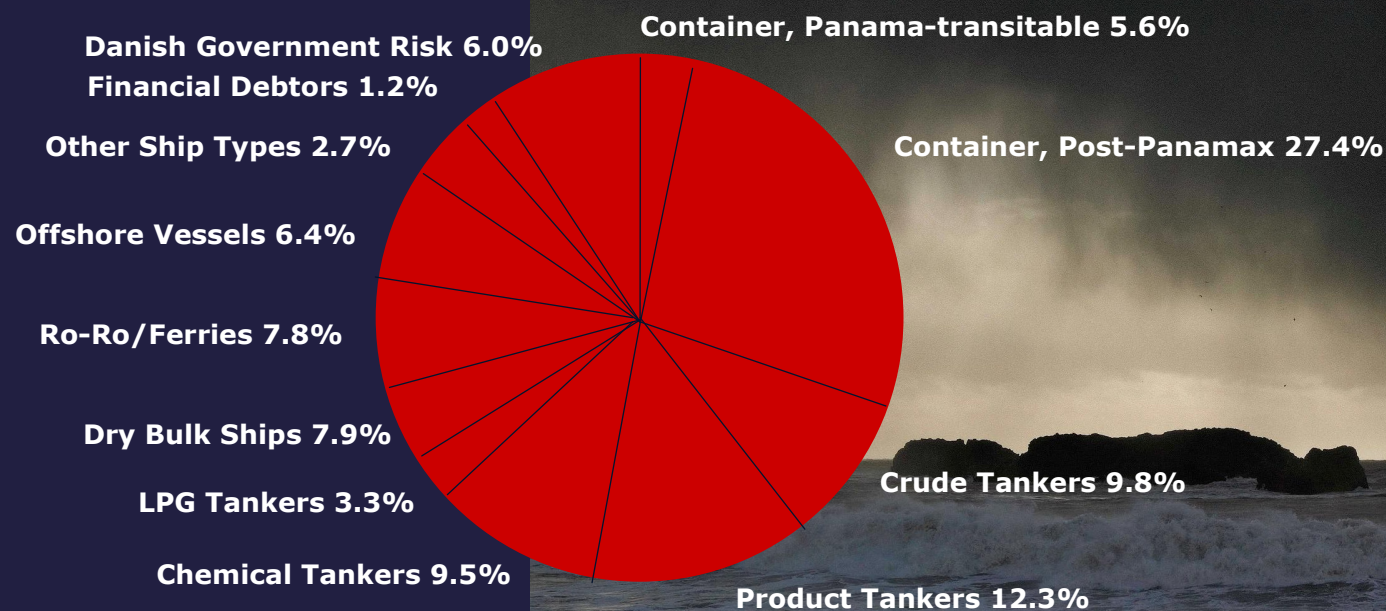


SHIPPING MARKET REVIEW – 1ST HALF 2005

DSF loan portfolio by shipping segment As of June 30th 2005



ISSN 1604-2816



**Danish
Ship Finance**

Please read carefully the disclaimer at the end of this research report.

This report reviews the central developments in the period from January to June of 2005 for the main shipping segments in which Danish Ship Finance (DSF) has exposure.

General Review & Outlook

In the early months of 2005, almost every singly ship segment experienced rising ship prices, and if not rising freight rates, then still freight rates at extremely healthy levels.

But, as 2nd quarter of 2005 ran its course, reality set in for most of the larger ship segments when freight rates began to level off or fall dramatically. Subsequently, ship prices began to drop – although so far only slightly.

The recent developments mark a significant shift in market direction and confidence, and should be noted with great respect. Although we believe, the shipping markets are far from crashing anytime soon, we nonetheless believe it marks the definite end of a fantastic three-year period of almost relentlessly rising ship prices and record-high freight rates.

For some few ship segments, particularly the offshore supply vessels, there may indeed be upside left, but for the bulk of the shipping segments, the next years may most likely be characterized by a downward trend.

The world economy currently is overflowing with structural imbalances, bottlenecks and constraints that need to be worked out before shipping again will experience demand growth rates similar to those experienced during the recent three-year period.

In the US economy, there is a structural need for higher savings and lower consumption to counter the growing current account and trade deficits, at the same time as there is a need for reducing the federal budget deficit. Also, we cannot expect the monetary policy to be highly accommodative or real estate prices to maintain their upward trajectory. All of this is bound to have a negative effect on long-term consumption growth and thus on long-term container import growth.

In China, the amazing inflow of foreign capital along with the extreme trade surpluses have led to a similarly amazing growth in fixed asset investments and manufacturing capacity. Without the simultaneous closure of state owned enterprises, it has caused an apparent oversupply of manufacturing capacity leading to an underlying deflationary pressure on consumer prices. At the same time, the Chinese population is reluctant to consume because of fears of future pension benefits and loss of job. These problems are not solvable by increased exports, but instead must be solved e.g. by encouraging the consumers to consume more and save less, revaluing the Renminbi against the USD, and by cutting back on excess production. These measures will most likely have a dampening effect on the long-term growth rate of the raw material imports, but a beneficial effect on imports of consumer goods and thus on container imports.

The bottlenecks are particularly obvious in China's over-stretched infrastructure, which in all its shapes – roads, railways, harbours, utilities, etc. - is running above its sustainable capacity, thereby hampering economic growth, leading to increased production costs and squeezing manufacturers' profits. Additionally, the large ports inside and outside China, which handle dry bulk commodities, are showing clear signs of congestion. But, the dry bulk port congestion has so far *not* been a serious deterrent to demand growth, but merely led to sky-rocketing dry bulk freight rates, further adding to production costs.

Lastly, but not least, the extreme growth in basic raw material consumption (oil, coal and iron ore) for the last three years has by now pushed output to its outmost bounds, thus demanding great investments to increase output in future years. As there is a time lag from investment to actual output, we may in coming years experience relatively low supply growth, leading to lower demand growth for ships and most likely to much lower port congestion as the ports will have sufficient time to catch up with demand.

As the global economy is still showing robustness, and as many of the above issues will only lead to subtle and drawn out changes, shipping is not to be severely affected by them, but will instead feel them through relatively lower demand growth in coming years ■

Executive Summary

- *Ship Building:* Newbuilding prices have probably peaked and contracting activity is down. Within the next 12 months, the yards need a significant and highly unlikely, pickup in contracting volumes in order to keep prices from falling too steeply.
- *Container Ships:* Demand for containerized imports to the Western nations is showing signs of a slowdown, causing freight rates per teu on the large head-haul routes to tremble. In future years, the growth rates of containership supply and demand imply lower fleet utilization.
- *Crude Tankers:* The peak is behind us, as a much lower oil output growth has taken the steam out of the market. Nonetheless, ship prices have continued up. The outlook for 2nd half 2005 spot earnings are still very positive, but the longer-term outlook looks increasingly troubled.
- *Product Tankers:* Western hemisphere inventory surplus and Asian inventory deficit, combined with high global refinery utilization supported a strong trade in refined oil products. Contracting of newbuildings is markedly up, but prices may have peaked. The short-term outlook for freight rates is still positive.
- *Chemical Tankers:* High fleet utilization and robust global demand for chemicals supported a high spot market, and led the term charter rates to record highs. The short-term outlook continues to be positive, but a large orderbook and a slowdown in global economic growth may impact freight rates negatively in the longer run.
- *LPG Tankers:* Large LPG tankers have experienced a large setback, but medium and small LPG tankers are still in record territory. Contracting volumes have exploded, keeping newbuilding prices from falling and leading secondhand prices to rise substantially.
- *Dry Bulk Ships:* The negative consequences of a global steel overproduction is beginning to be felt throughout the dry bulk sector, leading to de-stocking and falling freight rates. Earnings are still expected to remain at healthy levels, but much rests on China to behave well disciplined.
- *Car Carriers:* Tight charter market pushes charter rates further up and contracting of newbuildings continue albeit at lower levels. A large orderbook may have an impact on charter rates but an old fleet may counteract a large drop in fleet utilization.
- *Ro-Ro/Ferries:* Still tight market with lack of suitable tonnage drives charter costs up and some routes to close. Newbuilding and secondhand prices are markedly up, thereby proving as a deterrent to further newbuilding contracts.
- *Offshore Support Vessels:* An exceptionally strong offshore market as rig operators scramble to secure the required number of ships for their drilling campaigns. Ship values are up and contracting of new ships continues unabated. The short-term outlook continues to be remarkably good.

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Ship Building

Newbuilding prices have probably peaked and contracting activity is down. Within the next 12 months, the yards need a significant, and highly unlikely, pickup in contracting volumes in order to keep prices from falling too steeply.

CONTRACTING PRICES

Small correction, the start of a slow descent or of a collapse?

Contracting prices for every single type of merchant ship are now 8-11% higher than 6 months ago, and an astonishing 35-90% above the low levels of 2002.

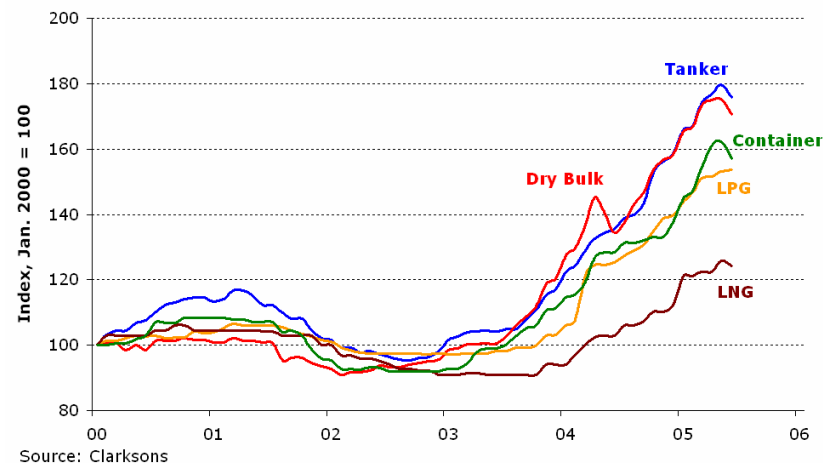
But, prices seem to have peaked in late April, having fallen by 1-3% since then, according to data from Clarksons. This is the first real reduction since the remarkable ascend began in late 2002.

Although prices on heavy grade steel plates for ship construction have dropped ever so slightly from recent record levels, we do not suspect this to be the only nor the primary explanation behind the drop in newbuilding prices.

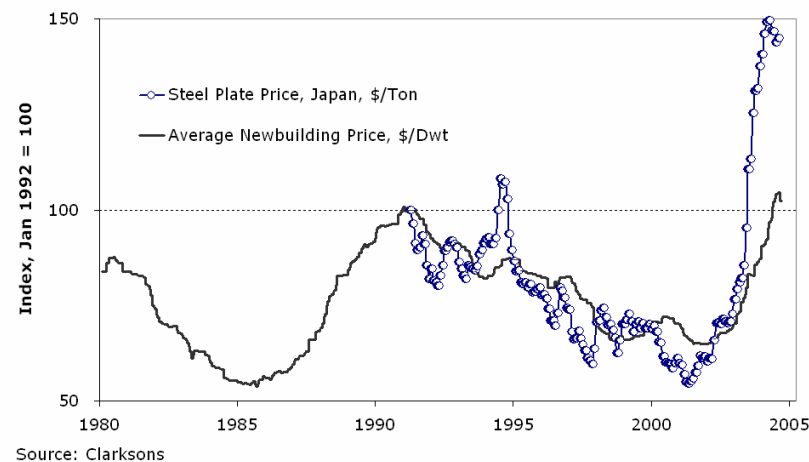
Instead, the recent price reduction may merely be an indication of price reductions in order to make the shipowners accept the longer delivery times, and not an indication of a serious shift in market sentiment, as of yet. From 1q05 to 2q05, the average weighted delivery time has increased from 3.2 years to 3.3 years in (see top graph on page 5).

Nonetheless, still more signs point in the direction that the recent fall in newbuilding prices is more than just a mere short-lived correction. Compared to 6 or 12 months ago, steel prices generally are beginning to show signs of wavering, ship contracting volumes are down, and most importantly, most of the large shipping freight markets are showing distinct signs of slowing demand growth, leading to less demand for new ships at record price levels.

Newbuilding Average Price Index



Steel and Newbuilding Prices



CONTRACTING ACTIVITY

A contracting slowdown is detected at last

Despite ever increasing prices and ever longer delivery periods, the fear of too little shipyard capacity, too much cash lying idle in the bank accounts, and over-optimistic expectations of future demand growth, all seem to have driven the shipping companies into continuing their buying spree of new ships.

Fortunately for future freight rate levels, the overall contracting level is somewhat down, but is still above the historic average. In 1st half 2005, around 42 million dwt of new orders have been contracted, according to Clarksons' data. This is 19% down from the contracting volumes during 1st half 2004, and 14% down from the contracting volumes during 2nd half 2004.

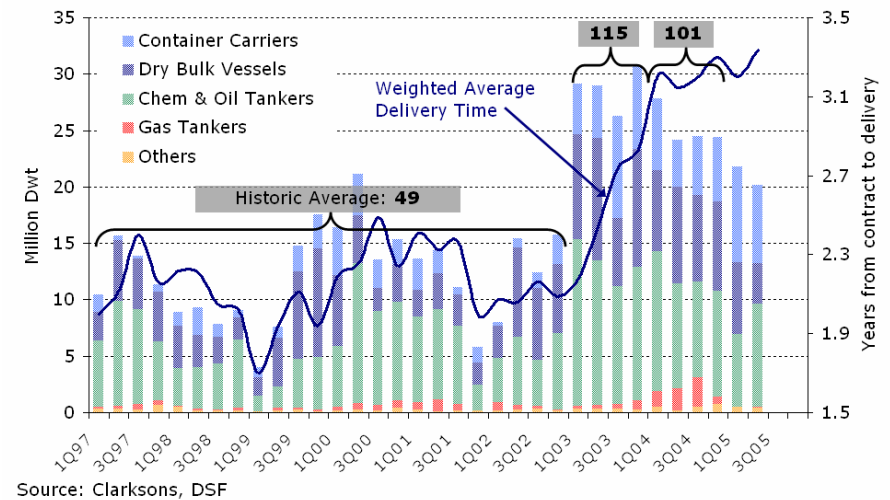
Yes, it is indeed almost impossible to find shipyards capable of delivering within 1½-2 years, and for specific ship types such as large containerships, it may furthermore be very difficult to find available shipyard space with delivery before sometime in 2009. But, for other ship types, it does *not* seem to be just as difficult to find earlier delivery (see the four graphs on page 7).

In particular Japanese yards seem to be running low on dry bulk orders with delivery as early as 2007, and almost every of the other large shipbuilding nations to a large extent seem to be short of tanker and dry bulk orders for 2008 delivery.

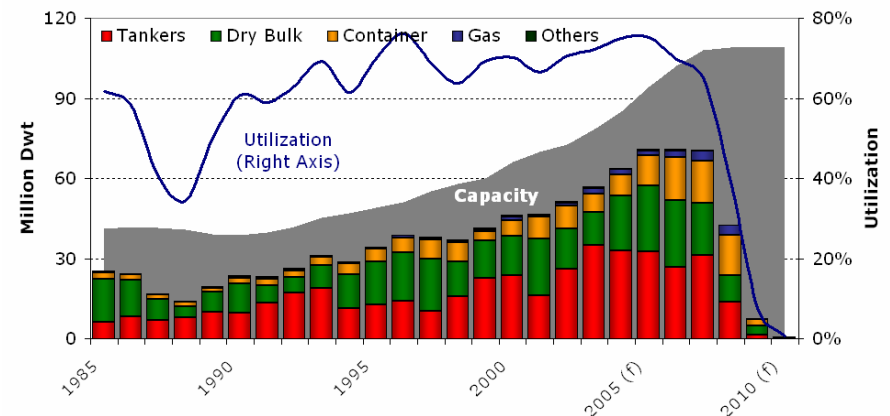
Please notice, that in particular the Japanese figures on uncommitted shipyard space may be somewhat unclear, as the Japanese yards may be holding space for the use of domestic shipowners.

Conclusively, the urgency and anxiety which seem to have caught hold of the shipowners, leading them to commit to ever increasing delivery times at record prices, at the moment seem to be somewhat unsubstantiated. Although, in the segments of the LNG tankers and the very large containerships there is still a real strain on yard capacity, which in part could vindicate the shipowners for paying such high prices.

