's High Court, leading IRISL to claim to the Financial Times that it was in good health: 'We definitely face no risk in Asia', said Mohammad-Hossein Dajmar, the company's managing director, though he acknowledged that IRISL is in effect shut out of European ports.

Adam Szubin, head of the US Treasury's Office of Foreign Assets Control, which is responsible for implementing the sanctions, insisted that the sanctions were working, and stated that the ships were only released after the company repaid in full the US$200mn outstanding on the debt. 'Its successive loan

defaults and its threadbare insurance coverage have left it facing massive debts on the ships it is sailing, and unable to pay for ships it has ordered.'

International Lines Caught In The Crossfire

Iran's persona non grata status extends into the global shipping sector, with lines that offer services to Iran cautious of the extent of their involvement with the country. In early 2010, French container line **CMA CGM** went out of its way to put distance between itself and claims from Iranian newspaper the Tehran Times that the company's Simba vessel pulling into the Iranian port of Bushehr was the start of significant operational activity by CMA CGM in Bushehr. The French container line denied that it had struck a deal with the Iranians, and stated that the berthing of the Simba at Bushehr was 'exceptional', and that increased activity at the port was not planned.

A US-led protest group linked to the Obama administration, United Against Nuclear Iran (UANI), was in April putting pressure CMA CGM to halt its business operations with Iran.

CMA CGM is not the only firm to be targeted by the group; **Maersk Line** was in UANI's sights in autumn 2010. A statement released by UANI stated: 'While the international community is taking steps to isolate Iran for its pursuit of an illegal nuclear weapons programme [CMA CGM] conducts extensive business in Iran and is actively courting, indeed increasing its business activities in Iran.'

The statement went on to say: 'More disturbing is the danger that CMA CGM shipping vessels are being used, as they have in the past, to ship items into and from Iran in violation of sanctions passed by the United Nations, United States and the European Union.'

The controversy over dealing with Iran has led to CMA CGM establishing an 'Iran desk' to ensure that none of its vessels are used for the transportation of contraband materials covered by the sanctions in future.

The ramifications of involvement in Iran's shipping sector was further highlighted in August 2010 when Maersk Line paid fines of US$3.1mn for violating US sanctions against shipping to Iran and Sudan. The company's statement read: 'We recognise our obligation to follow US trade sanctions, and we regret the violations.'

The caution that lines will have to exercise to ensure they stay on the right side of sanctions could, we fear, lead some lines to question whether their exposure to the Iranian box shipping sector is really worth it. If lines start to pull out of the country then this will have a detrimental effect on Iran's container-shipping sector. The fear has been intensified by the fact that the country's container port development has not been able to tempt western investors and companies.

In August 2010, Japanese shipping line **NYK** made the decision to pull out of its dealings in Iran. In a customer notice the company stated that it had made the decision in consideration of 'the current political and business difficulties related to Iran'.

However, in July 2010 one company introduced a new call to Iran. Geneva's **Mediterranean Shipping Company** (MSC) revealed that it had added a feeder service to call at Bushehr, in south-west Iran. The feeder service will be transhipping from Dubai's port of Jebel Ali.

Global Port Developers Steer Clear

In January 2010, German supply chain logistics consultancy **Hamburg Port Consultancy**(HPC) signed a contract with the Bandar Abbas port operator, **Tidewater Company**. According to **BMI** research, HPC was likely to have worked on the second phase of the second container terminal at the Shahid Rajaie port (also known as Bandar Abbas) complex, which came online in 2010, and is to boost capacity at the facility to 3.5mn 20-foot equivalent units (TEUs) per annum. The Fars News Agency reports Tidewater Company's managing director, Abdolhamid Malahzadeh, as stating that HPC was set to replace Singaporean firm **Overseas Port Management** (OPM) as the port's manager, as OPM's contract was coming to an end. However within the space of a couple of weeks following Israeli diplomatic pressure on Germany, HPC pulled out of the contract.

BMI believes that as international firms pull out of developing Iran's freight transport network, the void will be filled by domestics companies. In July 2010, IRISL signed an agreement to control and invest in the Iranian Pars Port Complex. We believe that this strategy is likely to continue, meaning that Iran's container shipping sector will miss out on the benefits that international companies can bring in terms of modernising and streamlining the country's port sector.

Too Tempting For Some

While some companies are distancing themselves from involvement in Iran's box shipping sector, for others the potential this market has to offer is too strong to resist.

In May 2010 South Korea's **Hyundai Merchant Marine** (Hyundai MM) was enticed back into Iran's container shipping trade after a 10-year hiatus. According to Hyundai MM's shipping schedule, the port of Shahid Rajaee features as a port of call on the line's Far East-Middle East (FM1) service. The route is a loop that calls at major Chinese ports, the Middle Eastern ports of Jebel Ali in the UAE and the Saudi port of Dammam, and Bandar Abbas on the outward leg before pulling into the Asian container hub of Singapore on the return leg.

Iran's container shipping sector could also be further bolstered by the fact that some countries do not hold as strong a line on Iran as the US and EU. Iran and Brazil are currently investigating the possibility of operating a joint shipping line that would cater for growing trade between the two nations.

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The threat of further sanctions and the potential damage to a company's reputation should it get caught up in transporting goods under sanction without realising it is a major deterrent for carriers wishing to get involved in the Iranian box shipping sector. Having said that, the Iranian consumer story, and therefore demand for containerised goods, may be just too tempting for lines to miss out on.

Defying Downturn And Sanctions

Iran's demand for containerised shipments defied the global downturn in box trade, with container throughput at the port of Bandar Abbas increasing year-on-year (y-o-y) by 17.5% in 2010 to 2.59mn TEUs. When compared with the other major container ports in the Middle East, the port of Bandar Abbas ranks fifth out of nine, behind the UAE's Jebel Ali, Oman's port of Salalah, Saudi Arabia's port of Jeddah and Egypt's East Port Said. **BMI** notes that the majority of these ports (Jebel Ali, Salalah and East Port Said) are transhipment hubs. Bandar Abbas has not developed its transhipment potential, so throughput at the port is a good indication of the domestic demand for containerised goods in Iran.

Unsurprisingly, given that the country had an estimated population of 73.9mn in 2010, the largest in the Middle East, demand for containerised goods is strong. Iran's population is forecast to expand in the medium term (2011-2015), with **BMI** projecting a yearly average increase of 1.2% over the period. Population is projected to reach 78.6mn in 2015.

The country's demographics further support Iran's positive consumer outlook, with the country boasting a young population, the demographic group that typically has more disposable cash and inclination to spend. According to **BMI** estimates, in 2011 46% of Iran's population is younger than 25 years old.

Iran's consumers are, however, not as rich as others in the Middle East, with the country's GDP per capita estimated by **BMI** at just US$6,205 in 2011, well below the regional GDP per capita average of US$26,622.

Iranian private final consumption dominates the country's GDP, accounting for an estimated 56.6% of total GDP in 2010. This further supports our positive demand outlook, with **BMI** typically favouring private consumer orientated economies over trade-reliant states because of their typically greater resilience to further global demand weakness.

But Double-Digit Growth About To Come To An End

Although the Iranian consumer outlook continues to look rosy, the country's ports sector was dealt a blow in Q311 when ports operator Tidewater was added to the list of Iranian companies with which US entities are prohibited from doing business. The company is designated by the US as being involved with the proliferation of weapons. Furthermore, it is owned by the Iranian Revolutionary Guards, the military organisation suspected by the US government of taking greater control of the Iranian economy as the sanctions begin to restrict private enterprise. The move against Tidewater took place on the same day that

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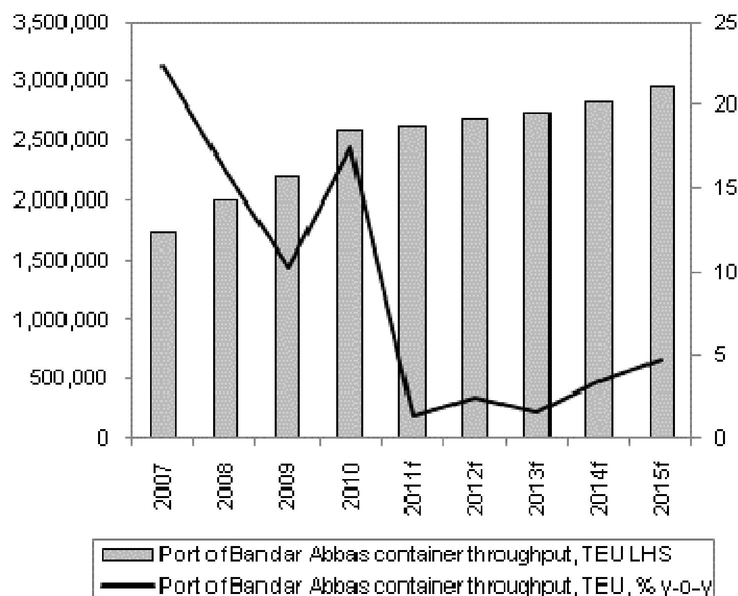
Industry Forecast

Bandar Abbas Container Throughput

BMI's throughput forecast for containers at the port of Bandar Abbas remains unchanged from last quarter, despite monthly throughput results which may have led to the contrary. The facility handled 1.2mn 20-foot equivalent units (TEUs) to the end of May, an increase of 4.8% on the 1.15mn TEUs handled in the corresponding period in 2010. The month of May saw 255,038 TEUs pass through the port, month-on-month growth of 14.5%.

Double Digit Growth To Come To An End

Bandar Abbas Throughput



Source: Tidewater, BMI. f = BMI forecasts.

However, while this is a reasonable rate of growth, at the end of June **Tidewater**, the company which operates the container terminal at Bandar Abbas, in addition to a number of other Iranian ports, was added to the US' sanctions list. Maersk Line is just one company to have come out and said it will no longer be serving the port.

In light of this we are sticking with our forecast of just 1.4% growth at the port in 2011. This is a drastic dip from the years of double-digit growth preceding this (growth in 2010 was 17.5%, impressive when the US sanctions are considered). If this growth rate is realised this year then the port will handle 2.63mn TEUs, from 2.59mn TEUs handled in 2010. From 2011 to 2015 we project the slower growth rate to be the new norm, averaging 2.7% per annum from 2011 to 2015. There is significant downside risk to this forecast from ongoing US sanctions.

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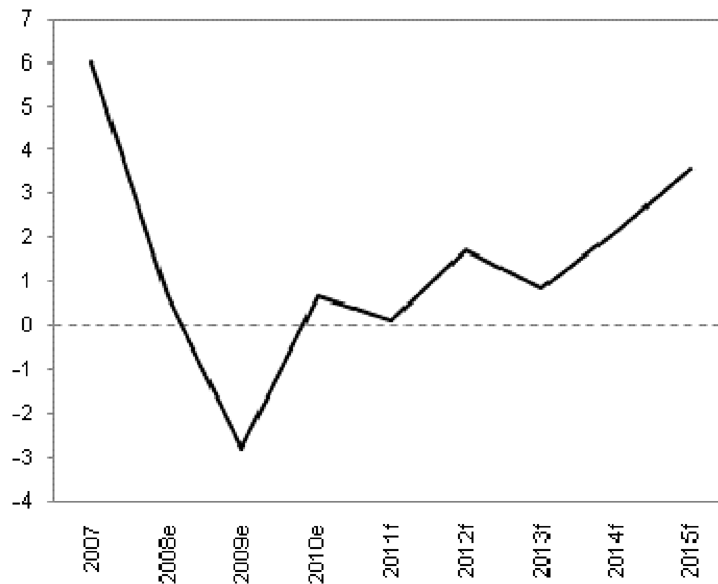
Trade

Our country risk team's forecasts are also unchanged from last quarter. We project that Iranian total trade real growth will be slow in 2011, reaching just 0.11%, based on imports real growth of 1.80% and negative growth in exports of -1.59%. According to **BMI** forecasts this growth will rise slightly to 1.73% in 2012, and we expect total trade real growth to average 1.69% from 2011 to 2015. In nominal terms, we forecast that 2011 growth will be 9.68% for total trade, taking Iranian trade in 2011 to US$185.2bn. This will comprise imports of US$82.2bn and exports valuing US$103bn.



Source: National statistical authority, BMI. e/f = BMI estimates/forecasts

In 2009 Iran's primary trade partner in terms of imports was the UAE, at US$8.97bn, followed by China at US$8.72bn, Germany, South Korea and Italy. Number-one export partner was China (US$12.02bn), due to oil exports to the Asian dragon, followed by India (US$9.61bn), Japan, South Korea and Turkey, for the same reasons as China.

Table: Major Port Data, 2008-2015

	2008	2009	2010	2011f	2012f	2013f	2014f	2015f
Port of Bandar Abbas container throughput, TEU	2,000,230	2,206,476	2,592,522	2,628,747	2,692,673	2,735,104	2,827,513	2,963,131
Port of Bandar Abbas container throughput, TEU, % y-o-y	16.12	10.31	17.50	1.40	2.43	1.58	3.38	4.80

Source: Tidewater, BMI. e/f = BMI estimates/forecasts. Forecasts assume existence of spare capacity and the correspondence of national trade trends at local port level.

