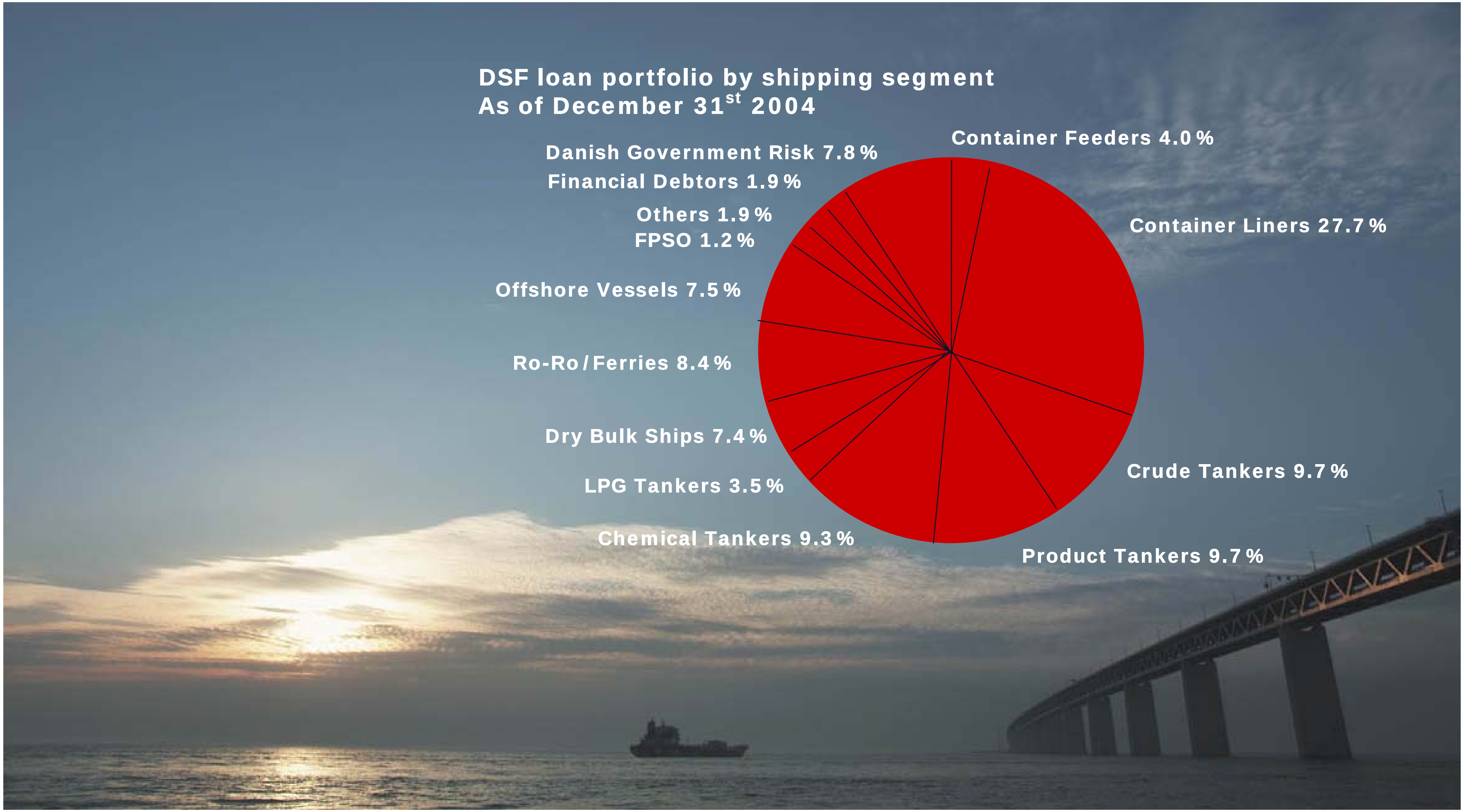
Danish
Ship Finance

Shipping Market Review – 2004



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Shipping Market Review – 2004

Introduction

This report reviews the central developments of 2004 for the main shipping segments in which Danish Ship Finance (DSF) has exposure.

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General Developments

Apart from a very few shipping sectors, the leading range of shipping markets, from car carriers to oil tankers to dry bulk vessels, have all displayed extraordinarily large returns during 2004, almost rivalling the IT-sector's returns in the boom-days of 1999-2000. Reassuringly, the returns of shipping, compared to that of the IT-boom, have one very distinctive difference in the fact that, apart from the unpredictable ship prices, the returns of shipping companies have been real cash income and not based primarily on expectations of future earnings.

Unfortunately, the large amounts of cash generated from the daily operations have a few potential drawbacks that may be in the process of amplifying the highly cyclical nature of shipping – magnifying the current boom and worsening the following bust.

When so much excess cash is generated, the shipping companies are forced to either pay large dividends, to reinvest or to pay off debt. After paying off the most expensive debt, the option of reinvesting is often seen as the most obvious choice. This has led to huge numbers of new ships being contracted at the shipyards at ever higher prices and furthermore led to the prices of secondhand ships being driven sky-high. Naturally, much of the contracting at the shipyards and a large share of the price increases are purely down to an improved outlook for the future shipping demand, and thus perfectly justifiable. But a noticeable part of the contracting and price increases is unfortunately also because of an extensive liquidity surplus, leading to excess investment in new capacity and added willingness to pay higher prices.

These adverse effects and the quickly changing nature of shipping ought to be a cause for great apprehension for everyone involved in financing ships.

The high earnings for shipping in 2004 were caused by a never before seen synchronized growth in GDP for both the OECD area and the larger economies outside the OECD. Particularly the large economies of China and USA have shown exceptional demand for raw materials and energy commodities with direct impact on commodity prices and on demand for seaborne transport.

As high commodity prices reduce overall demand growth and the Chinese economy continues to walk a thin line between over-heating and a soft landing, the outlook for 2005 is a slowdown in global economic growth. This may have negative repercussions for everything from demand for raw materials to commodity prices in general. For shipping, the lower economic growth may ultimately turn into less port congestion, lower shipping demand and thus lower earnings and ship prices.

On the positive side, the dollar weakness is not expected to impact demand for shipping in 2005 in a significantly negative way. Continuing the trend of 2004, European manufacturers may be forced to outsource further of their production to China, thereby leading to growing transport requirements. And in the US a low Dollar may lead to increased exports and industrial production, thus preventing the negative effects from the high energy prices from being too visible on consumption growth.

In conclusion, the outlook for 2005 continues to be favourable, but a return to more normal levels of earnings and ship prices may be expected for all shipping sectors within coming years.

Executive Summary

- *Ship Building:* Contracting prices continued to rise strongly carried by an ordering frenzy and rising building costs. New shipbuilding capacity is continuously added possibly leading to a return of a significant surplus shipbuilding capacity in a few years' time.
- *Container Ships:* Euro-strength drives European outsourcing and growth in Chinese exports. Charter rates put past records to shame whereas freight rates per teu only reluctantly edges upward. The outlook for demand growth continues to be supportive of high earnings, but is partly relying on congested ports to stay heavily congested.
- *Crude Tankers:* 2004 exceeded all expectations on earnings, ship prices and contracting activity. But the crude tanker market may just now have passed its peak as high oil prices and improved stock levels take the edge of shipping demand growth in 2005.
- *Product Tankers:* Global refineries run at high utilization levels supporting a strong trade in refined oil products. Contracting of newbuildings is down and prices continue to rise. The short-term outlook is somewhat clouded by significantly lower demand growth than in 2003-2004.
- *Chemical Tankers:* Strong global demand for chemical products as well as a generally high demand for product tankers drew chemical spot and CoA rates to new highs. Outlook continues to be positive, but a slowdown in global economic growth may impact charter rates.
- *LPG Tankers:* First the coastal ships and then the entire range of LPG vessels witnessed exceptionally strong rates with clearly positive consequences for ship prices. The 2005 outlook continues to be positive, but rates may come down from their record levels of 2004.
- *Dry Bulk Ships:* So far, the efforts of slowing China's steel production doesn't seem to be much effective. The persistently high growth has had amazingly positive effects on ship earnings and prices. Demand growth is expected to ease in 2005, thus earnings are expected to be lower but still at healthy levels.
- *Car Carriers:* As global car sales show robust growth and the PCC market is in acute under-supply, charter rates have gone sky-high. Despite ever rising contracting prices the orderbook is now extraordinarily big. The outlook is still very sound but the fleet may be catching up.
- *Ro-Ro/Ferries:* Larger EU and congested roads provided positive cargo growth, but cheap airfares continue to take passengers away from ferry lines within Europe. An elderly fleet and attempts to reduce road congestion may turn into more orderings of newbuildings.
- *Offshore Support Vessels:* Finally, the long-lasting miserable charter rates showed extraordinary strength as exploration and drilling activity advanced worldwide. Future supply ship demand is expected to grow further, in the North Sea partly because of improved taxation and licensing conditions.

Contracting prices continued to rise strongly throughout the year carried by an ordering frenzy and rising building costs. New shipbuilding capacity is continuously added and may possibly lead to a return of a significant surplus shipbuilding capacity in a few years' time.

CONTRACTING PRICES

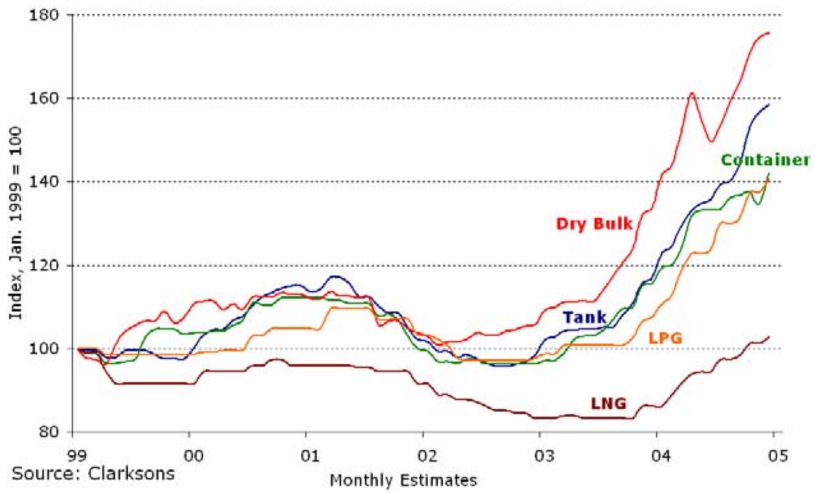
20-40% y-o-y average increase in contracting prices
Throughout 2004 average contracting prices have exhibited an almost relentless rise, surging 20-40% since the end of 2003, with some ship types witnessing even greater rises. This is a continuation of previous years' price increases and corresponds to an accumulated average rise of about 20-80% above the 10-year lows of 2002.

Rising steel prices is the main culprit behind the rising contracting prices, and together with a depreciating USD against most major shipbuilding currencies (KRW, JPY and EUR) the shipyards have persistently been forced to raise ship contracting prices. According to Clarkson data, the spot price on steel plates in Japan has risen about 170 % since early 2002. For a shipyard relying completely on short-term supplies, the steel price increase would cause the total shipbuilding costs to have risen by an estimated 25-50%.

For shipyards relying on short-term supplies of steel the higher prices have had damaging effects on their financial performance. This has led some yards to try to renegotiate shipbuilding contracts, threatening to not honouring the shipbuilding contract on grounds of the refundment guarantee from the bank not being issued making the shipbuilding contract null and void.

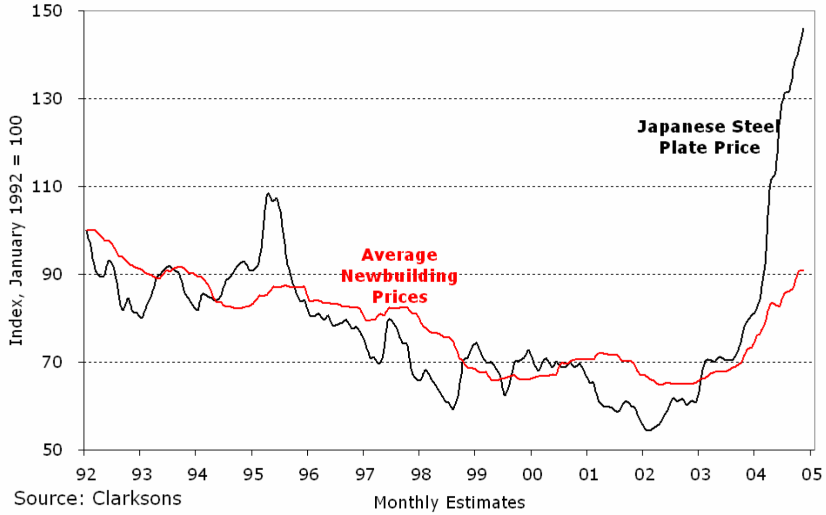
Abruptly rising prices on steel and the raw materials used for producing steel – mainly coking coal, steam coal and iron ore – have been a wake-up call for almost every shipyard and steel mill around the world. In response to the rising costs and insecurity of supplies, the procurement of raw materials and steel is to an

Newbuilding Average Price Index, 1999-2004



Source: Clarksons

Average Newbuilding and Steel Prices, 1992-2004



Source: Clarksons

increasing extent done on long-term contracts thereby reducing the possibility of future increases in steel prices and thus ultimately ship contracting prices.

Contracting Activity

Contracting activity continues to power worryingly ahead
Despite the noticeable increases in contracting prices and a continued lengthening of the delivery time, the shipping companies did not seem to be discouraged from continuing their buying spree from 2003 all throughout 2004. From end of 2003 to end of 2004 the average delivery time has lengthened by ½ a year from 2.7 to 3.2 years.

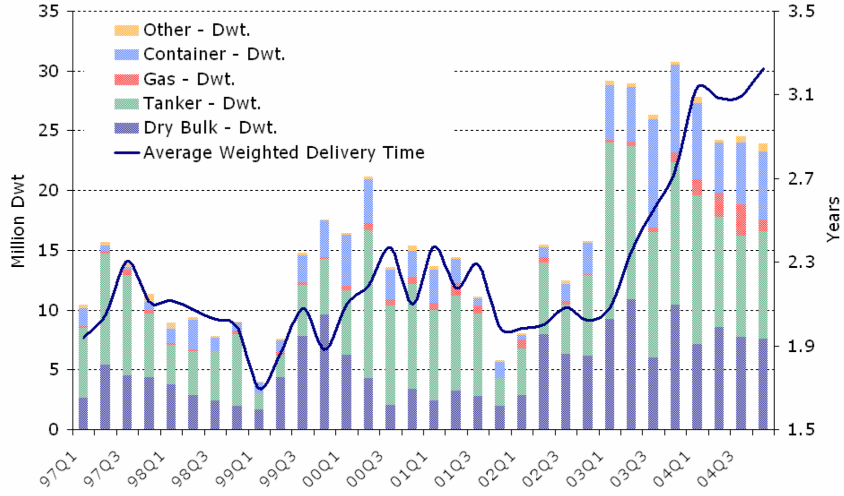
At the beginning of 2004, most orderbooks of the major Asian shipyards were already occupied at least 2½ years ahead leaving shipping companies with the desire of earlier delivery with only a few and expensive options. Thus either they in 2004 turned to the predominantly more expensive European shipyards, contracted at the smaller and less experienced Asian shipyards or paid top price for early delivery at the major Asian shipyards.

Despite the much higher prices the shipping companies' desires to obtain early delivery have meant that during 2004 a sizeable 5.3 million dwt has been contracted with expected delivery in 2005. Respectively, 22.6 million dwt has been contracted in 2004 with delivery in 2006, 51.7 million dwt with delivery in 2007 and 20.9 million dwt with delivery in 2008 or later.

The above contracting numbers of 2004 stand to testify that even despite a general notion of shipbuilding capacity being completely utilized, shipping companies nevertheless almost always are capable and willing to seek out more shipyard slots – even though the slots are only available at a much higher price. And more importantly, the shipyards are quickly able to increase their production efficiency and capacity – e.g. by building on dry land instead of in dry-docks, or by adding new shipyards altogether.