Merchant Ship Contracting and Delivery Time



Total Shipyard Capacity, Output and Utilization
(given present orderbook and fleet)



Total shipyard capacity is measured as the sum of every individual shipyard's historic maximum annual dwt output for every shipyard in operation at the given year.
Source: Clarksons, DSF

OUTLOOK

Shipyards are slowly losing their pricing power

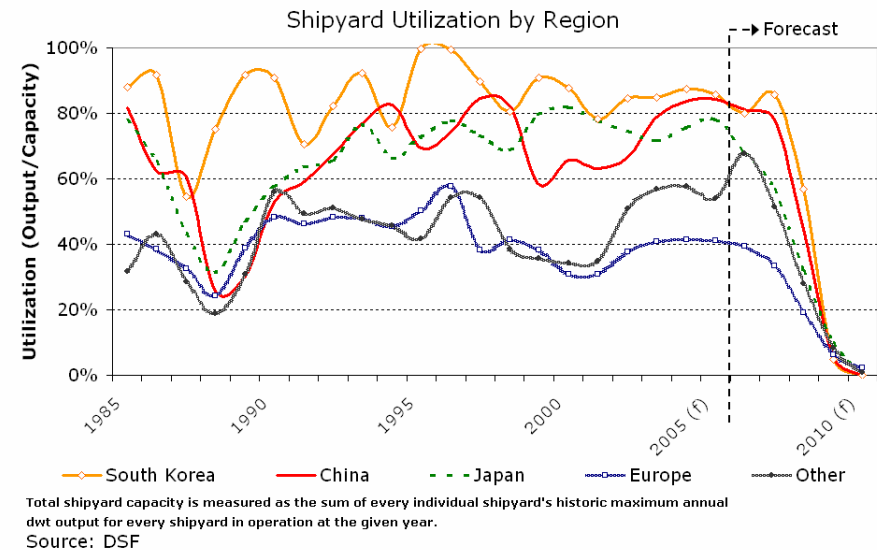
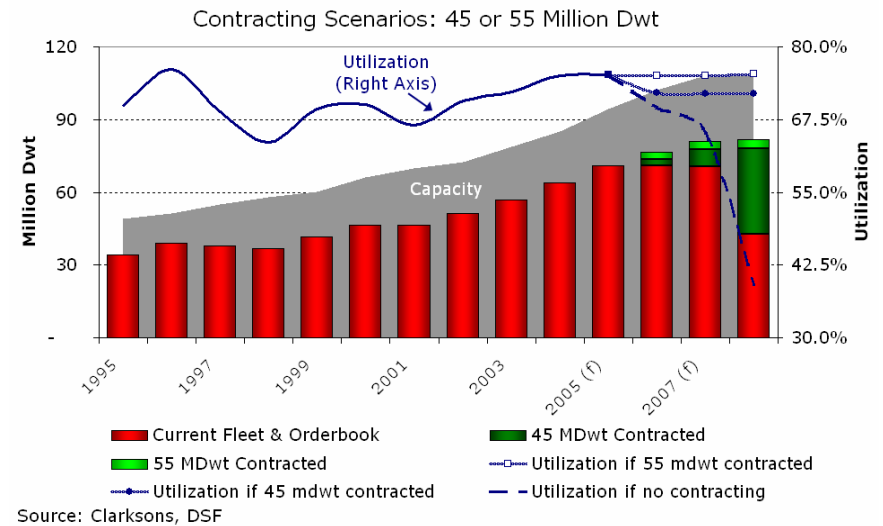
During the coming 12 months an extra 45-55 million dwt of newbuilding contracts are as a minimum needed in order for the shipyards just to maintain their overall degree of utilization until 2008. As the latest 6 months have provided the yards with 42 million dwt, almost the same volume over twice as long time should not be a great problem for the yards.

But, in order for the yards *also* to maintain their forward cover of at least 3 years until 2009, the yards will have to secure an additional 70-75 million dwt during the same 12 months. In total, it adds up to a requirement of at least 115-130 million dwt of new orders during the coming 12 months in order for the shipyards to maintain their forward cover and implied pricing power.

Compared to the record 100-115 million dwt contracted a year in 2003-2004, 115-130 million dwt for the next 12 months are without a doubt completely unattainable in the current environment of an already massive orderbook, wavering freight rates and record high newbuilding prices.

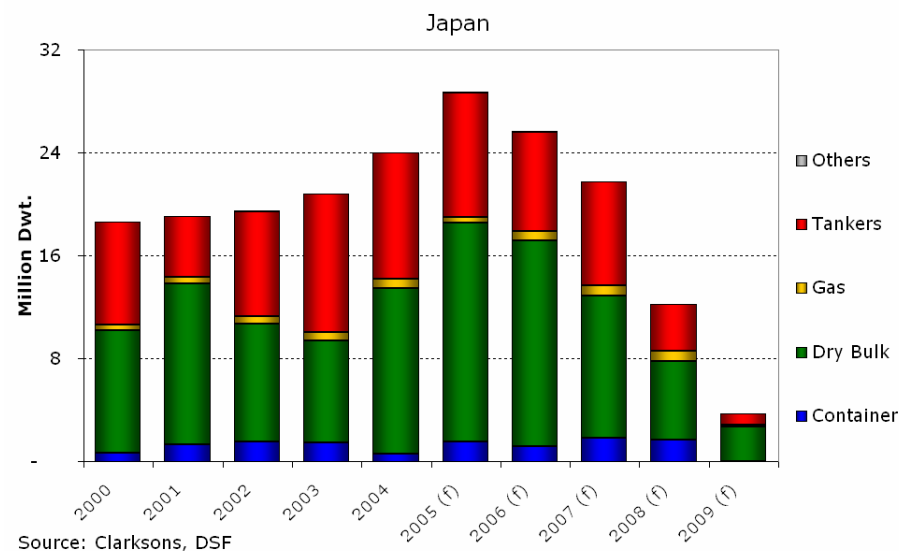
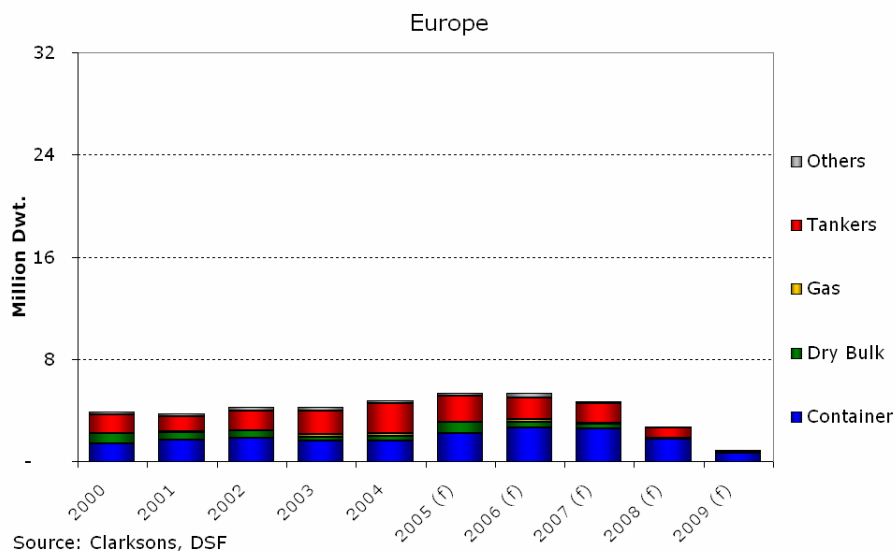
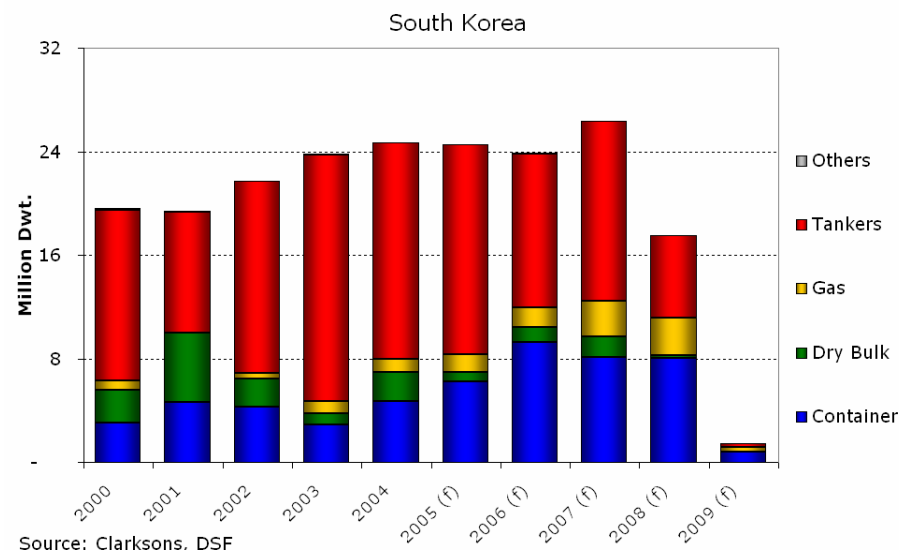
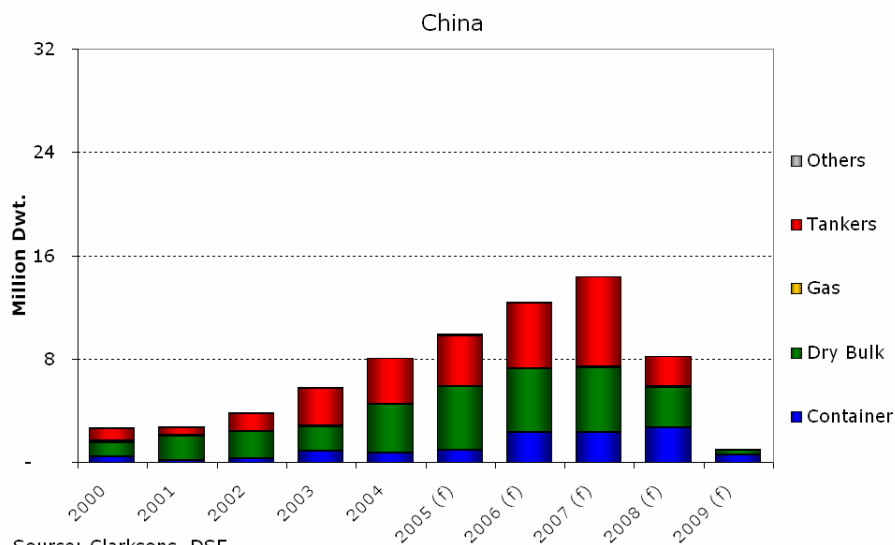
Instead, toward the end of the coming 12 month period, we may expect to see the average delivery period shortening significantly, and, as new orders fail to live up to the continuously growing global shipbuilding capacity, that shipyards find it increasingly difficult to maintain the current high capacity utilization. Thus eventually, as the shipowners and shipyards come to the realization of this pending imbalance, newbuilding prices may most likely fall more violently than experienced in recent months.

Even despite the unlikely scenario that ship plate prices should continue to rise strongly, the growing competition among the shipyards to secure a full orderbook may most likely lead to depressed margins and falling newbuilding prices ■



Current Fleet & Orderbook by Region of Build and Year of Delivery

(Excludes allowances for possible slippage from scheduled delivery dates)



Container Ships

Demand for containerized imports to the Western nations is showing signs of a slowdown, causing freight rates per teu on the large head-haul routes to tremble. In future years, the growth rates of containership supply and demand imply lower fleet utilization.

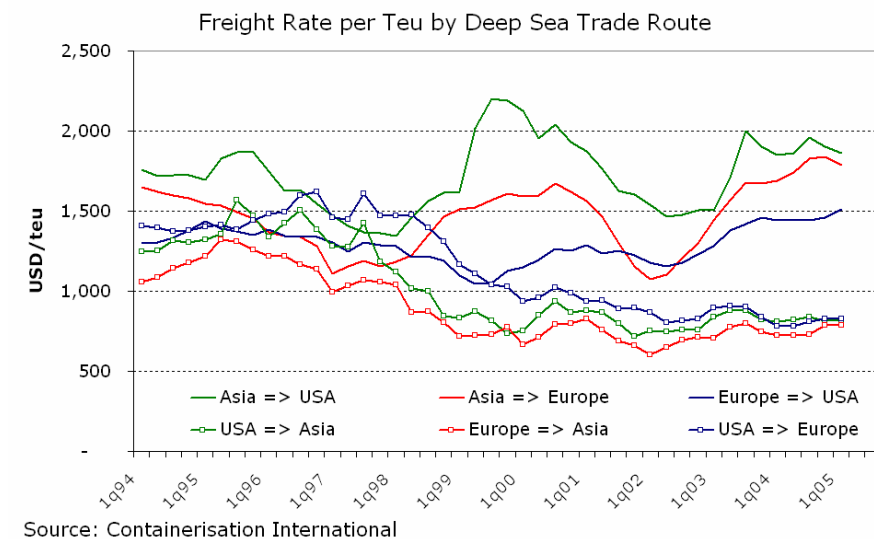
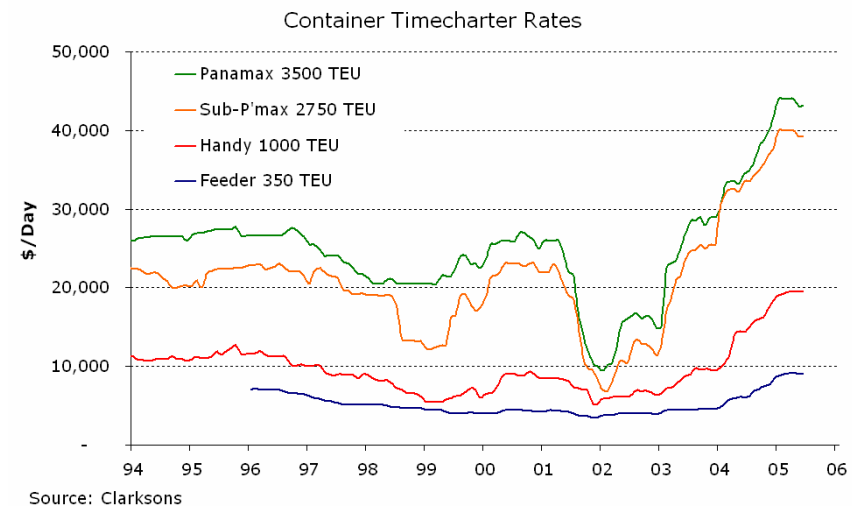
FREIGHT RATES

Payment per box has fallen, but T/C rates are notably up

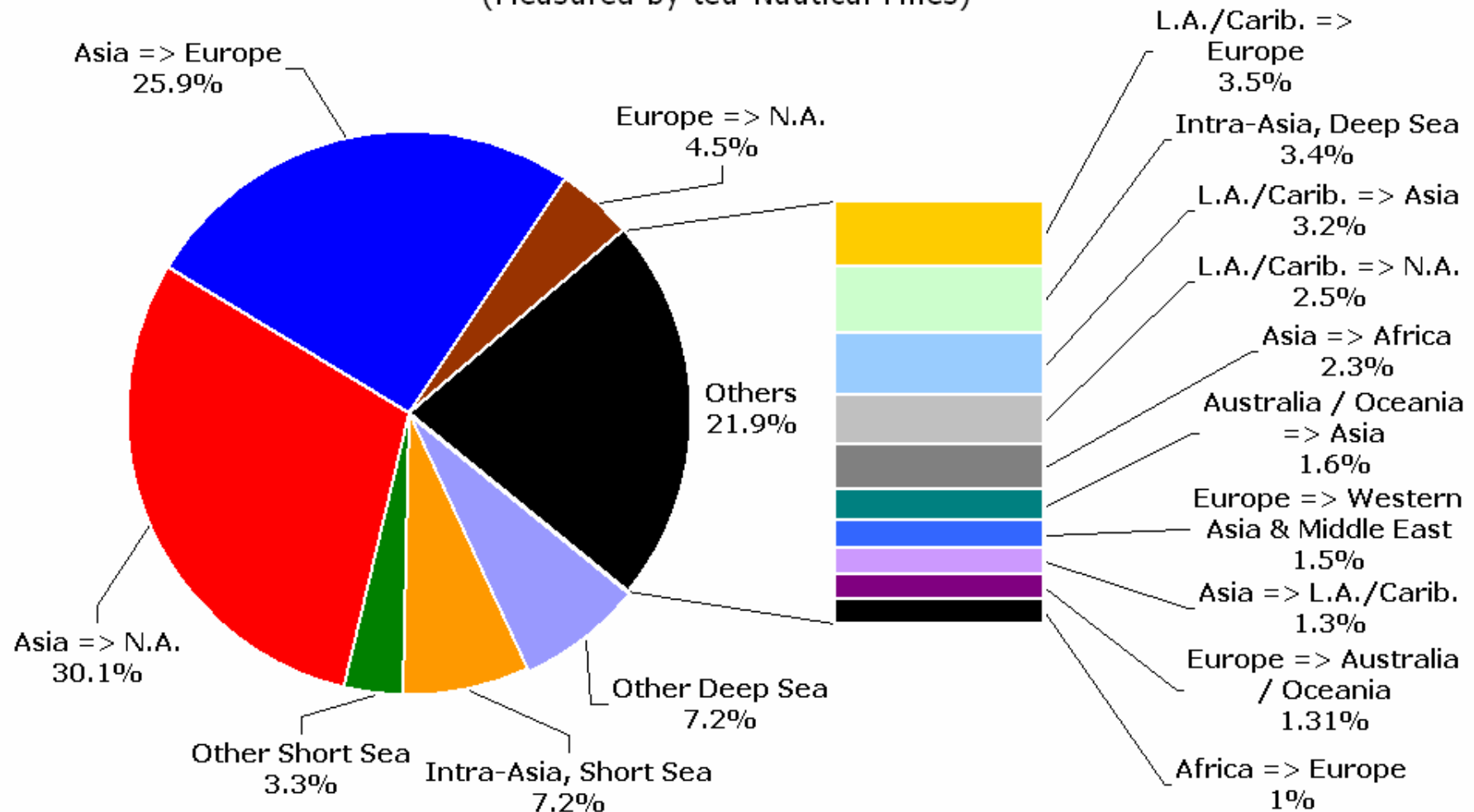
Timecharter rates for the containerships on the charter markets (generally smaller than 4,000 teu) have continued markedly upwards during 1st half of 2005, but now seem to show a levelling trend. As the availability of promptly vacant vessels is still extremely low, the recent softening in timecharter rates could to a limited extent be a sign of rate discounts in exchange for longer running charter periods. But, as the average fixture period has continued to fall from around 3 years duration in February 2005 to around 2 years by May 2005, the recent levelling in charter rates may to a greater extent be a sign of a change to the worse in market sentiment.

Conversely, freight rates per teu in 4q04 and 1q05 on most of the large deep sea trade routes showed budding signs of increased competition among the containership operators, naturally leading to stable or falling freight rates (note that graph to the right, below ends at 1q05).

The levelling or fall in freight rates per box on the large deep sea routes comes despite significantly rising operating costs for the containership operators, and could thus imply that the competition among the containership operators has risen more than previously expected. Rising charter costs, bunker costs, canal fees, terminal charges, repositioning costs, container prices and congestion problems have meant persistently rising operating costs for all container carriers. Fortunately for the carriers, the ship utilization is still much higher than in 2002, providing the carriers with higher revenue per ship and good financial performance.



