Q3 2017 Earnings Call

Company Participants
• Petros Alexandros Pappas
• Simos Georgios Spyrou
• Hamish Norton
• Christos Begleris

Other Participants
• Frank Galanti
• Noah R. Parquette
• Fotis Giannakoulis
• Amit Mehrotra
• Herman Hildan
• Magnus Fyhr
• Harsha Gowda

MANAGEMENT DISCUSSION SECTION

Operator

Thank you for standing by, ladies and gentlemen, and welcome to the Star Bulk Carriers Conference Call on the Third Quarter 2017 Financial Results. We have with us, Mr. Petros Pappas, Chief Executive Officer; Mr. Hamish Norton, President; and Mr. Simos Spyrou and Mr. Christos Begleris, Co-Chief Financial Officers of the company. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session.

I must advise you the conference is being recorded today.

We now pass the floor to one of your speakers, Mr. Pappas. Please go ahead, sir.

Petros Alexandros Pappas
Thank you, operator. I'm Petros Pappas, Chief Executive Officer of Star Bulk Carriers, and I would like to welcome you to the Star Bulk Carriers conference call regarding our financial results for the third quarter of 2017. Before we begin, I kindly ask you to take a moment to read the Safe Harbor Statement on slide number 2 of our presentation.

Let us now turn to slide number 3 of the presentation for a summary of our third quarter 2017 financial highlights in comparison to the same period last year. In the three months ending September 30, 2017, net revenues adjusted for non-cash items, less voyage expenses, amounted to $63 million, 44% higher than the $43.7 million for the same period in 2016. Adjusted EBITDA for the third quarter 2017 was $28.6 million versus $11.9 million in the third quarter 2016, an increase of 141%.

Adjusted net loss for the third quarter amounted to $5.3 million or $0.08 loss per share versus $20.3 million adjusted net loss or $0.44 loss per share in Q3 2016. Our Time Charter Equivalent Rate during this quarter was $9,619 per day compared to $6,885 per day in the same quarter last year. Our average daily operating expenses were $3,947 per vessel per day.

On the commercial side, we have expanded our vessel operating capability with a new Geneva-based subsidiary, Star Logistics. The new entity will focus on expanding our cargo flow on Kamsarmax, Ultramax and Supramax vessels through direct contact with end users of dry bulk commodities. On the financing side, we have refinanced our senior notes due in 2019, effectively pushing back the maturity by three years to 2022.

I will now pass the floor to our co-CFO, Simos Spyrou, for an update on our operational performance for the quarter.

Simos Georgios Spyrou
Thank you, Petros. Slide number 4 highlights Star Bulk's strong liquidity position. We currently have an all-in cash breakeven, which including OpEx, corporate overhead, interest, lease payment and drydock provision, is approximately $7,600 per vessel per day. Our lower breakeven has enabled the company to have positive free cash flow of $15.7 million during the third quarter of 2017. On the right-hand side, we provide recent balance sheet information on our cash and debt positions.

As of November 17, 2017, our total cash balance stood at $263.7 million. Total debt as of the same date stood at $1,044.5 million. Both figures above are adjusted for the acquisition of the Cape Triumph, which will be delivered to us within December.

The remaining CapEx on the three new Kamsarmax vessels that we are due to take delivery of is $103.5 million, all of which is expected to be due in Q1 2018, when we will be taking delivery of the three vessels. One of the three vessels has variable financing with fixed debt amounts and no LTV test at drawdown. The remaining two newbuildings are being financed with $30 million of delivery financing for each vessel that would leave around $3.5 million of cash required in order to take delivery of all three vessels.

Finally, on the bottom right-hand side of the slide, you can see the evolution of our adjusted EBITDA, which has been growing continuously as the market has been improving from the historical lows of the first quarter 2016. We aim to continue keeping our costs low in order to be able to increase our profitability as charter rates improve.

At this point, we would like to highlight that Star Logistics will be using freight derivatives to hedge its market exposures. Accounting standards may result in recognizing gains or losses on the derivatives before recognizing the revenue which is being hedged. Star Logistics' net market exposures will, however, be very small.

In slide 5, we want to update you on our fleet employment. We have fixed 28 vessels, mostly on short-term periods with three deliveries around the end of the second quarter

2018. In addition, four index-linked Newcastlemax vessels are employed with a major miner for a series of consecutive voyages, and another Newcastlemax vessel is employed on a time charter contract with a major trading house at BCI + 32%.