Table: Trade Overview, 2008-2015

	2008e	2009e	2010e	2011f	2012f	2013f	2014f	2015f
Imports, real growth, % y-o-y	4.00	-2.00	2.00	1.80	3.00	3.00	5.00	5.00
Exports, real growth, % y-o-y	-2.69	-3.55	-0.65	-1.59	0.47	-1.25	-0.71	2.15
Total Trade, real growth, % y-o-y	0.65	-2.77	0.68	0.11	1.73	0.88	2.15	3.58
Imports, US$bn	74.09	70.41	75.40	82.20	89.72	97.25	104.93	113.01
Import growth, % y-o-y	12.63	-4.96	7.08	9.02	9.15	8.39	7.90	7.70
Exports, US$bn	96.32	79.60	93.46	103.00	111.42	120.25	128.85	138.33
Export growth, % y-o-y	-5.91	-17.36	17.41	10.21	8.17	7.93	7.15	7.35
Total trade, US$bn	170.41	150.01	168.85	185.20	201.14	217.50	233.78	251.34
Total trade growth, % y-o-y	1.34	-11.97	12.56	9.68	8.61	8.14	7.48	7.51

Source: National statistical authority, BMI. e/f = BMI estimates/forecasts

Table: Key Trade Indicators, 2008-2015

	2008	2009e	2010e	2011f	2012f	2013f	2014f	2015f
Agricultural raw materials, imports, US$mn	1,129,360.3	1,018,359.5	1,064,155.7	1,112,241.6	1,172,830.0	1,237,053.6	1,305,130.6	1,377,292.3
Agricultural raw materials, imports, % y-o-y	-6.06	-9.83	4.50	4.52	5.45	5.48	5.50	5.53
Agricultural raw materials, exports, US$mn	329,121.5	259,709.7	263,588.9	274,593.5	282,230.8	292,383.7	309,210.8	324,231.5
Agricultural raw materials, exports, % y-o-y	20.00	-21.09	1.49	4.17	2.78	3.60	5.76	4.86
Ores and metals, exports, US$mn	2,258,859	1,655,984	1,694,165	1,802,476	1,877,645	1,977,574	2,143,192	2,291,031
Ores and metals, exports, % y-o-y	30.31	-26.69	2.31	6.39	4.17	5.32	8.37	6.90
Ores and metals, imports, US$mn	1,443,113.8	1,286,651.6	1,350,816.5	1,418,549.0	1,502,475.9	1,590,859.6	1,685,423.4	1,786,263.8
Ores and metals, imports, % y-o-y	-13.22	-10.84	4.99	5.01	5.92	5.88	5.94	5.98
Iron and steel, exports, US$mn	1,518,277	1,330,281	1,361,228	1,435,775	1,495,201	1,572,736	1,690,028	1,795,022

Table: Key Trade Indicators, 2008-2015

	2008	2009e	2010e	2011f	2012f	2013f	2014f	2015f
Iron and steel, exports, % y-o-y	-8.43	-12.38	2.33	5.48	4.14	5.19	7.46	6.21
Iron and steel, imports, US$mn	6,001,090	5,258,024	5,380,344	5,674,994	5,909,880	6,216,342	6,679,944	7,094,939
Iron and steel, imports, % y-o-y	-13.43	-12.38	2.33	5.48	4.14	5.19	7.46	6.21
Manufactured goods, exports, US$mn	9,423,852	7,400,358	7,533,942	7,912,891	8,175,886	8,525,508	9,104,959	9,622,206
Manufactured goods, exports, % y-o-y	21.40	-21.47	1.81	5.03	3.32	4.28	6.80	5.68
Manufactured goods, imports, US$mn	39,184,214	38,774,998	40,553,027	42,419,959	44,772,292	47,265,765	49,908,847	52,710,513
Manufactured goods, imports, % y-o-y	18.14	-1.04	4.59	4.60	5.55	5.57	5.59	5.61
Fuels, exports, US$mn	72,494,613	54,991,511	55,694,476	57,688,634	59,072,603	60,912,429	63,961,696	66,683,620
Fuels, exports, % y-o-y	31.90	-24.14	1.28	3.58	2.40	3.11	5.01	4.26
Fuels, imports, US$mn	7,175,788	5,500,599	5,834,884	6,185,885	6,628,145	7,096,940	7,593,864	8,120,603
Fuels, imports, % y-o-y	42.89	-23.35	6.08	6.02	7.15	7.07	7.00	6.94

Source: UNCTAD, BMI. e/f = BMI estimates/forecasts

Table: Main Import Partners, 2002-2009

	2002	2003	2004	2005	2006	2007	2008	2009
Imports From United Arab Emirates (US$mn)	1,847.88	3,135.08	5,476.41	7,285.42	8,979.83	10,080.80	13,198.50	8,973.10
Imports From China,P.R.: Mainland (US$mn)	959.88	1,468.52	1,623.36	2,410.76	2,585.29	3,883.30	8,851.67	8,715.91
Imports From Germany (US$mn)	3,480.09	2,836.78	4,114.25	5,118.93	5,215.37	5,180.95	6,301.91	5,724.30
Imports From Korea (US$mn)	972.97	1,199.20	1,774.48	2,134.56	1,912.63	2,341.79	4,776.81	4,391.09
Imports From Italy (US$mn)	1,187.46	1,621.90	2,358.63	2,353.99	1,930.97	1,727.31	3,506.02	3,110.43

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Source: IMF Direction of Trade Statistics

Table: Main Export Partners, 2002-2009

	2002	2003	2004	2005	2006	2007	2008	2009
Exports To China,P.R.: Mainland (US$mn)	2,133.47	3,014.31	3,960.60	6,178.10	9,041.88	12,118.10	17,801.20	12,020.60
Exports To India (US$mn)	240.62	240.63	332.65	572.18	5,360.43	9,175.87	12,730.30	9,612.73
Exports To Japan (US$mn)	4,311.01	6,764.36	7,515.33	9,361.64	9,886.57	11,598.60	16,587.20	8,461.27
Exports To Korea (US$mn)	1,214.01	1,677.00	2,213.93	3,213.51	4,590.14	5,892.57	7,475.51	5,223.41
Exports To Turkey (US$mn)	837.25	1,691.53	1,782.76	3,154.28	5,114.82	6,012.54	7,454.26	3,096.35

Source: IMF Direction of Trade Statistics

Company Profile

NITC

Strengths	▪ NITC is the eighth-largest oil tanker company in the world. ▪ It has a diversified fleet with different classes of vessel, including a large number of VLCCs.
Weaknesses	▪ NITC's association with Iran causes problems for the company. ▪ The tanker operator struggled to renew its insurance in 2011 as a result of sanctions.
Opportunities	▪ Iran could become a major exporter of LNG if it manages to develop the expertise in the face of sanctions. ▪ NITC has a major fleet expansion programme in motion.
Threats	▪ Middle Eastern political instability is a major concern. ▪ Western sanctions against Iran could make operating still more difficult for the tanker operator. ▪ Rising bunker costs have impinged on shipping companies' profits. ▪ The liquid-bulk shipping sector is already struggling with overcapacity, and NITC's new VLCCs will exacerbate this.

Company Overview

NITC was formerly known as the **National Iranian Tanker Company**, prior to its rebranding in 2010 in an effort to distance itself from the Iranian pariah state and the western sanctions currently imposed upon it. It is a major tanker operator primarily involved in the shipping of crude oil, and operates on the international stage.

Strategy

Fleet

According to Tanker Operator's top-30 tanker companies list, NITC's fleet makes it the eighth-largest in the world in terms of deadweight tonnage (DWT). The company owns and operates 43 tankers in total, made up of 28 VLCCs, nine Suezmaxes, five Aframaxes and one Handysize. **BMI** notes that the company has the most ambitious expansion plans in the sector, with a programme that should take it into third-place in the world in terms of DWT. This includes the acquisition of 22 additional VLCCs, six Caspimax shuttle tankers for use on the Caspian Sea, one LPG carrier and two product carriers. The new additions to the fleet will make the average age of NITC vessels less than five years, making it one of the world's youngest fleets, according to the company website.

Some 90% of NITC's fleet is chartered out to international companies

The company also has long-term plans to become involved in LNG shipping. Iran has proven gas reserves and once the country has the technology to enter the sector, NITC has stated that it will develop a fleet to transport it. The company has previously stated that 80-plus vessels would be needed to cope with demand.

Chinese Loan To Help Iranian Fuel Exports

BMI believes that a Chinese loan to Iran to develop the country's oil tanker fleet will help cement the energy trade relationship between the two nations as Iran's oil exports are driving ahead. This could prove to be particularly important to the Islamic Republic as Iran's ability to export liquefied natural gas (LNG) anytime soon is now in doubt given recent wariness of international companies to invest in the sanctions-stricken country.

NITC has secured a loan from Chinese state banks for 12 of its planned VLCCs to be built in Chinese shipyards. NITC will pay a 10% deposit for the ships, and the rest of the money will be lent mostly by **China Eximbank**. The VLCCs, to be delivered from 2011 to 2013, will be built by **Shanghai Waigaoqiao Shipbuilding** and **Dalian Shipbuilding Industry Corporation**, and will cost US$103mn each. The loan will total US$1.2bn. The ships were originally to be built in Korean shipyards, but Korean banks could provide only 50% of the capital.

BMI notes that as China is the number-one importer of Iranian oil, this loan is mutually beneficial to Iran and the Asian dragon. Iran has huge oil reserves, and with tougher and tougher sanctions being imposed by the West it needs oil exports to China to continue to grow apace. **BMI** forecasts Iranian fuel exports to grow by an average of 8.8% year-on-year from 2010 to 2014. China has been a net importer of oil since 1993 and is reliant on the fuel for its energy needs, so securing markets through deals such as this is important for its continued supply.

Although oil exports look set to continue despite Western sanctions, one sector that looks set to be hit is LNG exports. There were claims in June that six LNG carriers were on order from Chinese shipyards, which would have been the first in the fleet, but NITC later scotched these rumours.

Iran had been hoping to export its first LNG in 2013, leaving the country less reliant on gas pipelines through neighbouring Iraq and Turkey. **BMI** forecasts that as much as 10bcm of Iranian LNG could be exported by 2013, with this set to increase over our forecast period to 2020 to reach 55bcm. However, the managing director of state-run **National Iranian Oil Company** (NIOC), Ahmed Galabani, has said that Iran's oil ministry will shift its focus back to gas exports via pipeline, giving significant downside potential to our forecasts. The Iraqi government in Baghdad announced in August 2010 that it had agreed terms with Iran over a pipeline that would deliver Iranian gas to Syria through Iraqi territory. As part of this shift, NIOC has chosen to abandon the Persian LNG project.

The Persian LNG project sought to liquefy gas from phases 13 and 14 of the South Pars field, located in the Persian Gulf. The project is to produce 14-16mn tonnes per annum (tpa) of LNG upon completion in 2014. **Royal Dutch Shell** and **Repsol YPF** were in negotiations with NIOC for the US$5bn upstream component of Persian LNG. But their hesitation to commit to Iranian investment - in light of tightening international sanctions against Iran - led to NIOC suspending negotiations. Contracts were subsequently awarded to local players in June 2010. According to Iranian media reports, contracts were awarded to firms including **National Iranian Drilling Company** and **Iranian Offshore Engineering Company**.

The UN and US passed sanctions against Iran in June 2010 based on its non-compliance with the International Atomic Energy Agency over its nuclear programme. In combination

with subsequent EU sanctions, substantial investments from Western companies in Iran's oil and gas sector carry significant penalties, as do related financial transactions. As a result, Western oil and gas companies have been withdrawing from Iranian investments. Deprived of the know-how of industry majors, Iran's LNG plans face an uncertain future. There has been Chinese investment, and **BMI** has reported how in March 2009 three unnamed Chinese companies signed a US$3.3bn deal to help develop LNG from the South Pars gas field. Galabani's words, however, seem to indicate that Western investment will be sorely missed, and although oil exports look set to grow, LNG shipments may still be some way off.

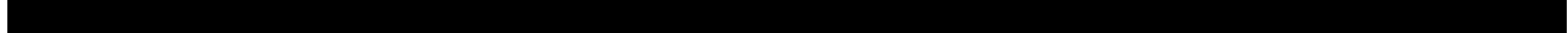
NITC Distances Itself From Iran

Despite not being a state entity, **BMI** notes that NITC, formerly known as National Iranian Tanker Company, has still been negatively affected by its association with Iran. NITC has undertaken rebranding to distance itself from a country whose shipping operations are now under the microscope of the international community.

Although the company is not state-run like the **Islamic Republic of Iran Shipping Lines** (IRISL) as it was privatised in 2000 and taken over by three pension funds, meaning that it is not a direct target of the sanctions, the 'I' in NITC does nothing to stem industry rumours. NITC had to issue a denial regarding a story in July 2010 that a vessel supposedly chartered by NITC, the product tanker *Lia*, was stopped from sailing from Turkey to Iran by the ship's owner.

NITC is trying to distance itself from its association with Iran. The company launched an English-language website in 2010 and has rebranded with a new logo placing an emphasis on its name NITC. The firm's chairman and managing director, Mohammad Souri, has stated 'we are officially introducing our new corporate logo. This is intended to reinforce the group's brand - NITC - in its own right, and not as the abbreviation of an earlier name.'

BMI believes the company's rebranding and new English-language website will go a long way to lessen the company's association with Iran. We believe that shipping lines will wish to decrease their links with the country as the political situation concerning sanctions continues to be a flashpoint in Iran. The country's President Mahmoud Ahmadinejad recently warned 'you should know whoever takes a decision against the Iranian nation, such as the so-called inspection of the Iranian ships or so and so towards its aircraft, will immediately receive Iran's reaction'.



Financials

2010

not available

Latest Activity

NITC To Boost Market Position: NITC announced in May it will boost its market position in order to evolve into the second largest oil tanker operator by 2013. Further, NITC Managing Director Mohammad Souri revealed that the company possesses 50 very large crude carriers (VLCCs) with cargo capacities ranging between 300 and 320 tons, and accounts for 10% of the total VLCCs in the world. Additionally, NITC area manager had earlier said the company is likely to increase its fleet by 72% by 2013, and boost its position to become one of the three leading tanker operators across the world.

Islamic Republic Of Iran Shipping Lines (IRISL)

Strengths

- Throughput at Iranian ports continued to grow through the downturn.
- IRISL is state-owned.

Weaknesses

- IRISL has had severe operational difficulties as a result of sanctions against it.
- The company has had a number of its ships impounded over payment issues.
- Iran's political isolation limits the company's ability to attract new investment funds and acquire the latest technology.

Opportunities

- Strong Iranian demand story offers IRISL growth opportunities catering for the domestic market.

Threats

- Container lines have been unable to push rate rises through so far in 2011. Maersk Sanctions against Iran and IRISL may be strengthened, making it impossible for the company to operate at a profit.
- Middle East unrest continues to spread. Should Iran undergo widespread political turmoil it could impact on IRISL's business.
- Given political and trade restrictions IRISL may lose market share to other Gulf and Middle Eastern shipping lines.
- A number of IRISL's subsidiaries and affiliated companies have now been added to the US's blacklist.

Company Overview

Islamic Republic of Iran Shipping Lines (IRISL) was founded out of **Aria Shipping** in 1979 following the Islamic Revolution. Many of the company's vessels were lost during the Iran-Iraq war, and subsequently IRISL's vessels have been named for the names of the war's 'martyrs and cities', according to the liner's website. It is involved in container and dry-bulk shipping and has some 7,000 employees.

Group subsidiaries include the 51:49 **Irano Hind Shipping Company** JV with **Shipping Corporation of India** , which owns eight ocean-going vessels that transport crude oil, bulk and general cargoes. **Khazar Shipping Lines** provides marine transportation services in Caspian Sea area calling at Bandar Anzali, Nowshahr and Amirabad to the ports of Aqtau, Astrakhan, Makhachkala, Turkmenbashi and Baku. **Valfajre-8 Shipping Company** transports cargo and passengers between countries in the Gulf and Oman Sea. The group has over 110 representative offices.

Strategy

Fleets

IRISL is involved in container and dry-bulk shipping, though the company has been transferring its shipping operations to associated companies of late in a bid to evade western sanctions. According to the company's website, its dry-bulk arm has a fleet of varying sizes, from Panamax to Handysize. It is involved in the shipping of both clean and dirty products such as grain and rice and coal and iron ore.

In late 2009/early 2010 IRISL transferred its container-shipping operations to hitherto

unknown company **Hafiz Darya Shipping Lines** (HDS Lines). The company is said to be privately-owned and separate from IRISL, though little information is available regarding its management structure. According to AXS Alphaliner, HDS Lines currently operates the 22nd-largest container-shipping fleet in the world, with a total of 24 vessels making up a total of 88,744 20-foot equivalent units (TEUs). This gives the company 0.6% of market share, unchanged from last quarter.