Total Head-haul Container Trade in 2004 by Route (Measured by teu-Nautical Miles)



Source: Global Insight, DSF

SUPPLY & DEMAND

Port congestion may have forced ahead seasonal peak trade

According to figures from Drewry and the Japan Maritime Development Association, global port handling of containers in 1q05 was up by around 11.8% over the corresponding period of 2004. This is a slowdown from the average annual growth in global port handling for 2004 of 13.4%.

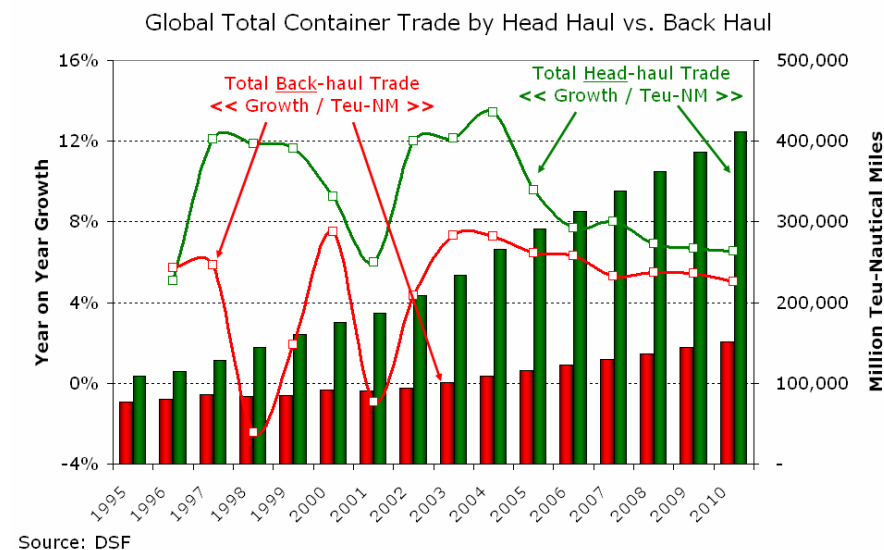
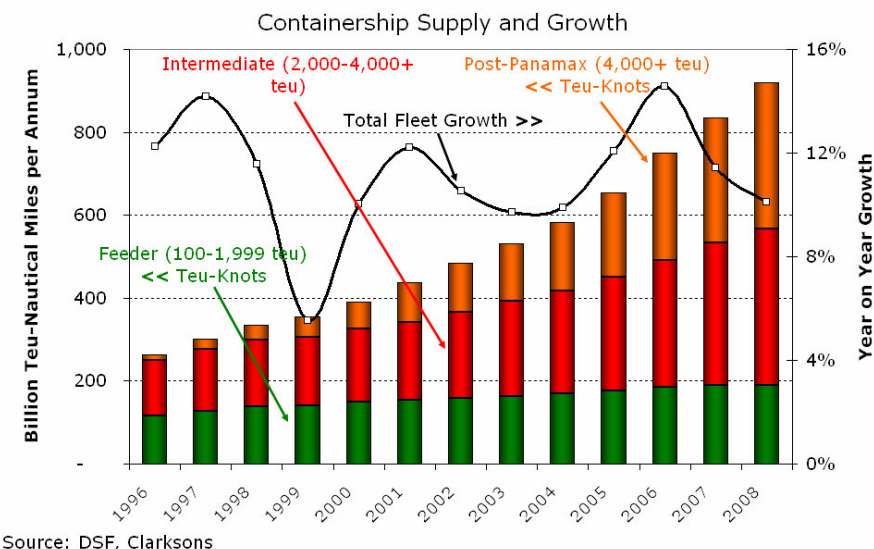
Compared to the year-on-year growth for the 1st quarter of 2005, preliminary figures for 2nd quarter global port handling imply a pickup in year-on-year growth. But, whether the basis for the higher growth in the 2nd quarter is based on solid economic fundamentals or on temporary issues is still unclear, we believe.

We suspect, that in order to avoid the horrific situation from last year when congestion caused significant delays and large build-ups of ships particularly at the US West coast container terminals, the big retailers this year have opted to have a part of their cargo transported ahead of the usual peak season running from July to November, thus boosting 2nd quarter trade growth to the detriment of 3rd and 4th quarter growth.

At the very early stage of the peak season, Californian ports reported of non-existing congestion, and although the evidence is still sketchy it still tells a tale of lower trade growth compared to last year.

2005 has so far been marked by geopolitical developments, which unfortunately may have long-lasting negative repercussions for the growth in world seaborne containerized trade. The fear of globalization and outsourcing of western jobs to low-cost countries, manifested by the Chinese export boom, has particularly in the USA and in the EU gathered momentum, and in some instances led to actual trade restricting measures.

In the USA, Chinese clothing imports, including man-made fiber shirts, blouses, cotton trousers, knit-shirts and a range of underwear, will now be subject to quota limits, allowing the imports in these products to grow by 7.5% over a 12 month period.



Similarly, the EU has entered into an agreement with China, which allows for gradually rising caps on increases in Chinese textile exports to Europe over the next three years, with all limits to be done away with in 2008.

In 2004, Chinese manufactured apparels, i.e. not only textiles, only made up 6-7%, measured in teu-nautical miles, of total Asian containerized exports to North America and Europe. The importance of Chinese textiles exports on total demand for containerships is thus largely insignificant. Nonetheless, the overall signal from the European and American politicians is thus of great importance, as it signals that at least for now an undefined threshold for Western outsourcing may have been reached, thereby limiting the likelihood of future growth-spurts in global containerized trade.

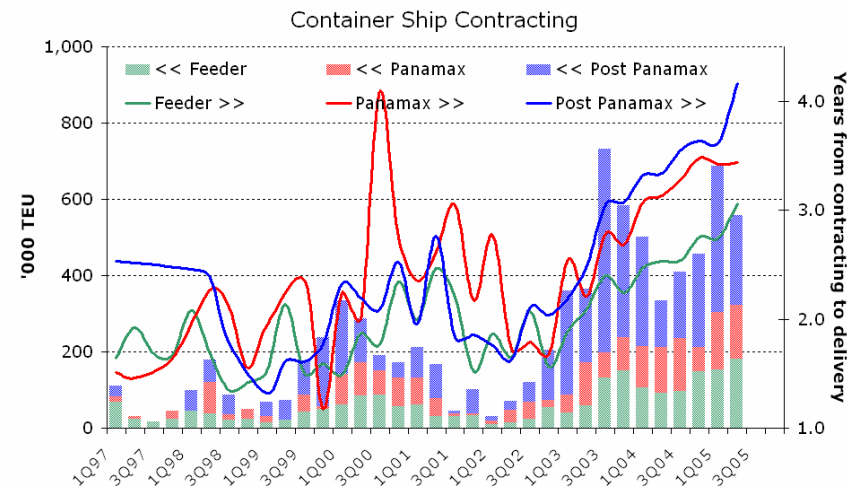
CONTRACTING & SHIP VALUES

Second highest contracting volumes, and prices continue up

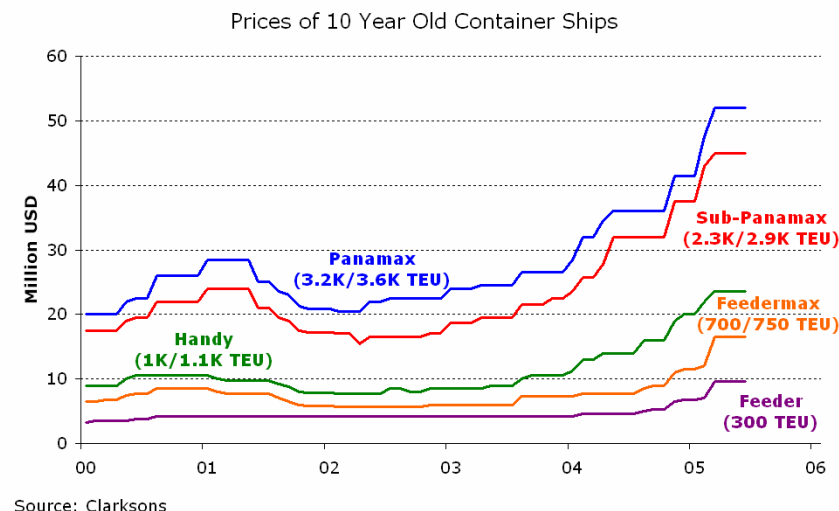
Completely disregarding the fact that the orderbook already at the turn of the year represented a worryingly 50% of the fleet, containership owners contracted the second highest volume of new ships during the first six months of 2005. With a total of 1.2 million teu contracted during 1st half of 2005, it is only 5% less than the record from 2nd half 2003, according to Clarksons' data.

The combination of an absolute fear of not having enough shipyard capacity and highly optimistic expectations for the future demand growth has propelled the containership companies into a frantic buying spree, thereby providing the shipyards with ample ammunition for newbuilding price hikes on top of already elevated levels.

In the very short time span from December 2004 to June 2005, newbuilding prices have risen by around 12-18%, and secondhand prices of 10 year old container ships have increased a remarkable 15-45%, according to figures from Clarksons.



Source: Clarksons, DSF



Source: Clarksons

OUTLOOK

Distinct demand slowdown ahead, but fleet growth is up

Unfortunately, the outlook for the supply and demand balance does not bode well for the future freight rate levels.

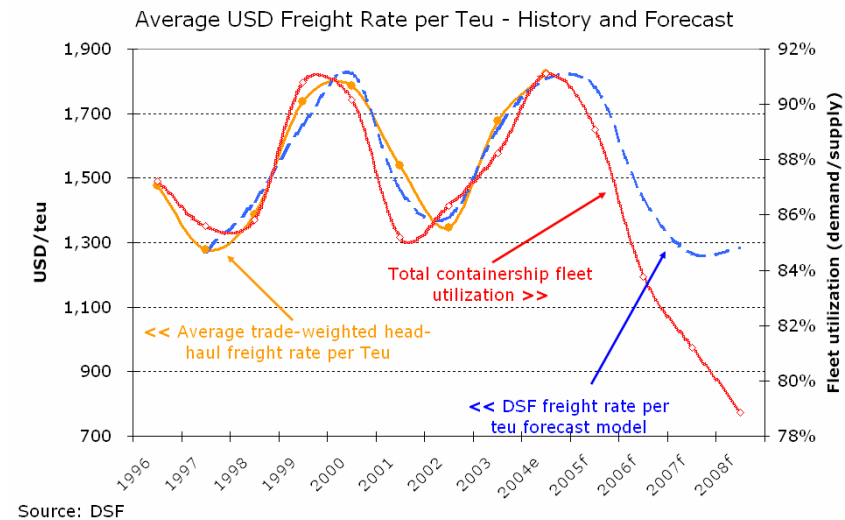
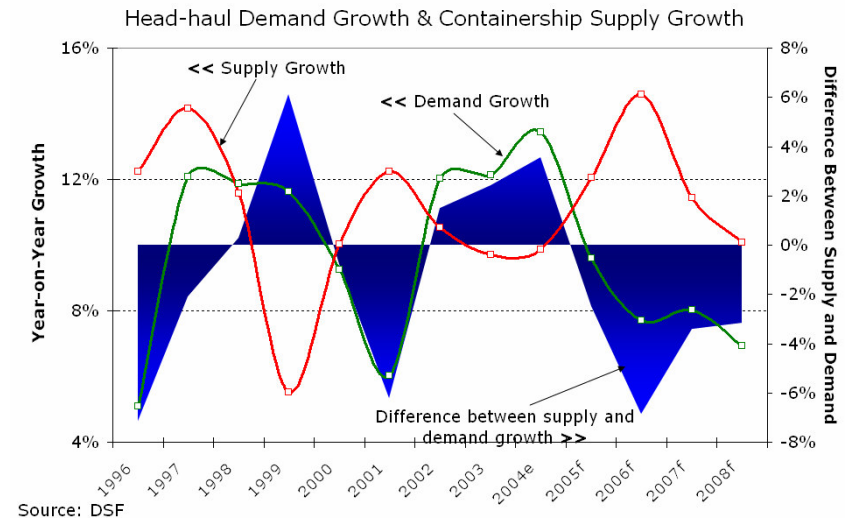
We expect overall demand for containerships, measured in teu-nautical miles, to grow by around 10% in 2005, down from 2004's record 13.4% growth. In 2006-2007, overall head-haul growth is expected to be even less (8%), followed by a further slowdown in 2008 (7%).

On the contrary, overall containership fleet (fully cellular containerships and multi-purpose ships) is expected to grow by 12%, 15%, and 11% in 2005, 2006 and 2007, respectively, measured in teu-knots. For 2008, the orderbook already presages a 10% growth. Supply is therefore set to outpace demand by a large margin in every single year for the next 3-4 years.

The future fleet growth is indeed impressive, and for the future containership market it implies a much lower utilization of the containership fleet, leading to a higher degree of competition among the containership companies, naturally followed by a clear down-revision in freight rates per teu, particularly in 2006-2007.

In the short run, the expected slowdown in trade growth first and foremost reflects a slowdown in consumption growth in most of the Western world, particularly caused by high(er) oil prices that reduce the business' and households' purchasing capability, and also by stable or rising interest rates, which cause real estate prices to slow down or even fall with direct effect on private consumption, and furthermore promotes higher savings rates.

On account of the very loose monetary policy ever since 2002, leading to falling interest rates and rising real estate prices, the US house owners increased their mortgage borrowing by USD 223 billion in 2004. According to the US Federal Reserve, half of this was used for immediate consumption. Put differently: About 40% of the increase in US consumption in 2004 originated from increased home owner debt – a feature which cannot be repeated to the same extent in 2005 or 2006 in the face of rising or stable



interest rates and a slowdown in the house price growth.

In most of Europe in 2003, 2004 and 2005, much similar figures for increased debt and consumption growth can probably be found.

Luckily for China, the significant loosening of the global monetary policy and following consumption binge in the western world came at a time when China was liberalizing its economy, thereby providing the western world with a considerable opportunity to expand manufacturing and consumption *without* hitting serious bottlenecks that creates extraordinary wage pressures and immediate inflation, thereby prolonging the period of low interest rates and the period of high consumption and import growth in the western world.

I.e. what many believe has been trade growth driven almost purely by the relocation of manufacturing from Europe and North America to labour-rich and cost-competitive China, it to just the same extent can be explained by a consumption binge by the European and American consumers led by very low interest rates.

The negative consequences of a high production growth, such as large-scale bottlenecks and inflationary pressures, which the Western world to a large extent failed to experience in 2003-2004, partly because of outsourcing to China and Eastern Europe, are now showing its ugly head in China.

The bottlenecks and subsequent cost increases are particularly obvious in China's over-stretched infrastructure, which in all its shapes – roads, railways, harbours, utilities, etc. - is running above its sustainable capacity. In addition to the above significant restraints, concerns over an over-exploited environment and concerns over labour welfare are beginning to be ever more strongly voiced in China. Furthermore, within a number of sectors the access to reliable labour with the right qualifications is also diminishing fast, leading to poaching and wage escalation.

Manufacturers already in China, and Western manufacturers

considering to relocate to China, are thus facing increases in production and investment expenditures. Expenditures, which may increase even further in coming years when the Chinese Renminbi probably is revalued further against the U.S. dollar.

Furthermore, most large container terminals in Europe and North America have in recent years experienced increasing congestion problems. On top of congestion surcharges to cover the containership operators' additional costs, congestion has led to longer travel distances and to containerships having to wait longer to on- and offload. This has led the shippers to loose faith in the just-in-time concept, and thus to ship ahead of the peak season thereby increasing their inventory levels throughout the entire supply chain, causing the total production costs to rise even further.

All of the above additional costs associated with outsourcing production to distant countries may indeed prompt western companies to rethink their outsourcing policies in the future.

The negative repercussions from transportation congestion and Chinese infrastructure constraints, in addition to further Renminbi revaluations, may thus for years to come be significantly slower growth in Asian containerized exports to the Western parts of the world.

Add to that, the considerable U.S. imbalances in the form of record high trade deficits, current account deficits, federal budget deficits and very low national savings, which all have to be improved upon in the future.

Conclusively, the most likely outcome is that total trade growth on the large head-haul routes is probably to be markedly lower in future years than the 10% average annual demand growth experienced since 1995.

Unfortunately, the massive containership orderbook is already stretched 3-4 years into the future, completely shattering any chances of a quick adjustment to the likely future slowdown in trade growth, or of a quick fix to the balance of containership supply and demand ■

Crude Tankers

The peak is behind us, as a much lower oil output growth has taken the steam out of the market. Nonetheless, ship prices have continued up. The outlook for 2h05 spot earnings are still very positive, but the longer-term outlook looks increasingly troubled.

FREIGHT RATES

The peak is behind us – reality is beginning to settle in

From a quarterly average of 156,000 USD/day in 4q04, the spot earnings of the modern VLCCs have receded significantly during 1st and 2nd quarter of 2005 to around USD/day 67,000 and 40,000, respectively, according to Clarksons.