Please turn now to slide number 6, where we summarize our operational performance for the third quarter 2017. The combination of our in-house management and the scale of the group provide us significant advantages in terms of cost and quality, which our customers and shareholders can enjoy. OpEx was $3,947 per vessel per day for the quarter, in line with our performance over the previous quarters. Net cash G&A expenses adjusted for one-off restructuring expenses were $1,074 per vessel per day for the quarter. Our low cost structure is complemented by excellent ship management capabilities as Star Bulk is ranked in the top three among managers evaluated by Rightship. We are focused on having the highest standards of vessel safety and maintenance to meet the requirements of our strictest and most demanding clients.

Slide number 7 shows that Star Bulk is one of the lowest cost operators among U.S.-listed rival peers based on the latest publicly available information. Star Bulk is one of the leaders in cost efficiencies among the industry with OpEx approximately 10% below the peer average. In addition, we have been ranked number one in the latest Shipping Benchmarking Initiative of the Boston Consulting Group, with OpEx 15% below the peer average. The dry bulk sample includes 26 reputable peers owning and managing 755 dry bulk vessels, and is based on the 2016 financial year. This is the fifth consecutive year we have participated in this benchmarking exercise as we remain committed to improve our overall management practice and optimize our daily running costs in order to maximize shareholder value creation. We always continue paying a lot of attention on the condition of our vessels in order to remain at the top of the list of our commercial partners.

I will now pass the floor back to Petros for a market update and his closing remarks.

Petros Alexandros Pappas

Thank you, Simos. Please turn to slide 8 for a brief update on supply. During 2017, the dry bulk fleet has grown by 2.9%, a total of 36.5 million deadweight tons has been delivered, and 13.3 million deadweight tons has been sent to demolition for a 23.1 million deadweight tons net inflow.

Dry bulk contracting during 2017 has remained relatively low with a total of 22.5 million deadweight tons reported by Clarksons as firm orders, but also, with approximately 25 million deadweight tons of identified LOIs and options pending to be confirmed or canceled.

The dry bulk order book, therefore, ranges between 8.3% and 11% of the fleet, depending on the percentage of LOIs and options that will ultimately materialize. This compares to 12% order book during the same period last year and 18% the year before.

As previously projected, full year net fleet growth is expected to end up around 3% during 2017, up from 2.2% during 2016. This is the result of a slowdown in demolition activity from 29.3 million deadweight tons during 2016 to around 14 million deadweight tons during full 2017. Dry bulk fleet growth is expected to be around 2% during 2018 as both scheduled deliveries and scrapping are bound to decrease.

Let's now turn to slide 9 for a brief update of demand. As per Clarksons' latest report, during 2017, total dry bulk trade will grow by 4.2% in tons, up from 1.3% during full year 2016. Dry bulk ton miles will expand at a higher pace, closer to 5.3% from 2.1% during 2016. We expect ton miles trade to continue to grow at a higher pace than tons during 2018 and 2019 due to Brazil iron ore and West Africa bauxite mine expansion, increasing distances for coal trade, and healthy grain trade from the Atlantic to the Pacific.

During Q3, international steel prices and steel mill profitability experienced a strong increase, which has supported the 6.9% year-on-year increase in global steel production. Apparent crude steel consumption in China has increased by 14.8% during the same period on the back of infrastructure and real estate investment growth, and substitution of low-quality steel from induction furnaces. These shutdowns have led to regional shortages of steel, and have provided strong support for blast furnaces and big iron production.

Looking forward, we expect steel mill utilization to correct on the next months due to seasonality and steel cut mandates to lower pollution. This is expected to lend support to steel prices and profitability over the next months, and inflate iron ore consumption as of March 2018 forward.

Strong growth in China hydro power generation and the rebalancing of domestic production has kept coal imports relatively flat during the third quarter. Having said that, coal imports have rebounded by 13.7% during the first 10 months of 2017, on the back of strong electricity demand growth. We find it encouraging for medium-term coal import prospects that domestic coal production growth has slowed down.

Domestic production currently ranks below 2014 levels, while total electricity generation during the same period has increased by approximately 15%. Furthermore, it is worth mentioning that coal stocks at Indian power plants have decreased to extremely low levels, and are expected to support imports in the short term.

We're generally positive about the market for at least the next couple of years where supply will be relatively restrained and demand will remain solid. Thereafter, the impending environmental regulations will contribute to vessels scrapping and slow steaming, as well as reduced vessel utilization and efficiencies.

However, if [indiscernible] has embarked a massive and disciplined new building ordering, such a regulation-led market upturn may prove to be short lived.

I will now pass the floor over to the operator to answer any questions you may have.

Q&A

Operator

Thank you, sir. Your first question comes from Ben Nolan of Stifel. Please ask your question.