HDS Lines owns only four ships, with a capacity of just 4,712TEUs. It charters in 20 vessels, however, with a total capacity of 84,032TEUs, making its chartered vessels account for 94.7% of the fleet. Despite this disparity there are no vessels currently on HDS Lines' orderbook, perhaps reflecting the poor position Iranian shipping companies are in when it comes to finding funding.

Iranian Ports Forced To Look For Investment At Home

Although IRISL has been active in trying to separate its shipping activities from the brand of IRISL, it is still acting as an investment vehicle in the shipping sector. The company signed in 2010 an agreement to control and invest in the Iranian Pars Port Complex. **BMI** believes Iranian ports now have no choice but to look for investment from domestic sources, but with sanctions against Iran set to continue it may be some time before investors see any returns.

Under the terms of the transfer, IRISL will take over the operation of seven docks, and is to invest IRR400bn (some US$40mn) in the port's infrastructure and establishments. The Pars Port Complex is situated in the Pars Special Energy/Economic Zone (PSEEZ), in Bushehr Province in Iran's south-west. The complex sits on 100km^2 of land and incorporates a number of petrochemical complexes and refineries. The contract between IRISL and PSEEZ will run for 15 years initially, and can be extended thereafter in five-year periods.

BMI believes that this contract has obvious benefits for the Iranian shipping company, giving it the chance to move up the supply chain and diversify into port management. The shipping line has been singled out as a target for sanctions, and no doubt is hoping the port will offer it an opportunity to diversify its revenue stream.

IRISL has had sanctions imposed directly against it by the US, which believes that the company provided logistical services to Iran's Ministry of Defence and Armed Forces Logistics (MODFL). Under the sanctions, the Iranian national carrier is banned from making transactions with US citizens, and all IRISL assets under US jurisdiction have been frozen.

BMI believes that the PSEEZ had no option but to sign the agreement with IRISL. Given the sanctions, and diplomatic pressure put on any companies still prepared to invest in Iran, there was little option but to look for investment at home. In January 2010, pressure from the Israeli government convinced German supply chain logistics consultancy **Hamburg Port Consultancy** (HPC) to pull out of a contract signed in January 2010 to renovate the Iranian Port of Bandar Abbas.

Financials — **2010**

not available

Latest Activity — *IRISL To File Lawsuit Against EU*

IRISL decided in June to file a lawsuit at the international courts against the EU over illegal sanctions imposed by the bloc against it, according to the company's legal advisor Maryam Taher. The company will claim compensation as it is barred by the EU from carrying out shipping operations at the European ports. The EU imposed sanctions against more than 30 holding companies of IRISL in May 2011 with an aim to put pressure on Tehran to stop its nuclear programme. The US and its Western allies alleged that Iran is developing nuclear weapons under the cover of a civilian nuclear programme, but Iran rejected such allegations.

New York Legislators Fire Warning Shots In IRISL Sanctions Battle

The risk of doing business with any company with possible links to IRISL was further highlighted in June week by a 317-count indictment filed in New York against the company and 10 alleged alias corporations. The contagion is such that French shipping line CMA CGM, accused by a number of US politicians of being lax in their checks up to now, has set up a special 'Iran desk' to ensure no further contraband cargos are carried on their vessels.

The US is seeking to curtail all activities by IRISL, which it accuses of being complicit in an alleged nuclear weapons programme in Iran as the main transporter of its procured goods. In addition to charges against IRISL and the 10 other companies, five people have been charged with misleading international banks. These include some of the world's biggest names in the banking sector, such as Citibank, HSBC and Deutsche Bank.

According to a statement filed by the New York district attorney the individuals and companies used the banks to move as much as US$60mn in transactions between them. The deception was necessary as IRISL needs access to US dollars in order to operate effectively in international shipping, but US sanctions have closed its access to the currency. The banks have not been accused and are helping the authorities with their investigations. It is hoped that the investigation will encourage other banks that may be turning a blind eye to similar activities to halt them. Adam Kauffman, executive assistant district attorney, said that ignoring links to IRISL links 'is criminal conduct and could expose banks to criminal liability'.

US Advised Israel Over IRISL Strategy

In June it was revealed that the US government had requested Israel in 2008 to caution its private companies from carrying out business transactions with IRISL, according to a diplomatic cable released by WikiLeaks on the weekend of June 4-5 2011. The US government had also informed Israel about the actions it took against several countries in order to compel them to enforce sanctions on shipping companies carrying out business deals with Iran. The diplomatic cable was sent to the US Embassy in Greece in September 2008.

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Maersk Line

Strengths	▪ As the world's largest container shipping line, Maersk Line has a greater share of global seaborne container volumes than any other carrier. ▪ Its large, expanding fleet offers it the ability to capture trade volumes. ▪ Maersk Line is part of A.P. Møller-Maersk, a diversified company with activities in the oil and gas and terminal-operating sectors that synergise with its shipping operations. ▪ Flexibility as a result of fleet size and type. ▪ The company was one of the few carriers to post profit in Q111.
Weaknesses	▪ The dominance of the Asia-Europe trade route (accounting for 38% of volumes carried) in Maersk Line's service portfolio leaves the company heavily exposed to a downturn on this route. ▪ With such a large fleet, Maersk is constantly running the risk of overcapacity, which could prove a drain on resources if business slows. ▪ Its presence in the oil and gas and terminal operating sectors means that Maersk risks an over-reliance on the sector as an integrated whole. This could be dangerous if one sector's activities fail to hedge the other - for example, if oil prices are at odds with bunker prices.
Opportunities	▪ The company is increasing its exposure to intra-Asia, which is widely considered to offer huge growth potential for the container shipping sector. ▪ The company looks set to remain number one, and has cemented its position as a global leader with an order for 10 18,000TEU vessels. ▪ The line's emerging markets routes focus is wise, not only as a diversification strategy from over exposure to the 'big money' routes, but also as a way to get into high growth potential markets early.
Threats	▪ Container lines have been unable to push rate rises through so far in 2011. Maersk Line is due to try again on August 1 2011, but its failure to do so causes BMI to fear for its bottom line. ▪ Maerk Line's offices along with some of its peers we raided by EC officials in May 2011 investigating antitrust claims. If a shipping company is discovered to have acted inappropriately it will be in line for a hefty fine. ▪ The company trades in kroner, which means that it is vulnerable to changes in the US dollar. ▪ Although the group operates in the oil and gas sector, disparities in the price of oil and bunker costs threaten profits.

Company Overview	**Maersk Line** is the main container shipping unit of the highly diversified shipping and energy conglomerate **A.P. Møller-Maersk Group**. The other box shipping subsidiaries of the group are **MCC**, which operates the group's Intra-Asia route network, and **Safmarine**, which

transports boxes to and from Africa and the Middle East.

The company is based in Denmark but boasts a global presence with 325 offices in 125 countries. The shipping line has 16,900 employees and 7,600 seafarers.

Maersk Line is the largest container shipping company in the world, boasting a fleet with a capacity of 2.18mn 20-foot equivalent units (TEUs) and one of the largest box shipping networks. The company is heavily exposed to Asia-Europe, but is increasing its role in intra-Asia trade, where it already possesses expertise in the form of MCC.

Strategy

Maersk Line continues to dominate the global container shipping sector, holding a 15.5% market share, according to AXS Alphaliner, still some way above its nearest rival, **Mediterranean Shipping Company** (MSC), which boasts a market share of 12.8%.

Routes

Maersk Line's tactics have seen it develop a considerable exposure to the big-money routes with the line operating 10 transpacific services and 10 Asia-Europe services. The line is also heavily committed to Intra-Asia, offering 15 routes. Maersk Line's presence in Asia is mainly through its Intra-Asia subsidiary MCC, which operates the group's intra-Asia services.

In terms of volumes handled on Maersk Line's services, Asia-Europe dominates. In 2010 the route accounted for 38% of the total, a slight slip of 2% on the previous year's 40%. Africa is the company's second-largest route, accounting for 15% of the total; Safmarine operates in this area with a focus on the transportation of containers to and from Africa and the Middle East. Transpacific and Latin America both account for 13%, while intra-Asia currently makes up a small percentage of the volumes carried by Maersk Line, at just 6% (in 2010). **BMI** expects intra-Asia's role in Maersk Line's service portfolio to increase over the mid term with the company, along with its peers, placing huge emphasis on the growing demand between Asian states. We note that in the space of a year the distribution of volumes across Maersk Line's route portfolio has seen intra-Asia increase by 1%.

While holding its dominate position on the 'big money' trade routes Maersk Line is also increasing its exposure to emerging trade routes (ETRs). These include intra-Asia, intra-Europe and West Africa. **BMI** considers this as a wise strategy, as competition continues to expand on the Asia-Europe and transpacific pushing rates down.

ETRs offer a diversification away from the big money routes and as well as less competition offer high growth potential. There are, of course, obstacles on these ERTs as they link up emerging markets. However, Maersk Line's tactic of hiving off a specific unit, in the case of intra-Asia MCC, is, in **BMI**'s view, a sound strategy. **BMI** also highlights the lack of infrastructure at many of the port on ERTs and notes Maersk Line's way of getting round this problem by developing vessels with cranes on board to negate this risk to their operations.

Fleet

Maersk Line boasts the largest fleet in terms of capacity in the world with 2.18mn 20-foot equivalent units (TEUs), comprising 586 ships. The fleet's dynamics are fairly evenly split between owned and chartered with a split of 50.6% and 49.4% respectively. Despite Maersk Line operating a smaller capacity in terms of chartered vessels it does operate more

chartered vessels in terms of ship numbers, 382 vessels compared with the company's owned fleet of 204 vessels. Maersk Line appears to be employing a strategy of chartering smaller vessels, while owning and operating larger ones. This could be because of the prestige of owning a large fleet, but **BMI** believes it is also partly because there is a larger supply globally of smaller vessels, which Maersk Line can charter in as needed.

Maersk Line's largest percentage of vessels in terms of size is 4,000-5,000TEU ships. Maersk Line operates 46 vessels accounting for 25% of the company's total container fleet. Via this strategy **BMI** notes that the company has flexibility to move ships between routes, with vessels in this size bracket able to be used for both direct services and feeder lines. The company has also invested heavily in larger vessels, with 29.77% of the company's fleet 8,000TEU or over. The company boasts eight of the largest vessels afloat, the 15,000TEU 'E' class.

Maersk Line is implementing a strategy that should in the mid term ensure it remains the market leader in terms of capacity. The company originally ordered 10 18,000TEU vessels. The line has now increased that by another ten. The first 10 vessels will be delivered in 2013 and 2014; the second 10 vessels are scheduled for delivery in 2014 and 2015. The deadline for exercising the last option for an additional 10 vessels is the end of December 2011. At this point Maersk Line does not intend to exercise the option. However, it reserves the right to hold off on any final decision until the deadline. **BMI** notes that while volumes on the Asia-Europe route have picked up after the downturn, ordering vessels that can only operate on one route heightens risk.

Financials

2011

Q111

Maersk Line appears to have defied the decline in shipping rates, posting a year-on-year (y-o-y) revenue increase of 10.8% in Q111. The company's profit has also increased as rates and volumes on the company's container services ticked higher. **BMI** highlights, however, the y-o-y weakening of growth in both volume and rate terms, which could be a cause for concern, illustrating that the decline in rates has not left Maersk Line completely unscathed. We also note a reversal in the major driver of revenue for the company: volume growth has outpaced rate growth in Q111. In our view this will prove a more reliable growth model for the company, with revenue growth depending on a trade recovery rather than successful rate increases, which with the current overcapacity in the market have proved difficult to implement.

The carrier's revenue reached US$6.4bn in the first quarter of 2011, up from the US$5.79bn the line posted in Q110. On the back of this Maersk Line has been able to record a profit of US$438mn, a massive rise on the US$169mn posted in Q110.

Maersk Line's positive results are attributable to both the increase in the volumes of containers carried by the company and the increase y-o-y in rates charged for the shipment of these boxes. In terms of volumes the company handled 1.84mn 40-foot equivalent units (FEUs) in Q111, a y-o-y increase of 4.5% from the 1.76mn FEUs carried in the same period the year before. Rates have also increased, with the average rate for FEUs shipped rising by

1.57% to US$2,908 per FEU from US$2,863 a year ago.

BMI notes that perhaps the biggest surprise has been Maersk Line's ability to increase its rates despite depressed rate levels on the 'big money' markets of Asia-Europe and the transpacific, both of which the carrier is heavily exposed to. **BMI** believes that Maersk Line's ability to weather the recent decline in rates on this route is largely attributable to the carrier's strategy of diversification, which in recent years has seen the company expand into emerging trade routes (ETRs), which are less oversubscribed. **BMI** highlights Maersk Line's rapid expansion and exposure to the intra-Asia trade route via its subsidiary MCC Transport and we note that the company's increased exposure to ETRs is set to continue, with the carrier launching vessels (Wafmax and Sammax) specially designed to cater for the West African and South American markets.

2010

Maersk Line's revenue increased by 30.65% year-on-year (y-o-y) to US$26bn in 2010 compared with US$19.9bn in 2009. The increase enabled Maersk Line to return to the black with a full-year profit of US$2.6bn, following a loss of US$2.1bn, which the shipping line posted in 2009.

The recovery in revenue was driven by the global uptick in both volumes and demand in the container shipping sector. In terms of total volumes carried, Maersk Line's box levels shipped increased by 5%. The major driver of Maersk Line's recovery, however, was the company's ability to increase rates. Y-o-y rates grew by 29%; Asia-Europe saw the greatest rate rise of 52% y-o-y, followed by the transpacific, where rates increased by 33%.

The trend **BMI** notes from Maersk Line's results is that in all but one case rates increased considerably more than volumes. The exception to the rule was intra-Asia, where volumes on the route grew by 37% while rates rose by 19%. This growth in volumes further cements BMI's view that intra-Asia trade routes hold massive growth potential for the box shipping sector.

2010's results suggest that the line may face threats to its bottom line in 2011. The company achieved its recovery in 2010 mainly through rate rises, but like its peers the line has struggled so far in 2011 to implement planned increases. With growth in volumes shipped y-o-y set to remain steady, Maersk Line's bottom line could also remain static.

We note that it was not simply the uptick in volumes and rates that enabled Maersk Line to improve its financial position y-o-y. The firm has continued its strategy of slow-steaming, ensuring a saving on bunker fuel. **BMI** expects this strategy to continue as demand in the market for express services has not yet materialised.

Latest Activity

Expanding Further

Maersk Line is maintaining its strategy of ensuring it remains the market leader in terms of capacity, having exercised its option with Korea's Daewoo Shipbuilding & Marine Engineering for an additional 10 Triple-E ships, the world's largest container vessels. The agreement follows Maersk Line's order in February this year for 10 Triple-E vessels with two options for an additional 20 ships.