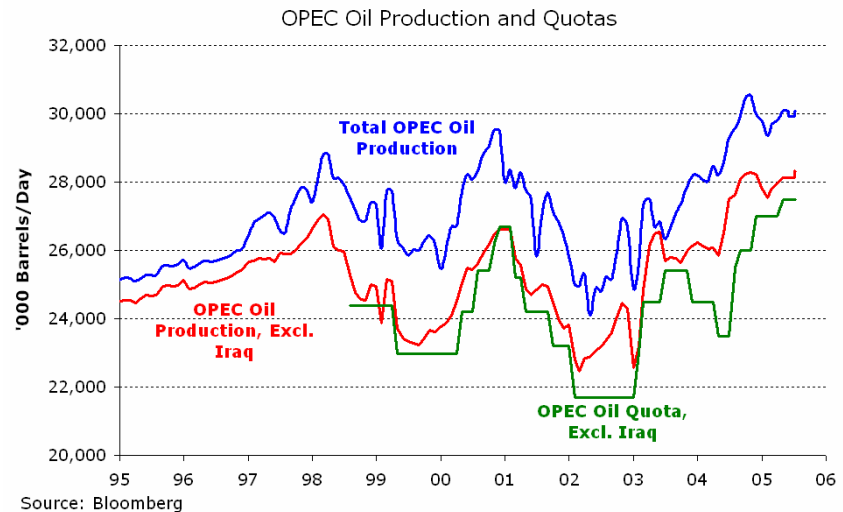
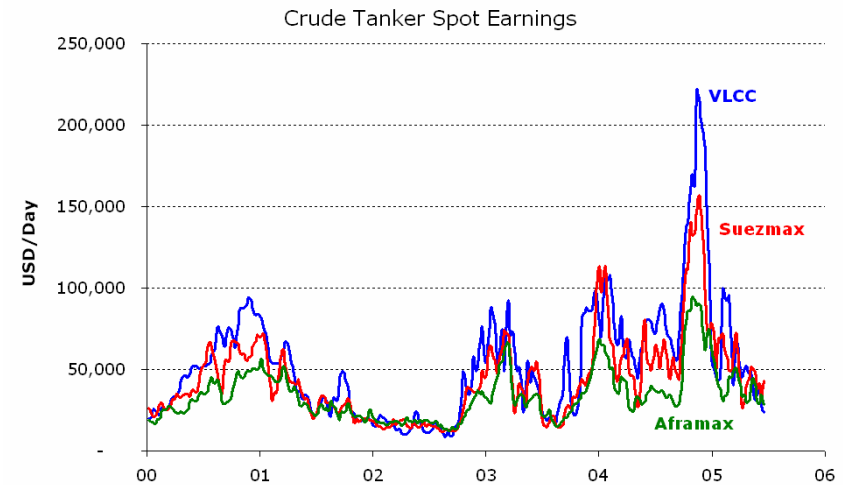
Although, the 2005 spot levels are still highly profitable in historical terms, the significant descend from 2004's record level came as a surprise to most market observers. The market was entirely relying on a continually high fleet utilization to keep freight rates from falling, but many failed to realize that in order for freight rates to remain high, the rate of growth for tanker demand (i.e. oil production/supply growth) also has to be as high as in 2004.

According to our VLCC spot earnings model, the growth rate of global oil production is actually just as significant in explaining the crude tanker spot earnings on a quarterly basis as is the overall level of tanker fleet utilization (see graph page 17).

SUPPLY & DEMAND

Major Chinese slowdown, but US crude oil inventory build-up

The extreme 32% growth witnessed last year in China's oil imports has virtually disappeared in the 1st half of 2005. According to preliminary figures from the IEA, Chinese net petroleum imports during the 6 first months of 2005 were actually 5% lower than the same period of 2004. Although, the imports of crude products continued to grow briskly, the imports of refined products fell commensurately and exports of refined products actually grew, thereby keeping *net* petroleum import growth at a very low level.



On the contrary, the growth rate of US net imports is still positive at 1% for 1h05, according to the EIA, although from a high base level in barrels per day. The increase in US net imports comes despite a clear slowdown in consumption growth from 3.7% in 1h04 to 0.1% in 1h05, and implies a large build-up in the US oil inventories. US crude stocks are by now significantly above their 5-year average range, whereas product stocks are trading at the upper end of their 5-year average range.

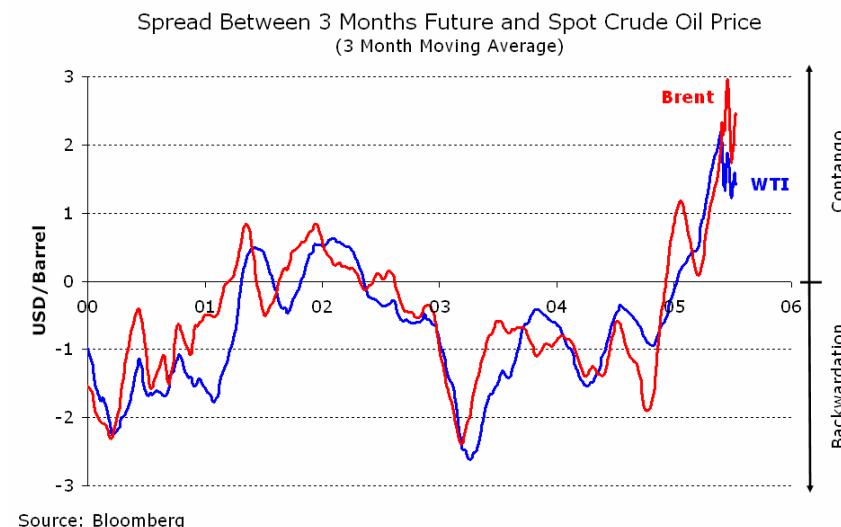
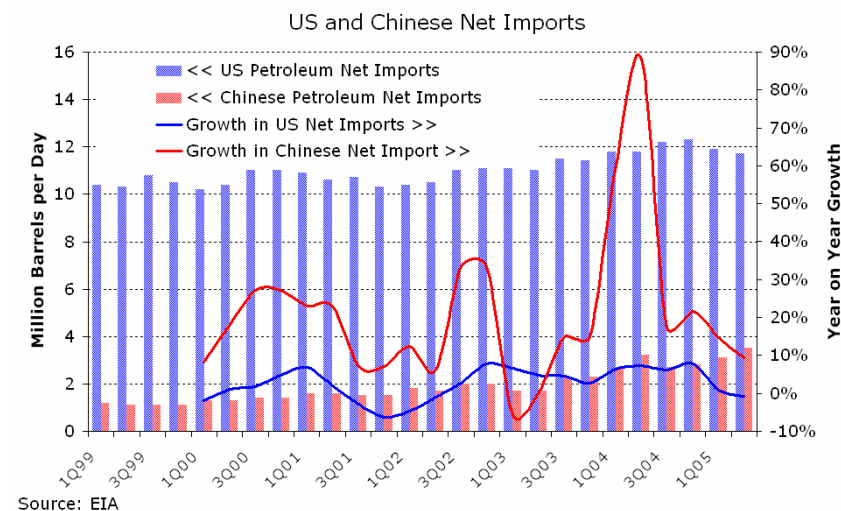
In OECD Europe, similar growth figures are evident. Overall oil consumption in the 1st half of 2005 has fallen by 1%, whereas net imports are up by 3.3% over the corresponding period of 2004, according to the IEA, and despite a continuing fall in North Sea output, European oil inventories are now significantly above last year's level.

For the crude and product tanker markets, the build-up in inventories has led to higher demand during the 1st half of 2005 and thus to higher freight rates than the growth in fundamental oil consumption would otherwise have implied for the period.

The main reason for the large build-up in oil inventories in both Europe and North America can be found in the forward pricing structures of the crude oils related to the WTI and the Brent crude oils. At least since November 2004, the 1-5 month forward crude oil prices on Brent and WTI have been higher than the spot price (a situation called contango).

Usually, in a situation of high spot prices, the forward curve is rarely in contango because expectations are that prices will fall from current highs when supply catches up with demand. But at present, the current limited spare production capacity, the time-lag between investment and the eventual oil output, and the subsequent need to hold stocks make the current contango structure seem much more logical.

With a forward price above the current spot price, the oil market climate is thus supportive for stock builds as refiners and traders believe they can buy cheaper now rather than wait until later. Even including storage, finance and insurance costs, the contango structure has for a while been supportive of stock building.



Thus effectively, the refiners and traders have brought forward peak summer and winter tanker demand at the same time.

In China, the surprisingly large drop in net import growth for the 1st half of 2005 is partly believed to be caused by government policies which limit increases in the domestic price of key products. According to the IEA, this has discouraged imports, encouraged exports, and depressed the use of fuel oil in power production.

With economic growth in China still running at a high rate, the very low import growth implies a large draw on the Chinese oil inventories. To support this view, according to IEA, there is anecdotal evidence that China's oil inventories indeed were increased in the latter part of 2004 and drawn from during the first quarter of 2005.

CONTRACTING & SHIP VALUES

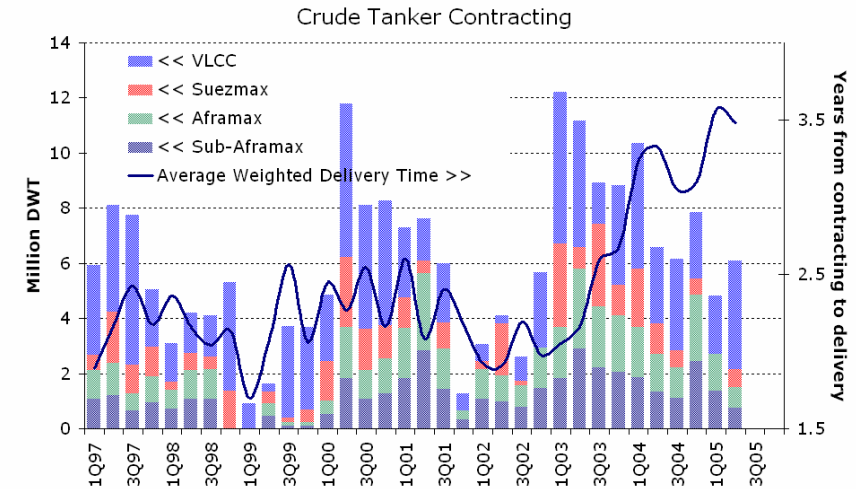
Lower contracting numbers, but at a much higher risk

At 9 million dwt, contracting volumes during 1st half 2005 are less than half the volumes of the peak in early 2003, when the Prestige accident had just set off a wave of newbuilding requirements.

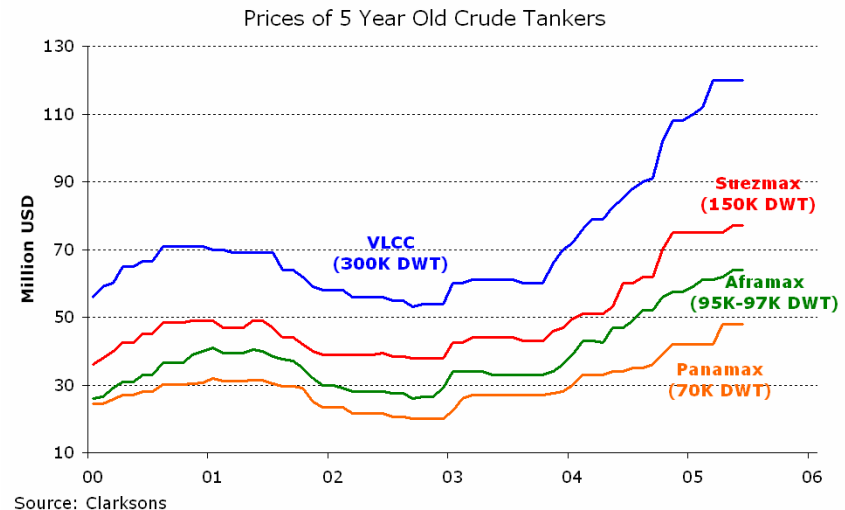
Although constituting much lower volumes, the new contracts are committed at about 11% higher prices than just 6 months ago, and the average delivery time has increased to a record high 3½ years. Thus the downside risks for the buyers have increased significantly, but the perceived lack of shipyard space, particularly for the large VLCCs, has led to the continued contracting.

Despite much lower spot earnings, secondhand prices on double-hulled 5 year old crude tankers have increased by around 3-11% from December 2004, and 10 year old double-hulled vessels have increased even further. Single-hulled vessels have lost value.

In recent months, the resale activity has almost ground to a halt, signifying an overall prevalent lack of direction for prices, and possibly a looming downward adjustment in secondhand prices.

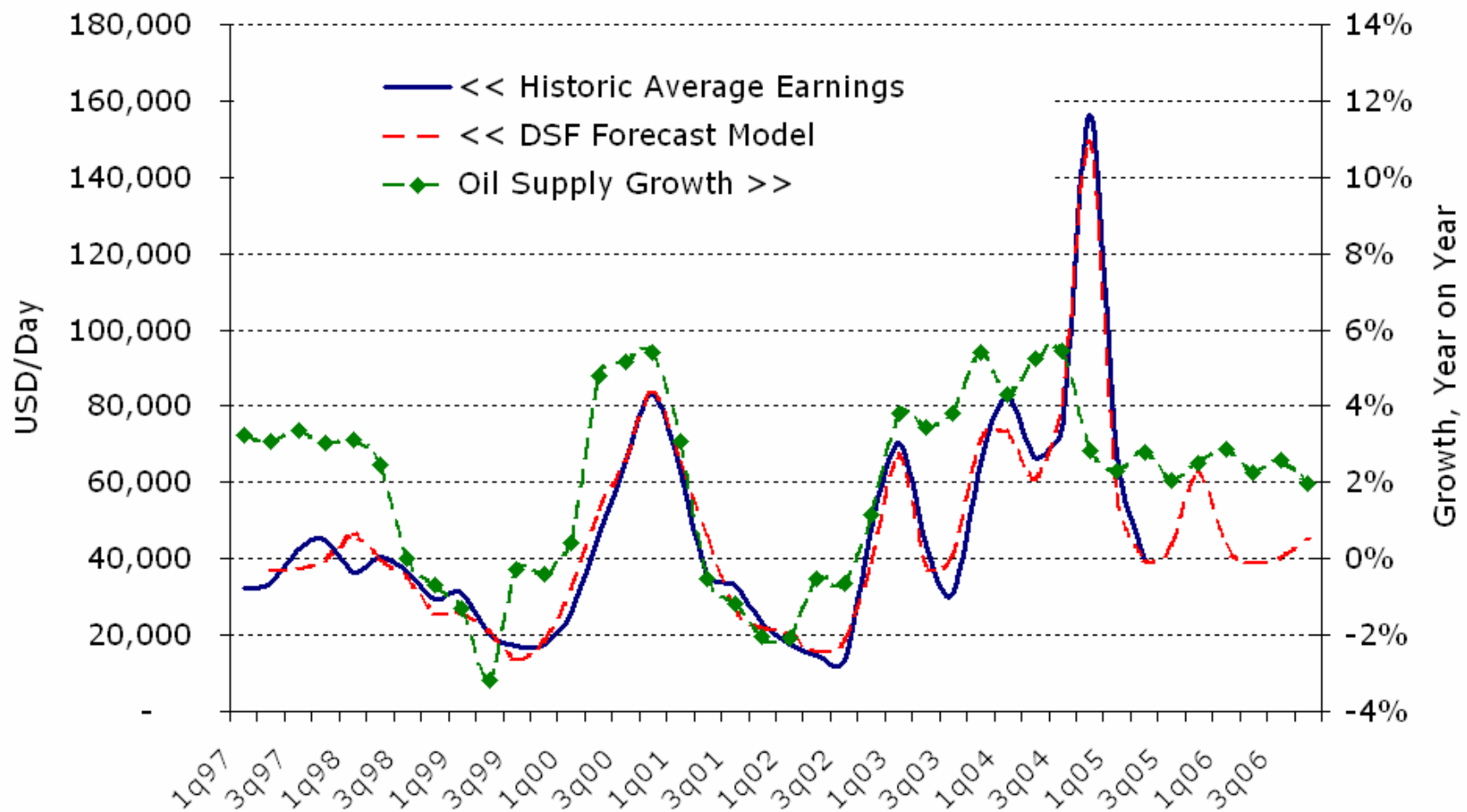


Source: Clarksons, DSF



Source: Clarksons

Quarterly Average VLCC Spot Earnings



Source: DSF, Clarksons, EIA

July 13 2005

DSF forecast on average spot earnings of modern VLCCs, USD/day

2002	2003	2004	1q05	2q05	3q05	4q05	2005	1q06	2q06	3q06	4q06	2006
23,293	52,474	94,878	66,940	39,708	43,400	62,500	53,200	43,400	39,000	40,200	45,300	42,000

Grey shaded areas signify actually realised average earnings for the given year/quarter.

OUTLOOK

Still upside chance for 2005, but not much for the longer term

The EIA predicts an average 2.3% and 2.4% year-on-year growth in global oil output for the 2nd half of 2005 and for all of 2006, respectively. Resting on EIA's output predictions, our forecast model for the crude tanker spot earnings foretell a slight improvement in 3rd quarter average spot earnings and a much larger 4th quarter pickup in spot earnings, but also of a just as quick return to average levels in all of 2006 (see graph page 17).

We believe, particularly two large uncertainties surround our near-term forecast.

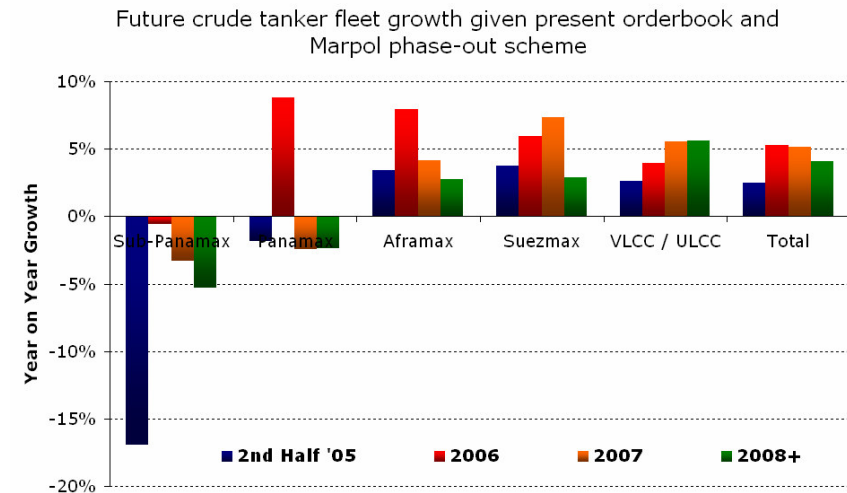
1) On the upside, the supposedly low Chinese oil inventory levels could provide for much increased oil demand in the second part of 2005, when the underlying Chinese consumption growth and a possibly inventory rebuilt have to be satisfied by larger imports.