<Q - Frank Galanti>: Yeah. Hi. This is Frank Galanti on for Ben. Just had a question regarding scrubbers. I know you talked about it last quarter, but wanted to get your thoughts on timing, particularly, when you guys would think about bringing which vessels you're starting to put scrubbers on to shipyards, kind of how long does it take to install? And then if you guys anticipate any delay issues from kind of an oversubscription of people trying to install scrubbers at the shipyards.

<A - Petros Alexandros Pappas>: Our scrubber expert is Hamish. Hamish, please respond.

<A - Hamish Norton>: Yeah, sure. So, Frank, first of all, the actual time it takes to install a scrubber once it has been delivered to a shipyard and then shipping that to shipyard is really quite short. And would, for example, not add to the time of standard dry docking and it probably can be accomplished within a couple of weeks. And there's certainly no danger of too many people wanting to install scrubbers soon. In 2020, that may change.

<Q - Frank Galanti>: Okay. So, then kind of following up on that. Do you anticipate any additional OpEx increases? I know you guys had talked about a kind of a one to two-year payback period. But is there any idea on kind of increased expense from crew training or dealing with the waste product from scrubber technology?

<A - Hamish Norton>: That depends how complex and how complex a scrubber that you install. The scrubbers that we've been considering would not increase OpEx in any material way. There would have to be a certain amount of crew training but not a tremendous amount and there would not be issues of waste disposal. A scrubber in operation typically consumes maybe 1% or 1.5% more fuel than operating the same ship without a scrubber. But, of course, operating with a scrubber, you're burning much cheaper fuel. And that goes into voyage costs, which if the ship is time chartered, those voyage costs are picked up by the charterer. So, I hope that's relevant to your question.

<Q - Frank Galanti>: Yeah. Yeah. It's actually – it's very helpful.

<A - Hamish Norton>: Frank, by the way, whilst we have been studying this matter for the last 14 months in-depth, we have not yet taken the final decisions about which way we're going to go, just so that you know.

<Q - Frank Galanti>: Yeah. That's very helpful. And that's all for me. Thanks so much.

<A - Hamish Norton>: Thank you.

Operator

Thank you. Your next question comes from the line of Noah Parquette of JPMorgan. Please ask your question.

<Q - Noah R. Parquette>: Thanks. I wanted just to follow up on the logistics business you're starting. Can you talk a little bit? Is there certain commodities that you aim to focus on? And with this, is there a portion of your fleet that you plan on devoting to the business?

<A - Hamish Norton>: Thank you. You mean on what kind of commodities we will be carrying with the Star Logistics Cargo? Is that what the question was about?

<Q - Noah R. Parquette>: Yeah. Is there a plan devoting to coal or is there anything or just kind of more about the strategy?

<A - Hamish Norton>: Well, perhaps that gives me also the opportunity to talk a bit about Star Logistics and why we're doing it also. First of all, most of the trades, to answer your question, are going to be grain trades, which is good because it is a trade that doesn't damage the vessels' hauls. The reason why we're going towards the Star Log solution is – there's a number of reasons, actually. First of all, it's going to source employment for our vessels in the future for our own vessels. Then we get a lot of market information, and we get it from the dark side. The dark side is chartering, is charterers, and I don't mean it in any clandestine way. I mean that us owners basically are mostly in the dark as far as what the market is doing and what cargos are coming and when and all that stuff.

And I think that by immersing ourselves in that business as well, we have to learn a lot and we get information that will help us in fixing our own vessels as well. Then it is also a cheaper solution in a way. I mean, when you charter a vessel at half, you basically pay almost – [ph] 3.75% of less commission, plus one or two brokers depending on who you get the business from. By having our own company, we'll probably be able to lessen that to much less than [ph] 3.75% . And through that, we will cover our overhead cost of that company. But overall, if we have a lot of business going through the company, that is going to make it cheaper for us overall.

Then we'll be able to take advantage of opportunities. If we see an owner who is very afraid about the future and he's willing to fix below FFA levels, maybe we can charter in and then hedge it on FFAs and make a nice margin in between. Then we'll finally get some optionality ourselves. We, ship owners, are used to giving optionality. Perhaps we get the opportunity of getting some optionality going forward.

And of course, we'll improve our relationships with cargo owners and cargo movers. And hopefully then, we will even make a trading profit out of this company. So, you gave me the opportunity to talk about Star Bulk a little bit.

<Q - Noah R. Parquette>: Okay. That's interesting, okay. And just another question on – you touched on the Chinese environmental regulations. Do you guys it will change the – about the seasonality of dry bulk trades particularly Q4 and

Q1? Do you have any thoughts to that, the effects that would have?