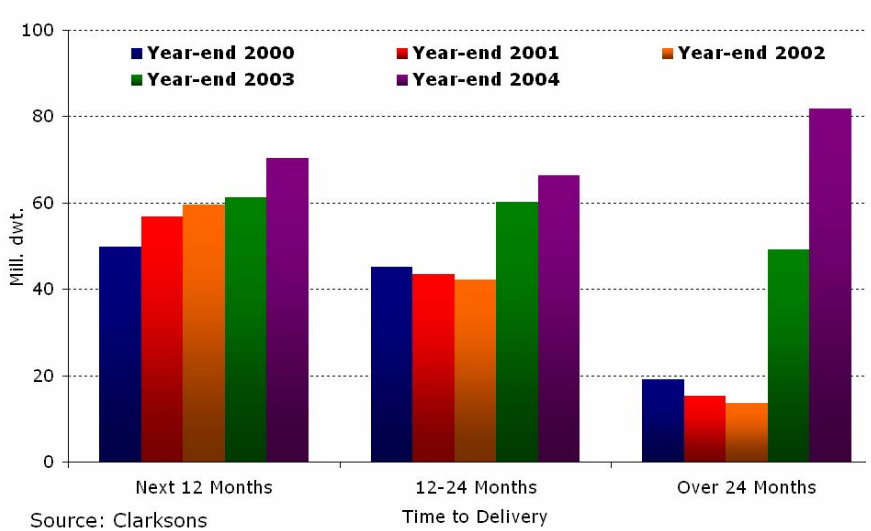
In particular the European shipyards have benefited from the tight capacity situation at the Asian shipyards, with the contracting at

Total Merchant Ship Contracting, 1999-2004



Source: Clarksons

Total Merchant Ship Orderbook by Time to Delivery



Source: Clarksons

EU shipyards being rather obviously affected by the deadline March 31st 2004 for contracting ships to be built with state subsidy. EU has subsequently decided to extend the deadline one year. Up to the initial deadline, contracting of particularly containerships has shown the highest levels ever. Past the initial EU subsidy deadline, contracting dropped considerably but still maintained some momentum motivated by the desire for early delivery of feeder-sized container ships and the extended deadline.

Despite the revived contracting the European shipyards have been dealt a significant blow during 2004 as the Euro continued to appreciate against the USD, notably during 4th quarter, rendering the European yards less cost-competitive against their Asian competitors. This comes at a time when the large European yards are looking hard for orders of cruise and Ro-Ro ships.

OUTLOOK

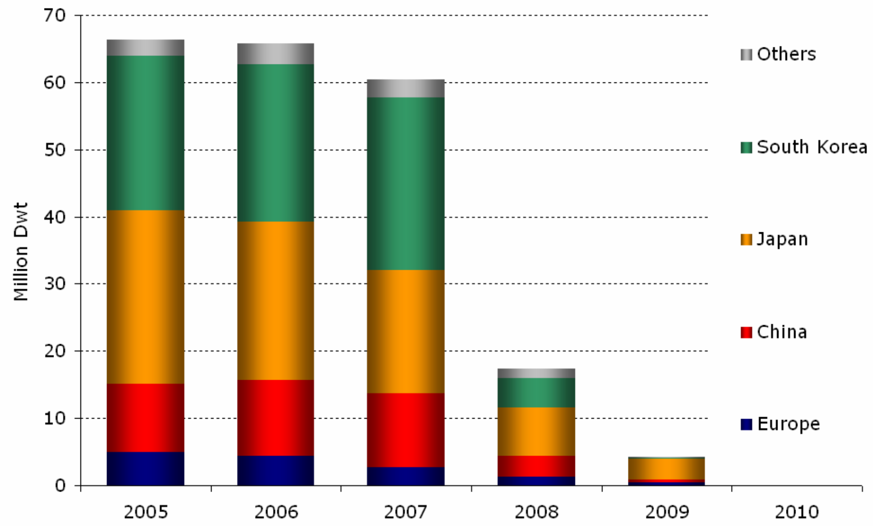
Much lower contracting activity may lead to falling prices
Almost every large Asian shipyard has its orderbook fully booked 3 years ahead, and even some European shipyards are almost fully booked 2-3 years ahead. This unique situation provides the shipyards with a considerable pricing power and may in the next year or two most likely keep contracting prices from falling too fast or too deep.

But apart from a few ship segments, the overall supply of ships is expected to outpace demand growth and thus has negative implications for freight rates, ship values and ultimately contracting activity. Not looking at steel and other building costs, the above imply that shipyards may once again come under pressure to lower prices in order to retain market share.

In addition to expectations of lower contracting activity, global shipyard production capacity is expected to keep growing. In the longer term this may lead to a return of a significant excess building capacity and thus a negative pressure on building prices.

For 2005, the shipyards' desire to recoup recent losses from rising steel prices and a lower USD may nonetheless keep shipbuilding prices from falling to a worryingly extend.

Current Orderbook by Year of Delivery and Region



Source: Clarksons

+ *Asian and to a certain extent European shipyard capacity is occupied until end of 2007 providing shipyards with considerable pricing power thereby keeping the prices from falling too fast or too deep.*

+ *European shipyards in particular may gain from the future need of fleet replacement in the Ro-Ro segments.*

+/- *Changes in steel prices and currency exchange rates may both negatively and positively impact contracting prices.*

\- *With shipping demand expected to slow down in the short term, average earnings may fall with negative consequences for prices and contracting activity.*

\- *The currently very large backlog of orders could bring the shipyards to expand their capacity thereby causing a very high surplus of shipyard capacity once the current orders have been delivered.*

Container Ships

Euro-strength drives European outsourcing and strong growth in Chinese exports. Charter rates put past records to shame whereas freight rates per teu only reluctantly edges upward. The outlook for demand growth continues to be supportive of high earnings, but is partly relying on congested ports to stay heavily congested.

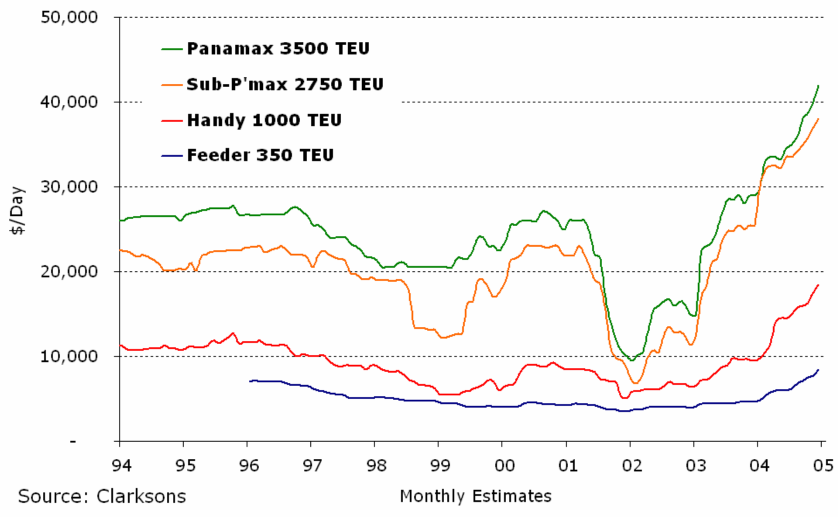
Freight Rates

Unparalleled charter rates and slowly rising income per box
For the container ship chartering markets these are surely unprecedented times. The almost total lack of investment in new ships for the charter market (generally smaller than 4,000 teu) during the last 2-3 years is now clearly evident in the charter rates of these ships as they almost daily post new record levels. In combination with a strained shipbuilding capacity, thereby limiting future fleet growth, the escalated deficit of ships on the charter market has resulted in ships being chartered more and more in advance of the particular ships coming off their previous contracts, and furthermore resulted in new charter contracts being agreed on for increasingly longer periods.

Conversely the freight rates per teu showed only small signs of improvement during most of 2004 (note that graph to the right, below ends at 3q04). The largest rises (8-12 pct) in freight rates per teu were seen on the main routes from Asia to Europe, whereas the Transatlantic trade remained at relatively low and almost constant freight rate levels.

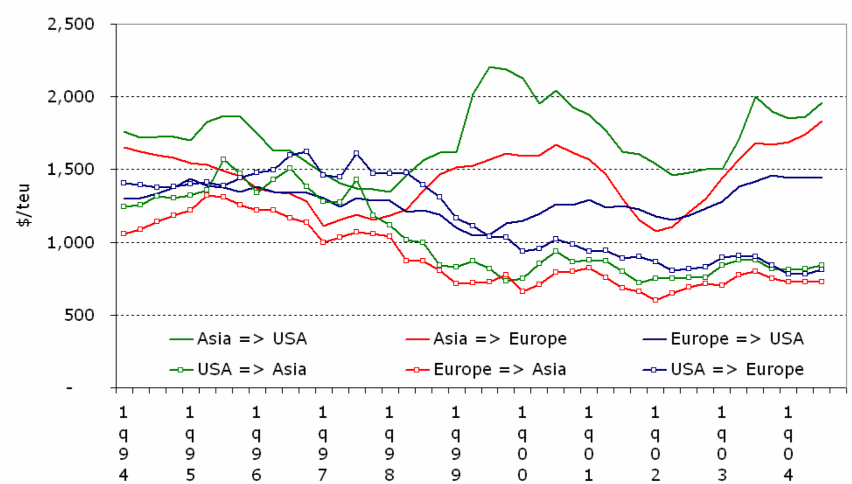
For container carrier companies who rely heavily on chartering external ships for their carrier operations, the rising charter costs and only slight increases in average income per box have posed particularly challenging circumstances. Moreover, rising bunker costs, canal dues, terminal charges, repositioning costs, container prices and congestion problems have meant persistently rising operating costs for all container carriers. But fortunately for most carriers the higher ship utilization has given higher revenue and much better financial performance.

Container Timecharter Rates, 1994-2004



Source: Clarksons

Average Freight Rates per Teu, 1994-2004



Source: Containerisation International

EUR strength drives changing and growing container trade

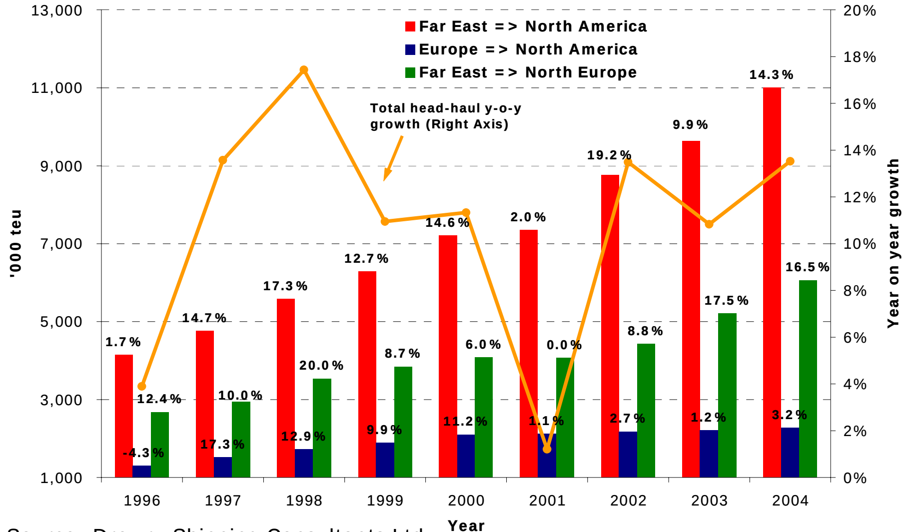
Throughout 2004 European container imports from the Far East continued to show impressive strength growing by around 16.5%, according to preliminary data from Drewry. This is a slight reduction from the 2003 growth levels of an impressive 17.5%. Conversely, North American container imports from the Far East seemed to regain strength with container trade growing by 14.3% in 2004 up from a lesser 9.9% the year before.

Though slightly less in 2004, European import growth continues to outpace the North American equivalent. Particularly the sustained strength of the Euro against the USD, and accordingly against the Chinese Renminbi, has strengthened the comparative advantages of Chinese manufacturing, thereby supporting a further relocation of production from Europe to China.

Another consequence of the appreciated Euro has been that European exporting companies have had to cut costs in order for its exports to remain competitive on the large US market. Thus, to the detriment of the US-bound Transatlantic container trade, which has stayed flat throughout 2004, the European manufacturing industry has had to relocate parts of its production from Europe to low-cost countries such as China. This has at least for a short number of years been instrumental in boosting Chinese export growth to both Europe and North America.

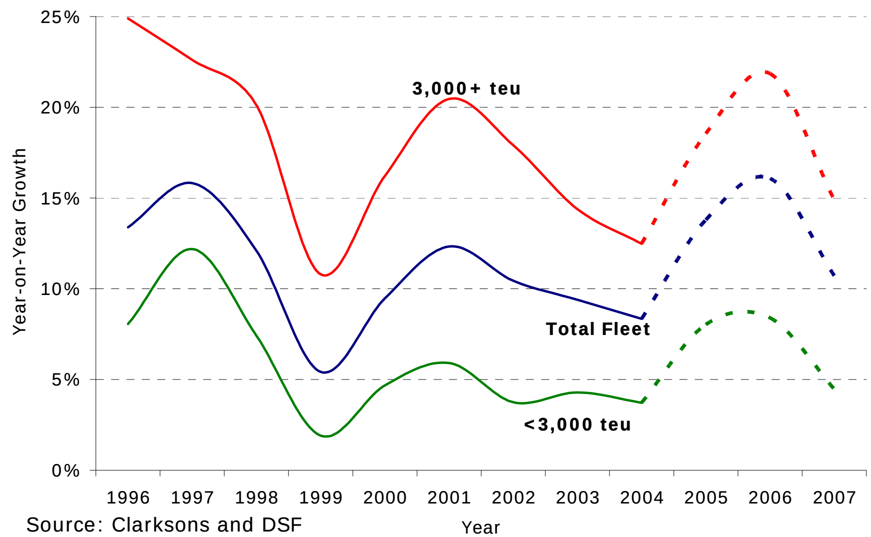
Not only the container volumes going out of China are experiencing an enormous growth, but also the Chinese imports are flourishing. Measured in numbers of containers, particularly the European exports to China are experiencing almost similar growth levels as the European import growth. In addition to a large number of containers with disassembled factory equipment that is being relocated from Europe and North America to China, Chinese imports of containers have been boosted by a significant growth in semi-finished goods produced in Europe and elsewhere for final assembly in China.

Major Head-haul Container Trade, 1996-2004



Source: Drewry Shipping Consultants Ltd

Growth of Fully Cellular Container Fleet, 1996-2007



Source: Clarksons and DSF

The high growth in trade has had similar implications for the demand for containers. Consequently carriers have experienced increasing problems finding available containers within Asia and seen increasing costs when relocating empty containers from the Western markets.

In addition, container carriers have had to fight a growing problem with congested container terminals around the world, causing increasingly longer time spent in port waiting to discharge. Mainly in the major US West coast ports as well as in the larger European ports, terminal operators have experienced serious problems in keeping up with the rapidly growing exports from Asia. For US imports this has led to container ships being diverted to other West coast ports or sent through the Panama Canal, thereby adding further tonne-miles to shipping demand. As a result, port congestion has added further impetus to shipping demand and helped in soaking up all available shipping capacity.

Contracting & Ship Values

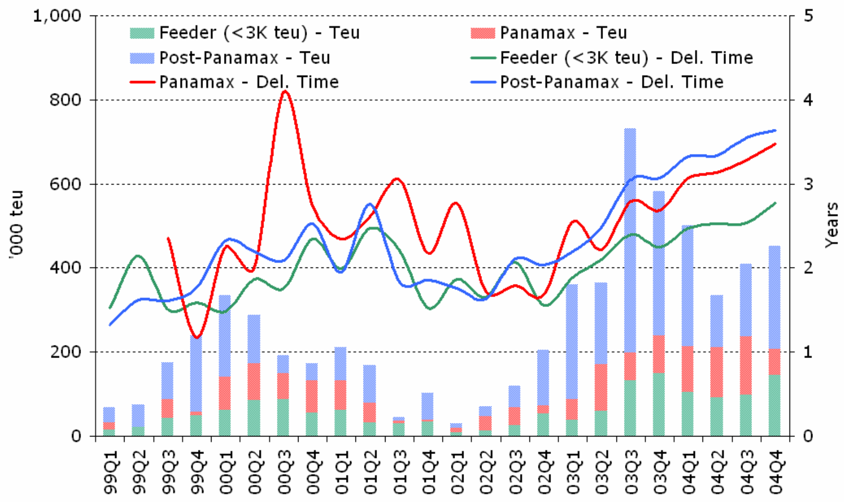
Ship contracting virtually indifferent to soaring prices

In spite of container contracting prices having increased by 10-25% over the year and an already massive orderbook, total contracting activity has only gone down from a total of 2.04 million teu in 2003 to a total 1.7 million teu in 2004. Contracting of ships smaller than post-panamax has actually gone up by 21% since 2003, clearly indicating the prevalent lack of tonnage in these smaller segments.