'I am very excited to have signed a contract with Daewoo for 10 more Triple-E ships. We now have 20 Triple-E on order. They underline our strong commitment to the Asia-Europe trade and fit well with our current ambitions and expectations for the future development of the trade,' said Eivind Kolding, CEO of Maersk Line. Maersk Line expects demand on the Asia to Europe route to increase 5-8% a year during 2011-2015. As such, it is introducing the Triple-E vessels from 2013 with the intention of being able to meet the increasing demand as well as maintain its market share. The first 10 vessels will be delivered in 2013 and 2014; the second 10 vessels are scheduled for delivery in 2014 and 2015. The deadline for exercising the last option for an additional 10 vessels is the end of December 2011. At this point Maersk Line does not intend to exercise the option. However, it reserves the right to hold off on any final decision until the deadline.

ETR Focus

After Intra-Asia Comes Intra-Europe

Maersk Line continues to increase its focus on emerging trade routes (ETRs) launching an intra-Europe strategy in May 2011. The tactic has echoes of the carrier's successful intra-Asia tactic, which it launched in 2009 via its MCC Transport subsidiary. **BMI** believes that Seago Line, a feeder shipping line subsidiary of Maersk, will play a vital part in the company's 18,000TEU vessel strategy; as ships get bigger we believe fewer ports of call will be used, leading to an increased need for intra-European feeder services.

Seago Line will 'focus on the short hauls in intra-Europe trade', according to a Maersk statement. Maersk Line and Safmarine are due to transfer their current intra-Europe operations and European feeder services to Seago Line in June 2011. Seago Line will therefore likely operate Maersk Line's current feeder services from Northern Europe to Baltic and Scandinavian ports, its feeder lines from the western Mediterranean and Portugal to Algeciras, and from Giora Tauro to the Eastern Mediterranean and the Black Sea. Maersk Line's strategy appears to be aimed at increasing the line's market share on the intra-Europe trade lanes. The carrier has outlined a goal to increase its current market share of 6% to 15%. According to AXS Alphaliner Maersk Line is currently ranked second on this route after Swiss-based Mediterranean Shipping Company (MSC).

West Africa Focus Intensifies

Another ETR which is of great interest to Maersk is trade links with West Africa. In March Maersk Line further cemented its role in container shipment in West Africa with a fleet of specifically designed box vessels that will cater for ports in the region. The strategy highlights Maersk Line's plan to not only be a big player on the major routes but also to get in early and make its mark in niche developing markets.

Maersk Line's fleet of 22 4,500 20-foot equivalent unit (TEU) vessels, which have been dubbed 'Wafmax' ships, are due online via a staggered strategy across this year and into 2012. The first Wafmax vessel, the Maersk Conakry, named after the capital of Guinea, has already had its naming ceremony.

The vessels are being constructed by South Korea's Hyundai Heavy Industries and boast a length of 249.1m, a beam of 37.4m and a draft of 13.5m, with Maersk Line stating that they have been specifically designed to these specifications, as this is the maximum vessel size

that can pull into West African ports. Some vessels will also be equipped with onboard cranes allowing these ships to operate on routes where the ports of call do not have ship-to-shore cranes.

Russia Expansion On The Cards

BMI also expects further growth in Maersk Lines exposure to the Russian market, with its sister company APM Terminals announcing Kalinigrad as its latest area of interest for port development. APMT is reported to be considering investing in the new port of Baltiysk, in the Kaliningrad region. The port would be able to handle 6mn TEUs a year. It is not yet known whether APMT would invest in the whole project or just a part, if it decides to join the development.

Should APMT join the project **BMI** would expect greater liner connection on Maersk Line's services with the port as the company complement one another's operations.

Niche Services Offer Lack Of Competition And High Returns

As well as developing new routes to high growth potential markets Maersk Line has been expanding its services as and when demand appears. The carrier is is set to increase its exposure to the Black Sea with a service linking Latin America with ports on the Black Sea. The service demonstrates the carrier's ability to not only cater for the major trade routes but also niche markets that lack competition. **BMI** believes that in is this period of rate declines on the big-money routes such a strategy of diversification is wise.

The service, which will be a reefer service, is due to be launched in September 2011 with a tentative rotation of Guayaquil (Ecuador), Balboa (Panama), Manzanillo (Mexico), Algeciras (Spain), Izmit (Turkey), Ambarli (Turkey), Novorossiysk (Russia) and Illichivsk (Ukraine). Containerisation International reports that other Latina American and Caribbean ports, such as Puerto Limin and Puerto Moin in Costa Rica, could be added at a later date.

The liner currently has minimal coverage of the Black Sea with only one direct service, the Asia-Europe 3 (AE3), linking Black Sea ports with Asia. The carrier does, however, have considerable feeder coverage.

The route is due to cater for the banana trade. **BMI** notes that Maersk Line's strategy of seeking exposure to niche shipping routes is sound, especially with the current rates decline on the big-money routes of Asia-Europe and the transpacific. Maersk's ability to diversify its operations to include services catering for high demand markets as well as routes catering for niche markets is one of the reasons why the line has retained is market-leader status.

Maersk Line has previous experience in catering for the banana trade. **BMI** notes that in 2010 Maersk Line launched a direct service linking ports in Ecuador to the Russian port of St Petersburg to meet banana demand. Once again, a Russian port (Novorossiysk) is on the rotation. This is unsurprising, with Russia estimated to import 180,000 tonnes of the fruit each month.

Mediterranean Shipping Company (MSC)

Strengths	▪ MSC is the second-largest container shipper in the world. ▪ The company has a forward-thinking strategy, with a fleet of 14,000 20-foot equivalent unit (TEU) vessels. ▪ The company is not averse to chartering. This has permitted MSC to expand its fleet.
Weaknesses	▪ With such a large fleet, MSC is constantly running the risk of overcapacity, which could prove a drain on resources if business slows. ▪ With 46 vessels on order, the company has the second biggest new-build orderbook globally, at a time when container rates are depressed due to overcapacity.
Opportunities	▪ The company has announced several planned rate increases to be introduced in August. It remains to be seen, however, whether these will be successfully implemented. ▪ The shipping sector has proved lucrative in the past two decades, with trade volumes growing year-on-year (y-o-y) since 1982. Although the downturn negatively affected the company, the mid- to long-term opportunity for trade growth is ever present, and MSC is well positioned to capture these volumes.
Threats	▪ The line's desire to become number one could be hampered by Maersk Line's plan to order a fleet of 18,000TEU vessels. ▪ Rising fuel prices pose a threat to shipping companies' bottom lines. ▪ Rates for shipping containers on the traditional routes remain depressed.

Company Overview

Mediterranean Shipping Company (MSC) was founded in 1970 in Geneva, Switzerland. It launched its first service between the Mediterranean and South and East Africa in the mid-1970s. In 2003, the company became the second-largest container shipper in the world, and remains in that position.

The carrier operates 200 direct and combined services weekly, calling at approximately 335 ports. The carrier has 390 offices across 146 countries, and employs more than 30,000 staff.

Strategy

MSC continues to snap at **Maersk Line**'s heels, holding a market share of 12.9% compared with Maersk Line's 15.4%, according to AXS Alphaliner. **BMI** believes that MSC will continue to battle for the top position, with the MSC by some measurements in fact having overtaken Maersk Line to claim top position. In February 2011 Containerisation International reported that MSC had overtaken Maersk Line in terms of capacity. This measurement was derived from just taking into account Maersk Line, not the **Maersk Group**, which includes **Safmarine** and **MCC Transport**. Taking the group as a whole into account, Maersk Line still holds the top position.

Routes

MSC is heavily exposed to the 'big money' routes, particularly the transpacific, with the line operating five services from Asia to US west coast ports. The line also caters from the east-

coast US market, with an all-water service.

The line operates four Asia-Europe services, two services (Silk Express and the Lion Service) to north Europe ports and to routes (Dragon Express and Tiger Service) to ports in the Mediterranean.

MSC also caters for the intra-Asia trade with its New Shogun service linking China and Japan and its TongKing Service connecting China with Vietnam. Some of the lines other services also link intra-Asia nations, such as the Cheetah Service, linking Chinese ports with the Taiwanese port of Kaohsiung, before travelling to cater for in Africa.

BMI believes that there is room for expansion in MSC's intra-Asia portfolio, however, with the potential for more intra-Asia specific routes either operated solely or in partnership as MSC in comparison with its peers has only a small exposure to the intra-Asia market, which is set to be a major growth area for box carriers in the mid term.

Fleet

MSC boasts the second-largest container fleet in the world, operating 471 vessels with a total capacity of 2mn TEUs. The fleet's dynamics are fairly evenly split between owned and chartered with a split of 39.3% and 60.7% respectively. MSC appears to be employing a strategy of chartering smaller vessels, while owning and operating larger ones. It has an owned fleet of 95 vessels with a capacity of 506,799TEUs, while its chartered fleet of 298 vessels have a combined capacity of 783,284TEUs. This could be because of the prestige of owning a large fleet, but **BMI** believes it is also partly because there is a larger supply globally of smaller vessels, which MSC can charter in when they are needed.

The exact breakdown of MSC's fleet is unavailable, but the line is a member of the ultra large container ship club, with a fleet of seven 14,000TEU vessels.

The line is preparing to take on more box ship tonnage in the future, both in the form of ownership and chartered and these vessels are likely to comparatively large in terms of capacity. So far in 2011 the line has taken on the second of its fleet of nine 12,500TEU vessels, the MSC Lauren. The line is also due to add to its fleet of 14,000TEU in the mid term, although Gianluigi Aponte, in an interview with Lloyd's List, stated his company had no intention of following Maersk Line's lead and ordering 18,000TEU, with Aponte announcing that 'he was only interested in ships up to 14,000TEU'. It should be noted, however, that originally Aponte was not interested in ordering vessels of 14,000TEU, yet his company has since done so, therefore **BMI** will not completely rule out MSC looking to develop vessels larger than 14,000TEU in the future.

According to AXS Alphaliner MSC's orderbook stands at 46 vessels, with a total capacity of 492,308TEU or 24.6% of its current fleet, the second largest orderbook in capacity terms in the top 100 container lines.

The line is expected to also expand via chartering in more tonnage. MSC has backed the order for 10 8,800TEU vessels (six have been ordered with the option for four more) at South Korea's Hyundai Heavy Industries. The order was placed by Germany's Bernard Schulte and Israel's Ofer Brothers and is due online in 2012. The new builds are reported to be set for long-term charters with MSC.

Financials

2010

MSC does not publish its financials. However, in 2010 the line has seen an increase in its operating fleet and the amount of cargo carried. In 2010 the line operated 432 vessels, a y-o-y increase of 14.3% from the 387 ships operated in 2009 and above the company's pre-downturn fleet of 410 vessels. Despite the downturn in 2009 the fleet's capacity continued growing, 1.4mn TEUs in 2008, 1.467mn TEUs in 2009 and in 2010 it reached 1.815mn TEUs, demonstrating MSC taking on larger capacity vessels over this period.

The real indicator of improvement in MSC's operations is, however, the number of containers carried. This grew by 17.6% y-o-y to reach 12.1mn TEU in 2010 following a y-o-y decline of 10.5% in 2009. 2010 levels reached and surpassed the pre-downturn handling level of 11.5mn TEU indicating MSC has recovered from the downturn and coupled with rate raises in 2010, which were implemented across the board, was in the black in 2010.

Latest Activity

Confusion Surrounds Possible MSC ECT Rotterdam Deal

Conflicting reports are circulating regarding Geneva-based Mediterranean Shipping Company (MSC)'s possible acquisition of a 49-50% stake in the port of Rotterdam's ECT Delta Terminal. **BMI** believes that such a deal, if it went ahead, would benefit both parties as MSC's services would be ensured priority at an increasingly busy port and ECT Delta Terminal would be guaranteed a client, which is vital as inter-terminal competition is expected to heat up in the mid-term.

Dutch paper Nieuwsblad Transport reported that MSC, the second-largest container shipping company in the world was set to acquire the stake in the terminal. The paper stated that neither ECT, which is a unit of the Hong Kong-based Hutchison Port Holding (HPH), nor MSC were available to comment, but that the port of Rotterdam's CEO, Hans Smits, has confirmed the deal. ECT spokesperson Bob Bagchus, however, has since stated that there is no truth in the report.

MSC has been gradually increasing its calls to the port of Rotterdam, adding it to another route rotation in February 2011. In 2010 MSC was calling at the port of Rotterdam on five of its services. In the space of a year MSC's throughput at Rotterdam has increased from 100,000TEUs to 700,000TEUs. This uptick in calls comes despite MSC operating a terminal at the competing Northern Europe port of Antwerp, which ranked second in terms of container throughput after the port of Rotterdam in 2010. The MSC Terminal at Antwerp is, however, reaching its operating capacity, leading MSC to look for another call point.

BMI would consider it a wise move for MSC to acquire a stake in a terminal at Rotterdam as such a move would ensure that MSC vessels were given priority at this major European maritime facility. The terminal would also ensure MSC ships a port of call, should the company wish to expand its fleet from its current 14,000TEU. The River Scheldt leading to MSC's terminal at the port of Antwerp had to be dredged to ensure the 14,000TEU vessels could enter and a further deepening could be required for the next generation of mega vessels.

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CMA CGM

Strengths	▪ The group has the third-largest container fleet in the world. ▪ CMA CGM has acquired a number of diversified subsidiaries, catering for different markets across the globe. ▪ Its terminal operating business, Terminal Link, supports the growth of the shipping division and the group's subsidiaries. ▪ Its multi-modal divisions also bolster growth, providing the customer with an integrated 'door-to-door' service.
Weaknesses	▪ With such a large fleet, the risk of over-capacity is ever present. ▪ The firm is not as diverse as its competitors, such as Maersk, COSCO and China Shipping, which operate services in the bulk and tanker sectors as well.
Opportunities	▪ The three-pronged acquisition of US Lines, COMANAV and Cheng Lie Navigation offers the opportunity to capture traffic volumes to and from three different regional markets. ▪ The partnership with the Yildirim Group will enable to company to return to a strategy of growth rather than being preoccupied with managing its debt.
Threats	▪ Despite having cancelled a number of new-build orders, the company's large orderbook is still a threat. ▪ The company must ensure it does not place the importance of its market share above that of its recovery. ▪ CMA CGM has faced calls for US sanctions against the company, as it has been caught shipping contraband materials linked to Iran, the company has now set up a compliance desk specifically to deal with Iran. ▪ Debt restructuring is leading to less diversity in the company's operations portfolio, with the group selling off stakes in one of its major terminals and its cruise ship company. ▪ CMA CGM's offices along with some of its peers we raided by EC officials in May 2011 investigating antitrust claims. If a shipping company is discovered to have acted inappropriately it will be in line for a hefty fine.