Furthermore, in the likely case in coming years that the Chinese Renminbi should be revalued against the USD, or the government's oil pricing policy should be more market based, both developments may most likely lead to a boost in Chinese oil consumption and oil imports.

But, as the global oil production facilities currently are running at very close to maximum capacity, any sudden increase in oil demand from China may instead of increased global oil production and seaborne trade cause a spike in global oil prices.

2) On the downside, if oil inventories in North America and Europe for the remainder of 2005 continue to improve or just trend significantly above the historical average, coupled with a mild winter in the Northern hemisphere, a mild hurricane season and lower economic growth, any autumn and wintertime rush for oil imports and subsequent push for higher tanker spot earnings may be completely stifled.

In the longer term (2006+), the chances of large or long-lasting spikes in spot earnings unfortunately look increasingly miniscule.



Source: Fearnleys

Theoretically, the historically high degree of fleet utilization should for years to come translate into high freight rate volatility and a generally high freight rate level. But unfortunately, global oil production is currently stretched almost to its utmost bounds, and future production output is expected only to grow at a low pace – all of which translate into small chances of any upside volatility in global oil output and henceforth for tanker demand.

Instead, the tanker market should probably settle in for a stop-and-go ride with somewhat average rates most of the time and only short-lived peaks when unforeseen events and the seasonal peaks momentarily upset the tanker market's balance of supply and demand.

Furthermore, with the considerable crude tanker orderbook stretched out over an extended period, signifying a future fall in fleet utilization, the chances of a quick return to the very high spot earnings of 2003 or 2004 may become increasingly limited ■

Product Tankers

Western hemisphere inventory surplus and Asian inventory deficit, combined with high global refinery utilization, supported a strong trade in refined oil products. Contracting of newbuildings is markedly up, but prices may have peaked. The short-term outlook for freight rates is still positive.

FREIGHT RATES

Momentary break-out from the crude tankers' shadow

In particular the smaller product tankers seem to have been better able to withstand the downward trend, that otherwise seem to have caught hold of the crude tankers throughout most of 1st half of 2005.

Product tanker earnings are still on a very high level, and the forward-looking timecharter rates are still close to their record levels, signifying unscathed belief in future high earnings.

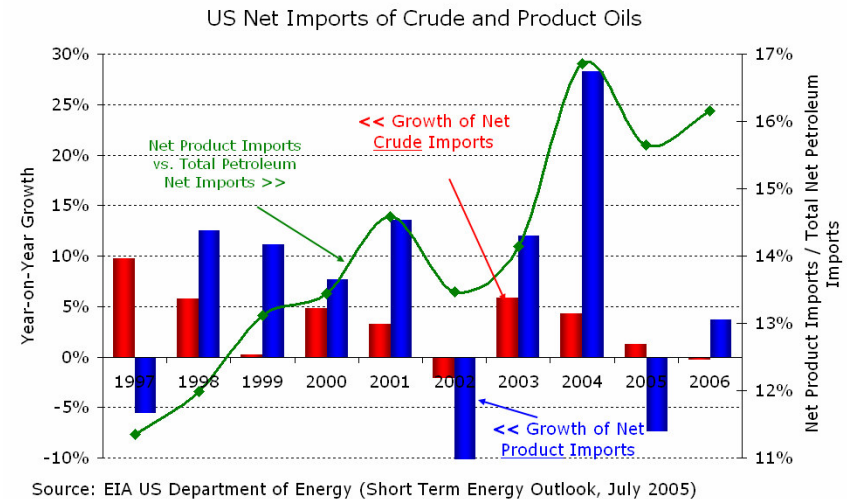
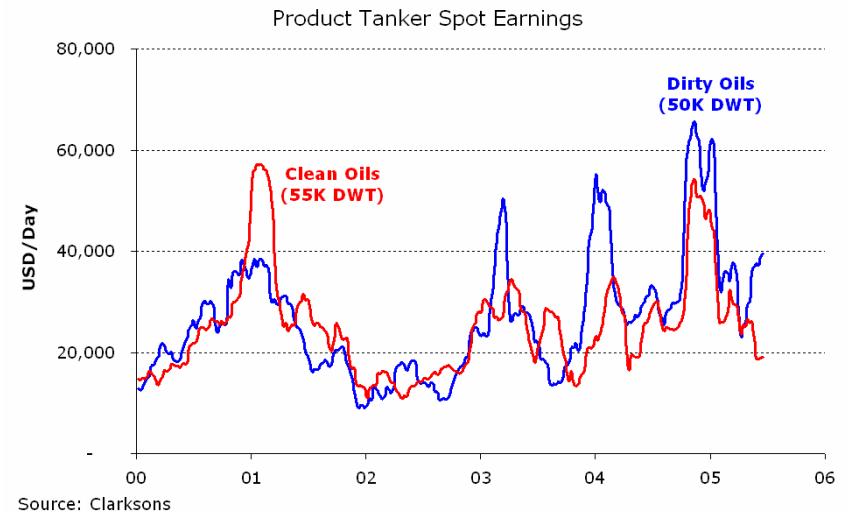
SUPPLY & DEMAND

Short-term factors compensate for a fundamental slowdown

Somewhat counterintuitive, the high spot rates in the product tanker segments and the better performance than the crude tanker segment came despite both China and the USA having displayed a fall in net imports of refined oil products, but a rise in net imports of crude oils.

A part explanation to the conundrum can be found in a striking divergence between the somewhat comfortable or rising storage level in the Western world and the strained and rundown storage situation in the Asian part of the world.

In both the US and Europe, the large facilities which store crude and refined oils are reporting tightened capacity utilization, thereby restraining the likelihood of further large increases in storage levels. Furthermore, the much improved storage situation has reduced or completely reversed any price arbitrage between



the two continents and thus limited the incentives to ship incremental crude or product oil across the Atlantic from Europe to the US.

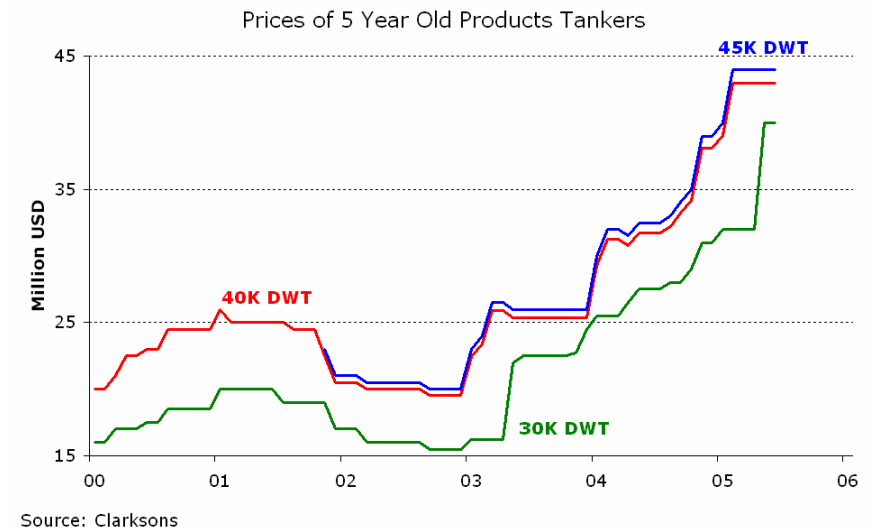
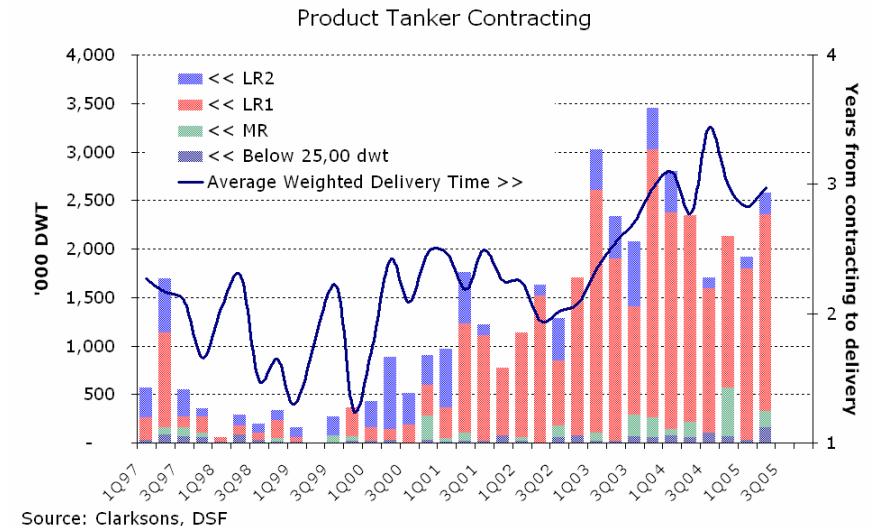
On the other hand, Asian refiners have experienced spot prices above forward prices (a situation called backwardation) signifying a current tight market with refiners scrambling for prompt supplies and a low storage level of both crude oils and product oils.

This situation, of European and North American oil storages in positive territory and Asian refiners clearly in need of oil, has caused increased exports of both product and crude oils to Asia from Europe, North America, Venezuela and Western Africa.

As the distance from Europe, North America and West Africa to Asia is far greater than that from the Middle East to Asia, the overall demand for tankers has benefited greatly. But, as the individual cargo sizes traded from European, American and African refineries and oilfields to the Asian refineries are smaller than the cargo sizes exported directly from the Middle East to Asia, the elongation of trade distances has probably benefited the smaller crude tankers and the product tankers relatively more than it has benefited the larger crude tankers.

In addition to the elongated trade distances and thus increased demand for product tankers and smaller crude tankers, the product tankers particularly have benefited from an increasingly tighter refinery utilization at the same time as the requirements for the quality of the refineries' output have increased and the quality of their input, crude oil, has fallen.

The combination of an already strained refinery sector, an increasing share of the global oil consumption being met by heavy and sulphur-rich OPEC crude oil, the European and North American regulators trying to limit the emission of sulphur, and the US trying to cut down on the use of MTBE in car fuels, have all led to a flourishing cross-trade of refined petroleum products between the refineries in order for them to have the required product mix, consequently leading to higher demand for product tankers.



CONTRACTING & SHIP VALUES

10-30% higher prices and higher contracting activity

In only 6 months, prices on secondhand product tankers have climbed 10-30%, according to Clarksons, thereby outperforming their big sisters – the crude tankers.

Contracting of new product tankers at the shipyards has continued at a brisk pace throughout 1h05, and actually picked up speed in the 2nd quarter. For the small product tankers below 25,000 dwt, 2nd quarter contracting volumes were actually a record high despite newbuilding prices also being at their historic peak.

OUTLOOK

Still good 2005, but fleet growth and demand slowdown loom

The outlook for 2nd half of 2005 continues to look positive on much the same reasons as for the crude tanker outlook – e.g. seasonal pickup in oil output along with China probably returning as a large importer.

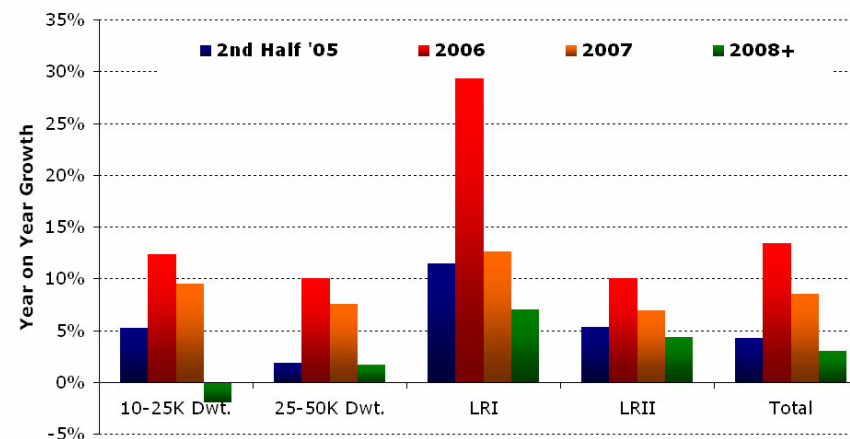
Furthermore, the extra demand for product tankers as a result of the strained refinery sector is expected to persist for some years ahead, although its relative importance to the product tanker sector is expected to gradually diminish.

In addition, as the main share of future growth in refinery capacity is expected to occur in the Middle East, far from the consuming countries, especially the larger product tankers (LR1 and LR2) are expected to see the relatively highest long-term demand growth among the crude and product tanker segments.

In other words, because of the lack of new refinery capacity located close to the consuming countries, the overall demand for product tankers is set to grow relatively faster than that of the crude tankers.

Unfortunately, even when taking account of the mandatory phase-out of single-hulled tankers, fleet growth for the remainder of 2005

Future product tanker fleet growth given present orderbook and Marpol phase-out scheme



Source: Fearnleys

looks set to outpace demand. And in following years, the chances of demand growth keeping up with fleet growth look even worse – in 2006, the total product tanker fleet is expected to grow by up to 13%, followed by 8% growth in 2007.

In addition, future fleet growth has the possibility to become even higher if some of the single-hulled or double side/bottom tankers should opt for a rebuilt in order to be allowed to continue sailing past their initial phase-out deadline.

Fortunately, a part of the current product tanker orderbook is not meant to be deployed directly in the product tanker trades, but may instead trade as regular crude tankers, thereby alleviating some of the negative pressure on the product tankers' earnings.

But, even though the fundamentals governing the product tanker sector look somewhat better than those of the crude tanker sector, it is almost inevitable that the product tanker sector will not be able to withstand the negative pressures from the crude tanker sector in the longer run ■

Chemical Tankers

High fleet utilization and robust global demand for chemicals supported a high spot market, and led the term charter rates to record highs. The short-term outlook continues to be positive, but a large orderbook and a slowdown in global economic growth may impact freight rates negatively in the longer run.

FREIGHT RATES

Spot market choppiness but strong term-market improvement

Generally, the spot rates for the large deep sea routes in the 1st quarter of 2005 followed the trend of the previous quarters – rising further or maintaining high levels. But, 2nd quarter spot rates proved less resilient, displaying some downward movement.

On most of the intraregional routes, spot rates also showed improvement throughout the majority of the 6 month period.

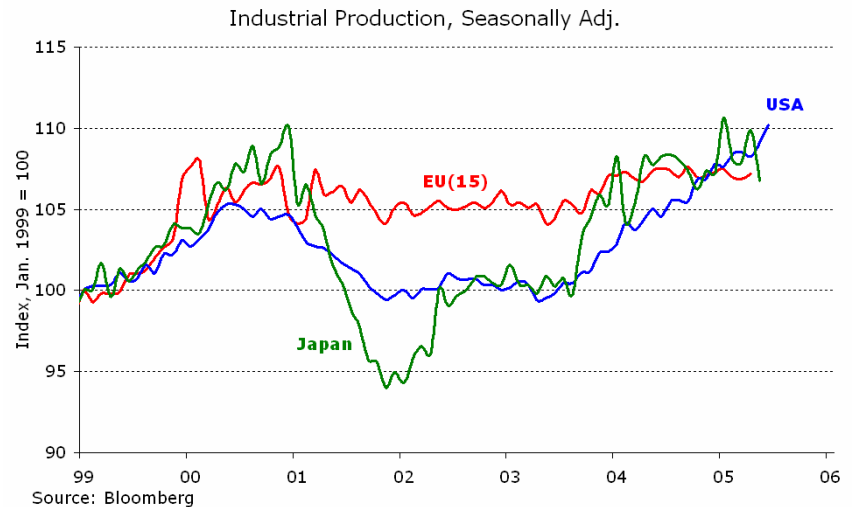
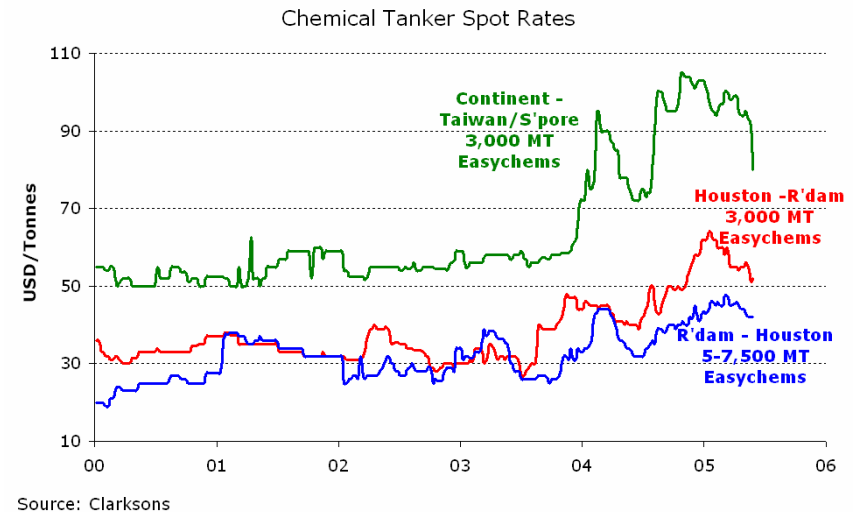
Because of the generally high spot rates and a positive outlook, contract of affreightment (CoA) charter rates were settled at significantly higher levels in both of the 1st and 2nd quarter rounds of contract renewals. This speaks for much improved profits for the chemical ship operators in the short as well as in the longer term, despite any momentary downside volatility in spot rates.

SUPPLY & DEMAND

Very tight ship capacity, enhanced by strong CPP market

In the first half of 2005, the continued robust growth in US industrial production along with a still strong industrial production in Asia seemed to be able to make up for a stagnant European industrial production.

The increased demand for chemical tankerships caused by the increased global industrial production, underpinned the already high level of tonnage utilization.



Additionally, the high level of chemical tanker utilization was further supported by high freight rates in the clean product tanker segments, which led some refineries and chemical companies to use chemical tanker space for the transport of their products, and tempted some chemical tankers to function as actual product tankers instead of sailing with lower grade chemicals.