The diverging trends in contracting activity between the small and the large container ships is partly down to shipbuilding capacity of the very large ships being almost completely occupied well into 2008. The lack of ship berth capacity has even prompted some shipping lines to convert some of their existing orders into larger ships instead of ordering additional ships. By now the largest ships on order approach or exceed 10,000 teu a piece.

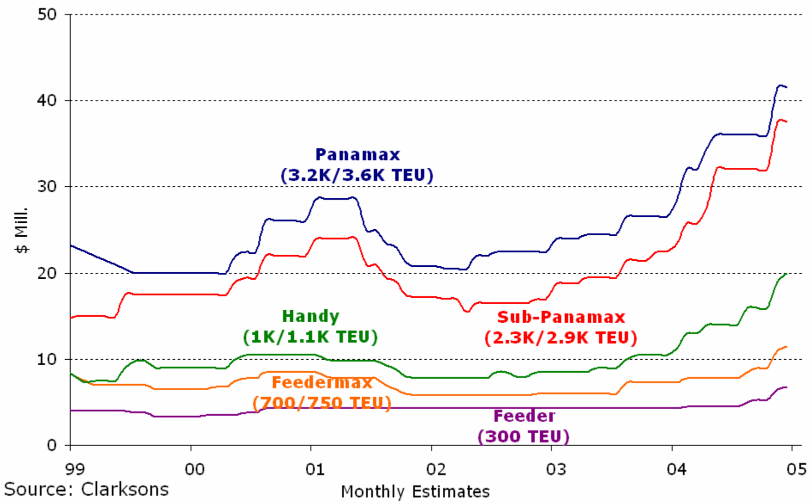
According to Clarksons figures, the increased timecharter rates and newbuilding prices has led to an increase in secondhand prices of 10 year old container ships of around 55-90% during 2004.

Container Ship Contracting, 1999-2004



Source: Clarksons

Prices of 10 Year Old Container Ships, 1999-2004



Source: Clarksons

OUTLOOK

Fleet growth to take giant steps upward in coming years
With fleet growth in 2003 and 2004 being some of the lowest in a decade it is not so surprising that the last two years have been phenomenal years for the container shipping companies (see lower graph page 8). And this low supply growth was at a time when container shipping demand grew strongly as the significantly positive effects from China's WTO membership and following production relocation was at it highest.

By contrast, the fully cellular container ship fleet is in 2005 and 2006 set to grow at a pace close to the fastest experienced in a decade – 14% in 2005 and 16% in 2006.

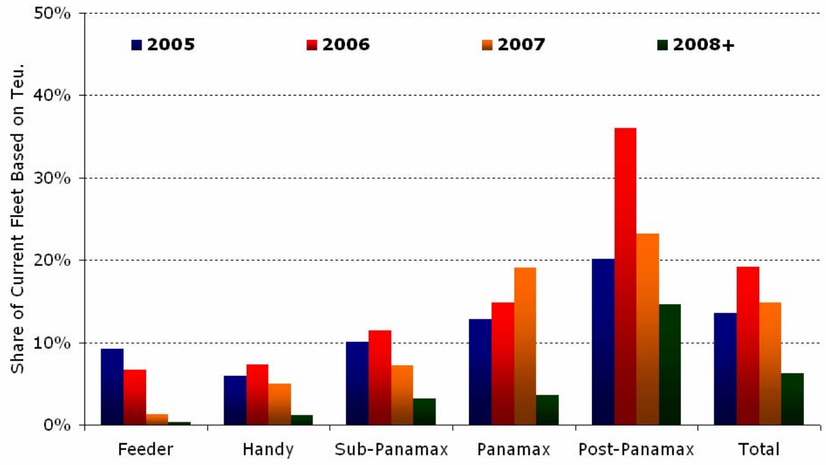
Particularly the ships servicing the major inter-regional trade lanes are in the coming years going to experience a remarkable 18-22% annual growth in capacity. Compared with a historic annual average growth in demand on the head-haul trades of around 10% these are staggering supply growth figures and may lead to some concern.

Conversely the intermediate and feeder segments show a much lower fleet growth of around 8% in the coming years. As the short sea segments show an increasing share of ships older than 25 years the 2006-2007 growth figures may turn out even lower.

Despite fleet growth picking considerable up in the coming years, the general market consensus is that total ship supply will only outgrow demand by a small margin. The confidence in particularly the charter market to stay tight for a very long period is now so strong that ships are fixed up to 2 years in advance and for considerably longer periods in order to ensure adequate berth coverage.

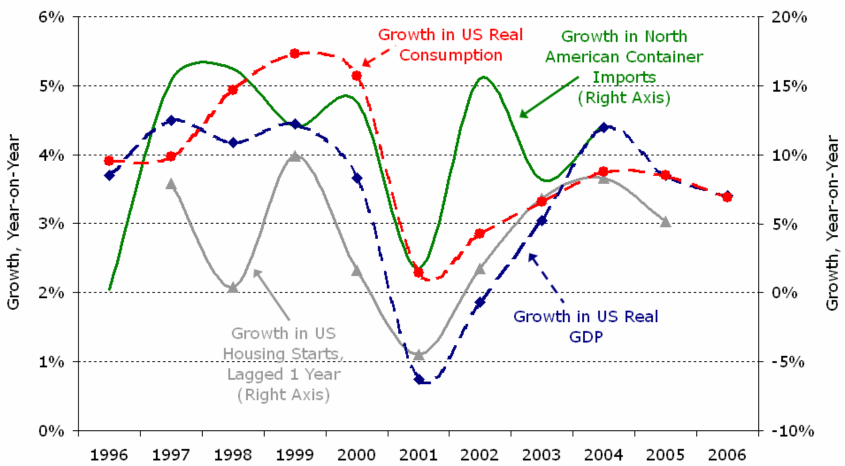
On the charter market it is particularly the low fleet growth that is leading to confidence in continually high charter rates.

Container Ship Orderbook by Year of Delivery



Source: Clarksons

North American Container Imports and US Economics



Source: US Fed.Gov.Stat., Drewry and JPMorgan ("World Financial Markets 2005", 12.15.04)

But on the inter-regional deep sea trade lanes it is to some extent the congested ports that add strength to the belief of a continued tight supply-demand balance in the coming years. This may in the longer run be seen as a worrying sign, as a quicker than expected resolve to the congested ports may suddenly lead to a freeing of capacity and a sudden drop in fleet utilization. Reassuringly, the debottlenecking of container terminals around the world is not expected to be an easy or fast manoeuvre, and the congestion may most likely get worse before it gets better.

On the negative side, rising interest rates have led to a slowdown in the number of US housing starts, pointing to a lower US GDP growth for 2005 and thus potentially a lower growth in North American container imports (see lower graph page 10). In Europe interest rates have remained low and are still believed to be in support of growth in investments and consumption.

Beside a helping hand from congested ports, container shipping demand is expected to see strong growth especially from Chinese exports of clothing and textiles to Europe and the US. This stems from the fact that as of January 1st 2005, European and American import quotas on Chinese manufactured textiles and clothing were lifted almost completely.

Moreover, container exports from China is expected to continue to grow strongly as the Euro-strength demands more cost-cutting measures and thus a continued relocation of production from Europe to China and other low-wage countries. In addition, a potential appreciation of the Chinese Renminbi against the USD is not expected to have a visible negative effect on Chinese exports, mainly because the Chinese comparative advantages still are much more significant than a 5-10% Renminbi revaluation.

In conclusion, despite that rising interest rates and very high oil prices have lead to a slight slowdown in global consumption growth, the fundamental container trade is nonetheless expected to remain strong in 2005. Thus, dependant on the port congestion to persist, ship supply growth on the deep sea trades is expected to slightly outpace demand, whereas the charter market is expected to stay very tight throughout 2005.

+ *Somewhat low numbers of smaller container ships in the orderbook and an ageing fleet in these segments support a long period of high charter rates in the charter market.*

+ *Lifting of US and European import quotas on Chinese manufactured textiles and clothing as of January 1st 2005 may most likely lead to a surge in Chinese exports of textiles and clothing.*

+ *Mounting port congestion may cause lower available ship capacity as ships wait to berth thereby alleviating any potential excess supply of ships.*

- *In the longer run, congested ports and railways may negatively influence growth in cargo volumes and thus curtail growth in demand for container ships.*

- *Very high numbers of deep sea container ships being delivered until 2007 add to the risk of a containership oversupply.*

- *Rising US interest rates may have a negative impact on US private consumption and housing construction.*

- *High oil prices may reduce growth in private and business spending.*

- *Protectionist behaviour and/or rhetoric by the US and Europe may reduce the incentives to outsource production to the Far East, thereby curbing future container trade growth.*

2004 exceeded all expectations on earnings, ship prices and contracting activity. But the crude tanker market may just now have passed its peak as high oil prices and improved stock levels take the edge of shipping demand growth in 2005.

FREIGHT RATES

A blisteringly hot spot market exceeds '03 by large margin
According to Clarksons data, the average earnings of a modern VLCC on the spot market have been a staggering USD 94,900 per day. By comparison, the same figure in 2003 was USD 52,500 per day, which at that time was considered as absolutely amazing. For all other crude tanker segments similarly incredible earning figures are to be found.

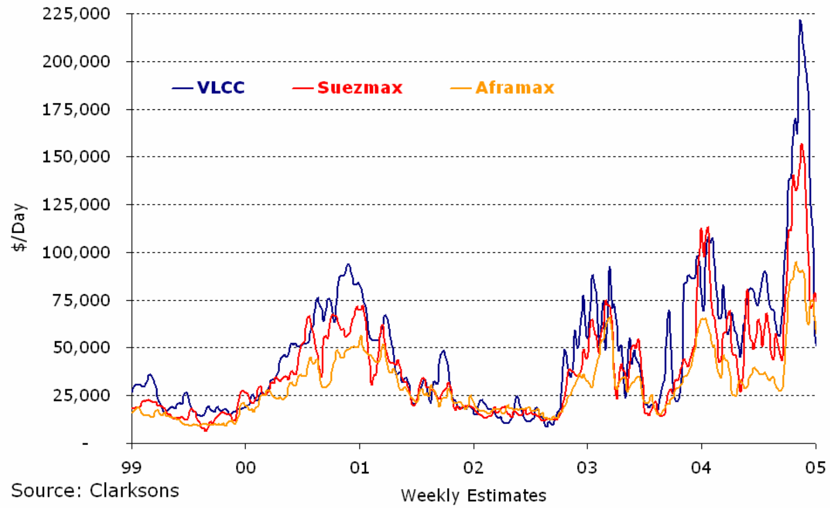
During the very last weeks of 2004 and into 2005 the spot freight rates fell very dramatically as OPEC signalled a cut-back of its oil production and high numbers of charter-free ships gathered in and around the Persian Gulf. For tanker companies, who were otherwise boasting with confidence, the significant drop in freight rates came as quite a surprise at a time that usually is the peak-season, and may imply that the market has been overheated.

SUPPLY & DEMAND

Fear of oil supply shortage trigger best ever tanker demand
Rapidly growing oil demand in China and the US has put increasing pressure on production facilities in the Middle East as well as in the western countries. In July 2004 the OPEC spare production capacity was down to an estimated 0.5-1.0 mb/day, according to the EIA, and has remained at that level throughout 2004.

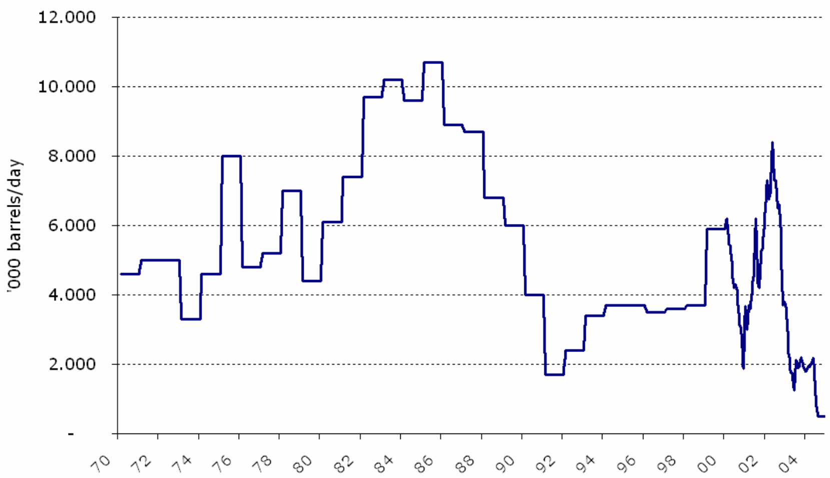
Global oil demand has been additionally boosted by the desire to build strategic oil reserves following the Iraqi war, political turmoil

Crude Tanker Spot Earnings, 1999-2004



Source: Clarksons

OPEC Spare Production Capacity, 1970-2004



Source: IEA and EIA

in Nigeria and Venezuela along with terrorist attacks against oil related facilities in the Middle East.

As short and middle range European and Former Soviet Union (FSU) oil production have been running at maximum capacity, the far-away Middle East producers and in particular Saudi Arabia to an increasing degree have had to act as swing supplier. On top of more oil being transported this has led to longer transport distances and thus more demand for oil tankers.

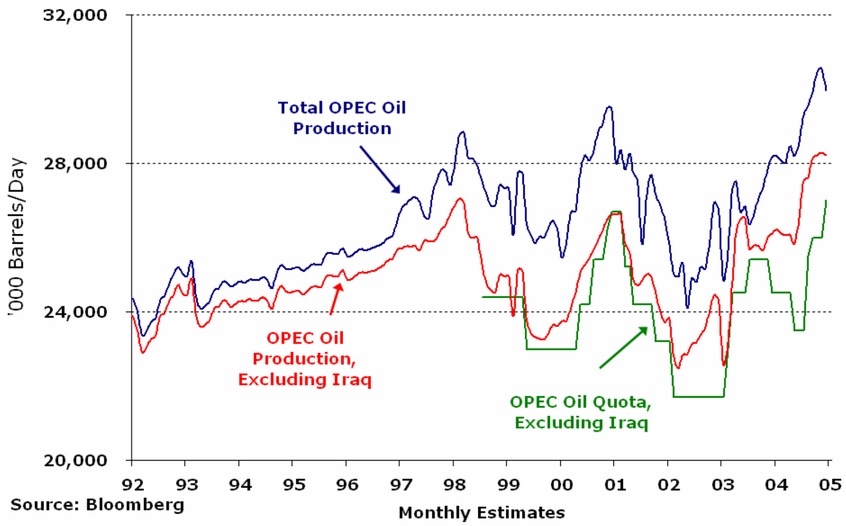
The growth in Chinese imports of crude and refined oils were primarily due to a wish to build oil storages, an increased industrial production and increased numbers of cars and trucks. In addition, widespread shortages of electrical power spurred companies to invest in back-up generators running on diesel oil. As these generators are less fuel efficient, the demand for oil was amplified.

According to the IEA, Chinese oil demand growth was drastically reduced from year-on-year growth of 22 % in the first half of 2004 to a much lower 8.4 % in the second half of 2004. In particular a marked tightening of the Chinese credit-giving and raised interest rates, but also increasing problems with bottlenecks in the oil related infrastructure, led to the conspicuous slowdown in oil demand. As the credit-tightening measures and bottlenecks are expected to persist for an extended period and because *non-oil* power generating capacity is expected to gradually catch up with power demand, the IEA expects Chinese oil demand growth to come down from 14.7 % in 2004 to 5.7 % in 2005.

In the US a similar slowdown in oil demand growth occurred between first and second half of 2004, as US oil demand growth fell from around 2.5 % to 1.7 %, measured year-on-year. For 2005, the IEA and EIA expect a US demand growth of around 1-2 %, tailing off in the second half of 2005.

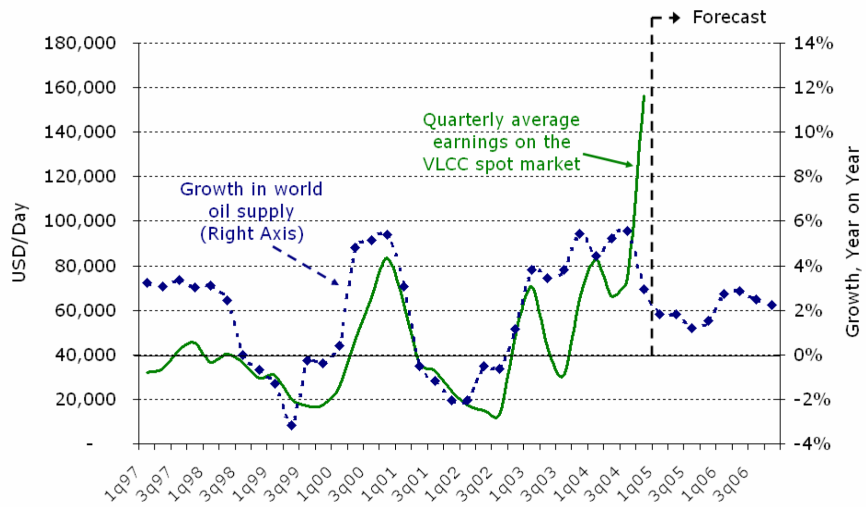
Despite demand growth in two of the most influential countries showing such large reductions in the second half of 2004, the market's overall fear of an oil shortage continued to escalate almost all throughout the year.