Company Overview

CMA CGM is the world's third-largest shipping line. Compagnie Générale Maritime (CGM) was formed in 1977 with the merger of the **Messageries Maritimes** (MessMar) and the **Compagnie Générale Transatlantique** (Transat). Compagnie Maritime d'Affrètement (CMA) was founded the following year, 1978.

In 1996 CMA CGM was privatised, and the following year made its first acquisition, of **Australian National Lines** (ANL). This was followed by a spree of acquisitions, beginning with UK-based **MacAndrews** in 2002. In 2006 CMA CGM purchased **Delmas**, an African shipping line previously owned by **Groupe Bolloré**. The acquisition propelled CMA CGM to third place in the world's container shipping lines, and strong growth enabled it to make three

purchases in 2007, with the acquisition of Taiwan-based **Cheng Lie Navigation Ltd**., Moroccan line **COMANAV** and US-based **US Lines**.

The group has operations in container shipping, with a special focus on reefer cargo, and also operates in the tourist industry through its subsidiary **Croisières et Tourisme**. **CMA CGM Logistics** operates 14 offices in China, Europe and the Middle East, and the group also owns **TCX Multimodal Logistics**, a bonded warehouse company that operates in many French ports. CMA CGM's multimodal subsidiaries include **French River Shuttle Container**; ocean freight forwarder **LTI France**; and **CMA Rail** and **Progeco**, the repair arm of CMA CGM's container business. **Terminal Link** is the group's terminal operating business.

Strategy

CMA CGM is the third-largest global container shipping company, holding an 8.3% market share, according to AXS Alphaliner. This puts it considerably behind second placed MSC with its 12.9% market share, but still a way off fourth-placed COSCON, which boasts a market share of 4%.

CMA CGM managed to ride out the downturn, despite a period where it looked like the French government might need to get involved to bail it out. The shipping line was determined to remain a family concern, with the company finding an investor, the Turkish Yildirim Group, which agreed to invest US$500mn and take a 20% stake in the shipping line, but left the Saadé family in charge with a majority of both shares and voting rights.

Debt restructuring is, however, affecting the company's diversity of operations, with the company selling its stake in the Marsaxlokk Malta Freeport terminal and its cruise ship company Compagnie du Ponant.

CMA CGM is a major player on the Asia-Europe trade route boasting a service network of 10 routes. The company is exposed to the transpacific with a route network of five services and is heavily involved in intra-Asia trade. CMA CGM offers more than 20 intra-Asia trade routes. These are, however, feeder services and it is the company's Asian subsidiary CNC Line that operates direct intra-Asia services. **BMI** expects CMA CGM to continue its strategy of developing its exposure to intra-Asia trade with the region considered to offer major box shipping growth potential.

Like its peers CMA CGM's fleet is getting bigger, not only in terms of vessel numbers, growing by 8.9% y-o-y in 2010, but also in terms of capacity. The company now operates a fleet of 13,000 20-foot equivalent unit (TEU) vessels, with eight vessels boasting more than 11,000TEUs of capacity coming online in 2011 alone.

The company has concentrated on developing its fleet via chartering in tonnage. Chartered tonnage accounts for 60.6% of CMA CGM's total TEU capacity. This tactic, **BMI** notes, offers the company considerable flexibility, as during periods of decline in volumes the company can return chartered vessels to owners when the charter period has finished, thereby decreasing its fleet and therefore its operating costs.

Financials

2010

CMA CGM's revenue increased by 36% in 2010 to US$14.3bn from US$10.5bn in 2009. The

increase enables the line to post a US$1.6bn profit following the company's loss of US$1.425bn in 2009.

The recovery in revenue was driven by the global uptick in both volumes and demand in the container shipping sector. In terms of total volumes carried CMA CGM's box levels shipped increased by 14.7%. CMA CGM states that 'Asia-Europe and intra-Asia lines enjoyed record business, which Asia-US lines returned to pre-recession levels.'

BMI believes that the volume uptick is just part of the story, and we note that volumes were up y-o-y and up on 2008 levels (by 4.4%). **BMI** believes that rate increases also played a massive role. CMA CGM has not released its y-o-y rate increase growth and so we do not have any figures to back this theory, but CMA CGM's peers such as Maersk Line recorded considerable rate increases in 2010, which enabled them to return to the black, and we believe that this was also the case with CMA CGM.

Latest Activity

Selling Up To Meet Debt Restructuring Pledges

The ongoing debt-restructuring program is seeing CMA CGM losing some of its diversity. The company has sold its 49% stake in the Marsaxlokk Malta Freeport terminal to Turkey's Yildirim Group and reports surfaced in May 2011 was dragging its heels concerning the company's plan to develop a US$470mn transhipment port in Batam in Indonesia. CMA CGM is also due to sell its stake in the Cruise company Compagnie du Ponant.

Wary Of Iran Connection

CMA CGM has been dragged into investigations surrounding Iranian sanctions with the shipping line accused of being lax in checking for contraband materials linked to Iran. In March 2011 the company was found to be shipping weapons destined for the Gaza Strip aboard its vessel the MV Victoria. Republican congressmen Mike Conaway and Peter King have been vociferous in their calls for US sanctions against the company. In response CMA CGM stated that 'As regards trade to and from Iran, CMA CGM diligently applies the rules prescribed by the United Nations, the European Union and the US.' Nevertheless, the company has set up a special in-house 'compliance desk' in order to double-check all dealings with the pariah state.

COSCO Container Lines Company Limited (COSCON)

Strengths	▪ The carrier has a good relationship with the Bank of China, which has provided the company a source of credit since the 1960s. ▪ COSCO's investment in a number of shipyards allows the company flexibility in adapting its order book to the economic climate. ▪ The company has a well-diversified fleet.
Weaknesses	▪ Parent company China Cosco Holdings Company recorded a net loss in Q111.
Opportunities	▪ The opening of direct shipping routes between China and Taiwan is likely to provide long-term growth opportunities for COSCO's container operations. ▪ The group is well poised to take advantage of growing intra-Asian trade.
Threats	▪ Container lines have been unable to push through many rate rises, which were the major factor behind companies' revenue recovery in 2010. ▪ Elevated bunker costs will impinge on companies' profit margins.

Company Overview

COSCO Container Lines Company Limited (COSCON) is one of the world's biggest container shipping lines and is the largest Chinese carrier, outgunning rival line **China Shipping Container Lines** (CSCL) in terms of fleet capacity.

COSCON is the container-transporting arm of China Cosco Holdings Company. The company dates back to 1961, and was originally engaged in transport solutions and did not become a shipping company until 1993. In 2005 the company issued an initial public offering (IPO), and now trades on the Shanghai and Hong Kong stock exchanges. China COSCO Holdings Company is the flagship and integrated platform of COSCO. The group is owned by the People's Republic of China.

Strategy

Routes

According to COSCON's website as of H110 the liner operates more than 100 international shipping routes, connecting 140 principal ports in 44 different countries and regions. The company has a further 21 domestic services.

As a Chinese company, COSCON is heavily exposed to the intra-Asia market, a region BMI believes is a growth area for shipping. In addition to 11 intra-China dedicated services, the company also has a large number of services connecting Chinese ports with ports in other Asian countries such as Vietnam and Indonesia. The company also has lots of exposure to the traditional East to West big-money routes of Asia-Europe and transpacific.

Fleet

According to AXS Alphaliner data, as of the start of July 2011 COSCON is the fourth-largest container shipping line in the world, with a market share of 4%. The liner has moved up the scale since our last quarterly report, when COSCON was in eighth position, with a market share of 3.6%. The company's container fleet has a capacity of 621,755 20-foot equivalent units (TEUs), up from 545,681TEUs three months ago. This is made up of 144 vessels. Of these the majority are Post-Panamax vessels with capacities of more than 4,500TEUs. The

largest vessels in the Cosco fleet are the Africa, America, Europe and Asia, all of which have a capacity of 10,062TEUs.

Of these 144 vessels COSCON has a fairly balanced ratio of chartered vessels, accounting for 44% of the fleet at 273,328TEUs. COSCON's owned fleet of 96 vessels makes up the remaining 348,427TEUs of capacity. COSCON's orderbook shows an ambitious growth strategy. According to Alphaliner, the liner company currently has 34 ships on order, with a total capacity of 270,352TEUs. This is a considerable 43.5% of COSCON's current fleet capacity, 621,755TEUs, and well above the top-10 orderbook average of 30.3%.

Financial Results

2011

Q1

China Cosco Holdings Company has released its results for the first quarter of 2011, with both volumes and revenues up. During the three months to March 31 COSCON transported 1.46mn TEUs, up 12.1% on the volumes transported during the corresponding quarter the previous year. Growth was achieved on all of the company's shipping routes.

Revenues were up by 4% year-on-year to CNY7.89bn, with an increase achieved on the transpacific route, other international routes and the China domestic trade. **BMI** notes that the rise in volumes is significantly greater than that in revenues, demonstrating the effect that the fall in rates has had.

Despite the rise in revenues for the COSCON, the China Cosco Holdings Company as a whole recorded a net loss for the quarter. Its revenues were down by 5.6%, from CNY17.41bn to CNY16.44bn, and the bottom line was a net loss of CNY503mn, as opposed to a profit of CNY883 in Q110. This will have been contributed to by both the disastrous performance of the dry-bulk shipping sector through the quarter, coupled with the elevated cost of bunker fuel on the back of Middle Eastern political unrest.

2010 COSCON's parent company's Q310 results show an improvement on the same period in the previous year. Its revenues were up by 34.2% over those of Q309, to hit US$3266.08mn (CNY21550mn). Profits were also up massively, by 397.4% to reach US$320.24mn (CNY2113mn). For the first three quarters of the year profits were up by 205.2%.

The company stated in January 2011 that COSCON increased its peak-season route coverage in 2010 by 39.8% on its transpacific services, and 42.9% on its Far East-Europe services. COSCON's managing director, Sun Jiakang, said: 'In 2010, with the crisis fading out, the world economy and global trade gradually speeded up the recovery. We arranged and adjusted our deployment according to the regional market demands and the business performance.'

Latest Activity

Seaspan Takes Delivery Of COSCO Glory Containership

In June Hong Kong-based **Seaspan** announced that it had taken delivery of its first 13,100TEU containership, named *COSCO Glory*, from South Korean shipbuilder **Hyundai Heavy Industries**. The new containership is the biggest vessel in Seaspan's fleet, and will expand the company's operating fleet to 61 ships. Further, the COSCO Glory is the sixth

ship delivered to Seaspan in 2011 and is chartered to COSCON as part of fixed-rate time charter for 12 years. Seaspan is scheduled to take delivery of seven more 13,100TEUs vessels through to March 2012.

Seaspan is an autonomous charter owner of containerships and has 69 chartered containerships. The company primarily charters the containerships under long-term fixed-rate time charters with key container shipping companies.

COSCON To Impose War-Risk Surcharge

In May COSCON announced it was to impose a war-risk surcharge of US$200 per TEU on freight shipments bound for Libya. The surcharge will be applicable once COSCON recommences its Indian Subcontinent and Far East services to Libya. This announcement followed UAE-based United Arab Shipping Company (UASC) and Germany-based Hapag-Lloyd's move to levy war-risk surcharges on Libya-bound cargo.

Transpacific Upgrades

In April COSCON announced that it, in conjunction with Hanjin Shipping, Pacific International Lines (PIL) and Wan Hai Lines, was launching a new joint service on the transpacific trade route. The rotation of the service will be Fuzhou, Ningbo, Shanghai, Yokohama, Long Beach, Fuzhou and back to Yokohama. The CLX Service (Central China - Long Beach Express) will have five vessels deployed upon it, with capacities of 3,600-3,850TEUs. Two of these will be supplied by COSCON.

Also in April the company announced an upgrade to its existing Far East to US east coast service (the USEC), which goes via the Suez Canal. The ship sizes on the service, operated in conjunction with Hanjin and Yang Ming Line, will be enlarged from 4,300TEUs to 5,500TEUs.

Hapag-Lloyd

Strengths

- It has a large global presence, with offices across the world and shares in two terminals.
- It is breaking into the Yangtze shipping route sector.

Weaknesses

- Hapag-Lloyd now operates in only one cargo market, the container market.
- The company had to rely on state aid to see it through the downturn.
- Lack of exposure to intra-Asia, which is widely considered to be the major medium-term growth market for the container shipping sector.

Opportunities

- The company is set to join the mega-vessel club, with four vessels with a capacity of 13,200 20-foot equivalent units (TEUs) each on order.
- Its association with Grand Alliance carriers enables it to enter into vessel-sharing agreements or jointly-operated services with ease.
- TUI is seeking to divest its stake in Hapag-Lloyd.

Threats

- Uncertain outlook for container shipping sector, with threat of overcapacity still looming.
- The company posted a loss in Q111 and BMI fears further losses in 2011 on the back of rate declines.
- Hapag-Lloyd's offices along with some of its peers were raided by EC officials in May 2011 investigating antitrust claims. If a shipping company is discovered to have acted inappropriately it will be in line for a hefty fine.
- Gains in the US dollar against the euro, in which Hapag trades, could erode profits.

Company Overview

Hapag-Lloyd has a 160-year history, dating back to the foundation of German lines **Hamburg-Amerikanische-Packetfahrt-Actien-Gesellschaft** (**Hamburg-America Line**, or **Hapag**) and **Norddeutscher Lloyd** (NDL) in 1847 and 1857 respectively. The two lines merged in 1970 to form Hapag-Lloyd AG. In 1997 the line became a subsidiary of German tourism giant **TUI AG**, which purchased 100% of shares in Hapag-Lloyd in 2002. In 2005 Hapag-Lloyd acquired Canadian liner **CP Ships**.

In March 2009 TUI sold Hapag-Lloyd to the Germany-based **Albert Ballin Consortium**. The consortium has a 56.67% stake in Hapag-Lloyd. It is made up of the City of Hamburg (40.67%), **Kuhne Holding AG** (26.55%), **Signal Iduna** (12.61%), **HSH Nordbank** (8.4%), **MM Warburg Bank** (8.4%) and **HanseMerkur** (3.36%). TUI has kept a 43.3% stake in Hapag-Lloyd.

TUI is looking to offload its stake in Hapag-Lloyd, potential buyers are so far reported to be an Omani state fund and China's HNA Group.

The company has stakes in two terminals: a 25.1% share in Hamburg's Container Terminal Altenwerder GmbH and a 20% stake in Montreal Gateway Terminals.

Strategy

Hapag-Lloyd has slipped to fifth place in AXS Alphaliner's top 100 container line rankings having reached the fourth position in terms of market share earlier this year. While Hapag-Lloyd continues to retain the same market share as fourth-ranked COSCON of 4% the German carrier is 4,018TEU behind the Chinese line. This small difference in fleet capacity could easily see Hapag-Lloyd regain its fourth position.

Routes

Hapag-Lloyd has developed considerable exposure to the big money routes. It operates nine trans-Pacific services and seven Asia-Europe services. It is also highly exposed to the trans-Atlantic route, offering a total of eight services.