The fall in spot freight rates in the late months of the 2nd quarter, is mainly believed to be because of a temporary slowing in the world industrial production and an inventory correction in Asia, all at the same time as the seasonal lull in demand.

CONTRACTING & SHIP VALUES

Lower contracting numbers, much higher secondhand prices

According to Clarksons, the total number of new contracts for newbuildings is somewhat down from the average level contracted during 2004, but still resides at a somewhat high level.

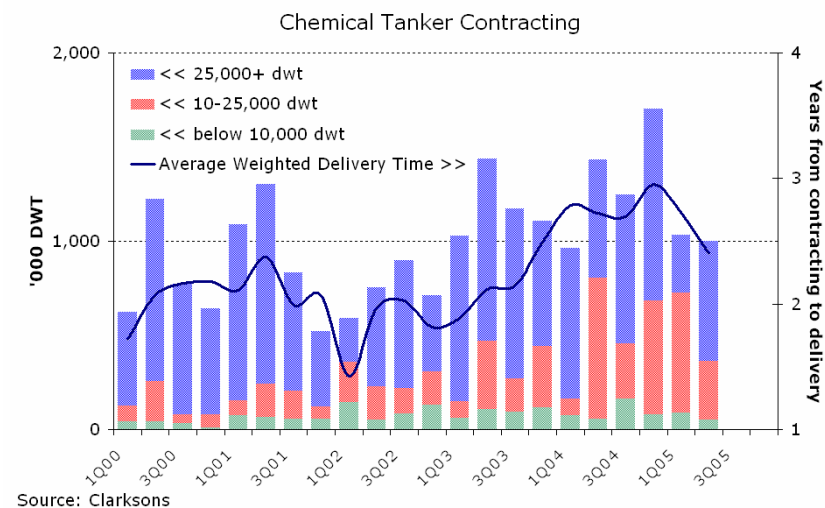
More importantly, the average delivery time has fallen markedly down from the average of 3 years in 4q04 to below 2½ years in 2q05. Particularly, the ever rising prices quoted by the Asian yards in combination with their very long delivery times, have prompted the shipowners to turn to e.g. Western and Eastern European yards which are able to deliver earlier and at competitive prices.

Newbuilding prices followed the general upward trend seen from other ship types. Although the newbuilding prices increased slightly, secondhand prices managed to increase even further – rising by 10-15% in just 6 months, with the largest percentage increases experienced by the younger chemical tankers.

OUTLOOK

Large orderbook but regulation and healthy demand growth

In future years, the present orderbook spell out a large fleet growth, which may lead to lower tonnage utilization and less likelihood of high freight rates.



But fortunately, future demand growth is believed to be almost as high, although the demand growth may slow somewhat down compared to recent years. A continued high fleet utilization should thus continue to be a positive influence on the spot and term freight rates.

Furthermore, in the short term, the still strong freight rates in the product tanker sector may continue to provide support to the chemical tanker sector, possibly leading to yet another rally for the chemical spot freight rates in the 2nd half of 2005.

During a short number of years after January 1 2007, the recently decided reclassification of almost all chemical products, vegetable oils and animal fats into higher IMO classification grades, may imply a tightened tonnage utilization.

Particularly the utilization of chemical and product tankers with IMO 2 classification is expected to become very tight, thereby requiring some of the IMO 3 tankers to act as temporary substitutes for the IMO 2 tankers ■

LPG Tankers

Large LPG tankers have experienced a large setback, but medium and small LPG tankers are still in record territory. Contracting volumes have exploded, keeping newbuilding prices from falling and leading secondhand prices to rise substantially.

FREIGHT RATES

VLGC plunged, but medium and small LPG carriers improved

Although from a very high level, the spot earnings of the Very Large Gas Carriers (60,000+ cbm) fell dramatically throughout the 6-month period. Despite the fall, the spot earnings are by now still at relatively healthy levels.

By contrast, the medium and small LPG tankers almost all experienced improved spot earnings throughout the 6-month period.

Particularly the very small coastal LPG carriers experienced exceptional improvements and have throughout the period remained at record levels.

SUPPLY & DEMAND

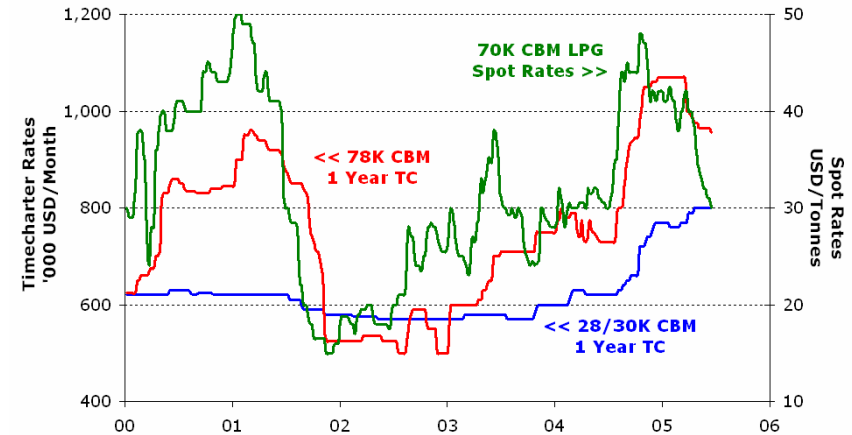
US pullback, but Asia strengthens and refinery troubles help

The fall in the large LPG carriers' spot earnings came as the number of available LPG tankers built up in the Arabian Gulf, and as rising propane and butane prices acted as a deterrent to Asian purchasers, thereby reducing the demand for LPG tankers.

Furthermore, the lower freight rates in the clean petroleum product tanker segment acted as a drag on particularly the larger LPG tankers' prospects for higher freight rates.

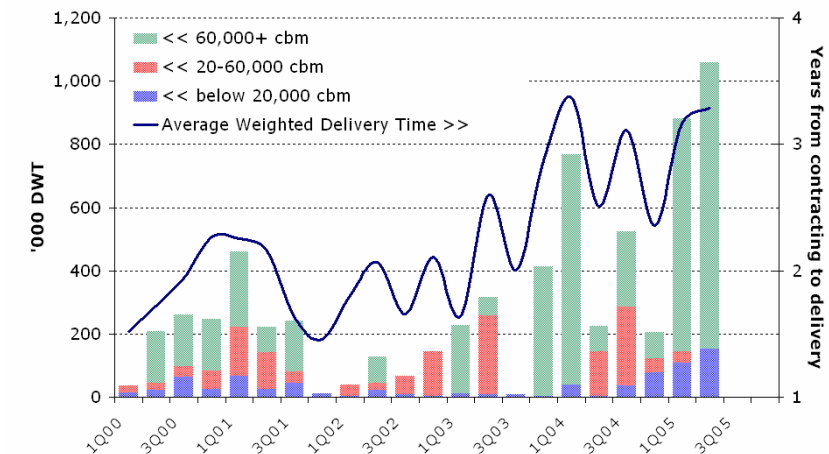
In Europe in particular, the small coastal and medium sized LPG tankers experienced increased demand as several refineries experienced production problems and had to use the LPG tankers as temporary storage, and as the North Sea LPG exports increased

LPG Tanker Spot and Timecharter Rates



Source: Clarksons

Liquefied Petroleum Gas Tanker Contracting



Source: Clarksons

by almost 10% during the first five months of 2005, according to Drewry.

Although the US seaborne imports of LPG products during the 1st half of 2005 appear to be down on the same period in 2004, the Asian imports of LPG products on the contrary maintain a somewhat strong growth. Combined Japanese, Chinese and South Korean LPG imports were up 2.7% in the first four months of 2005, according to Drewry. In particular the Chinese import growth is up from almost zero in 2004 to 8% year-on-year growth in 2005.

CONTRACTING & SHIP VALUES

Contracting explosion and 5-25% secondhand price increases

The prospects of an ageing and scrap-destined fleet in combination with highly profitable freight rates have encouraged the LPG shipowners to order new ships in record numbers. The high contracting volumes has resulted in a large total orderbook which now represents almost 30% of the total existing LPG fleet.

As a result of the extremely high contracting volumes during the last 6 months, the LPG newbuilding prices are the only newbuilding prices which have not displayed a tendency to fall in recent months.

Naturally, the improved spot earnings and higher newbuilding prices have led to an increase in the LPG tankers' secondhand prices. In 6 months, the prices have on average increased by 5-25% from already elevated levels.

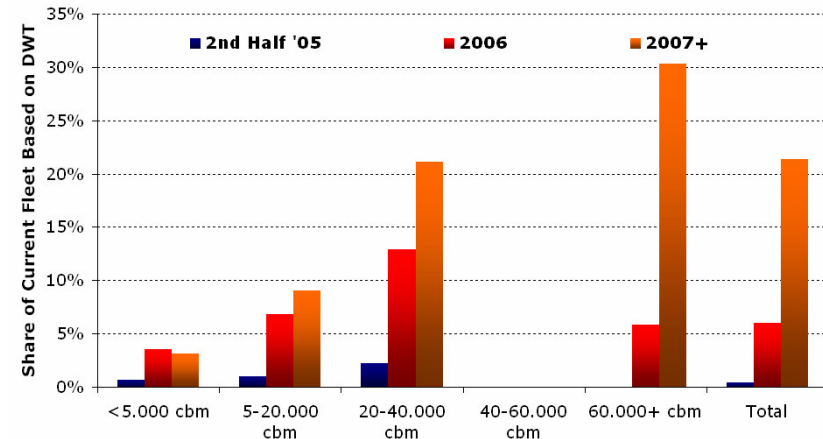
OUTLOOK

Large orderbook, but old fleet and healthy demand growth

Despite a record orderbook, the deliveries of the newbuildings fortunately are drawn out over the coming 3-year period, thereby reducing the negative impact of the apparently high fleet growth.

Additionally, the total orderbook of the VLGCs currently represents almost the exact same capacity of the fleet which by 2007 is 25

LPG Tanker Orderbook by Year of Delivery



Source: Fearnleys

years or older, and thus are likely to be scrapped in coming years.

Demand growth in coming years is expected to remain healthy. Particularly, the planned increases in LPG production and export facilities in the Arabian Gulf are targeting LPG exports to Asia, thus especially benefiting the larger LPG tankers.

In addition, the expected high growth in the number of LNG liquefaction and exporting terminals is in future years believed to provide extra demand for LPG tankers also. The link between LNG production and LPG trade arises as the production of Liquefied Natural Gas (LNG) produces petrochemical gasses as bi-products.

In the short term as well as in the longer run, the tonnage utilization is thus expected to remain tight, but a potential slowdown in global economic growth may curb growth in the demand growth for LPG tankers ■

Dry Bulk Ships

The negative consequences of a global steel overproduction is beginning to be felt throughout the dry bulk sector, leading to de-stocking and falling freight rates. Earnings are still expected to remain at healthy levels, but much rests on China to behave well disciplined.

FREIGHT RATES

Reluctant downturn followed by absolute freefall

On the face of it, the developments during 1st half of 2005 largely resemble the developments during the same period a year earlier – starting at an absolute peak and ending at a much lower level by midsummer.

But unfortunately, this year's fall in freight rates is believed to be driven by a fundamental slowdown in demand growth coupled with less port congestion, whereas the freefall during last year's spring was much more driven by momentarily wavering market sentiment coupled with momentarily less port congestion.

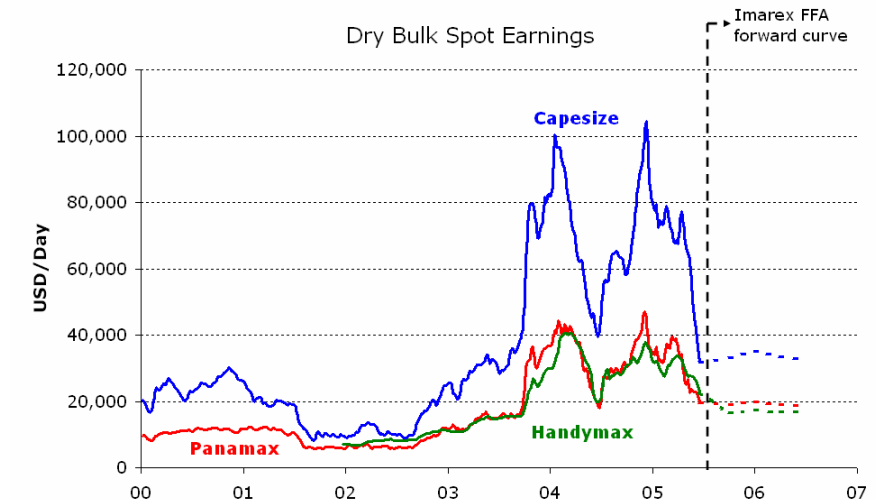
SUPPLY & DEMAND

Demand slowdown & overproduction followed by de-stocking

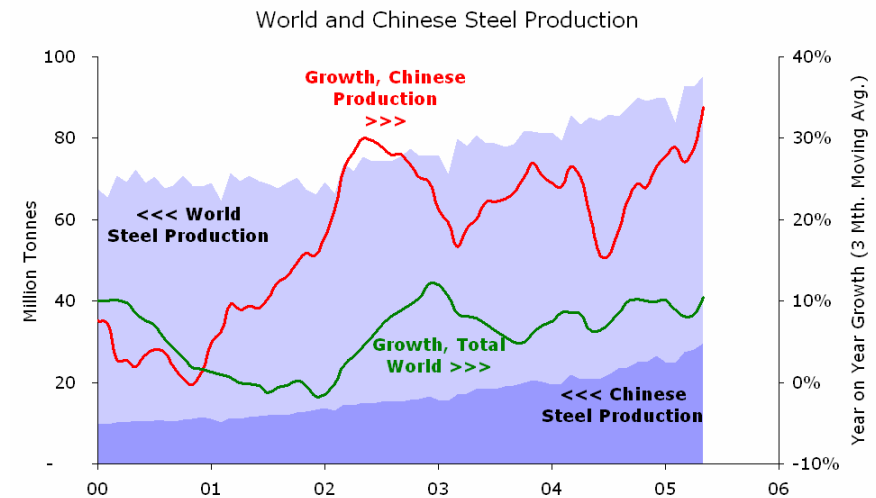
During the first 5 months of 2005 the Chinese production of steel grew by 27% compared to the corresponding period a year before, according to the *International Iron and Steel Institute*, and implies a pickup from 2004's growth of 23%. Throughout 2005, the growth rate of Chinese steel production growth has actually accelerated (see lower graph on right).

The very large growth in Chinese steel production has led to a record volume of iron ore imports to China, providing particularly the Capesize ships with a significant demand boost.

Counterintuitively, the aggressive growth in Chinese production comes despite a clear slowdown in Chinese steel consumption and large reductions in the price of steel, and implies a growing need to restructure the Chinese steel industry in order to make it more



Source: Clarksons and Imarex



Source: International Iron and Steel Institute

sensitive to price signals. From an average annual growth throughout 2002 to 1q04 of around 25%, growth in Chinese apparent steel consumption dropped to under 10% p.a. by 2q04 and has maintained that lower level well into 2005.

The much lower steel consumption growth is a result of the Chinese government's efforts to curb growth in some key markets, especially construction, in order to prevent the economy from overheating. The new measures have had obvious effects on steel consumption growth, but so far, have *not* led to any slowdown in steel production.

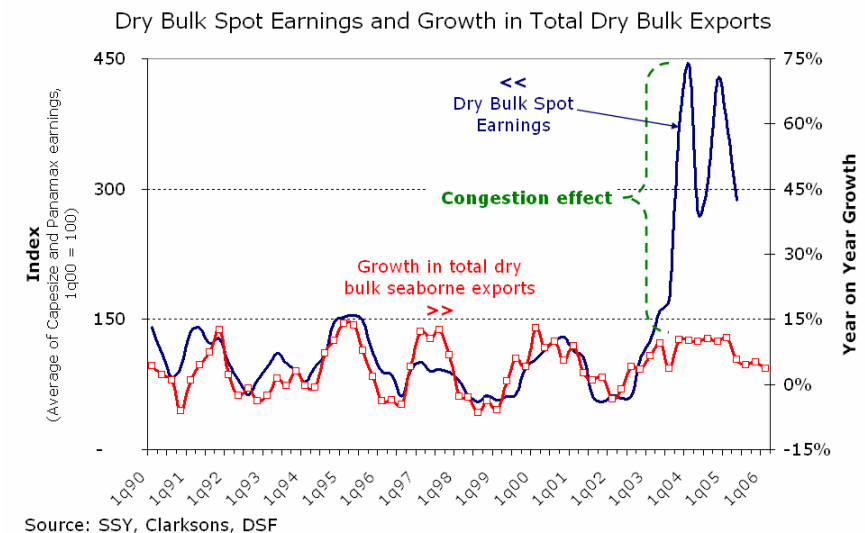
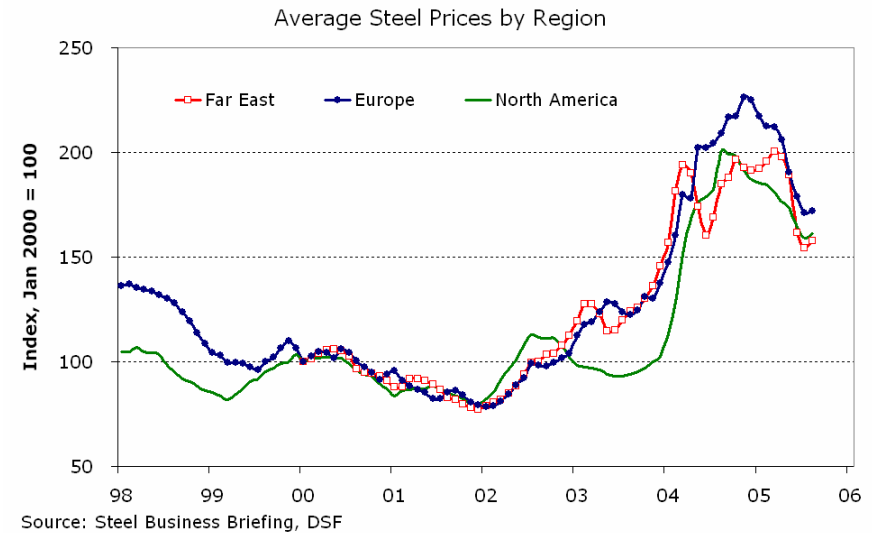
The increasing disparity between growth rates in Chinese steel production and steel consumption has in less than a year transformed China from the world's largest steel importer, to a net steel exporter. The reversion in China's steel trade has created a significant negative pressure on global steel prices, because the steel that previously was headed for China, in addition to the steel which now is exported from China, now have to find other buyers.