<A - Petros Alexandros Pappas>: Right. We have been discussing this internally. Well, first of all we think that it's not going to affect the total trade as a starting point. And the reason we think that is because we see that we still make healthy margins. We see that steel consumption in China is increasing by 14.8% this year. And we think that that is going to continue going forward. What may happen now – what may happen is that this trade could be moved for later on in time. So, the question is whether the Chinese will continue to import or not, will they continue to import and stock some iron ore because they will need that after the second quarter or not. It's possible they will do that to a degree. So, we do not believe it's going to happen to a great degree because if that happens, we will have a huge spike in the market now on Q2 next year.

So, our opinion is that it will happen to a degree, but not substantially because if they stop importing right now let's say from now on in Q1 and they start importing just Q2, they will just shoot themselves in the foot, and we will see a huge increase in the market. We will see somewhat of a better [indiscernible] (00:23:44) because it makes sense that there will be some slowdown in the next few months.

<Q - Noah R. Parquette>: Okay. That's all I have. Thank you.

Operator

Thank you. Your next question comes from the line of Fotis Giannakoulis of Morgan Stanley. Please ask your question.

<Q - Fotis Giannakoulis>: Yes. Yes. Hi, guys. Thank you. Petros and Hamish I think your balance it looks quite strong right now. Your net debt has dropped around 50% of your fleet value. And you have $260 million cash in your balance sheet. I wonder how much of

this cash is excess cash? How much do you want to keep it in order to navigate the volatility of as a safety to navigate the volatility of the Capesize market, and how much is available for acquisitions, or buybacks, and how are you planning to use it?

<A - Petros Alexandros Pappas>: Hamish, do you want that?

<A - Hamish Norton>: Sure. Look, Fotis, we are shareholders. The Pappas family are major shareholders. I am relative to my net worth, a major shareholder. And we're always looking at how do we make the most benefit for the shareholders, and obviously the cash is part of that. Some of it obviously, is needed to moderate the volatility of the dry bulk market, and some of it, we need to keep in reserve to make sure that we don't have any hiccups when it comes to refinancing our debt. But you can be assured that we're motivated like shareholders, and we're looking at ways to get as much cash into the hands of shareholders as possible.

<Q - Fotis Giannakoulis>: Thank you very much, Hamish. From your answer, I understand that the first priority for anything that is in excess would be returning capital to the shareholders, is that correct, rather than acquisitions?

<A - Hamish Norton>: We look at acquisitions from a point of view of shareholders. And we are really motivated to make sure the share price goes up and obviously increasing the liquidity of the share is good. If we can do that in a way that maintains or benefits shareholder value, but we are not motivated simply to increase the fleet unless that fleet increase benefits to shareholders directly. And that's not the case with every company, but it's certainly the case with us. So, we look at acquisition opportunities and we welcome them and sometimes they can make sense.

<Q - Fotis Giannakoulis>: Thank you very much, Hamish. That's very helpful. One more question about how you manage your risk. You mentioned about a new entity that you have established, that you're going to take some [ph] SSA positions. I was wondering how much would be the maximum value at risk of these positions? Is it something that you can quantify at this point?

<A - Hamish Norton>: Fotis, this is going to be extremely low. When we fix a vessel, it's like going along in a market. We will hedge it on the FFA right away. If we fixed on a period, then we would keep and hedge the optional period. Otherwise, I think that a great percentage of our fixtures one way or another is going to be hedged.

<A - Petros Alexandros Pappas>: Yeah. And, I mean, the policy is at least, at the moment, to have fewer than 500 days value at risk.

<Q - Fotis Giannakoulis>: Thank you. That's very helpful. Pretty much marketing-neutral from what it seems.

<A - Petros Alexandros Pappas>: Yeah.

<Q - Fotis Giannakoulis>: One last question about the market. Petros, you talked about the policy induced a slowdown China that you expect to come in the next couple of months. Have you seen any signs, any early signs of this seasonal or policy-induced slowdown? And what do you expect to be the reaction after that in March? Do you see that it can potentially be disproportionally higher increase after this seasonal slowdown?

<A - Petros Alexandros Pappas>: Yeah. Well, we've seen the market slowdown in the last two weeks, especially on the smaller sizes, but not that much on the Capes. We've seen a slowdown there, well, but not big one. It was more on the smaller sizes.