One area where the company currently has minimal exposure, but that is considered by the industry to have huge growth potential, is intra-Asia. The line embarked on expanding its presence on this trade route earlier in 2011 by forming a partnership to operate a service with Thailand's Regional Container Lines (RCL). **BMI** believes that if Hapag-Lloyd wishes to pursue a strategy of increasing its intra-Asia coverage, then it will likely do so with partnerships with lines based in the region.

In terms of volumes handled on Hapag-Lloyd services, the company's transatlantic routes dominate. In 2010 the routes accounted for 23% of the total cargo transported by the company. Asia to Europe is the company's second-largest route exposure, accounting for 22.5% of the total volumes shipped. The amount of cargo Hapag-Lloyd ships on the trans-Pacific and Latin America routes is roughly the same, with the routes accounting for 22% and 21.8% respectively of the total. Hapag-Lloyd's exposure to Latin America has increased. In 2009 the route accounted for 19.7% of the line's total volumes transported.

Fleet

Hapag-Lloyd boasts a fleet capacity of 619,401TEUs, with 141 vessels. Over the last quarter Hapag-Lloyd has increased its use of chartered vessels, with its chartered fleet increasing to 56.9% of the total. In terms of vessel numbers Hapag-Lloyd operates more chartered tonnage, at 85 vessels, than owned vessels, with a fleet of 56. Hapag-Lloyd appears to be employing a strategy of chartering smaller vessels, while owning and operating larger ones.

Hapag-Lloyd's largest percent of vessels in terms of size is 4,000-6,000TEU ships. It operates 38 vessels of this size, accounting for 40.4% of the company's fleet. **BMI** notes that this strategy means the company has flexibility to move ships between routes, with vessels in this size bracket able to be used for both direct services and feeder lines. It operates 18 very large container ships, and its current largest vessels offer a capacity of 8,749TEUs.

Hapag-Lloyd is set to join the ultra large container ship operating club. It has ordered four 13,200TEU vessels from South Korea's **Hyundai Heavy Industries**. As well as the four new builds, the US$1.4bn deal also includes the upgrade of six vessels Hapag-Lloyd already had on order at the yard, which were due to be 8,749TEU vessels, but will now be 13,200TEU ships. The vessels are due to come online between mid-2012 and the end of 2013, and will operate alongside the vessels of Hapag Lloyd's Grand Alliance partners (NYK and OOCL) on Far East-Europe routes.

Financials Results

2011

Q1

Hapag-Lloyd sailed into the red in Q1 with a loss of EUR22.1mn despite a revenue of EUR1.4bn, a y-o-y increase of 16.5%. The loss was attributed to high bunker fuel prices and increased competition.

Freight rate revenue in fact increased y-o-y by 10%, but **BMI** fears that with rates on major routes decreasing in the last few months the company's revenue for H1 will be hit by the rate declines

2010

Hapag-Lloyd's revenue increased by 87.9% year-on-year (y-o-y), to EUR6.2bn, up from EUR3.3bn in 2009. The increase enabled Hapag-Lloyd to return to the black, with a full-year profit of EUR428mn, following a loss of EUR402mn in 2009.

The recovery in revenue was driven by the global uptick in both volume and demand in the container shipping sector. In terms of total volumes carried, Hapag-Lloyd's box levels shipped increased by 6.7%. The major driver of Hapag-Lloyd's recovery was, however, its ability to increase rates. Annually, rates grew by 24.8%, Asia-Europe saw the greatest rate rise, of 42.2% y-o-y, followed by Australasia, where rates increased by 36.9%.

BMI notes from Hapag-Lloyd's results that case rates increased considerably more than volumes. Asia-to-Europe rates increased by 42.2%, while volumes on the route grew by 6.4% y-o-y. Australasia rates increased by 36.9%, but volumes on this route in fact fell by 18.2% y-o-y.

BMI wonders what 2011 holds for Hapag-Lloyd's bottom line. The company achieved its recovery mainly by rate hikes. However, like its peers it has struggled so far in 2011 to implement planned rate increases and, with growth in volumes shipped y-o-y set to remain steady, its bottom line could also remain static.

Latest Activity

Oman States Interest

An Omani state fund appears keen to buy TUI's stake in Hapag-Lloyd with the fund reported to have written to the German tourism giant about its intentions. China's **HNA Group** which owns **Hainan Airlines** has also been suggested as a potential buyer, but it is believed that HNA is seeking a majority stake, which TUI with its stake of 43.3% cannot offer.

Full Steam Ahead For Mega-Vessel Order

Hapag-Lloyd has succeeded in borrowing US$925mn to fund its ten 13,000TEU vessel fleet order. The loan comes from a syndicate of banks made up of **HSBC**, **Citibank**, **Deutsche Bank**, **KfW IPEX-Bank** and **UniCredit Bank**. The vessels are due to come online between mid-2012 and the end of 2013, and will operate alongside the vessels of Hapag Lloyd's Grand Alliance partners (NYK and OOCL) on Far East-Europe routes.

Evergreen Line

Strengths	▪ Evergreen operates one of the most globalised route networks, with strong coverage of major Latin American and Middle Eastern ports in addition to its core Asian, US and European services. ▪ The company's route-sharing agreements allow it to reduce capacity while still meeting clients' demands. ▪ It is highly exposed to the intra-Asia trade route, which is widely considered a major growth market in the medium term.
Weaknesses	▪ With a large container fleet and little diversification into other sectors, the risk of overcapacity is ever-present. ▪ The company's flagship services are Asia-orientated, so a shift in the dynamics of this region could make Evergreen vulnerable.
Opportunities	▪ The company was the first box line to return to the yards after the downturn, and in the medium term is planning to order 100 vessels, which will give it one of the youngest and most modern fleets in the container sector. ▪ It is well placed to take advantage of the growth in cargo traffic brought about the opening of direct routes between China and Taiwan.
Threats	▪ While the company has built up intra-Asian history and expertise, the region's growth potential is luring new players, increasing the competition Evergreen will face in this region. ▪ Box lines have so far been unable to raise rates, and we are concerned this could have a negative impact on carriers' bottom lines. ▪ Evergreen's offices along with some of its peers were raided by EC officials in May 2011 investigating antitrust claims. If a shipping company is discovered to have acted inappropriately it will be in line for a hefty fine.

Company Overview

Evergreen Line is the name and global brand under which five shipping companies operate. The brand was established in May 2007 and joins **Evergreen Marine Corp**., based in Taiwan, **Italia Marittima**, **Evergreen Marine (Hong Kong)** and **Evergreen Marine (UK)**. A fifth carrier, **Evergreen Marine (Singapore)**, signed a joint service agreement in May 2009.

Evergreen Line's main sea routes focus on the delivery of goods from Asia, particularly Taiwan, Hong Kong, China, South Korea and Japan. The carrier operates to and from the US east and west Coasts, South America, Europe, the Mediterranean, the Middle East and Africa. It also provides a container service between the east coast of South America and the east coast of the US and a service linking Panama with the US west coast. The carrier provides regular feeder services in the Caribbean and around the Indian sub-continent.

Evergreen is engaged in the port-operating sector, with terminals including the Taichung Container Terminal and the Kaoshiung Container Terminal in Taiwan, the Colon Container Terminal in Panama and the Taranto Container Terminal in southern Italy, in which Hutchison Port Holdings also has a stake.

Strategy

Evergreen Line has been knocked into sixth position and has lost its accolade of being the largest Asian container line to China's **COSCON**. According to AXS Alphaliner the line has a capacity of 612,960TEUs, just 6,441TEUs behind fifth-placed **Hapag-Lloyd** and some way ahead of **APL**, which has a capacity of 586,369TEUs.

Routes

Evergreen Line boasts a strong presence on intra-Asia trade routes and continues to launch new routes. The high growth potential of intra-Asia routes has seen a number of lines expand into this area. **BMI** believes, however, that Evergreen Line is positioned better than most, as intra-Asia is its traditional operating area and it has built up expertise and a client base in the region.

The company has, however, also developed a role on the 'big money routes', and has seven Asia-Europe services and 10 transpacific services.

Fleet

Evergreen Line's fleet boasts 167 vessels, with a capacity of 612,960TEUs. It operates slightly more owned vessels that chartered, at a ratio of 53.9% to 46.1%. It owns 88 vessels, with a total of 330,167TEUs, while it charters 79 vessels, totalling 282,793TEUs.

In terms of vessel capacity the fleet size is much smaller than its peers. Vessels range from 1,618TEUs to 7,024TEUs, with the company not operating a very large or ultra large container fleet. This strategy of a large fleet made up of smaller vessels ties it with intra-Asia routes, to which Evergreen Line is highly exposed. Until ports in the intra-Asia region are developed to take larger capacity ships, **BMI** believes Evergreen's owned tonnage will remain relatively small in capacity.

Evergreen Line appears prepared to take its capacity to 8,000TEUs. It has ordered a fleet of 'very large' container vessels. It appears unlikely, however, that the vessels will get much bigger, with the company's chairman and founder, Chang Yung-Fa, reported to be 'a noted sceptic about the industry trend towards far larger ships, believing that the need to fill them would end up driving down earnings.'

While Evergreen Line might be avoiding a strategy of ordering mega vessels, it is set to be a major client at Asian yards. The line was the first box carrier after the downturn to return to the yards. Chang Yung-Fa announced in 2010 that the line plans to orders 100 vessels. According to Chang, the fleet expansion will comprise 20 vessels with 7,024TEUs of capacity (S-type), 20 vessels of 5,364TEUs capacity (U-type) and 20 or more vessels that will act as feeders, with 2,000TEUs of capacity.

If this strategy is implemented it will help the company move toward Chang's reported aim of 'steering Evergreen into becoming the world's largest container line in his lifetime.'

Financial Results

2010

In 2010 Evergreen Marine Corp registered a revenue of US$3.5bn, a y-o-y increase of 39.9%. This enables the company to sail back into the black with an operating profit of US$403.1mn compared to the loss of US$473mn in 2009.

Latest Activity

Intra-Asia Expansion Continues

Evergreen's expansion into intra-Asia has continued over the quarter with the line launching a new Japan-Taiwan-South China Sea (JTS) service in March 2011. Three vessels with a capacity of 900TEUs each are deployed on the route, with the service offering a rotation of Tokyo, Yokohama, Nagoya, Osaka, Keelung, Kaohsiung, Shekou, Hong Kong, Hai Phong, Zhangjiang, Hong Kong, Shekou, Tokyo. Further intra-Asia expansion came in April, with Evergreen joining up with Wan Hai Lines and Interasia Lines to offer a Taiwan-India service, linking Taichung, Keelung, Hong Kong, Nansha, Shekou, Port Klang, Chennai, Penang, Port Klang, Singapore, Yantian, Hong Kong and Taichung. Evergreen operates on vessel on the service, with Wan Hai Lines supplying two and Interasia Lines the other one. The vessels' average capacity is 1,300TEUs.

Looking To Other ETRs

Intra-Asia is not the only emerging trade route (ETR) which Evergreen has been increasing its exposure on over the quarter. Evergreen is partnership with Wan Hai Lines, MOL and Seacon launched an Asia-East Africa (AEF) service in April 2011. The service operates with six ships of capacities of 1,200-1,350TEUs.

Increasing Exposure On The Asia-Europe

As well as expanding on ETRs Evergreen has increased its presence on the 'big money' route of Asia-Europe, despite rates continue to tick lower on this route. In April the line linked up with CSCL and Zim to launch a new joint weekly Asia-Europe service (CES2) with a 63-day port rotation covering Shanghai, Ningbo, Xiamen, Yantian, Tanjung Pelepas, Port Klang, Hamburg, Rotterdam and Antwerp. Evergreen is supplying five 8,000TEU vessels of the nine vessel fleet operating on the service.

New Vessels Ahoy

In May 2011 Evergreen headed back to the shipyards placing an order for another 10 8,000TEU ships, signing with **China Shipbuilding Corp**. At the same time containership-leasing company **Costamare** placed an order for five 8,000TEU vessels, which it is to charter out to Evergreen, at South Korea's **Sudong Shipbuilding & Marine Engineering**.

APL

Strengths

- APL's parent company, NOL, has developed a full-package approach to the container-shipping market offering shipment, terminal operations and logistics.
- The Singaporean government maintains a 67.4% stake (as of November 2006) in the company through its investment company Temasek Holdings, and its interest introduces an element of stability to the company's operations.

Weaknesses

- The carrier is now exposed solely to the box market.
- The group is primarily Asia and US focused, and relies heavily on major trade lanes, with a limited presence in less established markets, such as Africa and Latin America.

Opportunities

- APL's association with The New World Alliance (TNWA) carriers enables it to enter into vessel-sharing agreements or jointly operated services with ease.
- The company's intra-Asia focus should serve the line well, with the region widely considered to offer major growth potential for container lines.
- The company is expanding its fleet and is set to join the mega-vessel club in the mid term.

Threats

- Although the carrier has history and expertise on the intra-Asia trade route, more and more lines are increasing their exposure to the region, with APL facing increased competition.
- Rates on the 'big money' routes have continued to decline since the start of 2011, which will be a worry for all container lines.
- A weakened US dollar would affect profits, although it could act to stimulate trade volume growth.

Company Overview

APL is the container-shipping brand of Singapore-based **Neptune Orient Lines** (NOL). NOL was formed in 1968, but assumed its current form in 1997 when it merged with American President Lines (APL). NOL remains the holding company listed on the Singapore Stock Exchange. The Singapore government maintains a 67.4% stake (as of November 2006) in the company through its investment company **Temasek Holdings**.

NOL began life as Singapore's national shipping carrier, three years after the country became an independent state. The Singaporean government-owned company at first operated just five vessels, and achieved its first profit by the mid-1970s when its fleet had expanded to 20 vessels. It held a US$105mn initial public offering (IPO) in 1981. The group diversified into tanker operations in the early-1990s under the brands **American Eagle Tankers** (AET) and **Neptune Associated Shipping** (NAS).

US-based APL dates back to 1848. The company, originally called the Pacific Mail Steamship Company, began to focus on container shipping in the 1950s.

Since the merger, NOL has continued to direct its business towards the container market, divesting tanker subsidiaries AET and NAS in 2003. It established **APL Logistics** in 2001 in a bid to strengthen product supply chains and also operates a terminal operating business,

APL Terminals.

Strategy

With **COSCON**'s assent up the rankings APL is now the third-largest Asian container line, holding a market share of 3.8%. Globally the company is ranked seventh, according to AXS Alphaliner, holding its rank from last quarter. The company is currently sandwiched in between Taiwan's **Evergreen**, which is 26,591 20-foot equivalent units (TEUs) ahead of it, and **CSAV**, which is 27,604TEUs behind it.

Routes

Unsurprisingly, considering the line's base of operations in Singapore, APL operates a considerable intra-Asia service portfolio with 29 intra-Asia routes in total. The high growth potential of intra-Asia routes has seen a number of lines expand into this area. **BMI** believes, however, that APL is one of the best positioned, as intra-Asia is its traditional operating area and it has built up expertise and a client base in the region.