OPEC Oil Production and Quotas, 1992-2004



Source: Bloomberg

VLCC Earnings & Global Oil Supply Growth, 1997-2006



Source: Clarksons, EIA (supply growth forecast from STEO, January 2005)

Several one-off events of longer or shorter duration were instrumental in encouraging the supply fears. Throughout the year, persistent news of supply disruptions in Iraq and other Middle Eastern countries had significant bearing on the already prevalent supply fears. Secondly, Hurricane Ivan, sweeping across the Gulf of Mexico in mid-September, cut US oil production by around 10 % for more than 2 months whereby the US required extra imports from distant sources in order to meet demand. Furthermore, civil unrest in Nigeria and political uncertainty in Venezuela added to the fears of production shutdowns, and in Norway a long-lasting strike reduced Norwegian oil and gas production.

CONTRACTING & SHIP VALUES

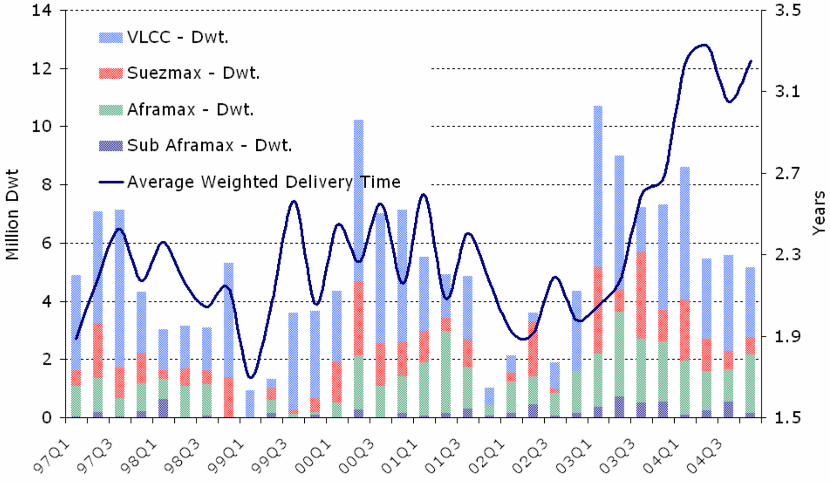
Contracting continues undauntedly and prices soar
Contracting of crude tankers continued throughout 2004 despite an already sizeable orderbook and contracting prices approaching or exceeding all-time highs. With a very few exceptions, new contracting is solely due to optimistic demand expectations, and not as previously on the back of stricter regulation commanding a large fleet replacement program.

According to Clarksons figures, secondhand prices of 5 year old crude tankers have increased by about 50-60% year-on-year, whereas contracting prices have risen by a lower 30-45%. With 5 year old ships now being priced at levels close to the newbuilding prices and recently delivered ships being priced 20-40% above newbuilding prices, current secondhand prices bear clear evidence that the market sees the very high earnings as a short-term event and not a more permanent condition.

OUTLOOK

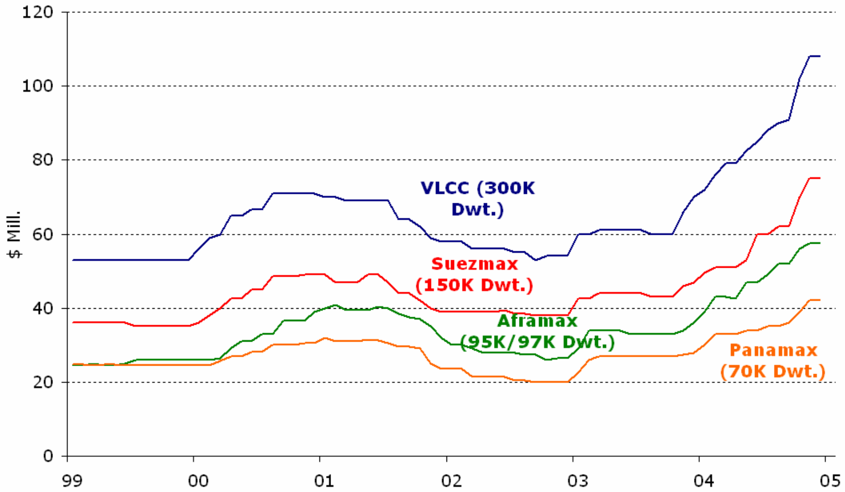
Sharp drop in growth of crude tanker demand for 2005
Growth in global oil demand is by both the Paris-based IEA and the US EIA expected to drop from around 3.3 % in 2004 to 1.7-2.5 % in 2005, leaving fears of a very sharp reduction in growth of oil demand because of high oil prices somewhat unfounded.

Crude Tanker Contracting, 1999-2004



Source: Clarksons

Prices of 5 Year Old Crude Tankers, 1999-2004



Source: Clarksons

Particularly in non-OECD countries, oil demand growth is expected to remain strong as consumers are partly sheltered from price increases and because the energy is intensely needed for a continued economic expansion.

But even more important for *shipping* demand, growth in world oil *supply* (production) is expected to drop all the more from 4.5% in 2004 to 1.6% in 2005. This is because a large part of the oil supply growth in 2004 has been to rebuild low oil stocks and was further boosted by a need to fill an increased total storage capacity. In 2005, the need for rebuilding oil stocks and the desire to expand storage capacity are expected to drop, thus bringing expectations of significantly less demand growth for tankers in 2005.

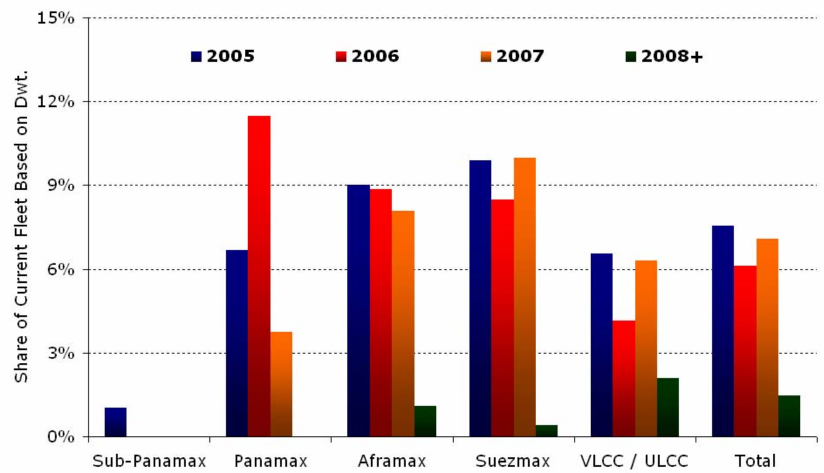
Though the orderbook of the crude tanker fleet is stretched out over an extended period, the tanker fleet is nonetheless expected to grow by 6-7% in 2005 and 5-6% in 2006, thus probably outpacing shipping demand growth.

Previously a large share of the future deliveries was meant for replacing single-hulled tankers that were mandatory to be phased out in 2005. But the very high earnings throughout 2003 and 2004 and the prospects of continued prosperous tanker markets have resulted in many owners of single-hulled tonnage opting to upgrade their ships for them to be able to continue trading. Thus the future deliveries from the shipyards are now mostly turning into incremental fleet growth.

As current crude tanker prices are based on exceptionally optimistic earnings expectations, the negative effects from a less optimistic outlook for the tanker markets on ship prices and contracting activity may be highly noticeable.

During the last two decades tanker demand has grown faster than fleet growth leading to increased utilization of the tanker fleet. In the last 5 years this has been ever more evident in progressively more erratic spot rates and on average higher earnings. Thus despite fleet growth expected to outpace demand growth in 2005, the fundamentals governing the tanker markets are still in support for an extended period of volatile, but thriving tanker markets.

Crude Tanker Orderbook by Year of Delivery



Source: Fearnleys

- + *An ever increasing share of the global oil consumption is carried by sea leading to higher growth in tanker demand than in global oil demand.*
- + *Historically high utilization of the overall crude tanker fleet.*
- + *Political unrest in the major oil supplying countries Nigeria and Venezuela may, if affecting oil production, mean significantly increased tanker demand.*
- \- *A significant slowdown in global oil supply may take the edge off tanker demand with significantly negative consequences for freight rate levels.*
- \- *Large orderbook in most crude tanker segments indicating above normal fleet growth in 2005-2006.*
- \- *China showing increasing signs of bottlenecks and lower growth in car sales could further curtail the future growth in oil demand.*

Product Tankers

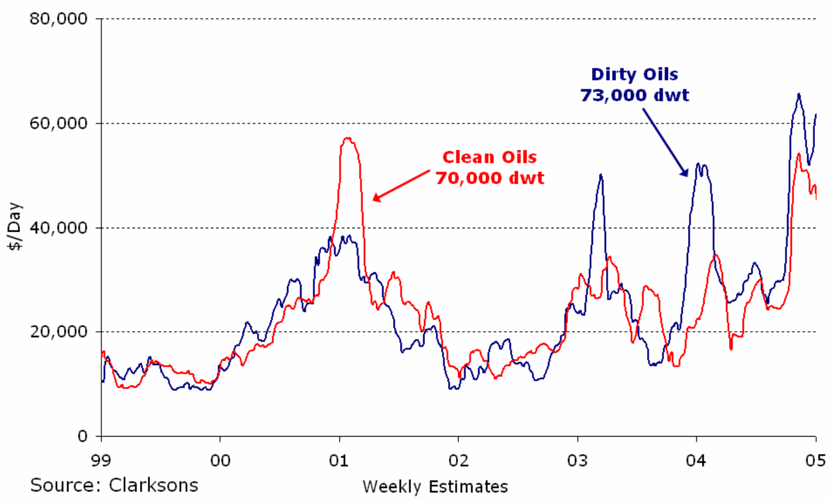
Global refineries run at high utilization levels supporting a strong trade in refined oil products. Contracting of newbuildings is down and prices continue to rise. The short-term outlook is somewhat clouded by significantly lower demand growth than in 2003-2004.

FREIGHT RATES

One of the best years ever ending on a peak
Despite a large number of product tankers being delivered during the year, high product demand and a positive demand-pull from the crude tanker segments managed in providing the product tanker segments with ample employment opportunities.

Spot rates for product tankers have almost all throughout 2004 outperformed expectations, with 2004 probably turning out as one of the best years ever for the product tanker sector. In line with the crude segments, product tanker spot earnings exhibited a distinct rise in late October as particularly the US inventories of heating oil remained low ahead of the winter heating season.

Product Tanker Spot Earnings, 1999-2004



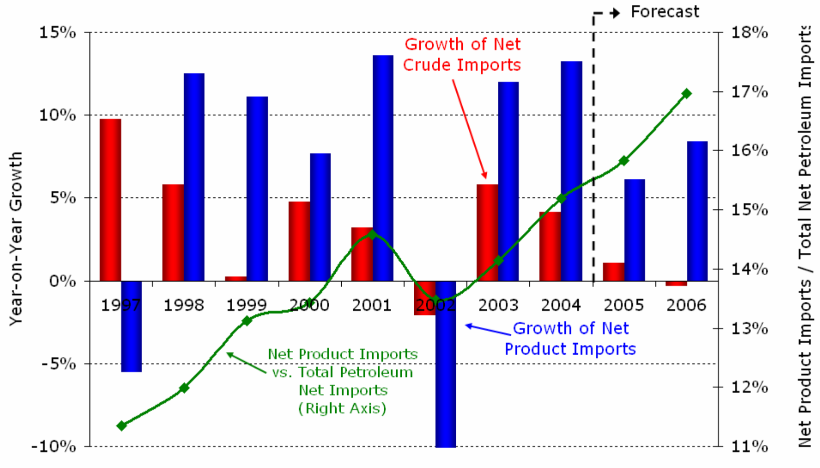
Source: Clarksons

SUPPLY & DEMAND

Strained oil refineries and lack of light, low-sulphur crude oils clearly benefited seaborne trade in refined oil products
Throughout 2004, high demand for refined oil products – primarily gasoline, heating oil, diesel and jet fuel – and low inventory levels have given rise to a continued strain on the global refinery capacity and thus added upward pressure on prices of refined oil products on top of the already high crude oil prices.

The struggle to keep up with rising demand, at a time when refinery capacity was already fully utilized, resulted in the global inventories of refined oil products to remain dangerously close to historical lows throughout most of 2004. Paradoxically, crude oil inventories have been continually rising and are now at reasonably comfortable levels.

Net US Crude and Product Imports, 1997-2006



Source: EIA US Department of Energy (Short Term Energy Outlook, January 2005)

The diverting trends between crude and refined oil inventories are a result of numerous factors. During the last couple of decades investments in adding refinery capacity have on average been insufficient in keeping up with demand, thus resulting in rising overall utilization. Moreover and possibly more importantly, environmental concerns have caused a continued desire to use less of the heavy and sulphur-rich crude oils and more of the light and sulphur-sparse crude oils. Because the heavy and sulphur-rich crude oils are more abundant it has added extra pressure on the refineries to invest in equipment in order to refine these lower grade crude oils into high-grade refined products.

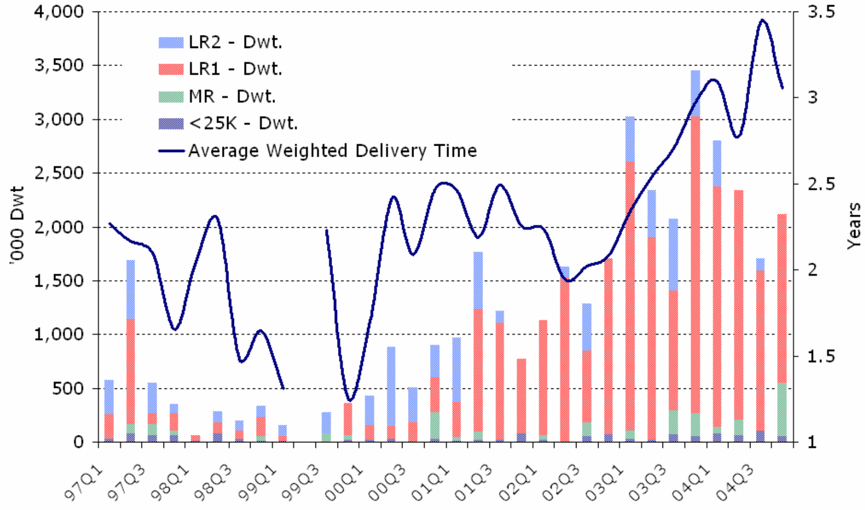
In 2003 and 2004, when global oil demand rose faster than seen during many decades the extra demand was mainly met by rising supplies of the heavy and sulphur-rich crude oils, particularly from the OPEC members, thus putting refineries under extra pressure to invest in refinery conversions and desulphurization capacity. A result of the lacking investment in refineries is thus that crude oil inventories are being filled with the less desired heavy and sulphur-rich crude oils, furthermore leading to a growing price-spread between the high-grade and low-grade crude oils.

Almost all of the above are of positive influence on the demand for product tankers. Not only is the high utilization of domestic refineries leading to higher growth in imports of refined oil products compared to crude oil imports, but the increasingly stricter environmental laws have meant a flourishing cross-trade of products between refineries in order to have the required product mix. Until the refineries have completed their required upgrades, product tankers are probably going to experience on average higher demand growth than that of the crude oil tankers.