I think this was the result of a number of things. It wasn't just the slowdown that we're talking about. I mean, in overall, there were a number of things. Like for example, hydropower production in China was strong and in the last couple of months and that actually influenced coal imports negatively. Then the U.S. grain market has not really gone to full steam yet. Then [indiscernible] railroad head is under maintenance and that has obliged coastal fleets in China to get out in the open market and increase competition. All these actually affect the smaller sizes. Also, we had lower iron ore imports in October like 79.5 million tons versus – but that may also be the – because we had very – record imports of iron ore in September, which was around 2 million, so there was a slowdown. On the other hand, however, we saw that 31% of these 79.5 million tons of iron ore imports came from Brazil instead of the average of 21%. So, those additional tons actually come from a triple distance away than from Australia. So, overall, I think that it is not just the environmental roles in China. I think it is a number of things that have influenced, but you see that does influence them a lot. And yes, we think that it is possible to a certain extent that the market might start improving in Q2 versus Q3 this year exactly because of all these divisions being mandate and the environmental regulations of China coming to an end at the end of March next year.

<Q - Fotis Giannakoulis>: Thank you very much, both. That has been very helpful.

<A - Petros Alexandros Pappas>: Thank you.

Operator

Thank you. Your next question comes from the line of Amit Mehrotra of Deutsche Bank. Please ask your question.

<Q - Amit Mehrotra>: Yeah. Thanks, everybody, for taking my questions. So, my first question is just a follow-up on the Geneva-based enterprise logistics or Star Logistics. It's not super clear to me or not clear to me why you would need to create a home enterprise to basically hedge with FFAs. It seems like that can kind of be done at Athens. So, there's obviously – the question is really related to this. Obviously a very big charter, if not the biggest charter of dry bulk vessels based in Geneva. And so, the natural question I guess from me is do you have any partnerships with large commodity houses or trading houses or companies like this that would maybe make this an interesting strategic sort of longer-term strategic move. Just any help there around why it's based in Geneva. Are there any partnerships? Anything to understand the long-term economics of this business would be helpful. Thank you.

<A - Petros Alexandros Pappas>: Thank you, Amit. First of all, at the beginning, we will not be chartering our own vessels. I mean, we're just at the first three weeks of this. So, what we're doing is we're charting vessels from the outside. And those need to be hedged. When we hedge our own vessels at Star, we basically charter them out for a certain period. Like for example in the last couple of months, we have taken a view that Q1 next year should be covered at relatively good rates that we've seen over that period and we have fixed a good percentage of our fleet through Q1, and that is because seasonally, Q1 is a difficult quarter, so we've done that. And that is hedging in the fiscal market.

We don't need really to hedge on the FFA market especially because the FFA market actually has been rather low and the fiscal market has been higher. It didn't make any sense to hedge there. What we're doing is we're – yes, we are close to some important charters, important owners of cargo or traders of cargo or traders of cargo. But if I can, I would not like to divulge the name right now. But, yes, we're close to people like that. We need to be in Geneva because that's where the center of trading is. We took over an operation that had stopped trading in – during the last few months, and therefore we started with very low operating expenses, start-up expenses, and the goal is to be able to fix our own vessels in the future but we're talking about Years from now.

At the beginning, we're starting very carefully with chartering in with a fixed in cargoes within the Atlantic mostly and then chartering vessels against them. When we fixed the cargoes, we also hedge them. When we charter the vessels, we don't hedge them. If we can do it at the same time and we see some profit there, we'll take that as well.

<Q - Amit Mehrotra>: Got it...

<A - Petros Alexandros Pappas>: Yeah. Go ahead.

<Q - Amit Mehrotra>: I'm sorry, Petros. I'm sorry, I interrupted.

<A - Petros Alexandros Pappas>: No, no, no. That's it. That was it.

<Q - Amit Mehrotra>: Okay. So, just if I understand then, it seems like it's a small step in a direction and may ultimately whether it's years from now lead to a more comprehensive strategic relationship between the asset owner and the cargo owner? Is that the right way I should think it? They're very longer-term in nature.

<A - Petros Alexandros Pappas>: Yeah. It could be. It could be. Yes.

<Q - Amit Mehrotra>: Okay. Okay. Thanks. And then just a couple of other quick ones for me. Petros, there's obviously been a lot of like one-off acquisition and divesture activities in the market and I think you guys have also participated in some of that one-off activity. But just wondering if there's been any appetite out there for something bigger whether it's a larger ship for share or ship for [ph] stock deal (00:36:39). It would be kind of appealing for Star Bulk I think because it allows you guys to invest to the recovering point of the cycle.

It expands, diversify the share capital base which I think is somewhat needed. You could argue and I would obviously be very appealing. So, just any thoughts there in terms of the scope of what you see in the market if there's scope for actually that to happen and if you're thinking about potentially engaging and something like that, if the right opportunity comes by.

<A - Petros Alexandros Pappas>: Hamish would you like to take that?