APL, also rather unsurprisingly considering its US-orientated history, also boasts a considerable transpacific route network, with a total of 13 services catering for the trade needs of Asia to the US. APL is also somewhat exposed to the Asia-Europe trade route, offering nine services on this trade lane.

APL's route strategy therefore displays a company keen to expose itself to the global market via the 'big money' routes, but at the same time retain its presence in its traditional area of operations, intra-Asia. This exposure to intra-Asia should work well for the line, with the region set for growth on the back of FTAs between China and the ASEAN 5.

In terms of volumes handled intra-Asia also dominates. In 2010 the route accounted for 39.95% of the total. It is also the route that appears to offer the most growth potential and could in the future account for even more of APL's total volumes shipped, with container levels transported on this route growing by 26% year-on-year (y-o-y) in 2010. **BMI** believes the APL will face competition on this route, however, with its peers expanding their services in the area.

Transpacific and Asia-Europe routes account for the second- and third-largest volumes carried by APL respectively. In 2010 the routes accounted for 32.96% and 16.2% of the total respectively.

Fleet

APL operates a fleet of 146 vessels, with a total capacity of 586,369TEUs. APL's fleet is heavily weighted toward chartered vessels, which account for 71.1% of the company's total fleet. This large percentage of chartered fleet enables APL to implement a strategy of downsizing should a downturn hit, with the line able to return chartered vessels to their owners when their charters are up if the operating environment is not conducive to profits. Lines with a high ownership ratio would be forced to lose money by laying up vessels if faced with the same situation.

APL's fleet is highly diversified, ranging from feeder vessels with a capacity as small as 319TEUs to a fleet of six very large container ships of 8,110TEUs. APL is implementing a strategy of expansion and with it an increase in vessels' capacity, placing an order for two

8,400TEU vessels in 2010.

In 2011 APL announced a strategy to join the mega-vessel club with an order for 10 14,000TEU vessels at South Korean yards. At the same time the liner ordered two 9,200TEU capacity vessels. The 14,000TEU vessels are to be deployed on Asia-Europe services, with the 9,200TEU vessels on APL's transpacific routes.

Financials

2011

Q1

Despite the NOL's revenue increasing by 16% from US$2.098bn in Q110 to US$2.443bn in Q111, the company still posted a net loss of US$10mn, although it should be noted that the loss was not as severe as the previous year when the NOL recorded a net loss of US$98mn. The loss in Q111 was attributed by NOL's President and CEO Ronald Widdows to the fact that 'rising fuel costs have interrupted our momentum'.

APL accounted for US$2.1bn of NOL's revenue in Q111. APL's container liftings increased by 9% y-o-y, with average rate per 40-foot equivalent unit also increasing y-o-y by 3%. The company's vessel utilisation for the period was 92%.

2010

APL's revenue increased by 47% to US$8.3bn in 2010, with a core EBIT of US$490mn compared with a loss of US$698mn in 2009.

The recovery was driven by an uptick in volumes shipped and also by y-o-y rate increases. The volume of containers APL carried in 2010 rose by 23.6% y-o-y, with average revenue per 40-foot equivalent unit (FEU) increasing by 22% y-o-y. **BMI** notes that although many carriers saw their revenues increase mainly on the back of rate increases, APL's recovery appears to have been driven just as much by volume increases as by rate rises.

We believe that this was down in part to the growth y-o-y of volumes on APL's intra-Asia routes, which increased by 26% and Asia-Europe routes, which grew by 28.6%.

Latest Activity

APL Continues Intra-Asia Expansion

APL has continued its route expansion in intra-Asia, launching two new services this quarter. The first was launched in April when APL extended its North Asia Philippines Express (NPX). The service added the port of Manila to the link. Three vessels of 1,100TEUs operate on the service. The second intra-Asia route expansion was unveiled by APL in June 2011 with APL expanding its China-India Express service by adding a weekly call at India's port of Pipavav.

Gaining Priority Access To China

Singapore-based NOL and China's **SITC International Holdings Company** have formed a partnership with Qingdao Qianwan United Container Terminal Company to operate a two-berth container terminal that is due to open at the port in H211. The terminal will to add 1.5mn TEUs to the port of Qingdao's container capacity. NOL will operate the terminal under a 30-year concession.

The Qingdao terminal will be NOL's first foray into the Chinese port sector. It currently operates terminals at the port of Kaohsiung in Taiwan, Kobe and Yokohama in Japan, and at the US ports of Los Angeles, Oakland, Seattle and Dutch Harbour. NOL is developing terminals at ports in Vietnam and Thailand, and as part of the Maasvlakte 2 port development at Rotterdam.

The rationale behind NOL's expanding port operations is to ensure future access to high-demand ports. Its container shipping unit, APL, can thus be assured access to some of the world's busiest ports. The new terminal at Qingdao will primarily service APL and SITC vessels.

Going Big

APL is set to join the mega-vessel club, placing an order for 10 14,000TEU vessels in June 2011, at the same time the carrier also upgrading two vessel orders to 9,200TEU ships. The 14,000TEU ships are to be deployed on Asia-Europe services, with the 9,200TEU ships on APL's transpacific routes. The ships are due to be delivered in 2013-2014.

CSAV

Strengths	▪ The Chilean carrier is long-established, and is the biggest shipping company in the Americas. ▪ A Chilean mining company has bought a 10% stake in the company.
Weaknesses	▪ CSAV is heavily reliant on charter-vessels, potentially leaving it open to fluctuations in price. ▪ Despite its bailouts CSAV still has significant debts. ▪ The line is continuing to expand its fleet, exposing it to the threat of overcapacity at a time when the recovery in global container shipping is not yet assured.
Opportunities	▪ Strong consumer domestic consumer demand within Chile should see increasing demand for imports of containerised goods. ▪ The company is in discussions on a route sharing agreement with CMA CGM and MSC, which could boost revenues while reducing the company's exposure to volatile rates.
Threats	▪ Overcapacity is still putting downside pressure on rates, and container lines have been unable to push through rate rises, which were the major factor behind the companies' revenue recovery. ▪ Rising fuel prices present a threat to shipping companies' bottom lines.

Company Overview

Compañía Sud Americana de Vapores (CSAV) was founded in Chile in 1872 and has been traded on the Santiago Stock Exchange since it opened in 1893. The company initially concerned itself solely with coastal shipping, but this soon grew to include the whole west coast of South America. This was later extended to include services to the US, then Europe, followed by the Far East, South-East Asia and the east coast of South America.

Today CSAV is the largest shipping company in the Americas, offering services transporting containers, dry bulk, fresh and frozen products, and vehicles to five continents. The Chilean carrier has the right specification of ship for carrying these varying cargoes, either owned by CSAV or chartered. CSAV has a large number of fixed itineraries through which it is able to provide year-round deliveries to various ports, and has in recent years introduced intermodal services, combining different modes of transport to provide a door-to-door package. This intermodal element is provided by CSAV's subsidiaries, **Sudamericana Agencias Aéreas y Marítimas** (SAAM), a cargo-shipping agency, and **COSAN**, a container terminal in Santiago.

Strategy

In May 2010 CSAV entered the top 10 of the world's container shipping lines, in terms of both market share and fleet capacity. With 3.8% of market share CSAV is in eighth place, almost on equal footing with **APL** in seventh place, with 3.8%.

Fleet

The Chilean shipping company's 20-foot equivalent unit (TEU) capacity is, as of July 2011, 542,765TEUs. CSAV's capacity is spread over 137 ships. Of these just nine ships are owned by CSAV, or 44,501TEUs, which accounts for just 8.2% of the total TEUs of CSAV's fleet. The remaining 128 ships are chartered, and these make up the remaining

498,264TEUs.

CSAV appears to be following a policy of expansion, like many of the top ten, as market share is important to the container shipping industry. The carrier currently has 12 vessels on its orderbook, amounting to 98,589TEUs of capacity. This amounts to 18.2% of current fleet capacity.

Routes

CSAV has said it is negotiating the possibility of joint-operating agreements and forming consortia with **Mediterranean Shipping Co.** (MSC) and **CMA CGM**. CSAV has had a difficult year amid plummeting container shipping rates, so **BMI** is unsurprised by this announcement. We believe that sharing routes will lessen the company's exposure to volatile rates at a time when overcapacity is plaguing the sector.

CSAV said the services being discussed include routes between Asia and Africa, Brazil and the Mediterranean, the Pacific Coast of South America and North Europe, and the east coast of South America and the Middle East. At this point the three companies have agreed upon the basis for the joint operating agreements and are in the process of drafting a memorandum of understanding (MoU) that will set out the steps for the signing of fixed agreements. CSAV said the discussions are in line with a strategy outlined by its board and management of increasing profitability and reducing exposure to volatile rates.

BMI notes that the route-sharing agreements represent a new direction in CSAV's strategy. Previously the line's reaction to volatile container shipping rates was to axe routes. In June the company pulled its ASIAM Service, which linked India, South East Asia and China to the US west coast, and earlier in 2011 the carrier dropped its Asia-US east coast AMEX service. **BMI** considers this a dangerous strategy as once lines have exited a route it is costly to return, as clients will move to other lines and carriers normally have to slash rates to win a new client base.

As such we welcome the route-sharing plan as it allows CSAV to continue operating popular routes while minimising its exposure to fluctuating rates. We also highlight that CSAV is looking to other routes that are less affected by overcapacity and offer high growth potential. In May 2011 the company announced a new service to link Latin America with South Africa and Asia.

We note that the carrier badly needs to employ strategies such as route sharing in order to bolster its revenues. The company's net loss for Q111 was US$186,355mn.

Financial Results

Q111

The company's net loss for Q111 was US$186,355. CSAV's volume of transported containers increased 6.8% in May over April, but the average revenue per container declined. The Chilean carrier transported 303,300TEUs in May, compared with 283,900TEUs in April. May container volume grew 35.7% over the same month a year ago. CSAV said average revenue per TEU dropped by 3.3% from April, and was down 17.4% year-on-year.

2010

CSAV had a significant increase in liftings in 2010, up 61% from 1.79mn in 2009 to 2.89mn

last year. Revenues were also up, by 80% from US$3.03bn to US$5.45bn. The company's performance went from a 2009 loss of US$656.4mn to a 2010 profit of US$170.8mn. The company's performance turned around on the back of its fleet growth and the increase in rates container companies were able to impose as trade rebounded over the first half of the year.

However, even this turnaround in performance has not generated profit enough to clear CSAV's crippling debt. Que Pasa reported in March that losses of US$50mn had already been incurred by CSAV since the start of the year, and that the company still owes Korean company **Samsung** US$60mn to be paid by June. In a bid to avert any more crises the shipping company has announced it is to sell up to 49% of ports-operating subsidiary **SAAM** in order to raise capital. There was some positive news for the line in March with mining group **Luksic**'s purchase of a 10% stake in CSAV.

Latest Activity

Luksic Displays Further Vote Of Confidence In CSAV

In April Chilean mining company **Grupo Luksic** has purchased an additional 8% stake in CSAV from its largest shareholder **Maritima de Inversiones**. Luksic previously bought a 10% CSAV stake from **Marinsa** in March 2011. Luksic is a business conglomerate which operates in mining, financial services, manufacturing, beverages and food sectors. **BMI** believes that Chilean mining company **Grupo Luksic**'s purchase is good news for the beleaguered shipping line, which is US$60mn in debt. We believe CSAV's dry-bulk service will look to take advantage of its new connection with the mining company, given that its container shipping service remains plagued by overcapacity.

Luksic made the purchase through its holding company **Quiñenco**, acquiring 202,925,890 shares at a price of CLP285 (US$0.60) per share. Quiñenco will now be CSAV's second-largest shareholder after **Marinsa CSAV**. The vice-president of CSAV, Arturo Claro, said the group was satisfied with the entry of Quiñenco to CSAV, noting that it will be an important contribution to the shipping company. Claro told the Diario Financiero that the sale of 10% of the company was agreed 'primarily because we have confidence with them...they will support the company'. He said that Luksic 'knows how to handle business... With this, the situation of the company in the medium and long term will be completely different. This leaves us in a position more solvent than our competitors who are pushing down rates.'

BMI notes Luksic's interest in CSAV will give Chile's main shipping company a boost. Although it recently announced a surge in profits in 2010, going from a loss of US$656.4mn in 2009 to a profit of US$170.8mn in 2010, this turnaround in performance has not generated enough profit to clear the company's crippling debt. Furthermore, while the company experienced a strong comeback last year, container shipping is suffering once again. The rate rises imposed last year helped shipping companies make their way back to the black, yet as the recovery slowed rates have dropped once again, causing the company to cancel some routes. According to a company statement the decline in rates 'has created a very complex scenario which in the short term is affecting the operational results of CSAV and the industry in general'. The company's new chairman has warned of negative results once again for the first quarter of 2011.

Hanjin Shipping (Container Operations)

Strengths

- The company is part of the world's biggest shipping alliance, the CKYH Alliance, which it formed with COSCO, K Line and Yang Ming. Cooperation on key long-haul trade lanes minimises costs and means rapid adjustments may be made in the case of market volatility.
- The line has considerable exposure to intra-Asia and continues to increase its services in the region.
- The line was one of the first to offer Vietnam as a port of call on an Asia-Europe service. Hanjin Shipping's Vietnam focused strategy is also displayed via its operation of the Cai Mep container terminal.

Weaknesses

- Despite a diversified route portfolio the company is heavily exposed to the transpacific trade route, with the route accounting for 47.98% of box volumes shipped in 2010, leaving the company at risk if volumes on this route decline.
- Hanjin Shipping holds a large orderbook relative to many of its major competitors (the fourth largest in the top 10), with an additional 182,927 20-foot equivalent units (TEUs) of capacity awaiting delivery.

Opportunities

- Recent expansion into more niche, potentially high-growth, regions, notably Vietnam and the Latin America, may prove lucrative.

Threats

- Container lines have been unable to push through rate rises, which were the major reason behind the companies' revenue recovery in 2010.

Company Overview

Hanjin was formed in 1977 and in 1988 merged with **Korea Shipping Corporation**, becoming **Hanjin Shipping Company**. Until 2009, the company was part of the **Hanjin Group**, and has several subsidiaries, including **Keoyang Shipping**. Hanjin's previous German subsidiary, **Senator Lines**, discontinued its services in February 2009 as a result of deteriorating market conditions.

In September 2009, Hanjin Shipping Company split into two separate companies: **Hanjin Shipping**, which retained control of the group's core shipping businesses and terminal operations, and **Hanjin Shipping Holdings**, which manages the subsidiary operations including logistics and ship management.

The company is South Korea's largest shipping line, and is also diversified into the dry-bulk and liquid-bulk shipping markets, as well as having a terminal unit, Hanjin Pacific, which complements the carrier's box operations, boasting 12 dedicated terminals, including facilities at Long Beach, Tokyo, Kaohsiung, Busan and Cai Mep. The division is planning to open a new facility in Jacksonville.