At the same time as China has increased its steel production by an amazing 27%, Japan has increased its production by 2%, whereas on the contrary the EU-25 countries and the U.S. have lowered their production by 1% and 0.2%, respectively, according to the *International Iron and Steel Institute*.

The European and American production cutbacks come as a delayed response to global overproduction during 2h04 well into 2005, the threat from Chinese and Russian steel, a lower economic growth in 2005, increases in steel inventories throughout the industry, and the resulting large declines in global steel prices.

A part explanation for why steel prices have not fallen more, is probably more of a cost issue than a demand issue. The energy and raw material costs (iron ore, coke, scrap, coal) are still at record highs as China continued to draw in increasing amounts of raw materials to satisfy its rampant steel production.

In China, the authorities are increasingly recognizing the negative consequences of the growing imbalance of China's steel production and consumption, and have subsequently initiated a number of



measures to curb steel production, steel exports and raw material imports. Under usual circumstances exports are regarded as beneficial, but as China is heavily undersupplied of energy to support its manufacturing and private sectors, the exports of energy-intensive products, such as steel, is regarded as an inefficient use of a limited resource.

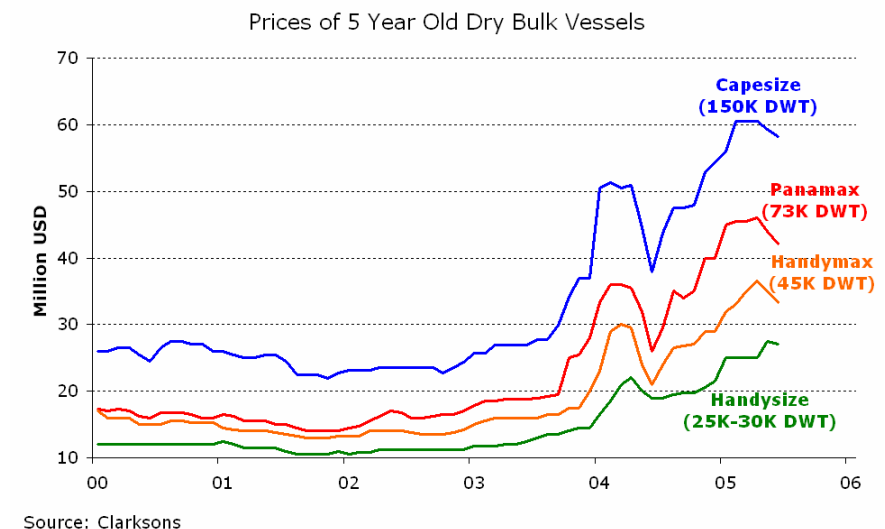
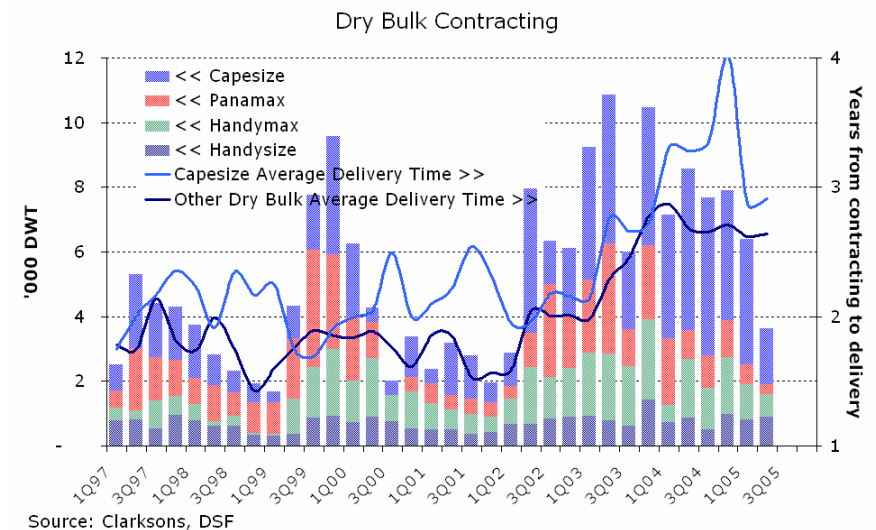
In order to curb the Chinese steel exports, the government has as of May 1 reduced the export rebates on wire rod and rebar from 13% to 10%, and the export rebates on billet and slab are completely eliminated. Furthermore, to reduce the imports of iron ore, the number of authorised steel mills and traders who are permitted to import iron ore after May 1 has been cut by almost 80%, leaving only the largest and most reputable importers to import in the future.

These measures among many, in addition to a market-initiated 71.5% increase in the price of imported iron ore after April 1, have encouraged a pre-emptive import and stock-building of raw materials in China prior to the proclaimed dates.

Following the stock-build of iron ore, the Chinese steel industry is now attempting to bring down the inventory levels, which has led to a significant slowdown in the imports of iron ore, e.g. by cutting sharply in the spot purchases and deferring some contract shipments from Australia, Brazil and India.

The slowdown in iron ore imports because of de-stocking of iron ore has furthermore been boosted by an over-supply of steel in China as the steel production has overshoot consumption and as the domestic buyers during 4q04 and 1q05 increased their inventories in anticipation of rising steel prices – inventories which now have to be brought down.

An important by-product of the Chinese import slowdown has been a clear decrease in the global port congestion, further exacerbating the downward pressure on dry bulk freight rates during April through to June. As is evident from the lower graph on page 28, port congestion has probably been the most important explanatory variable for dry bulk spot freight rates in recent years, and will probably continue to be so for a while yet.



CONTRACTING & SHIP VALUES

Prices have peaked and contracting is clearly down

In April 2005, dry bulk secondhand prices peaked at levels that were around 300% higher than the levels 3 years prior. By now, they are down 3-8% from the peak levels, according to *Clarksons*.

With a large number of recently failed shipping IPOs, it seems as if the financial markets have lost (at least a part of) their faith in the shipping market to maintain its amazing earnings. Consequently, with recent record prices on ships partly driven by the willingness of outside investors to pay extraordinary sums, secondhand prices of dry bulk ships and other ship types are probably to find it increasingly difficult in future months to maintain their current high levels.

The volume of new contracts signed with the shipyards has significantly fallen during 2nd quarter of 2005, implying a slightly lower confidence in future earnings and an unwillingness to commit to the longer delivery times and the higher prices.

OUTLOOK

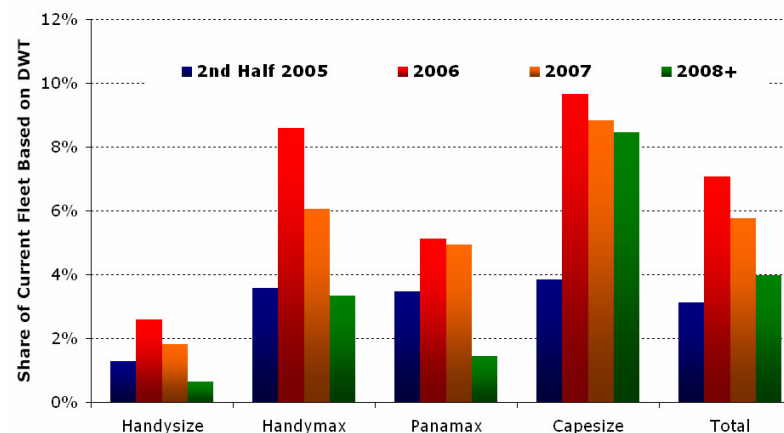
Slow controlled descent, or short-term rally followed by crash?

China's status as a net exporter of steel is neither conducive for a later rise in global steel prices, nor is it tolerated by the Chinese authorities. Consequently, China's production of steel will in future years have to slow markedly down or possibly in the short-term have to decrease in order to allow consumption to catch up with production.

But, the question remains if China's steel manufacturing industry is self-disciplined to the extent that it by itself is capable and willing to reduce output growth to better match consumption growth.

So far, the evidence is weighing heavily against it – implying that we during the 2nd half of 2005 may see further large increases in the Chinese steel production, and a subsequent need for higher imports of raw materials, possibly leading to a reappearance of

Dry Bulk Ship Orderbook by Year of Delivery



Source: Fearnleys

significant port congestion and yet another short-term rally in dry bulk spot earnings.

But, a lack of self-discipline will most likely lead to a subsequent need for an even larger correction of the Chinese steel production and iron ore imports, possibly leading to a transitory crash in dry bulk spot freight rates when the resulting build-up of steel inventories have to be brought back down.

If indeed, the Chinese steel manufacturing sector is able to quickly adjust itself to the lower steel consumption growth, the dry bulk shipping markets will in future years instead have to suffice with a descent to average, high freight rate levels as port congestion tapers off and the dry bulk fleet catches up with demand.

Irrespective of the above developments, should the unlikely happen that global port congestion quickly disappears, the freight rates may most likely fall quickly back to the high and healthy levels experienced during the boom periods prior to 2003 ■

Car Carriers

Tight charter market pushes charter rates further up and contracting of newbuildings continue albeit at lower levels. A large orderbook may have an impact on charter rates but an old fleet may counteract a large drop in fleet utilization.

SUPPLY & DEMAND

Still tight ship charter market and strong US car imports

The market for pure car (and truck) carriers remains extremely tight with only a very low number of charter contracts being settled. Consequently, charter rates have improved further and continue to test new record levels.

In the US, large incentive-programmes spurring car sales and a generally robust economic growth have helped to maintain a sales growth of around 1% in 1st half of 2005, compared to the same period a year prior – all despite rising fuel costs and rising financing cost for the consumers.

But partly on account of a stronger US dollar, the US imports of cars have grown faster than the overall sales, rising by 5% in 1st half of 2005 compared to the same period a year prior.

CONTRACTING & SHIP VALUES

Contracting slowdown and 5-15% rise in secondhand prices

The continual rise in newbuilding prices along with very few building berths available at the traditional PCC shipbuilders before well into 2008 has kept the PCC shipowners from contracting a vast amount of new ships in 1st half of 2005.

Consequently, the delivery time has started to come down a bit, although it still is above 3 years and has a considerable way to go before it reaches the average 2 year delivery period.

By now, the orderbook represents a fairly high 26% of the existing fleet when measured in number of ships, but when measured in car carrying the capacity the number rises to a hefty 35%.

On account of the rising newbuilding prices, some PCC operators have opted to lengthen their existing ships instead of ordering new ships.

Along with rising newbuilding prices and high charter rates, the secondhand prices on PCC ships have risen by 5-15% during the first 6-month period of 2005.

OUTLOOK

Large orderbook but old fleet and robust demand growth

The high number of deliveries during 2005-2008 may put negative pressure on charter rates. But the high proportion of elderly and scrap destined ships to a large degree ought to counteract the fleet growth, possibly leading to an extended period of a still tight PCC and PCTC charter market.

A weak USD, rising American interest rates and high gasoline prices may threaten the North American vehicles sales, preventing car imports from growing at a robust pace.

In Europe, the relocation of car production facilities to Eastern Europe is expected to create significant demand for PCCs and PCTCs, and may most likely lead to incremental shipping demand despite overall car sales in Europe showing lacklustre growth as fuel costs and a slowdown in the real estate prices dampens the desire for new cars ■

Ro-Ro/Ferries

Still tight market with lack of suitable tonnage drives charter costs up and some routes to close. Newbuilding and secondhand prices are markedly up, thereby proving as a deterrent to further newbuilding contracts.

SUPPLY & DEMAND

Unchanged market, tight capacity and rising costs

The general market for Ro-Ro and passenger ferries in Europe is somewhat unchanged from 2004. There is still an overall prevalent lack of suitable and modern tonnage, leading to increased charter costs for the few ships that eventually come free for charter.

As the competition is still fierce on the Baltic Sea, the ferry operators have found it difficult to increase ticket prices. Consequently some have opted not to continue a route because the higher charter costs were not matched by increased ticket prices. Additionally all Ro-Ro and ferry operators have felt the increased costs from rising fuel prices.

But, on the English Channel a high-speed ferry operator, partly by lowering fares, seem to have found a way to resist the competition from the Eurotunnel and the low-fare budget airlines, and some Ro-Ro operators have experienced increased cargo volumes following an increased focus on offering cargo-only services.

CONTRACTING & SHIP VALUES

Healthy contracting, and 5-20% secondhand price rises

Although still at somewhat healthy levels, the volume of new contracts signed for Ro-Ro and passenger ferries seems to be significantly down from 1st quarter to 2nd quarter of 2005. In particular rising steel prices, engine prices and a significantly longer delivery time seem to be the main deterrents to a continued contracting.

Because of rising newbuilding prices and rising charter rates, the secondhand prices of modern tonnage rose by 10-20% in just 6 months, whereas prices on older tonnage remained unchanged or slightly higher.

OUTLOOK

A continual move away from passengers to Ro-Ro cargo

Despite the overall lack of modern tonnage and an increasingly ageing fleet, the current very high newbuilding prices may most likely continue to act as a deterrent to further contracting.

Furthermore, as long as the competition on the passenger ferry routes is still preventing ticket prices from increasing, the ferry operators will continue to find it hard to justify the higher investment.

As the passenger ferry operators not only are facing competition from other ferry operators but also face competition from bridges and airlines, it may indeed take some time before ticket prices will again justify contracting a new ship at current prices.

Instead, the operators may continue their trend of focusing ever harder on pure cargo Ro-Ro services, but less and less on the passenger carrying ferry business.

As a continued high pressure on the road network within Europe is expected to lead to more cargo being moved by sea, and if a combined EU effort succeeds in reducing port costs in particular, short sea Ro-Ro shipping within EU waters may in the coming years experience continual demand growth ■

Offshore Support Vessels

Exceptionally strong offshore market as rig operators scramble to secure the required number of offshore support ships for their drilling campaigns. Ship values are up and contracting of new ships continues unabated. The short-term outlook continues to be remarkably good.

FREIGHT RATES

Exceptionally strong 1st half of 2005 all around the world

The sharp improvement in charter rates that began in late 2004 in the North Sea spot market, has so far continued well into 2005, only momentarily to lose some steam as the spring weather was unusually benign, thereby requiring less offshore support ships than is otherwise the norm.

In the Gulf of Mexico (GoM), the charter rates have maintained their upward momentum, but at somewhat lower levels compared to the North Sea. Although, the GoM support vessel utilization currently is almost full, charter rates have not yet reached the corresponding high levels as demand growth remains at a low rate.

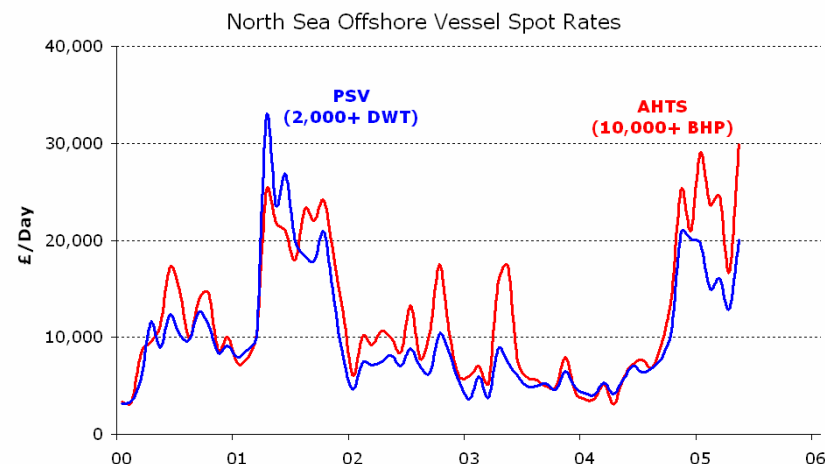
In other offshore drilling regions, charter rates have been very positive as demand continues to grow briskly. Particularly demand in the Asian Pacific waters continue to show highly positive growth. The negative pressure on charter rates from the superfluous North Sea ships that persisted during 2004, has this year almost completely disappeared.

More importantly, in the larger regions the concerns for vessel availability are growing, encouraging more inquiries for long-term charter contracts, which is to the unmistakable benefit of the ship owners.

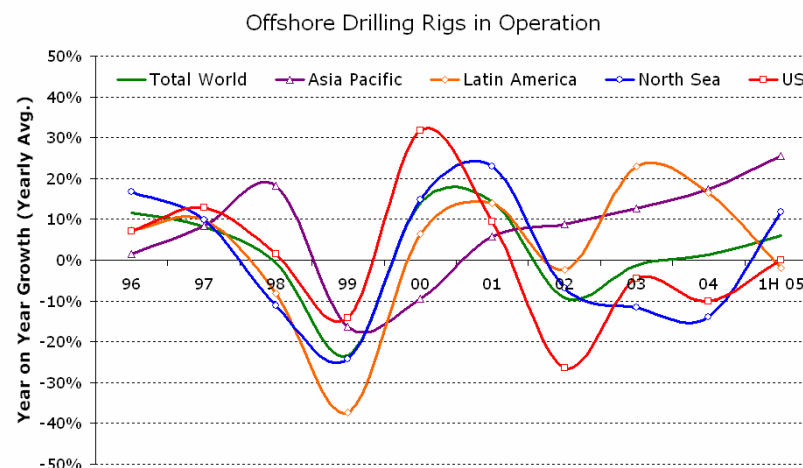
SUPPLY & DEMAND

Unremitting gas and crude oil prices bolster E & P spending

With no apparent or significantly negative effect on crude oil demand from crude oil prices above 25 \$/barrel since May 2003,



Source: Clarksons



Source: Baker Hughes Incorporated

and recently going above 60 \$/barrel, the energy companies which explore for and produce oil and gas have every reason to believe in even the relatively high-cost oilfields to turn a profit in future years. Consequently, the energy companies have boosted their Exploration & Production budgets and many deepwater discoveries are now moving into development after years of procrastination.