<A - Hamish Norton>: Sure. Sure. So, look we would love to do something like that. And for all the reasons, you talked about, it diversifies the shareholder base. It presumably increases the liquidity of the share. If it's structured properly, it should reduce our overhead per ship per day. And we look at pretty much every opportunity that's out there but the main hurdle it has to pass is it has at least to make sense from the point of view of the current shareholders. And if we see something that makes sense of the point of view of the current shareholders, we'd love to do it.

<Q - Amit Mehrotra>: Right. Okay. That's a fair answer. I appreciate that. One last question for me on the scrubbers, Hamish, just a follow-up. I mean, correct me if I'm wrong, but it just doesn't seem like it would probably make any sense for you guys to think about installing scrubbers until really probably late 2019? Before anything else, just given the deflation and the cost that will likely happen if you look at what happened on the ballast water treatment facilities, the cost came down precipitously over call it a couple of year timeframe, and then there's also this question about what you actually do with sulfur, whether it's kind of open or closed loop and there's questions around that.

And there's obviously propulsion technology, what that may look like to offset some of that. So, I mean, there's just a lot of variables. And so, is it safe to assume, I know a couple of quarters ago, Petros talked about financing potential.

But, I mean, it's fairly safe, you would say if not, please correct me if I'm wrong, to assume that there's really no decision that should be made on this for the next at least one year, I would imagine?

<A - Hamish Norton>: Well, you're certainly right that installing a scrubber on December 31, 2019 is the optimal date.

But there are issues of shipyard capacities, scrubber manufacturer capacity and so on that probably pushes the optimal date into a band before that. But we're looking into when the decision would have to be made to actually get everything installed. And trust me, we're paying a tremendous amount of attention to that question.

<Q - Amit Mehrotra>: All right.

<A - Hamish Norton>: But just as it, by the way, a technical answer to a question you didn't ask, closed-loop scrubbers put all the sulfur into the sea. And if all the oil and gas were scrubbed by ships and the sulfur placed into the sea, it would be a negligible increase in the sulfur content of sea water.

<Q - Amit Mehrotra>: Okay. That's helpful. One last one from me, if I could, since I'm, I think, at the tail end of the questions here. In terms of the average rates in the quarter, they were a little bit lower than what I had in my model.

And clearly, I know that this – my model is not necessarily the most perfect in terms of estimating rates exactly, but I just want to understand how you think about the performance relative to the benchmarks when you do have this cape-size pool-like structure – I know it's not a pool but a pool-like structure in terms of share information, you got the index links. Anywhere and any reason to sort of look at that performance in the quarter and say, maybe it should have been a little bit better, maybe – am I just over-reading it? Thank you.

<A - Hamish Norton>: Amit, when the market is going up, everyone, you will see that everyone will underperform the market. And when the market is going down, everybody will over perform their market. The reason is simple. You fix between 5 and 25 days your vessel, prior to opening.

<Q - Amit Mehrotra>: I know. I know that. But the question is even if you average out the average rate in the second quarter with the third quarter, you still – I mean, the company still underperformed those rates by a decent amount.

That's – I understand the lag effect and I think I'm taking into that into consideration. But maybe I'm just overlooking into it and there's nothing there to look at. I'm just wondering if there was any – anything to point out there.

<A - Hamish Norton>: Well, I – sorry, Amit. Actually – actually, you know what, the differences could be huge, like we have had vessels that over performed and underperformed through the market in single voyages by between 52% and 57% within two months. So, this can be – can be extremely high. So, also we have the three or four vessels chartered out from a year ago which kind of lowered our time charter income.

<Q - Amit Mehrotra>: Yeah...

<A - Hamish Norton>: Yeah. But generally, I think the main reason...

<A - Hamish Norton>: The main reason is – but that's not a lot bigger – a bigger part of the reason. Maybe, you will see next quarter better results.

<Q - Amit Mehrotra>: Yeah. Maybe my model was obviously a little bit optimistic as well, but that's okay. That's helpful. Thank you, all, so much for answering my questions. Have a good holiday if I don't talk to you before the end of the year. Bye-bye.

<A - Hamish Norton>: Thank you. Same to you, Amit.

Operator

Thank you. The next question comes from the line of Herman Hildan of Clarksons Platou. Please ask you question.

<Q - Herman Hildan>: Hello, everyone.

<A - Petros Alexandros Pappas>: Hello.

<Q - Herman Hildan>: My first question goes in Star Logistics. I'm just kind of curious on the size of investment that you're going to make into that [indiscernible] (00:43:12) in dollar amounts.

<A - Petros Alexandros Pappas>: The investment we'll make on that, well, we'll have the start-up expenses which are negligible. We have our overheads which, we think, will be in the very, very low seven figures. And then, the rest is going to be cash flow we may need for paying the chartered-in vessels and for hedging. That's it.

<A - Petros Alexandros Pappas>: Therefore, the investment, the immediate investment is almost nil.