CONTRACTING & SHIP VALUES

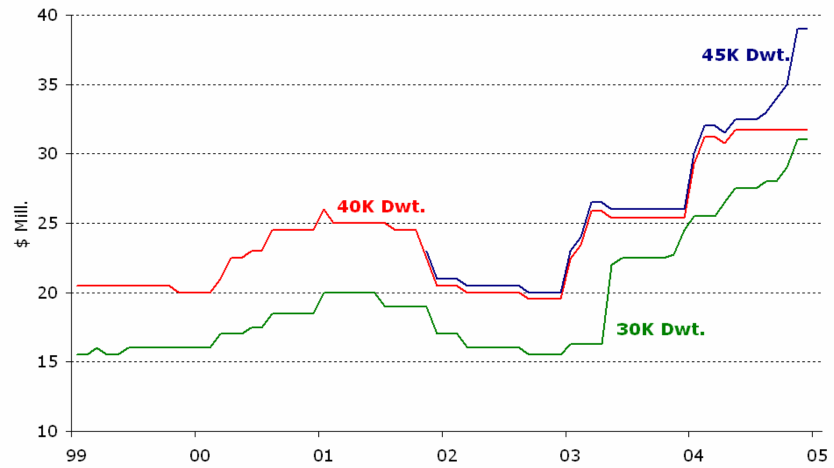
25-50% higher prices and mixed contracting activity
Prices on secondhand product tankers rose by a remarkable 25-50% whereas contracting prices rose by a lower 20-30%, according to Clarksons.

Product Tanker Contracting, 1999-2004



Source: Clarksons

Prices of 5 Year Old Product Tankers, 1999-2004



Source: Clarksons
Monthly Estimates

A lack of available shipyard berths with early delivery in combination with an already large orderbook and ever rising prices seemed to somewhat deter a continued high contracting.

OUTLOOK

Slowing demand growth and high fleet growth
Similar to the crude oil outlook, product tanker demand may most likely experience a significant slowdown in its growth rate.

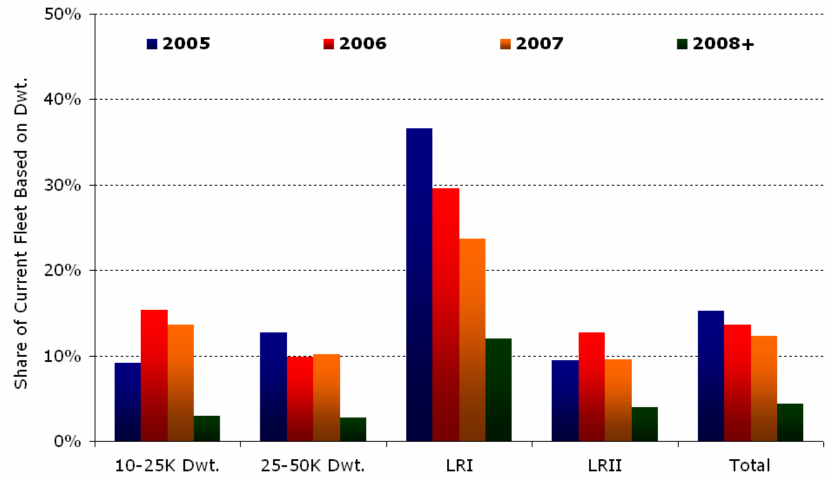
Particularly Chinese demand growth is by the IEA expected to slow down in the short to medium term and then to rebound somewhat during 2nd half 2005. The issuing of credit for car purchases has been restricted and truck loading limits are being enforced more stringently. Moreover and maybe more importantly, the use of backup power generators running on diesel is expected to diminish as non-oil power generating capacity is expected to gradually catch up with power demand.

In the US, import growth of refined oil products is by the EIA expected to slow down significantly in 2005, but still to exhibit a much higher growth than for crude oil imports (see lower graph on page 16).

Despite a relatively high number of deliveries from the shipyards within the next two years, net growth in the product tanker fleet is expected to be somewhat manageable. Stricter IMO regulations on the carriage of heavy fuels in non-double-hulled tankers are to be set in force by April 1st 2005, thereby forcing non-double-hulled tankers either to sail with clean and light oils or to be scrapped. For the panamax (LR1) segment in particular and for some of the smaller segments, the new rules are most likely to deem a relatively large share of the fleet obsolete. If fully enforced, the new rules may even lead to a short-tem lack of the small tankers.

With the overall tanker fleet expected to outgrow demand, earnings in 2005 are most likely to be lower than in 2003 and 2004. Continued low product stocks despite higher crude inventories may nonetheless speak for a continued high reliance on imported products, thereby keeping the product tankers from experiencing too low earnings.

Product Tanker Orderbook by Year of Delivery



Source: Fearnleys

+ *An ever increasing share of the global oil consumption is carried by sea leading to higher growth in tanker demand than in global oil demand.*
+ *Refineries located close to the consumer are running at high utilization whereby additional oil consumption has to be supplied from foreign refineries and transported by product tankers.*
- *A significant slowdown in global oil supply may take the edge off tanker demand with significantly negative consequences for freight rate levels in both the crude and product segments.*
- *A large orderbook in most product tanker segments indicates very high fleet growth in 2005-2006.*
- *The return to production of a further 5 Japanese nuclear powerplants may further reduce the need for product imports into Japan.*

Chemical Tankers

Strong global demand for chemical products as well as a generally high demand for product tankers drew chemical spot and CoA rates to new highs. Outlook continues to be positive, but a slowdown in global economic growth may impact charter rates.

FREIGHT RATES

Slow 2nd quarter followed by very strong finish to the year
1st quarter 2004 turned out to be one of the strongest quarters seen for years for the deep sea chemical tankers. Spot rates showed remarkable improvements on most of the benchmark routes, but from a weak base.

After a slow 2nd quarter, spot rates on the deep sea routes displayed a remarkable recovery that persisted for the balance of the year.

Because of the general lift in spot rates and an improved outlook, renewed CoAs have been settled at significantly higher levels.

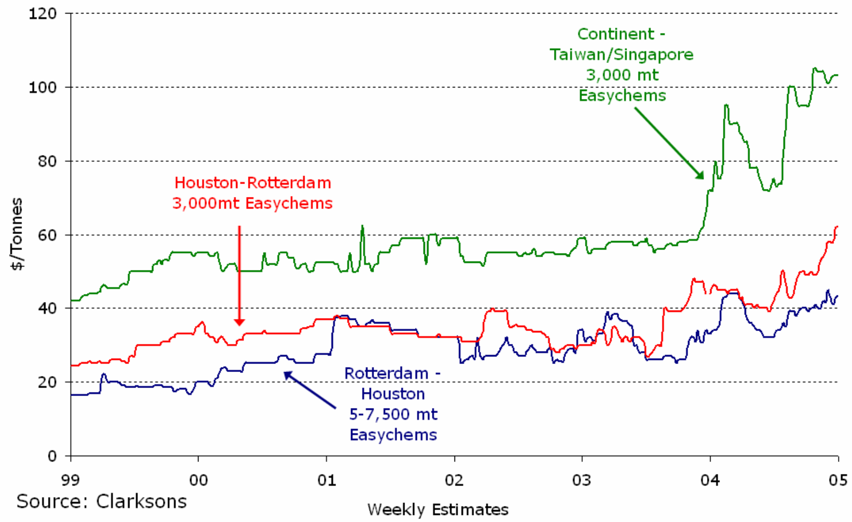
SUPPLY & DEMAND

Strong global chemical demand, boosted by the CPP market
A concerted increase in the industrial production in Asia, the US and Europe has led to a greater demand for chemical and vegetable oils around the world, and thus to the remarkable increases in charter rates for the chemical tankers.

Particularly Chinese demand for chemical products continues to grow at a strong pace, leading to increased demand for both short sea and deep sea chemical tankers. With increased exporting capacity coming on stream in the Arabian Gulf, particularly the large chemical tankers have benefited from the Chinese demand.

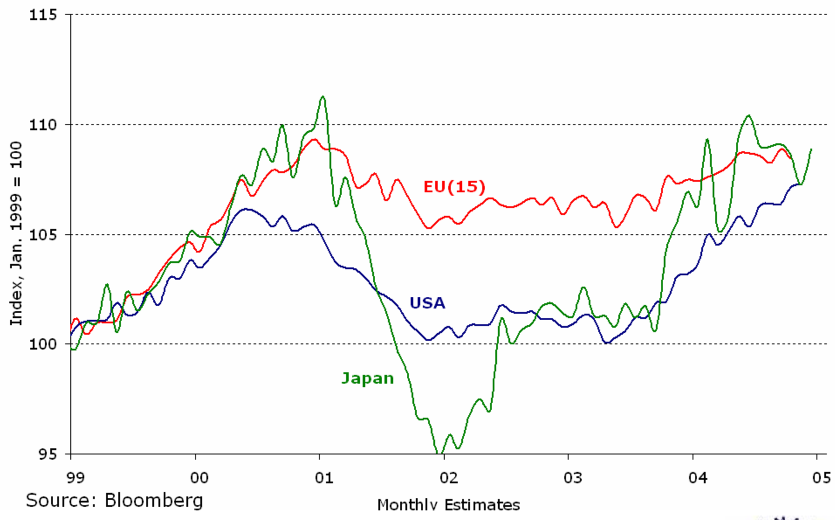
A factor which further tightened the chemical tanker market was the very high freight rates when transporting Clean Petroleum Products (CPP) in the product tanker market. These high rates tempted some chemical tankers to sail with CPP instead of sailing

Chemical Tanker Spot Rates, 1999-2004



Source: Clarksons

Industrial Production, Seasonally Adj., 1999-2004



Source: Bloomberg

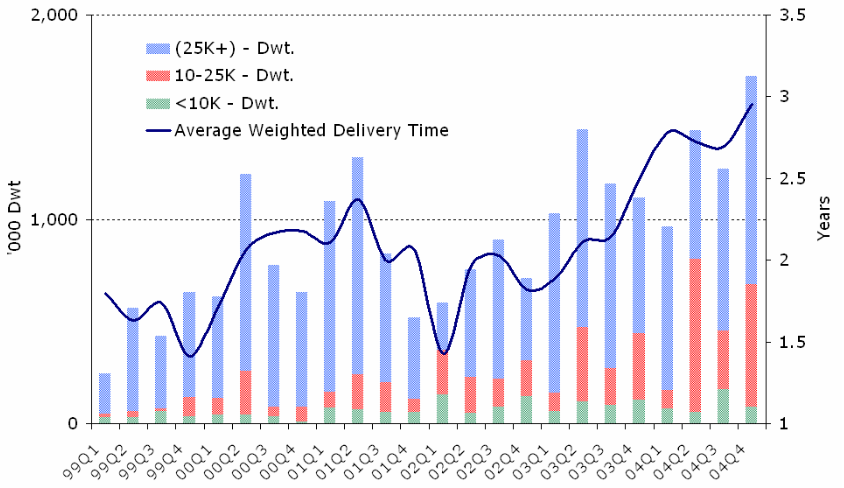
with lower grade chemicals, and thus tightened the supply-demand balance of the chemical tankers even further.

Contracting & Ship Values

Rate buoyancy spurs higher contracting numbers and prices
According to Clarksons, the total number of new contracts for newbuildings is up by 29%, with contracting of chemical/product tankers in the 10-25,000 dwt size showing an almost doubling in activity. Conversely contracting of large and specialized stainless steel chemical tankers is down, partly as shipyards have favoured to build more standardized types of ships.

Newbuilding prices followed the general upward trend seen from other ship types, and secondhand prices showed improvements of around 5-25% with the smaller chemical carriers experiencing the largest increases.

Chemical Tanker Contracting, 1999-2004



Source: Clarksons

Outlook

Positive outlook on improved industrial production growth
With China, India and Brazil along with the greater OECD area expected to show a slower but still resilient economic growth, demand for organic and inorganic chemicals and vegetable oils is expected to remain buoyant in 2005.

In 2005 and 2006 new chemical production capacity is expected on stream in the Middle East. This may entail that the old and maybe less cost-competitive European and North American chemical plants are driven out of competition for the Asian imports. Is this to happen, the distances that the chemicals are transported are to be shorter with a negative effect on the demand for chemical tankers. But so far, Chinese chemical demand has shown growth high enough to meet European, American and Middle Eastern output growth.

In the longer run, growth in deep sea chemical transports may be curtailed as large new chemical plants are being built in China. This might lead to less growth for the deep sea ships, but higher demand for the short sea chemical ships in the Asian region.

+ *Still stronger industrial production worldwide may most likely lead to growing demand for chemical tankers.*
+ *High scrapping prices and old fleet may induce higher scrapping of particularly the smaller chemical tankers.*
+ *A reclassification of certain vegetables oils from non-IMO class to IMO II and III, may from 2007 lead to more demand for chemical tankers.*
- *Lower freight rates in the CPP market may push down rates for the chemical tankers.*
- *The segments of large (above 30,000 dwt), low specification product/chemical tankers are in the coming years to see a high growth in ship numbers.*
- *Middle Eastern and Asian production capacity is set to grow, which may lead to shorter transport distances for the deep sea chemical carriers.*

LPG Tankers

First the coastal ships and then the entire range of LPG vessels witnessed exceptionally strong rates with clearly positive consequences for ship prices. The 2005 outlook continues to be positive, but rates may come down from the record levels of 2004.

FREIGHT RATES

Extraordinary rises in earnings within all LPG ship sizes
Although not shown on the upper graph to the right, spot earnings for the small (below 5.000 cbm) coastal vessels in Europe saw significant improvements in early 2004 and maintained a level well above past years' top levels throughout most of 2004.

Conversely, the medium and large LPG vessels maintained or slightly improved their earnings during 1st half 2004, but saw impressive rate increases almost all throughout 2nd half 2004.

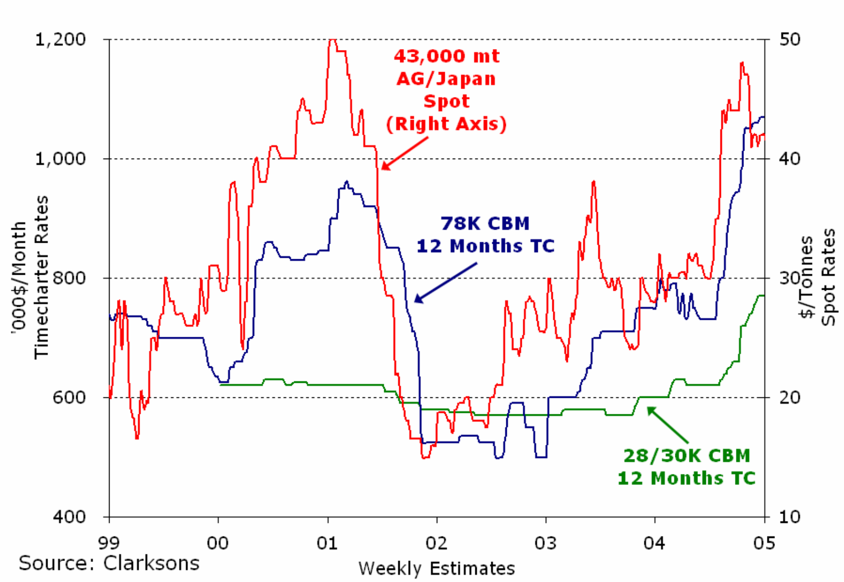
SUPPLY & DEMAND

Strong Asian and European demand growth in 2nd half 2004
The striking increases in earnings of the smaller coastal vessels in Northern Europe were mainly attributable to a tighter supply of ships and not so much a sign of a sudden increase in demand. Throughout 2004 spot activity remained subdued but transport agreements nonetheless were concluded at high rate levels.

During 1st half 2004 South Korean and Japanese imports of LPG products were down 8% and 0.1% respectively, whereas Chinese import growth only slightly made up for the Asian shortfall with a 2% increase, according to Drewry. These differing tendencies provided for a mixed demand picture for the large LPG vessels and thus little change in charter rates during the period.

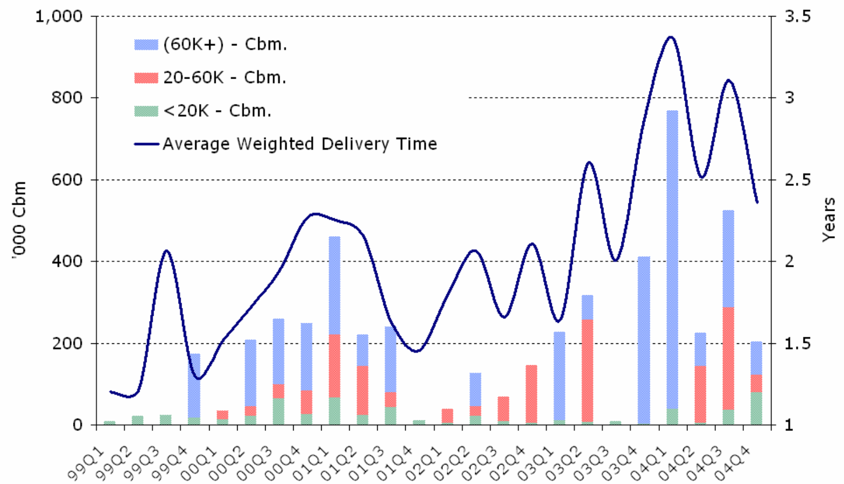
Global prices on LPG products and petrochemical gasses were notably up during most of 2004 partly on the back of strong oil and coal prices. This provided grounds for expectations of future growth in demand for transport of LPG products. In line with expectations, 2nd half 2004 showed a much improved demand

LPG Spot and Timecharter Rates, 1999-2004



Source: Clarksons

LPG Tanker Contracting, 1999-2004



Source: Clarksons

picture as both Chinese, US and European demand for a mixture of LPG and petrochemical gasses showed strong growth. As Europe was persistently short of ethylene and China in need for e.g. polypropylene and butadiene, US exports of all of these products showed great progress. European exports also benefited from the polypropylene and butadiene export. In the US the propane inventories showed low levels until late in the year with positive consequences for imports up to that point in the year.