The increased confidence, not to mention balance sheets, was evident in the British 23rd licensing round of North Sea and Atlantic Margin licences, which during 2005 received the highest number of bids for offshore exploration blocks for more than 30 years.

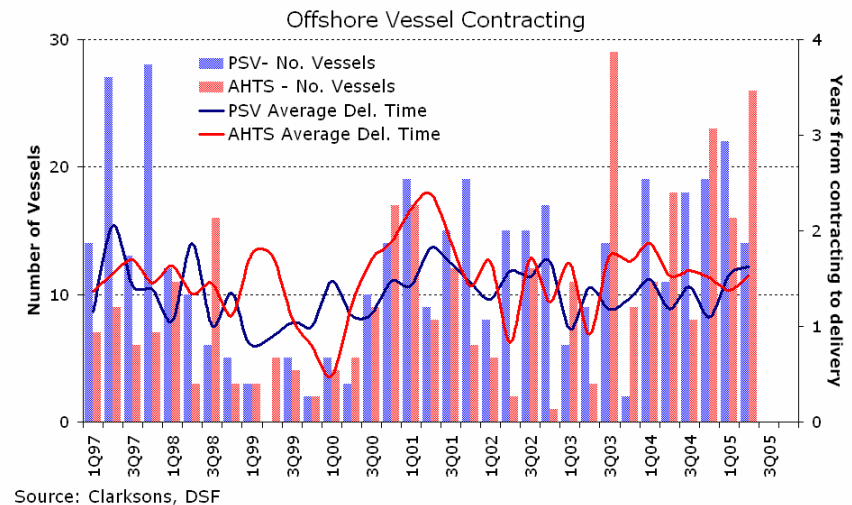
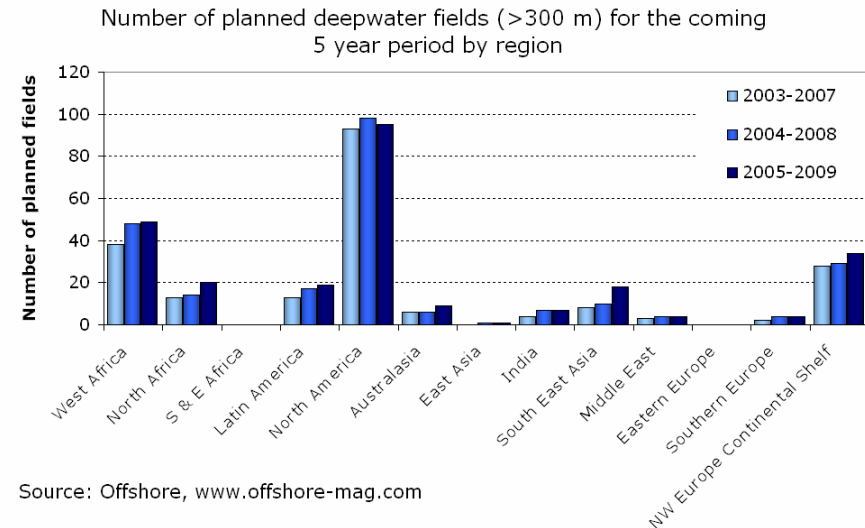
Furthermore, the increased E&P spending has led to a worldwide increase in drilling activity and a significant increase in the utilization of the world's drillships, semi-submersibles and jackup rigs.

As a higher number of rigs in operation is naturally followed by an increased demand for offshore support vessels to help tow, install and assist the rigs, the already dwindling number of free offshore vessel has left the rig operators and energy companies scrambling for the remaining free vessels to cover their drilling campaigns.

The large increase in rig utilization and the fact that only a very low number of new rigs are being build in the short term, have led to a suspicion of too few rigs available for the medium term. Subsequently, old rigs are being refurbished and orders for new rigs are committed at the rig-building construction yards.

In fact, the Norwegian Petroleum Directorate expects the number of exploration wells drilled on Norwegian fields in 2005 to be about 30, which is 5 wells less than the originally planned by the operators. The lower expectations by the NPD solely rest on the expectations of too few rigs available to the North Sea operators.

Although, the lack of available offshore platforms in the short term is *not* expected to have much of an impact on demand for offshore support vessels, it may in the longer term act as a momentary restriction on the demand for offshore support vessels.



CONTRACTING & SHIP VALUES

Very high ordering and naturally rising secondhand prices

According to Clarksons figures, 42 AHTSs and 36 PSVs were ordered during 1st half of 2005. This is the highest number of offshore supply ships ever contracted during any 6-month period, and presages a massive increase in the offshore support boat fleet.

Despite that future demand growth is probably to remain in very healthy territory for the foreseeable future, the current orderbook is unusually large, and may cause a noticeable negative pressure on charter rates following the delivery of the ships.

The large increases in charter rates have led to a 5-10% increase in secondhand values compared to the average market values 6 months earlier.

OUTLOOK

Excellent short-term outlook, but some constraints long-term

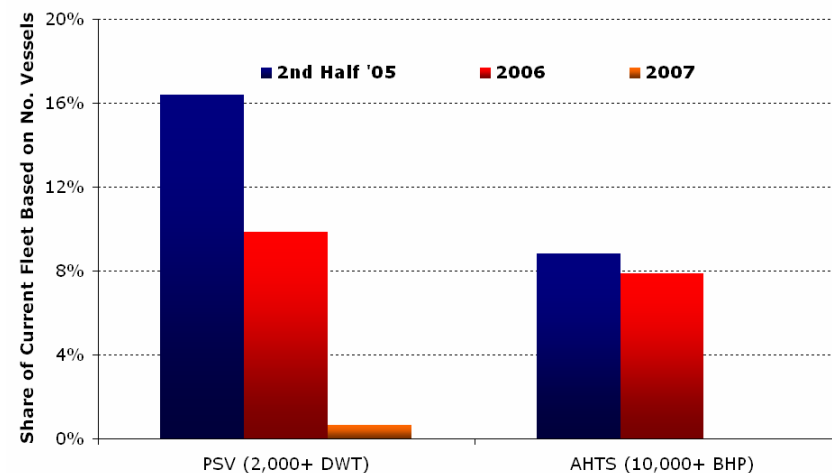
In addition to a widespread belief in continued high commodity prices, and the subsequent increased E&P spending, a large number of additional factors speak strongly for a long period ahead of above normal charter rates for the offshore support vessels.

In 2003 and 2004, the UK and Norwegian governments lowered taxes on offshore hydrocarbon production and exploration in hope of rekindling exploration in a region that otherwise was considered as mature and in chronic decline. Additionally, the UK and Norwegian governments have in their 2004 and 2005 licensing rounds put on offer the largest number of blocks ever.

Furthermore, by reopening the Barents Sea for exploration, the basis for a sustained growth in the demand for offshore supply vessels in the North and Barents Seas is indeed present.

In the Gulf of Mexico, the repairs after the Hurricane Ivan in September 2004 are still going on, and in future months the offshore support vessels in the region may probably experience

Offshore Vessels Orderbook by Year of Delivery



Source: Fearnleys

additional demand as several large hurricanes already have and are expected to cause damages to the offshore infrastructure as they pass through the GoM.

In other offshore exploration and production regions, the demand for offshore supply vessels is also growing strongly, particularly led by the high prices on crude oil and by the strong growth in the number of LNG fields.

But, although, the short-term outlook for the global demand for offshore support vessels fundamentally is excellent, the combination of a very large orderbook of offshore supply vessels and a low growth of the platform/rig fleets may cause some headache for the ship owners in the medium and longer term.

In conclusion, the outlook for the next 12 months is quite excellent, but in the longer run, until the newly ordered offshore platforms are delivered from the yards, the demand for offshore supply ships may reach a temporary upper boundary, that in combination with a still increasing fleet may lead to somewhat lower charter rates ■

Glossary

<i>Aframax:</i>	Crude oil tanker or product tanker too large to pass through the Panama Canal and below 120,000 dwt.	<i>CoA:</i>	Contract of Affreightment. Contract between shipping company and shipper concerning the freight of a predetermined volume of goods within a given period of time and/or at given intervals.
<i>AHTS:</i>	Anchor Handling Tug Supply. Offshore vessel used for jobs such as the relocation of oil rigs and anchors of the oil rigs.	<i>Dirty products:</i>	Refers to heavy oils such as crude oil or refined oil products such as fuel oil, diesel oil or bunker oil.
<i>Barrel:</i>	A volumetric unit measure for crude oil and petroleum products equivalent to 42 U.S. gallons, or approximately 159 liters.	<i>Drewry:</i>	Drewry Shipping Consultants Ltd. British shipping and transport research company. www.drewry.co.uk
<i>BHP:</i>	Break Horse Power. The amount of engine horsepower.	<i>Dwt:</i>	Dead Weight Tons. Indication of a vessel's cargo carrying capacity (including bunkers, ballast, water and food supplies, crew and passengers).
<i>Brent:</i>	Term used for crude oil from the North Sea. Brent oil is traded at the International Petroleum Exchange in London, and the price of Brent is used as a benchmark for several other types of European oil.	<i>EIA:</i>	Energy Information Administration. A subsidiary of the US Department of Energy. www.eia.doe.gov
<i>Bulk vessel:</i>	Description of vessels transporting large cargo quantities, including coal, iron ore, steel, corn, gravel, oil, etc.	<i>Fearnleys:</i>	Norwegian ship brokering company. www.fearnleys.no
<i>Bunker:</i>	Fuel for vessels.	<i>Feeder:</i>	Small container carrier.
<i>Capesize:</i>	Dry bulk carrier of more than approximately 80,000 dwt; too large to pass through the Panama Canal.	<i>FPSO:</i>	Floating Production Storage Offloading unit. Vessel used in the offshore industry to process and store oil from an underwater (sub-sea) installation.
<i>Cbm:</i>	Cubic Meter.	<i>Geared:</i>	Indicates that a vessel is equipped with a crane or other lifting device.
<i>Ceu:</i>	Car equivalent unit. Unit of measure indicating the car carrying capacity of a vessel.	<i>Gearless:</i>	Indicates that a vessel is not equipped with a crane or other lifting device.
<i>Cgt:</i>	Compensated Gross Tonnage. International unit of measure that facilitates a comparison of different shipyards' production regardless of the types of vessel produced.	<i>Gt:</i>	Gross Tons. Unit of 100 cubic feet or 2.831 cubic meters, used in arriving at the calculation of gross tonnage.
<i>Clarksons:</i>	British ship brokering company. www.clarksons.net	<i>Handy, tank:</i>	Crude oil tanker, product tanker or chemical tanker of between 10,000 and 25,000 dwt.
<i>Clean products:</i>	Refers to light, refined oil products such as jet fuel, gasoline and naphtha.	<i>Handymax, dry cargo:</i>	Dry bulk carrier of between approximately 40,000 and 60,000 dwt.

<i>Handysize, dry cargo:</i>	Dry bulk carrier of between approximately 10,000 and 40,000 dwt.	<i>Multi-Purpose:</i>	Dry bulk carrier with multiple applications, mainly as a feeder vessel or for special cargo.
<i>IEA:</i>	International Energy Agency. A subsidiary of the OECD. www.iea.org	<i>Nautical Mile:</i>	Distance unit measure of 1,582 meters, or 6,076.12 ft.
<i>IMO:</i>	International Maritime Organization. An organisation under the UN.	<i>Offshore vessel:</i>	Vessel serving the offshore oil industry.
<i>IMO I-III:</i>	Quality grades for tankers for the permission to transport different chemical and oil products. IMO I are the most hazardous products, IMO III the least hazardous.	<i>OPEC:</i>	Organisation of Petroleum Exporting Countries.
<i>Chemical tanker:</i>	Tanker with coated or stainless steel tanks (IMO I-III).	<i>Panamax, container:</i>	Container carrier with the maximum dimensions for passing through the Panama Canal (width of 32.21 metres, length of 291 metres) of approximately 3,000—5,000 teu.
<i>LNG vessels:</i>	Liquefied Natural Gas. Vessels for transporting liquefied natural gas (methane gas).	<i>Panamax, tanker:</i>	Crude oil tanker or product tanker with the maximum dimensions for passing through the Panama Canal (width of 32.21 metres and length of 289.5 metres) of approximately 50,000—80,000 dwt.
<i>Lo-Lo:</i>	Lift on – Lift off. Cargo carrying vessel that has its cargo lifted on and/or off. This type of ship may also have passenger carrying capacity (Pax-Lo) and/or Ro-Ro features (Ro-Lo).	<i>Panamax, dry cargo:</i>	Dry bulk vessel with the maximum dimensions for passing through the Panama Canal (width of 32.21 metres and length of 289.5 metres) of approximately 60,000—80,000 dwt.
<i>LPG vessels:</i>	Liquefied Petroleum Gas. Vessels used to transport ammonia and liquid gases (ethane, ethylene, propane, propylene, butane, butylenes, isobutene and isobutylene). The gases are transported under pressure and/or refrigerated.	<i>PCC:</i>	Pure Car Carrier. Car carrier built exclusively to transport passenger cars.
<i>LR1, product tanker:</i>	Long Range 1. Product tanker with the maximum dimensions for passing through the Panama Canal (width of 32.21 metres and length of 289.5 metres) of approximately 50,000—80,000 dwt.	<i>PCTC:</i>	Pure Car Truck Carrier. Car carrier built to transport small and large passenger cars (SUVs, MPVs, etc.), trucks and other contractor equipment.
<i>LR2, product tanker:</i>	Long Range 2. Product tanker too large to pass through the Panama Canal of approximately 80,000 dwt.	<i>Post-Panamax:</i>	Container vessel of approximately 4,000+ teu that is too large to pass through the Panama Canal.
<i>Medium, tanker (MR):</i>	Medium Range. Product tanker of between 25,000 and 50,000 dwt.	<i>Product tanker:</i>	Tanker vessel with coated tanks used to transport refined oil products.
<i>MTBE:</i>	Methyl Tertiary Butyl Ether. An oxygenate which is added to petrol to make the fuel burn more cleanly.	<i>PSV:</i>	Platform Supply Vessel. Offshore vessel serving the offshore oil installations.
		<i>Ro-Con:</i>	Ro-Ro vessel with container capacity.
		<i>Ro-Pax:</i>	Ro-Ro vessel with passenger capacity.
		<i>Ro-Ro:</i>	Roll On – Roll Off. Common description of vessels on which the cargo is rolled on board and ashore.

<i>SSY:</i>	Simpson Spence & Young. British ship brokering company. www.ssy.co.uk
<i>Suezmax:</i>	Crude oil tanker with the maximum dimensions for passing through the Suez Canal (approximately 120,000—200,000 dwt.).
<i>Teu:</i>	Twenty Feet Equivalent Unit. Container with a length of 20 feet (about 6 metres) which forms the basis of describing the capacity of a container vessel.
<i>Teu-knots:</i>	Unit of measure that takes account of the speed of the ships when estimating the actual supply of ships within a segment.
<i>Teu-nautical mile:</i>	Unit of measure indicating the volume of cargo, measured in teu, and how far it has been transported, measured in nautical miles.
<i>Ton-nautical mile:</i>	Unit of measure indicating the volume of cargo and how far it has been transported.
<i>Tonnage:</i>	Synonymous with "vessel".
<i>ULCC:</i>	Ultra Large Crude Carrier. Crude oil tanker above 320,000 dwt.
<i>VLCC:</i>	Very Large Crude Carrier. Crude oil tanker of between approximately 200,000 and 320,000 dwt.
<i>VLGC:</i>	Very Large Gas Carrier. LPG ship with capacity above 60,000 cbm.
<i>WTI:</i>	West Texas Intermediate. Oil price benchmark in the USA.

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Danish Ship Finance

DSF corporate division, contact details:

Head of Division

Erik I. Lassen, Senior Vice President
+45 3374-1011, eil@shipfinance.dk

Account Managers

Christian Behnke, Vice President
+45 3374-1047, +45 20754902,
cbe@shipfinance.dk

Anette Berg, Vice President
+45 3374-1042, +45 25361465,
anb@shipfinance.dk

Anne Jarling, Vice President
+45 3374-1045, +45 20752466,
aja@shipfinance.dk

Knud Jæger, Vice President
+45 3374-1024, +45 20752465,
knj@shipfinance.dk

Berit Koertz, Vice President
+45 3374-1032, +45 20754901,
bek@shipfinance.dk

Morten Snede Larsen, Assistant Vice President
+45 3374-1055, msl@shipfinance.dk

Henrik Soegaard Olsen, Vice President
+45 3374-1033, +45 40539666,
hso@shipfinance.dk

Hanne M. Pedersen, Vice President
+45 3374-1029, +45 20752468,
hmp@shipfinance.dk

Ole Stærgaard, Vice President
+45 3374-1027, +45 20752467,
ols@shipfinance.dk

Market Research

Nikolaj Frederik Kamedula, Analyst
(+45 3374-1063, nik@shipfinance.dk)

Tino Henriksen
(+45 3374-1017, tih@shipfinance.dk)

*For enquiries regarding this report,
please contact
Nikolaj Frederik Kamedula.*

Danmarks Skibskredit A/S
Sankt Annae Plads 3
DK-1250 Copenhagen K
Denmark

Phone: +45 33 33 93 33
Fax: +45 33 33 96 66
Email: danish@shipfinance.dk
Website: www.shipfinance.dk