<Q - Herman Hildan>: So, the question is relative to the core business, Star Logistics is not going to kind of become a sizeable investment for the company.

<A - Petros Alexandros Pappas>: No, it's not.

<Q - Herman Hildan>: Okay. Very good. The second question I have that you kind of touched upon briefly in the Q&A was obviously, now going into next couple of years with very low fleet growth, I guess, record low order book that's essential, the fleet, and already with a fairly decent leverage or manageable leverage position already. And what's the kind of – do you have any guidelines for how you expect to structure your balance sheet going forward? How do you kind of think about how you use the cash flow in the coming years? And whether you have any things on the agenda, for example, with the composition of your fleet that you would like to kind of grow or whether you're happy about your fleet position at this stage?

<A - Christos Begleris>: Herman, hi. This is Christos. As Hamish previously mentioned, we're always looking at accretive transactions to the shareholders, therefore, if there is an acquisition of a fleet that makes sense for us, we'll definitely go for it. As far as sort of main priorities on the balance sheet are concerned, we are here to see basically, our net debt going down in the next few years. Therefore, we hope that as we get operating cash flow from our vessels, we actually decrease our leverage in order for the next down cycle to find us with a very, very low, if not zero, net debt figure. Therefore, that remains one of our key priorities.

<Q - Herman Hildan>: But has there been any, call it, preliminary recessions on putting in place the buyback program or allowing to start to pay dividend at some point during 2018? Could you give some color kind of if there has been any discussions on that so far?

<A - Christos Begleris>: There have been discussions and reinstating dividend would be a second step after reducing our debt to levels that we feel comfortable with in order for us to be able to face the next down cycle with as low debt as possible. But yes, the second set would be reinstating a dividend policy.

<Q - Herman Hildan>: But could you then give us some color on kind of what the debt levels that you are comfortable with going into the next downturn, which hopefully, is quite some time away?

<A - Christos Begleris>: I mean, as I said before, the closest to a net debt zero figure, the more comfortable we are for the next down cycle. The goal here is for us to be a very low leveraged company that is able to distribute dividends both in down cycles, as well as in up cycles.

<Q - Herman Hildan>: Okay. Thank you. That's all for me.

Operator

Thank you. Your next question comes from the line of Magnus Fyhr of Seaport Global. Please ask your question.

<Q - Magnus Fyhr>: Yes. Hi. Just, Petros, you made a very bold prediction at the last conference call that rates would be over $20,000 at the time when I think rates were probably not approaching the teens yet. What does your crystal ball tell you for 2018?

<A - Petros Alexandros Pappas>: You mean I made that prediction for what, for Q4?

<Q - Magnus Fyhr>: No, for all of 2018.

<A - Petros Alexandros Pappas>: For all of 2018. Right. What does my crystal ball say? I've lost my crystal ball, but I think that 2018 is going to be better on average than 2017. Now, to what extent that is going to go, I don't really know. But as supply is going to be 2% and we expect demand to be above 3.5%, perhaps with ton miles even up to 4.5%, we think that is going to give a boost to the market. And the only thing we are worried about or what we're most worried about is Q1, which we're covering for. And otherwise, as I said, on average, I think it's going to be better. Whether that's going to be 10% or 30%, I don't really know. But I expect that we will see better rates.

<Q - Magnus Fyhr>: Thank you, Petros. I figure out I'll try. Thanks.

Operator

And your final question comes from Harsha Gowda of BlueShore Capital. Please ask your question.

<Q - Harsha Gowda>: Good afternoon, gentlemen. How are you?

<A - Petros Alexandros Pappas>: Good. Harsha, how are you?

<Q - Harsha Gowda>: I'm doing well, doing well. I just have – a lot of the questions were answered, but two maybe more conceptual questions. One, just from my experience, Petros, watching and being active in the dry bulk markets for many decades, the persistent strength that we've seen in the second half, especially in Capes, but even in some of the smaller vessels, is that an indication that we're finally balanced right now in the market? And the reason I ask that is because in light of the fact that 2018 and 2019 show, on a historical basis, probably record-low fleet growth, maybe going back until the 1980s before we saw less than this, is there a possibility that we could see a sort of a phase shift where rates really have a sharp reaction to an increase in demand over supply?