CONTRACTING & SHIP VALUES

Sky-rocketing secondhand prices and higher contracting
According to Clarksons data, 53 ships were contracted during 2004 which is significantly up on the 23 contracted during 2003. Measured in number of ships, particularly ships smaller than 20,000 cbm showed large increases in its contracting activity.

In line with other ship types, LPG contracting prices have increased by 25-70% during 2004, with the small coastal ships experiencing the largest increases. Similarly, secondhand prices for coastal vessels have also increased the most with an almost doubling of prices for a 15 year old 3,000 cbm LPG vessel, according to Fearnleys. Other secondhand prices have risen by 15-45%.

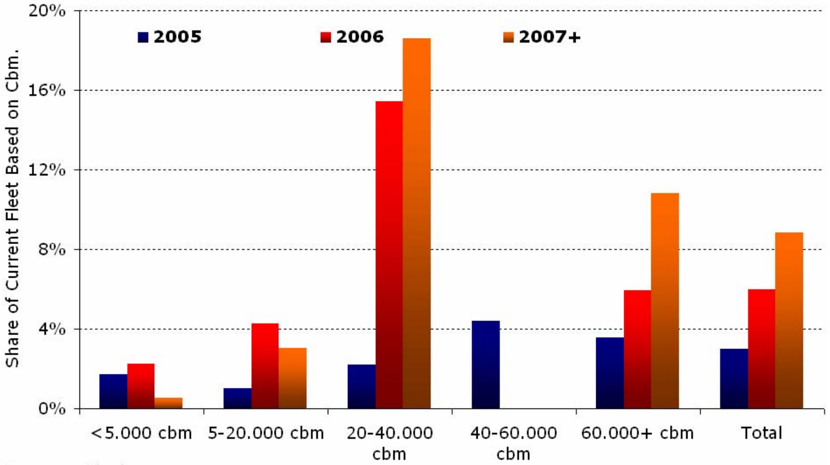
OUTLOOK

Small orderbook and old fleet may provide for buoyant 2005
Particularly the fully refrigerated fleet exhibit a large proportion of elderly ships, but also the smaller segments have similar tendencies. With a limited orderbook, which shows a picture of a low number of newbuilding deliveries until 2007, the total supply of LPG ships may even experience a negative growth before then.

Conversely, demand may show a slowdown in growth as global economic growth is expected to ease off its highs from 2004. But as the Chinese economy continues to grow at a strong pace its consumption of LPG is thus expected to increase in parallel.

In total, freight rates for the LPG tankers are expected to remain in lucrative territory throughout 2005, but may come off their current highs as demand growth slows down.

LPG Tanker Orderbook by Year of Delivery



Source: Clarksons

- \+ *Very small number of deliveries from the shipyards for the next 12 months and an ageing fleet is highly positive as it prevents the supply of ships from growing at an alarming rate.*
- \+ *Middle East production capacity continues to grow, which in combination with Asian consumption growth may most likely lead to increased demand particularly for the largest LPG vessels.*
- \+ *Future growth in LNG exporting capacity is expected to be very high the coming 5 years. As a large part of these exporting facilities are expected to extract the LPGs from the LNG before exporting the LNG, the demand for LPG ships is expected to benefit notably.*
- \- *A slowdown in global economic growth may lead to falling LPG prices and less demand growth for LPG ships. Until prices have once again found a stable base, demand for LPG vessels may be lower.*

Dry Bulk Ships

So far, the efforts of slowing China's steel production doesn't seem to be much effective. The persistently high growth has had amazingly positive effects on ship earnings and prices. Demand growth is expected to ease in 2005, thus earnings are expected to be lower but still at healthy levels.

Freight Rates

Absolutely stunning year for dry bulk earnings
Giant swings in freight rates have been the prevalent feature of dry bulk spot rates during 2004. Spot earnings of Capesize vessels reached a peak of 100,000 USD/day in early 2004, only to drop to 40,000 USD/day (still a remarkable level by historic standards) and then again to soar above 100,000 USD/day in late 2004.

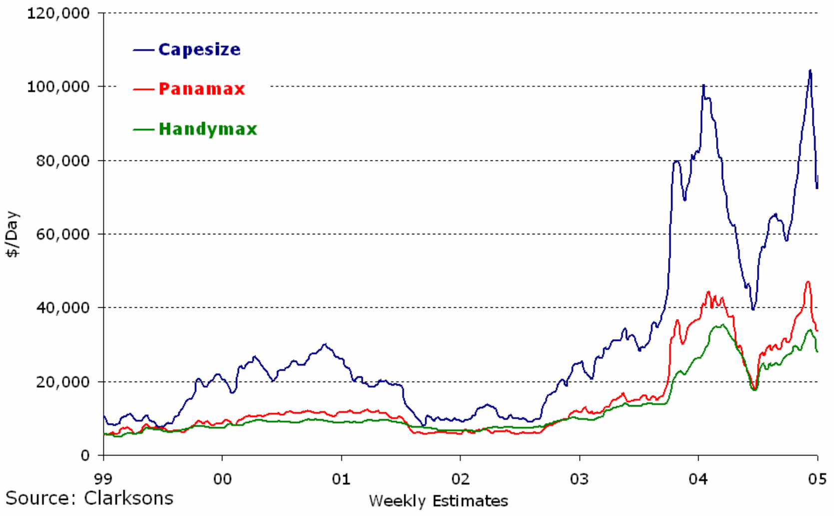
With daily operating costs excl. financing being around USD 5,000 for a Capesize vessel, the above earnings clearly demonstrate the absolutely extreme amounts of free cash that was generated by the dry bulk shipping companies during all of 2004.

Supply & Demand

China's steel production in command of dry bulk shipping
The mid-year fall in earnings was mainly caused by the Chinese government carrying through economic reforms, which targeted the Chinese steel manufacturing and housing construction industries. Moreover, the slowdown in shipping demand growth gave the badly congested ports a brief opportunity to clear their ports of waiting ships and to catch up with demand. At the height of the market an estimated 25% of the Capesize fleet were waiting at congested ports to load or unload.

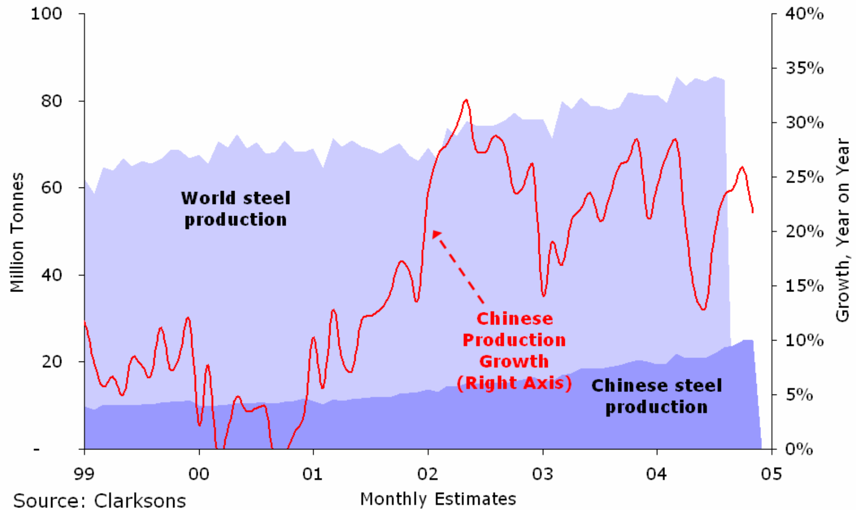
During the second half of 2004 it became more and more obvious that the Chinese demand wasn't about to slow down completely. And as growth in Chinese steel production once again grew stronger, shipping demand and port congestion returned in large scale. Compared to 2003, Chinese steel production is believed to

Dry Bulk Spot Earnings, 1999-2004



Source: Clarksons

World and Chinese Steel Production, 1999-2004



Source: Clarksons

have increased by 23% in 2004, which is a continuation of the 22% growth experienced in 2003.

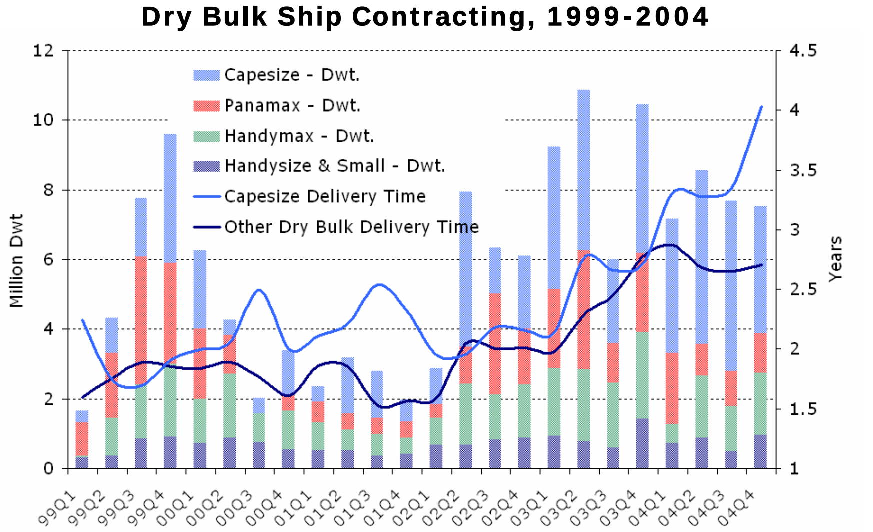
For the global steel markets the excessive growth in Chinese steel production and consumption has been most acutely felt by shortness in supplies of raw materials used to manufacture steel – particularly iron ore and coking coal. This comes at a time when rising industrial production in the EU, the US and Japan are fast approaching the highs of 2000, intensifying the need for steel.

The massive rise in China's production of steel (and thus increased use of coking coal) has meant that China during 2004 has cut its exports of coking coal by about 60%. Thus non-Chinese Asian steel mills instead have had to receive larger coking coal supplies from Australia, Canada and the USA, leading to longer transport distances and thus higher demand for dry bulk ships. On top of very high freight costs, the deficit of particularly coking coal supplies have resulted in very high steel production costs and a genuine fear of a shortage of steel products within the steel industries in Asia, North and South America as well as in Europe. This all led to dramatic increases in steel prices worldwide all throughout 2004.

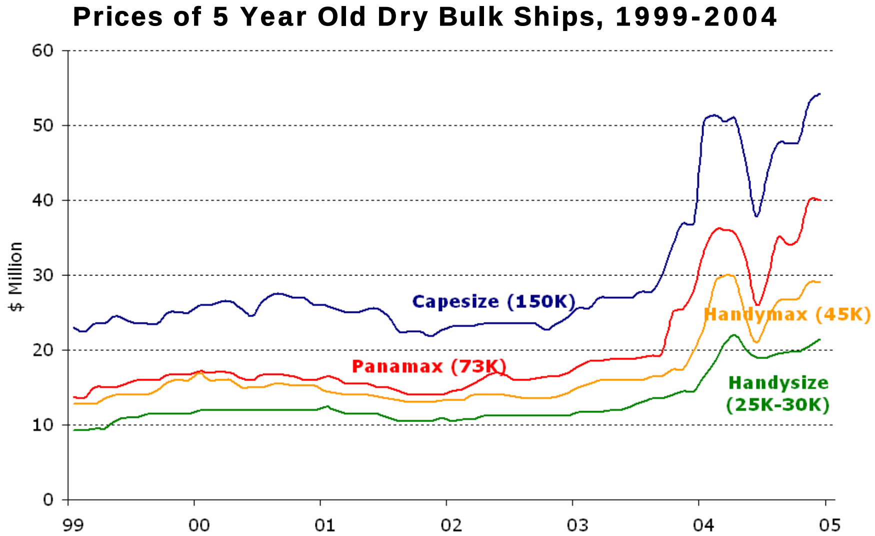
Somewhat reassuringly to the steel industry, SSY estimate that for 2004 the Chinese exports of steel products have risen by about 11 million tonnes – a 130% increase – and China has gone from a net importer to a net exporter of steel products. The growing exports of steel bear evidence that, after the last three years of very high production growth, Chinese steel production finally seems to have caught up with Chinese steel consumption. This is a notable warning sign of an impending slowdown in Chinese steel production and thus of a slowing shipping demand. If growth in steel demand inside and outside China doesn't pick up significantly it may lead to excess steel production and thus falling steel prices and finally a somewhat slower growth in Chinese steel production.

CONTRACTING & SHIP VALUES

A short hiccup in prices followed by continued upsurge
Because of suddenly falling spot earnings and timecharter rates newbuilding prices and secondhand prices dropped shortly during



Source: Clarksons



Source: Clarksons

2nd quarter of 2004. In response to the following rise in earnings, ship prices once again surged upwards. What the hiccup in prices should tell is that ship prices may fall just as quickly as they have risen once the freight rates start to show less optimistic trends.

At the end of 2004 secondhand prices of 5 year old ships were up by 40-50% year-on-year, and prices of newly delivered ships are now 30-40% above contracting prices for ships delivered in 1½ to 3 years time.

Throughout 2004 dry bulk owners have found it difficult to order new ships, mainly because shipyards have concentrated on getting orders for more expensive ship types. Consequently new Capesizes now have up to 4 years until they are delivered. This is 1-1½ years more than the other dry bulk vessels have to wait (see graph p. 24).

OUTLOOK

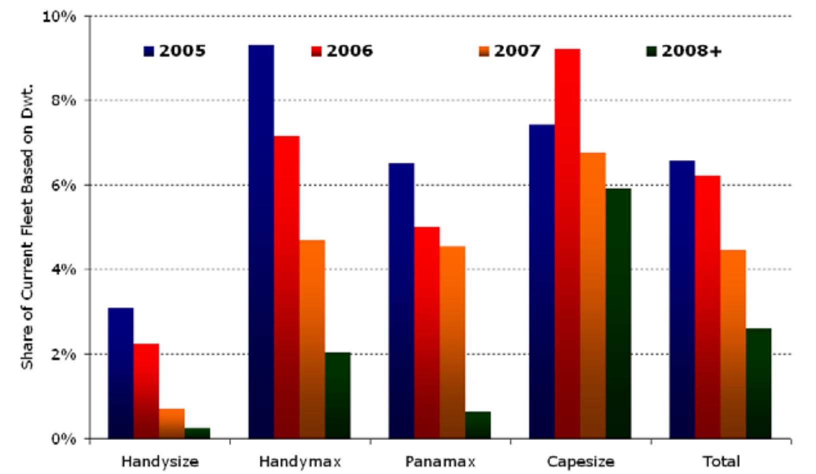
Raw material shortages together with port and inland bottlenecks support a still tight but very volatile market
Spot earnings in 2004 clearly show that the dry bulk market is still very tight with limited ability of the dry bulk fleet, and just as importantly also of the ports, to meet quickly growing demand.

Despite expectations of a continued strong demand for steel products, the actual production of raw materials for the steel industry is not in the foreseeable future expected to be able to catch up with demand. Thus paradoxically, despite strong demand for steel, shipping may experience a slowdown in the demand for transports of raw materials. For 2005, dry bulk shipping supply may actually outpace shipping demand with negative consequences for freight rates.

A slowdown in the growth of raw material production may furthermore lead to a debottlenecking of the ports and that the inland transport infrastructure is catching up with demand, thus freeing a significant number of ships previously held up in ports waiting to load or offload.

In conclusion, dry bulk freight rates is expected to remain very volatile but at healthy levels for the foreseeable future.