The company has three regional headquarters, 200 offices and 30 local corporations.

In 2001 the CKYH Alliance was formed, with Hanjin joining **COSCO**, **K-Line** and **Yang Ming** to share capacity on key trade lanes. The alliance enables Hanjin to offer a broader coverage and express services, and the alliance has plans to jointly develop new terminals in the future.

Strategy

Hanjin Shipping holds its position within the top-10 global box shipping operators, holding a market share of 3.3%, according to AXS Alphaliner. The line is likely to hold its ninth position in the rankings, with Hanjin Shipping 30,019TEUs behind the eighth-placed COSCON and 19,571TEUs ahead of CSCL.

Routes Hanjin Shipping operates a highly diversified route portfolio operating on both the 'big money' markets of transpacific and Asia-Europe and the potential high-growth route of intra-Asia. The line is most heavily exposed to the transpacific, with the carrier operating 19 services on this route. On the Asia-Europe trade route Hanjin Shipping operates 15 services and on intra-Asia 12 routes.

In terms of volumes handled on Hanjin Shipping's services the transpacific still dominates, accounting for 47.98% of the total box volumes in 2010, with 1.78mn TEUs handled. Asia-Europe accounted for 32.4% of the total shipped in 2010, with 1.2mn TEUs carried on the route that year. Intra-Asia services carried a total of 579,123TEUs in 2010, accounting for 15.6% of the total volumes handled worldwide.

BMI believes that owing to the company's position, being based in South Korea, the line is well placed to further expand its coverage of intra-Asia, which is widely considered to be the mid-term growth driver for the container shipping sector. **BMI** notes that in the space of just a year intra-Asia is playing a greater role in Hanjin Shipping's box operations. In 2009 volumes carried on the company's intra-Asia services accounted for 13.75% of the total; in 2010 this had increased to 15.6%.

Fleet

Hanjin Shipping boasts a fleet of 108 ships with a total capacity of 512,746TEUs, according to AXS Alphaliner. The line is continuing its strategy of reliance on chartered tonnage, with the company's chartered fleet accounting for 53% of the total operating fleet, with Hanjin Shipping's number of owned vessels standing at 47%. This large percentage of chartered fleet enables Hanjin Shipping to implement a strategy of downsizing should a downturn hit, with the line able to return chartered vessels to their owners when their charters are up if the operating environment is not conducive. Lines with a high ownership ratio would be forced to lose money by laying up vessels in this situation.

Until now the vessels owned by Hanjin Shipping have been smaller in size than some of the ships it has chartered in. The company's owned fleet is heavily weighted toward vessels of 4,000-5,000TEUs, with the line owning 13 of these vessels, the smallest of which is 4,024TEUs. Hanjin Shipping operates five vessels with a capacity of between 5,000TEUs and 6,000TEUs, but its largest owned vessels are a fleet of seven 6,655TEU ships.

However, in June 2011 Hanjin announced that it would be buying five mega-vessels of 13,000TEU capacity for US$846mn. The order was originally placed by a company that intended to charter the vessels to Hanjin, but now the liner will be taking over direct ownership of the ships itself. The first ship is scheduled for delivery in Q112.

Financial Results

2011

Q1

In the first quarter of 2011 Hanjin recorded an operating loss of US$11mn, which the company attributed to the rise in fuel costs through the quarter on the back of Middle Eastern unrest, in addition to the downturn in Asia-Europe rates caused by overcapacity in the fleet. The container division made a net loss of US$28mn; the overall result was mitigated by the success of the bulk division in turning a profit. The loss in the container division was despite a rise in transport volume - 22.7% growth in the westbound transpacific trade, 23.3% in Asia-Europe and 39.1% in intra-Asia, underlining **BMI**'s view that intra-Asia shipping is the area to have exposure to in these straitened times.

2010

Hanjin Shipping's container operations' revenue increased by 52.4% year-on-year (y-o-y) to US$6.75bn in 2010 compared with US$4.4bn in 2009. The increase has enabled Hanjin Shipping to return to the black, with a full-year operating profit of US$532mn, following a loss of US$652mn, which the shipping line's container operations posted in 2009.

The recovery in revenue was driven by the global uptick in both volumes and demand in the container shipping sector. In terms of total volumes carried Hanjin Shipping's box levels shipped increased by 15%. The major driver of this increase was intra-Asia where volumes increased y-o-y by 30.7%; volumes on the line's transpacific services were also a factor, with a y-o-y increase of 17.55%.

The major driver of Hanjin Shipping's recovery, however, was the company's ability to increase rates. Again it was the rate increases on the intra-Asia that were the major driver in the recovery, which increased y-o-y by 88.45%

Y-o-y rates grew by 69.9%; Asia-Europe saw the greatest rate rise of 52% y-o-y, followed by the transpacific where revenue increased by 33%. Revenue from the carrier's Asia-Europe services and transpacific lines increased y-o-y by 84.5% and 61.3% respectively.

A threat highlighted by these results in **BMI**'s opinion is what does 2011 hold for Hanjin's Shipping bottom line? The company achieved its recovery mainly by rate increases. However, the company, like its peers, has struggled so far in 2011 to implement its planned rate increases, and with growth in volumes shipped y-o-y set to remain steady Hanjin Shipping's bottom line could also remain static.

We note that it was not simply the uptick in volumes and rates that enabled Hanjin Shipping to improve its financial position y-o-y. The firm has continued its strategy of slow-steaming, ensuring a saving on bunker fuel. **BMI** expects this strategy to continue as demand in the market for express services has not yet materialised.

Latest Activity

Hanjin To Join Mega-Vessel Owners' Club

In June Hanjin announced that it would be taking over direct ownership of five 13,000TEU mega-vessels it originally intended to charter from a company. The vessels are currently under construction and the first is scheduled for delivery in the first quarter of 2012.

Hanjin Shipping To Resume Far East To Middle East Service

Hanjin announced in June that it will resume its Far East-Middle East service from July 7 2011. South Korean shipbuilder STX and South Korean container line Sinokor have been

replaced by Japanese-based carrier NYK as the partner on the route. The current fleet of six 4,500-5,300TEU vessels will be replaced by 6,200-6,500TEU ships, of which five will be deployed by Hanjin Shipping and one by NYK.

Container lines' interest in linking Asia with the Middle East stems from growth in trade between the two regions. Traditionally Middle Eastern ports have featured as ports of call on Asia-Europe services, but with demand increasing specific Asia-Middle East services have been devised. Chinese trade with the Middle Eastern region increased by US$104bn between 1999 and 2009. In 2009 trade between the country and the Middle East reached US$112bn, a slight decline on 2008's figure of US$144bn, but a fall that can be explained by the global downturn in trade, with **BMI** projecting the previous 10-year growth pattern to continue.

Hanjin Shipping Expands Its China-India Service

Also in June Hanjin announced that it is to expand its China-India service with effect from July 10 2011. UAE-based **Emirates Shipping Line** (ESL) currently operates the Hyper Galex (HGX) route, which serves the major ports of northern and southern China and India on a weekly basis. Hanjin Shipping will charter slots of 500TEUs from July 10 2011, while in return Emirates Shipping will take the same number of slots from Hanjin Shipping's FMX (Far East-Middle East Express) service. The HGX service calls at the ports of Qingdao, Shanghai, Ningbo, Xiamen, Hong Kong, Da Chan Bay, Singapore, Port Klang, Nhava Sheva, Pipavav, Karachi, Singapore, Hong Kong and Qingdao. Industry observers believe the expansion could help Hanjin Shipping enhance its operational efficiency and help it capitalise on trade opportunities.

China Shipping Container Line (CSCL)

Strengths	▪ The company has been one of the fastest growing international liners of the past decade. ▪ Multimodal operations, with a container freight rail segment to capture goods from ocean to land transport. ▪ A large presence in China's domestic coastal shipping market, and is active at more than 30 ports in northern and southern China. ▪ Owned by the Chinese government; as such benefits from a strong relationship with the country's major banks, which are state-owned.
Weaknesses	▪ The large majority of China Shipping's routes are to and from China, which means the company's growth is dependent on the growth of the wider economy, and in particular, the strength of China's export sector. ▪ Whereas other major liners offer diversified businesses, CSCL operates in only one cargo market, the container market.
Opportunities	▪ The opening of direct shipping routes between China and Taiwan is driving long-term growth in CSCL's intra-Asia trade revenues, with several new ports added to the original quota of ports authorised to offer cross-channel links. ▪ The company aims to expand its operations on the Yangtze River. The river carries about one-third of China's coastal and inland trade, which makes it a good source of potential growth for shipping companies. ▪ The company is keen to expand its fleet capacity, taking on board a 14,000TEU vessel in 2011.
Threats	▪ The line faces growing competition in the intra-Asia market, with a number of rivals entering or expanding their exposure to what is considered to be the major medium term box shipping growth market.

Company Overview

China Shipping Container Line (CSCL) was established in 1997, and is part of the **China Shipping (Group) Company** (CSG). The company is controlled by the Chinese government.

China Shipping became a company with limited liability in 1997, and in June 2004 it listed 2.4bn overseas public shares on the Hong Kong Stock Exchange. In late 2007 it issued 2.3bn domestic public shares on the Shanghai Stock Exchange.

The company is registered in Shanghai and is involved in owning, chartering and operating container vessels. It has several subsidiaries, including container storage and transport firms **Yangpu Cold Storage**, of which it acquired 60% in 2008, and **Yangshan International**, in which it acquired a 25% stake also in 2008.

CSCL operates domestic coastal routes and international container line services from China to Japan, South Korea, South East Asia, Europe, the Mediterranean, the US, West Africa and the Persian Gulf. The carrier is a dominant player in the Chinese freight market.

The company also operates multimodal transport, including a container railway line, **China**

Shipping No. 1, which transports ocean-going goods by land to key Chinese markets, and is a majority shareholder in a number of domestic container terminals.

Strategy

CSCL continues to hold its position in the top 10 global container shipping with a market share of 3.2%, according to AXS Alphaliner. The line is likely to retain this position, as it is 17,151 twenty-foot equivalent units (TEUs) behind its nearest rival, **Hanjin Shipping**, but 79,306TEUs ahead of **MOL**.

Routes

CSCL has developed a portfolio of services on the 'big money' routes, operating seven Asia-US services, three transpacific and four services to US East Coast ports. The line, while not publishing its exact intra-Asia route network, is exposed to the intra-Asia trade route, offering a China-Philippines service from March 2011. **BMI** expects the line to increase its exposure to intra-Asia over the medium term, with the route considered by the industry to offer high growth potential.

Another service area CSCL is involved in, which in our opinion also offers high growth potential, but does not have the same levels of competition with the major global players, is Chinese domestic maritime trade.

CSCL subdivision **China Shipping Domestic Containers Transportation Division** is China's main domestic shipping player. Its fleet has a capacity of more than 500,000TEUs. The division closely cooperates with road and railway to ensure complete coverage. It offers four domestic main route services, six domestic sub-route services and coverage of the Yangtze River, a major shipping growth area in **BMI**'s opinion, as China's factories move further inland and require longer supply chains.

Fleet

CSCL has the 10th largest fleet in terms of capacity, according to AXS Alphaliner, with 496,713TEUs of capacity and 141 vessels. The fleet's dynamics are heavily weighted to ownership, a strategy it shares with fellow Chinese shipping line **COSCON**, suggesting that China's strategy in wishing to increase its merchant maritime fleet (a trend we have seen in the liquid bulk sector) has trickled down to the box shipping sector. CSCL's ratio of owned to chartered vessels stands at 60.8% owned and 39.2% chartered, and CSCL operates the highest owned percentage of total fleet in the whole of the top 10. CSCL's owned fleet comprises 75 vessels, with a total capacity of 301,790TEUs, while its chartered fleet stands at 66 vessels, with a capacity of 194,923TEUs.

In terms of capacity, CSCL's fleet is dominated by tonnage with a capacity of 3,000-5,000TEUs. It operates 38 vessels with this capacity. It is continuing to increase its fleet with larger capacity vessels. CSCL currently operates 10 vessels with capacities of 8,000-9,000TEUs and eight vessels with a capacity of 9,000-10,000TEUs. At the beginning of 2011 the line joined the ultra large vessel club, taking on board the 14,074TEU CSCL Star, which operates on the Asia-Europe trade route.

CSCL appears keen to continue increasing its fleet of larger vessels, indicating that the line wishes to continue if not increase its presence on the Asia-Europe trade route. Seaspan Corp was reported in February 2011 to be looking to order 10 vessels of 10,000TEUs from

South Korean or Chinese yards, with the plan of chartering them to CSCL and Germany's **Hapag-Lloyd**. The vessels are due to be delivered in 2013-2014.

CSCL is also keen to expand its owned fleet. According to AXS Alphaliner, CSCL's orderbook currently stands at 13 vessels, with 107,970TEUs of capacity, equating to 21.7% of the current fleet.

Financial Results

2010

CSCL, like many container shipping lines, saw a huge reversal of fortunes in 2010, as the world emerged from the global economic crisis. Its revenues rose by 76.3%, from CNY19.74bn in 2009 to CNY34.81bn. The profit/loss for the year attributable to equity holders went from a loss of CNY6.45bn in 2009 to a profit of CNY4.21bn in 2010.

In terms of volumes carried, CSCL handled 6.9% more boxes in 2010 than in 2009, up from 6.74mn to 7.21mn. The greatest gainer was the Pacific trade lanes, which grew 19%.

Latest Activity

Mega Vessel Berths At Jeddah, Showing Port's Capabilities

In June 2011 the Jeddah Islamic Port, which is on the Red Sea coast and is Saudi Arabia's biggest container port in terms of box handling, received one of the world's largest container vessels, the CSCL Star. **BMI** notes that the arrival of the ship emphasises that Jeddah has become a leading container port. We believe the port will continue to develop as Saudi Arabian imports grow.

The CSCL Star, constructed by Samsung Heavy Industries, was delivered in February 2011. It has a capacity of 14,074TEUs, making it one of the largest vessels afloat. **BMI** notes that the vessel, one of an order of eight by the Chinese carrier, reflects a trend we have been following of shipping lines ordering ever-larger vessels in order to benefit from the economies of scale they provide. The CSCL Star has a draught of 14.5 metres (m), making it the biggest ship to be accommodated at Jeddah Islamic Port so far.

CSCL Expands Fleet

In May 2011 CSCL received a 14,074TEU vessel from South Korea's Samsung Heavy Industries, Steel Guru reports. The vessel, the firm's second in a series of eight, has been valued at US$170mn. The CSCL Venus will be deployed on the Far-East/Europe route AEX 1/CEM with the CSCL Evergreen.

CSCL, UASC Agree To Slot Swap Deal

In May 2011 CSCL agreed with the United Arab Shipping Company (UASC) a slot swap deal for their Asia-Europe services. The deal will cover 500 slots a week, with CSCL's AEX7 service and UASC's AEC2 service involved. The agreement was to take effect from May 20 2011.

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