<A - Petros Alexandros Pappas>: Harsha, as I said, I am positive about both years. Now, whether the difference of 2% or 2.5% between demand and supply is going to get the market to a boom, I'm not sure yet. This usually happens when it is totally balanced. I'm not certain it is totally balanced right now. It could be there, it might not be there. It's not easy to assess that. But I think that we'll definitely see better markets in the next couple of years. And my hopes actually are even higher for after – once 2020 sets in because I believe that the environmental regulations will have a major positive effect on shipping. Of course, that has a lot to do with what we will be ordering. If we start ordering like there's no tomorrow, this effect will be not as strong on the market. But that remains to be seen. For now, the new orders, the confirmed orders are not a lot. But including the LOIs, they are pretty much, of course, above one-third of what were those orders in 2013. In the five quarters of 2013 and the first quarter of 2014, there were about 110 million tons ordered, confirmed. And that then tilted the market.

So, I think the fundamentals are better this time around. It's also good that banks don't lend. It's good that the Chinese banks are very careful as well on who to support on their new buildings. So, I believe that things look much better going forward, and I want to rule out a very strong market in the next decade.

<Q - Harsha Gowda>: And two more questions for you, Petros. You talked about what happened in the past when the market really sold off heavily. And a lot of that, it seems, also due to the sharp drop in crude oil prices. Now, you see prices have picked a little bit, and also, a lot of doubts are increasing about the true extent of a potential supply growth. So, how could your impression of, say, 2018 and 2019 change if we see a real increase in crude oil prices, a sustainable increase from these levels?

<A - Petros Alexandros Pappas>: Harsha, if you remember, in 2013 – sorry, in 2014, the last couple of months of 2014, prices of fuel oil went from $700 down to $170. And this was one of the main reasons why the market fell so abruptly. A second reason was that China stopped importing bauxite, nickel and coal for a few months. And that started creating problems for the market. And then, of course, vessels started – the vessels that were ordered started pouring in. But the fuel oil was the beginning of the downturn.

This time around, I do not believe that we have – we'll see fuel oil going down. I think we'll probably see it going marginally up. And therefore, that has a positive effect on the market. We like more expensive fuel oil, but it also – this is an equation that has a lot to do with where charter rates are. So, the speed of vessels depends on price of oil and charter rates. So, if price of oil goes up, vessels slow down their speed, and then as a consequence, charter rates go up, speed will go up again. It's like a yoyo, depending on what happens on one thing, it's the reaction of the other thing. Of course, what is very important, I think, as well is the dollar. The dollar is – if the dollar is weak, this is good for shipping because it makes commodities cheaper, it makes freight rates cheaper in local currency terms, and therefore, it encourages trade. And also, it's good for vessel prices because if dollar is cheap, the Japanese ship-owner who will want to sell his vessels will ask for more dollars to get the same yen. So, the dollar is also important. And, of course, the dollar is related to the oil price as well. So, if dollar is down, oil price goes up. So, all of that is – goes together. But the fact that the dollar is weak is a good thing for us right now.

<Q - Harsha Gowda>: And – thank you for that, Petros. My last question is kind of in line with what Hamish was saying about being a shareholder and the focus on having the share price reflect the true value of the company. When I look at the share price now, and I'm sure it's confusing also to you, I believe it's pretty simply known that the net asset value of the stock is probably close to the $11, $12 range, and now the company is generating very good cash flows probably in the double-digit free cash flow yield range. And this fourth quarter looks to be profitable and possibly even the first quarter, which is a weaker quarter historically, yet the stock is at such a big discount.

Is there – what can the company do to remedy that? I like to hear the fact that you're thinking about dividends in the future, but this is such a sharp discount in – it doesn't seem very warranted.

<Q - Harsha Gowda>: Yes, that's true. I wish I could compete with Oaktree.

<A - Petros Alexandros Pappas>: Well, I think that part of the reason why stock prices are lower, perhaps, than their net asset value is that people are expecting to see whether this upturn has legs or not. I happen to believe that this upturn does have legs, but this is also a seasonal market. So, if Q1 is, due to the various reasons we already discussed, is down, people will be scared. I mean, it's normal. And then, of course, that gives opportunity to buy, as Hamish said.

<Q - Harsha Gowda>: Great. Great. Well, I hope you keep considering that dividend idea once the restructuring deadlines have past. But thank you very much.

<A - Petros Alexandros Pappas>: Thank you, Harsha.

Operator

Thank you. I would now pass the floor back for closing remarks.

Petros Alexandros Pappas. As I mentioned at the end of the previous investor call, the world is striving for a cleaner environment. We shipping people must do our part. I advocate that we should work towards a mandatory slowdown on vessel speeds as a short-term measure and whilst medium, long-term measures are being contemplated. As an example, a 15% speed reduction would result in a 27% immediate overall emission reduction when we're presently negotiating a 42% emission reduction by 2050. Why wait for 2050 when we can achieve 65% of that goal in one day effortlessly and at almost zero cost to us, but to the huge benefit of the environment.

That's all, operator. Thank you very much.