Dry Bulk Ship Orderbook by Year of Delivery



Source: Clarksons

+ *Lower exports of coking coal from China may lead to higher tonnes-miles as the other Asian steel mills instead have to purchase coking coal from more distant suppliers, e.g. Australia, USA or Canada.*

+ *Continued higher industrial production in North America, Europe and Japan supports continued high demand for seaborne transport of steel, iron ore, coking coal and thermal coal.*

+/- *Low production growth of the main raw materials may limit demand growth for dry bulk ships. But if production growth beats expectations ship demand may be quite positively influenced.*

\- *Steel production growth, and thus shipping demand growth may be slowing down. If that is the case, ports and shipping supply may quickly catch up with demand with significantly negative consequences for freight rates.*

As global car sales show robust growth and the PCC market is in acute under-supply of ships, charter rates have gone sky-high. Despite ever rising contracting prices the orderbook is now extraordinarily big. The outlook is still very sound but the fleet may be catching up with demand within a few years.

FREIGHT RATES

All-time record in charter rates for Pure Car Carriers
Charter rates for vehicles carriers ascended all throughout 2004 and clearly surpassed their previous record level from 1997. In the latter part of the year no significant number of charter fixings was signed as very few ships were available for charter.

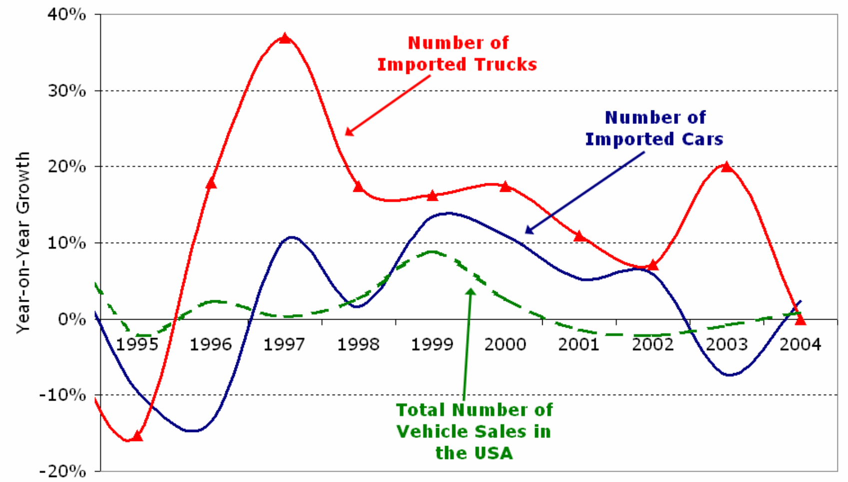
SUPPLY & DEMAND

Buoyant Asian and Middle Eastern trade in cars and trucks
With high oil prices driving flourishing economies and construction work in the Middle Eastern countries, car imports to the region have seen significant growth from both Asian exporters and US and European exporters.

Similarly intra-regionally in the Far East, particularly the Chinese economic growth has spurred a considerable growth in the car trade. Also exports from Europe and the US to China experienced healthy growth. But even though the Chinese car trade is flourishing, growth in Chinese car sales have performed below expectations as the credit-tightening measures of the Chinese government have negatively influenced sales growth.

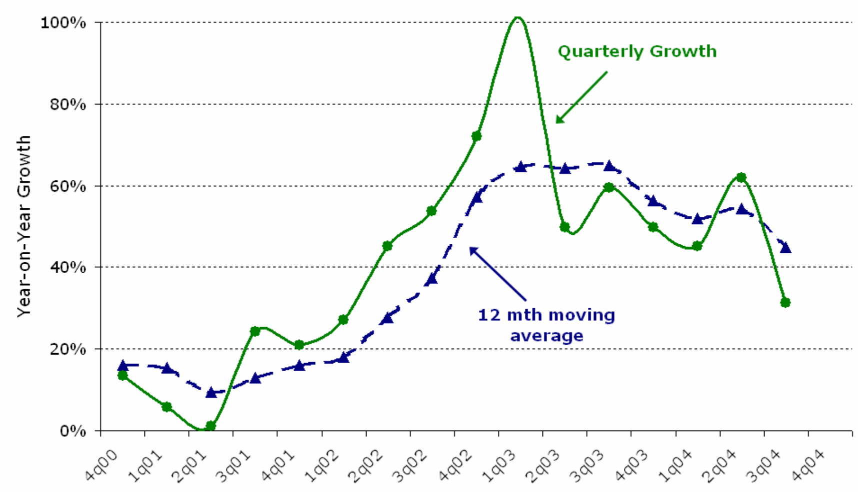
Additionally, the deep sea transport of cars has been given an extra boost by high exports from Asia into Europe, as the still low interest rates in the EU-area and a stronger Euro have benefited Asian exporters, South Korea and Japan in particular. In the US a weaker Dollar and rising interest rates have not yet significantly impacted on car sales as US seaborne car imports and overall sales are up on 2003's levels.

US Vehicles Sales and Imports, 1995-2004



Source: Bloomberg

Chinese Vehicles Sales, 2000-2004



Source: Bloomberg

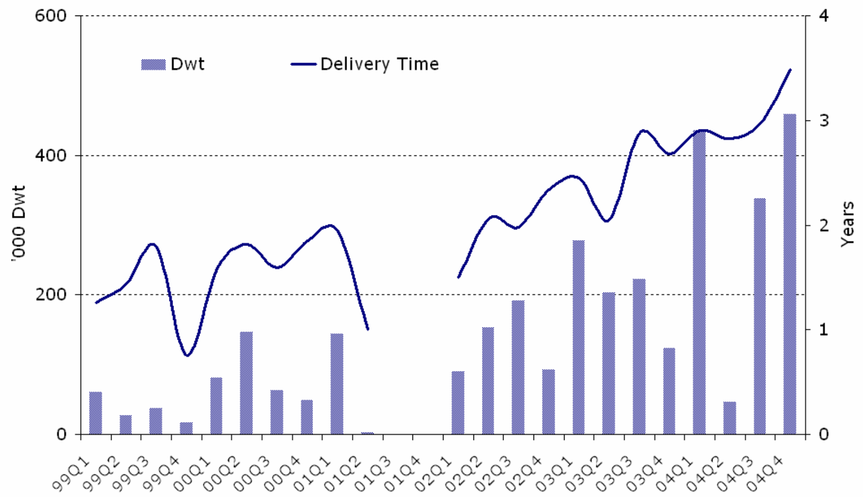
The robust growth in global car trade has meant that the deep sea market for vehicles carriers has experienced an apparent lack of tonnage on some trade lanes. Consequently some carriers were forced to decline the transport of cars not already contractually agreed on.

Contracting & Ship Values

Very strong contracting and rising prices
During 2004 a massive 76 PCC ships were contracted at the yards. This is up from 52 in 2003 and a low 30 in 2002, and thus the highest volume of new contracting for more than 10 years. The size of the newbuildings is also upgraded with the largest PCC under construction being 7.000 ceu.

With still increasing contracting prices and very few berths open before 2008 at the traditional shipbuilders, a significantly lower contracting number is expected for 2005.

Pure Car Carrier Contracting, 1999-2004



Source: Clarksons

Outlook

Still tight market, but lower demand growth and rising fleet
As high energy and raw material prices take their toll, global GDP growth is expected to slow down in 2005. Similarly, global sales of durable goods, thereof vehicles, is expected to slow down. Particularly in China the government still runs a tight race between a gradual slowdown and a hard landing, thereby trying to keep Chinese consumption, production and investments from rising too fast. Consequently credits for cars and trucks are expected to remain under restrain with negative effects on growth in car sales.

In the US a low USD may lead to growing US exports and thus a greater potential for private consumption, thus reducing some of the negative effects on car sales from the rising interest rates and high gasoline prices.

In conclusion, global growth in seaborne trade of cars in 2005 is expected to remain robust but at slower pace compared to 2004. Bearing the large orderbook in mind, ship supply may thus outpace demand but not at an alarming rate.

+ *A strong Euro compared to particularly the Asian currencies may lead to increased imports into Europe despite overall stable car sales.*

+/- *The somewhat high number of deliveries during 2005-2007 may put negative pressure on rates. But the high proportion of elderly and scrap destined ships ought to a large degree counteract the fleet growth.*

\- *A slowdown in growth of the Chinese vehicles sales may continue to negatively impact demand growth for car carriers.*

\- *A weak USD, rising American interest rates and high gasoline prices may threaten the North American vehicles sales, particularly from the Asian and European exporting countries.*

Larger EU and congested roads provided positive cargo growth, but cheap airfares continue to take passengers away from ferry lines within Europe. An elderly fleet and attempts to reduce road congestion may turn into more orderings of newbuildings.

SUPPLY & DEMAND

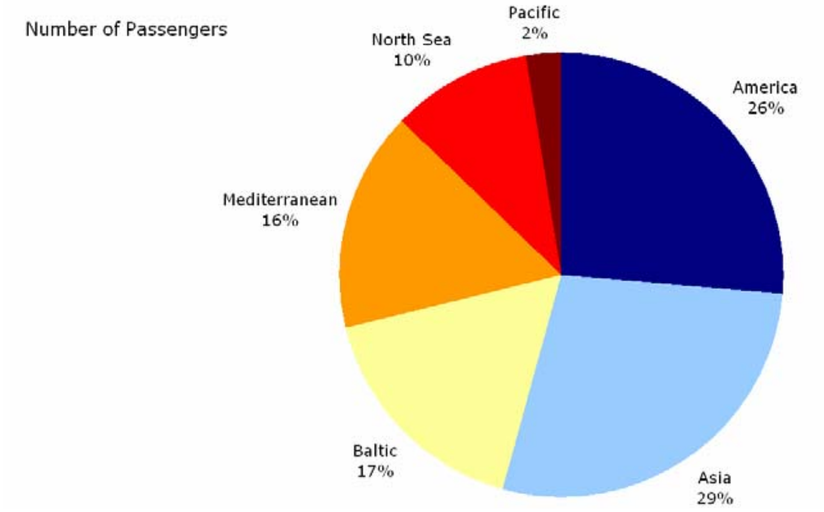
2004, the year of the expanding EU and its 'Sea Motorways'
The first round of allocating subsidies from EU's 'Marco Polo Programme' is now successfully completed. The 'Marco Polo Programme' has the sole objective of improving the conditions for the sea transport of cargo within Europe and thus to reduce the pressure on European roads. But with the greatest share of EU funding going to already established Ro-Ro-routes, the first allotment round unfortunately bears clear evidence that many new projects were deemed unfeasible or have not even been submitted, all because of an almost total lack of suitable and modern tonnage available for charter or for sale.

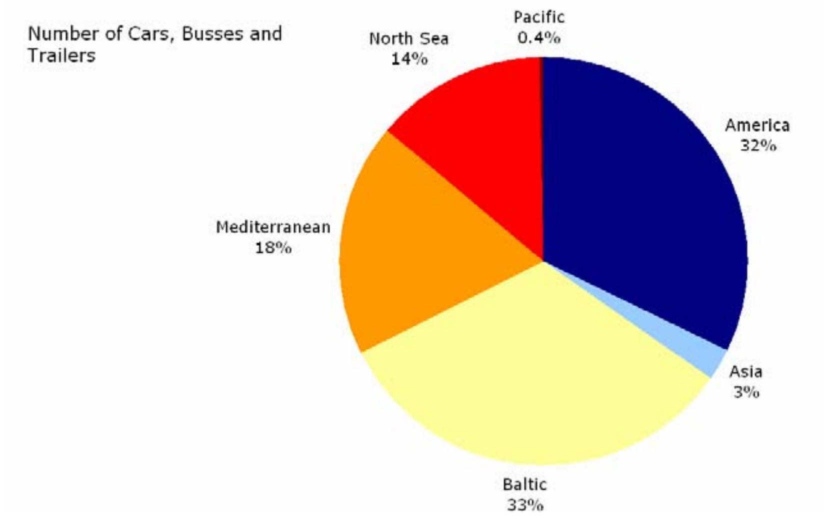
Not only has the increasingly congested European roads provided cargo growth for the Ro-Ro and container operators, but in addition much higher gasoline prices have made it comparatively less expensive to move cargo by sea than by road.

The inclusion of Estonia, Latvia, Lithuania and Poland as new EU member states as per May 1st 2004 has up to and following the EU enlargement brought with it a large growth in container and trailer traffic to and from the new member states.

Paradoxically, the EU enlargement, and thus reduced administrative burdens in relation to customs procedures on the road traffic, has led to a move of cargo away from the sea and onto the roads. This trend has been most obvious on the cargo routes that run along the shoreline in the Baltic Sea. Moreover, some Baltic passenger ferry routes have experienced lower revenues as the tax-free sale no longer exists. In response some ferry companies have set up border shops e.g. to promote one-day shopping tours.

Ro-Ro, Ferry and Cruise Traffic by Region, 2003





Source: ShipPax, Statistics 04

Among the passenger ferry companies within Europe the fierce competition among airlines and the advent of cheap budget airlines has been increasingly felt as much lower airfares have made it comparatively more preferable to travel by air than by ship. Moreover, new ferry operators have been set up with similar pricing structures – the earlier you book the cheaper it is – thus bringing additional competition to the established ferry operators.

CONTRACTING & SHIP VALUES

Contracting volumes show rising strength
According to Clarksons' data, 35 Ro-Ro freight/passenger/Lo-Lo ships were ordered during 2004, which is considerably up on the 2003 level of 17 ships. Of the 35, 8 went to Far Eastern yards.

A rise in ship scrapping and ship lay-up, because of stricter requirements that require new fire fighting sprinkler systems within EU waters before a January 2005 deadline, have on top of rising cargo volumes and an ageing fleet led to the boost in contracting activity during 2004.

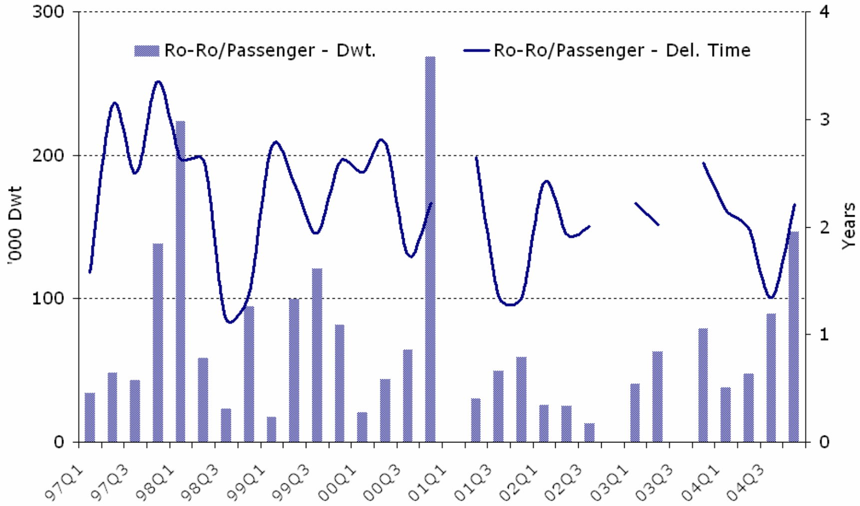
OUTLOOK

Old fleet and small orderbook indicate a future tight market
As economic growth in the new EU member states is expected to be well above the EU average, future port traffic in the Baltic region is expected to continue to grow at healthy rates. But in the longer run, Ro-Ro operators in the Baltic Sea may see increased competition from small and large containership operators.

A continued high pressure on the road network within Europe is expected to lead to more cargo being moved by sea. If a combined EU effort succeeds in reducing port costs in particular, short sea shipping within EU waters may in the coming years experience an even larger growth.

Because of the rising threat of fatal losses of old ships at sea, Greece has introduced an age limit on its ferries. And in other European countries age limits on passenger vessels are being considered. Given the large share of elderly ferries a continuing high level of newbuildings may thus be needed.

Ro-Ro / Ferry Contracting, 1999-2004



Source: Clarksons

+ *A large share of elderly Ro-Ro ships is expected to be scrapped in the coming years. Given the currently moderate orderbook the market may become significantly tighter.*

+ *European road traffic is expected to show robust growth throughout the next decade. In order to prevent the roads from becoming too congested several measures are being taken to move cargo from the road to the sea.*

- *Low airfares may continue to take away passengers from the ferry business.*

- *When the container volumes become big enough in the Baltic region, the fully cellular and dedicated container vessels may take away the cargo from the Ro-Ro operators.*

Offshore Support Vessels

Finally, the long-lasting miserable offshore charter rates showed extraordinary strength as exploration and drilling activity advanced worldwide. Future supply ship demand is expected to grow further, in the North Sea partly because of improved taxation and licensing conditions.

Freight Rates

Long overdue, supply ship charter rates finally rose strongly
In the North Sea charter rates exhibited miserable levels up until October. But in late October, following the resolution to the Norwegian offshore worker's strike and lock-out, which had lasted all since July, pent up demand for AHTSs and PSVs finally was unleashed. Subsequently charter rates soared to levels not seen since the record years of 1997 and 2001.

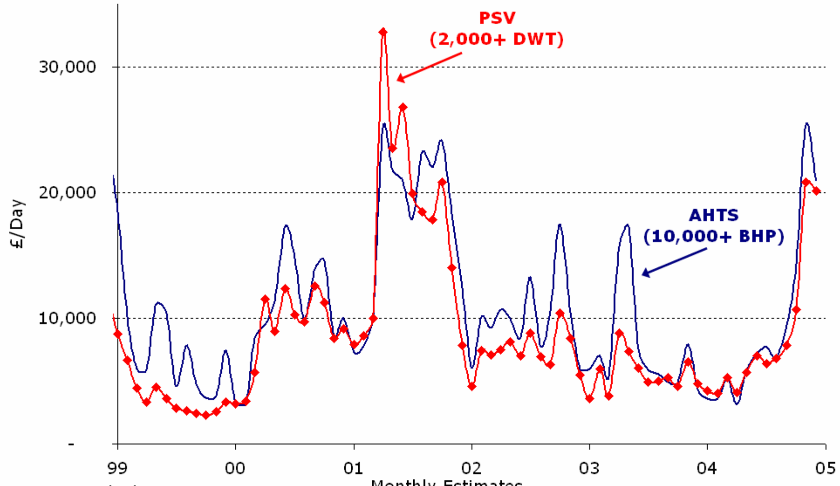
In the Gulf of Mexico (GoM) the charter rates were similarly dismal throughout the first half of 2004. These low rates have led to very high numbers of ships being scrapped or laid up in the GoM. With the extensive repair work required after Hurricane Ivan in mid-September and an increased number of drilling rigs in the region charter rates started to rise slowly in the latter part of 2004.

In other offshore drilling regions charter rates have been somewhat low partly because ships that left the depressed North Sea market generated a negative pressure on rates in these other markets. Conversely, the exodus of support vessels from the North Sea significantly improved the possibility of high charter rates in the North Sea when demand finally improved.

Supply & Demand

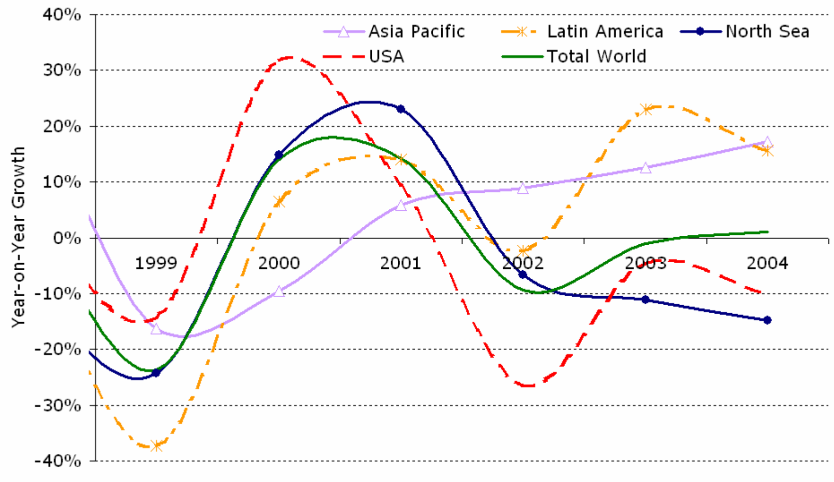
Optimism returns with big find and new exploration licenses
Despite high and rising oil and gas prices, energy companies in mature areas such as the North Sea and the Gulf of Mexico seemed to hold back spending on exploration activities. Through-out the main part of 2004 this had a dampening effect on earnings of supply ships almost all around the world.

Offshore Vessel Spot Rates, 1999-2004



Source: Clarksons

Offshore Drilling Rigs in Operation, 1999-2004



Source: Baker Hughes Incorporated

Probably the most influential rationale behind the reluctant stance of the energy companies in the North Sea were an apparent lack of suitable drilling acreage in combination with unfavourable taxation conditions, thereby limiting further profitable exploration and production in the mature offshore areas. Particularly the very large energy companies have instead targeted new areas outside the mature areas which hold better promises of large discoveries.

This hesitant attitude among the large energy companies seems to have changed following both the UK and Norwegian governments introduced a large number of new exploration and production licenses.

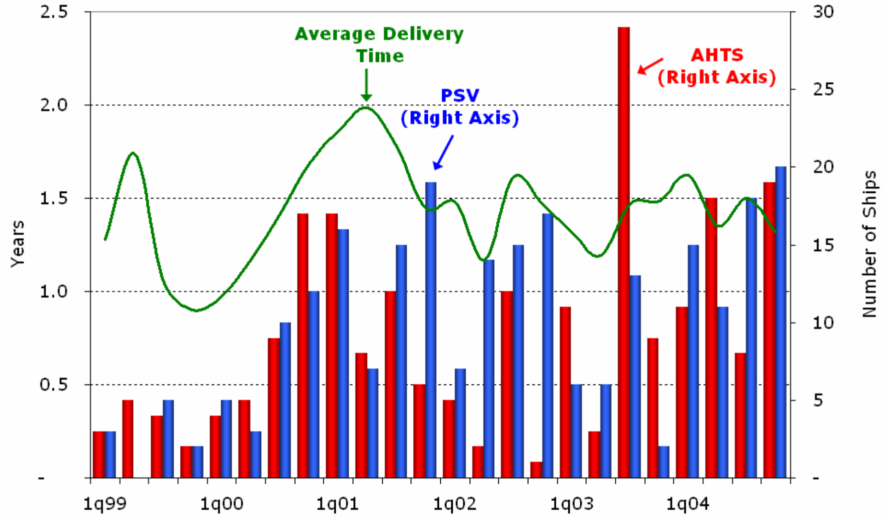
On top of the changed tax laws from 2003 the UK government introduced a "new frontier" license that allowed exploration companies to apply for larger acreage at significantly reduced costs and with a longer period to carry out the necessary exploration and development. Moreover, the UK government has in its 22nd license round offered 1,039 blocks, in the largest offering round since 1965. This offering included blocks in mature basin areas and more notably also in frontier areas West of Shetland.

Similarly, the Norwegian government offered substantial new acreage and put forward a proposal to lower taxes on oil production. These measures were in addition to a decision from 2003 to allow for all-year petroleum activity in the Barents Sea.

In reaction to these new conditions, and together with still rising oil and gas prices, demand for offshore supply ships picked up particularly in the UK sector of the North Sea. Following the resolution of the strike and lock-out of the Norwegian offshore workers the activity in the Norwegian sector also grew greatly.

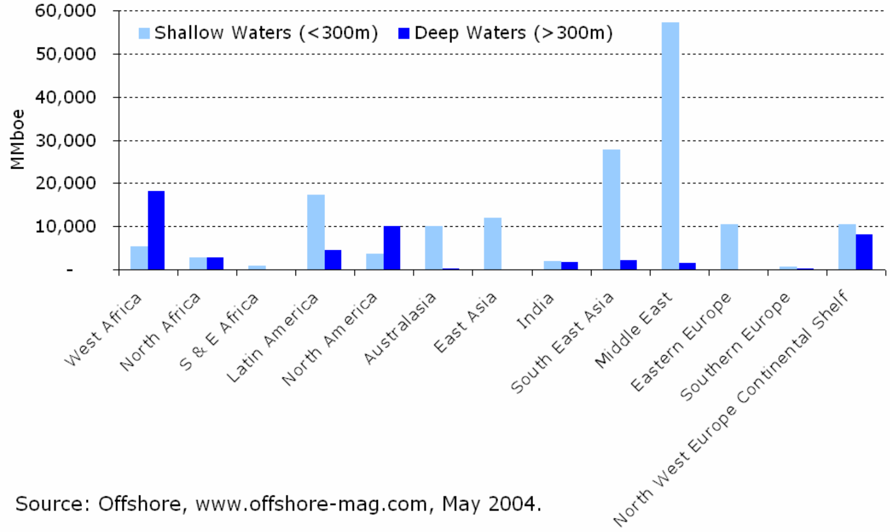
Adding considerably to the positive feelings was an announcement that the first major find in many years had been discovered in the frontier area of the Atlantic. The Atlantic frontier had long been regarded as the last great hope for the North Sea offshore industry, and with this announcement hopes of more large finds and continued activity were rekindled.

Offshore Vessel Contracting, 1999-2004



Source: Clarksons

Expected Offshore Field Developments, 2004-2008



Source: Offshore, www.offshore-mag.com, May 2004.

Contracting & Ship Values

Very high ordering and fairly steady secondhand prices
According to Clarksons figures, 56 AHTSs and 64 PSVs were ordered during 2004. This is the highest number of offshore supply ships ever contracted, and distinctly up on 2003's contracting level of 79 ships in total.

Despite that a significant part of the orderbook is for replacing old ships in the smaller segments, the current orderbook may nonetheless be regarded as being slightly large.

The low freight rates early in the year led to a slight reduction in secondhand values that until late in the year remained stable. As confidence returned to the market late in the year, ship values exhibited significantly positive signs.

Outlook

Higher deep sea activity and high North Sea charter rates
Globally high prices on oil and gas and expectations of the high prices to continue for the foreseeable future have already manifested itself in increased exploration and production budgets, signifying a future growth in the demand for offshore supply ships.

Currently in the North Sea and the GoM the availability of suitable tonnage is limited and the expectation for 2005 is a comparable or even tighter market.

In the years to come demand for particularly the larger offshore vessels is expected to benefit significantly as global deep sea exploration, development and production is increasing. Conversely, demand from shallow water exploration and production is in the longer run expected to decrease particularly in the North Sea and GoM. But the decline in demand for offshore support vessels may be momentarily offset by decommissioning of oil platforms and subsea installations.

In total, the 2005 outlook for offshore supply ships is quite positive, but partly rests on the markets outside the North Sea to continue to attract tonnage.

+ *As shallow water areas are increasingly being emptied global spending on deep sea exploration, development and production is expected to increase substantially in the years to come. Particularly the large, modern PSVs and AHTSs are expected to benefit from this development.*

+ *Confidence in continuing high gas and oil prices has led to increased exploration and production budgets by both the major and the independent energy companies.*

+ *Lowered UK and Norwegian taxes on offshore oil production and a large number of new exploration licenses may most likely lead to a further increase in the exploration activity in the North Sea.*

+ *The installation of large pipelines in the North Sea and the reopening of the Barents Sea for oil exploration and production may lead to increased demand for offshore support vessels in 2005 and 2006.*

+ *In the longer run decommissioning of oil platforms and related installations may lead to increased demand for offshore support vessels.*

- *The shallow water areas in the North Sea and the Gulf of Mexico are generally perceived as holding no new major oil discoveries, thereby limiting further investments.*

- *Suddenly falling oil and gas prices may most likely have a negative effect on long-term offshore oil and gas exploration and production.*

Glossary

Aframax: Crude oil tanker or product tanker too large to pass through the Panama Canal and below 120,000 dwt.

AHTS: Anchor Handling Tug Supply. Offshore vessel used for jobs such as the relocation of oil rigs and anchors of the oil rigs.

BHP: Break Horse Power. The amount of engine horsepower.

Brent: 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.

Bulk vessel: Description of vessels transporting large cargo quantities, including coal, iron ore, steel, corn, gravel, oil, etc.

Bunker: Fuel for vessels.

Capesize: Dry bulk carrier of more than approximately 80,000 dwt; too large to pass through the Panama Canal.

Cbm: Cubic Meter.

Ceu: Car equivalent unit. Unit of measure indicating the car carrying capacity of a vessel.

Cgt: Compensated Gross Tonnage. International unit of measure that facilitates a comparison of different shipyards' production regardless of the types of vessel produced.

Clarksons: British ship brokering company. www.clarksons.net

Clean products: Refers to light, refined oil products such as jet fuel, gasoline, diesel oil and naphtha.

CoA: 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.

Container conference: Collaboration agreement between a number of container shipping lines on trade routes or regions for the purpose of enhancing efficiency of the vessel capacity and harmonising price/teu.

Dirty products: Refers to heavy oils such as crude oil or refined oil products such as fuel oil or bunker oil.

Drewry: Drewry Shipping Consultants Ltd. British shipping and transport research company. www.drewry.co.uk

Dwt: Dead Weight Tons. Indication of a vessel's cargo carrying capacity (including bunkers, ballast, water and food supplies, crew and passengers).

EIA: Energy Information Administration. A subsidiary of the US Department of Energy. www.eia.doe.gov

Fearnleys: Norwegian ship brokering company. www.fearnleys.no

Feeder: Small container carrier.

FPSO: Floating Production Storage Offloading unit. Vessel used in the offshore industry to process oil from an underwater (sub-sea) installation.

Geared: Indicates that a vessel is equipped with a crane or other lifting device.

Gearless: Indicates that a vessel is not equipped with a crane or other lifting device.

Gt: Gross Tons. Unit of 100 cubic feet or 2.831 cubic meters, used in arriving at the calculation of gross tonnage.

Handy, tank:	Crude oil tanker, product tanker or chemical tanker of between 10,000 and 25,000 dwt.
Handymax, dry cargo:	Dry bulk carrier of between approximately 40,000 and 60,000 dwt.
Handysize, dry cargo:	Dry bulk carrier of between approximately 10,000 and 40,000 dwt.
IEA:	International Energy Agency. A subsidiary of the OECD. www.iea.org
IMO:	International Maritime Organization. An organisation under the UN.
IMO I-III:	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.
Chemical tanker:	Tanker with coated or stainless steel tanks (IMO I-III).
LNG vessels:	Liquefied Natural Gas. Vessels for transporting liquefied natural gas (methane gas).
Lo-Lo:	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).
LPG vessels:	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.
LR1, product tanker:	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.
LR2, product tanker:	Long Range 2. Product tanker too large to pass through the Panama Canal of approximately 80,000 dwt.
Mbtu:	Million British Thermal Unit. Unit of measure indicating the amount of energy included – equivalent to joule or calorie.
Medium, tanker (MR):	Medium Range. Product tanker of between 25,000 and 50,000 dwt.
MMboe:	Million Barrels of Oil Equivalent. Measure of the amount of barrels of oil/gas contained in a field.
Multi-Purpose:	Dry bulk carrier with multiple applications, mainly as a feeder vessel or for special cargo.
Offshore vessel:	Vessel serving the offshore oil industry.
OPEC:	Organisation of Petroleum Exporting Countries.
Panamax, container:	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.
Panamax, tanker:	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.
Panamax, dry cargo:	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.
PCC:	Pure Car Carrier. Car carrier built exclusively to transport passenger cars.
PCTC:	Pure Car Truck Carrier. Car carrier built to transport small and large passenger cars (SUVs, MPVs, etc.), trucks and other contractor equipment.
Post-Panamax:	Container vessel of approximately 4,000+ teu that is too large to pass through the Panama Canal.
Product tanker:	Tanker vessel with coated tanks used to transport refined oil products.

PSV:	Platform Supply Vessel. Offshore vessel serving the offshore oil installations.
Reefer:	Container vessel with cooling/freezing capacity.
Reefer vessel:	Bulk carriers with a large reefer capacity in the holds.
Ro-Con:	Ro-Ro vessel with container capacity.
Ro-Pax:	Ro-Ro vessel with passenger capacity.
Ro-Ro:	Roll On – Roll Off. Common description of vessels on which the cargo is rolled on board and ashore.
SSY:	Simpson Spence & Young. British ship brokering company. www.ssy.co.uk
Stand-by vessel:	Offshore vessel used to monitor and fight fires and environmental accidents on oil rigs.
Suezmax:	Crude oil tanker with the maximum dimensions for passing through the Suez Canal (approximately 120,000—200,000 dwt.).
Teu:	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.
Ton-nautical mile:	Unit of measure indicating the volume of cargo and how far it has been transported.
Tonnage:	Synonymous with “vessel”.
ULCC:	Ultra Large Crude Carrier. Crude oil tanker above 320,000 dwt.
VLCC:	Very Large Crude Carrier. Crude oil tanker of between approximately 200,000 and 320,000 dwt.
VLGS:	Very Large Gas Ship. LPG ship with capacity above 60,000 cbm.
WTI:	West Texas Intermediate. Oil price benchmark in the USA.

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